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BUSINESS VALUATION & FINANCIAL ADVISORY SERVICES

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VALUE FOCUS

Auto Dealer Industry

Editorial Focus: Impact of COVID-19 | Data as of Year-End 2019

Mercer Capital is a national business valuation and financial advisory firm. Valuations of auto dealers require special knowledge of the industry, hybrid valuation methods, and industry terminology. This newsletter provides useful statistical metrics of the auto industry as well as content about the unique industry factors and value drivers.

The economic impact of COVID-19 is being felt far and wide, and the auto dealer industry has been and will continue to be affected. In this issue, we address a few of the issues that the auto dealer industry is currently facing. These articles first appeared our new weekly blog, ***Auto Dealer Valuation Insights***. To receive the most current news and insights, ***subscribe here***.

For more information, feel free to reach out to Mercer Capital's Auto Dealer Industry Group Leader, Scott A. Womack, ASA, MAFF at **womacks@mercercapital.com**.

When Might Things Return to Normal?

The term "24-hour news cycle" doesn't do justice to the rate at which new information becomes available and is consumed by people trying to understand the significant impact COVID-19 is having on all of us. Stay-at-home orders have created a huge demand shock, which is particularly harmful to a largely service-based economy. In this article, we contextualize some of the fallout that has been experienced and try to answer the question "when will things return to normal?".

March SAAR

As expected, SAAR (a measure of Light-Weight Vehicle Sales: Autos and Light Trucks) declined considerably in March as the early effects of COVID-19 began to impact just about every industry across the globe. SAAR came in at 11.372 million, the lowest level since April 2010. This also represented a decline of 32.4% from February. The 32.4% decline was only the fourth time since 1976 (when the SAAR was first recorded) that a 30% month-over-month decline has occurred. The first two instances were during a 6-month period of extreme volatility between September 1986 and February 1987, including three monthly increases of over 22% and two declines of 31.6%. Despite these anomalies, the only other significant month-over-month decline occurred in September 2009 when SAAR declined 35.8%. However, SAAR had increased by 14.2% and 28.1% in the two preceding months, so that September's steep decline was only 6.1% below the preceding June.

While the huge drop in volumes in March was certainly historic, it included a couple of weeks that were relatively unscathed by stay-at-home orders. April is likely to show further declines with significant uncertainty about when we will reach the bottom.

Putting it in Perspective

While there have been many sharp one-month declines in the SAAR, we note that even seasonally adjusting the data can fail to capture certain calendar anomalies, specifically when one month has an extra selling weekend. In looking at other significant events, such as the stock market crash in '87 and 9/11, the drop caused by the market crash was relatively short-lived and auto volumes actually spiked in the month following 9/11 as the country braced for war. To better understand where we might be headed and when things might return to some level of "normal," we analyzed prolonged declines, focusing on the 1981-1982 recession, the Persian Gulf War, and the Great Recession. Though these events do not align perfectly with COVID-19, observing how periods of economic turmoil affect the industry and examining the length of recovery time historically can provide future insight as we seek to climb out of the current crisis.

There are numerous ways to measure recovery. For purposes of this post, we measure "recovery" as how long it takes to return to a "steady state" of vehicle sales. We use a steady state figure of **15.6 million annual sales** from a 2015 paper written by Austan D. Goolsbee (University of

When Might Things Return to Normal?

(continued)

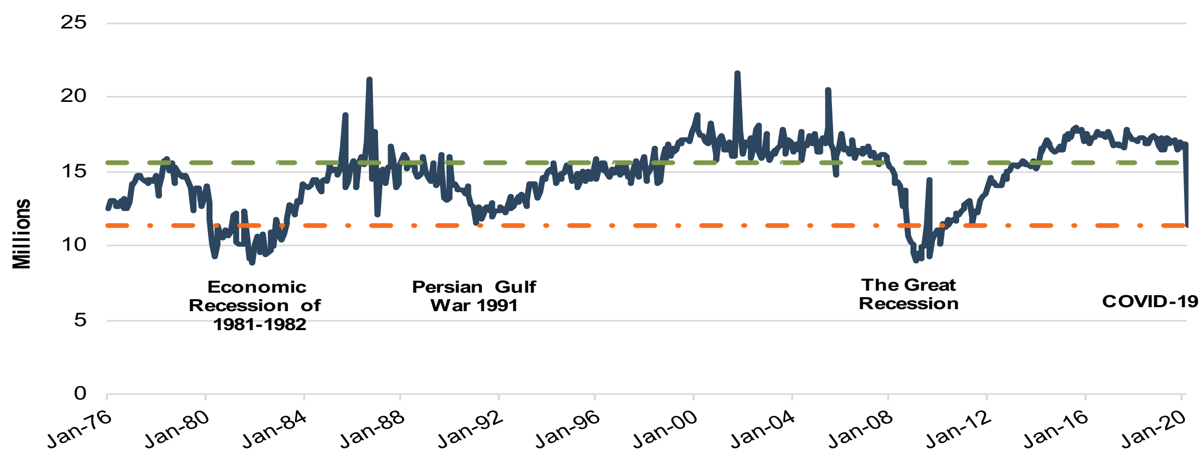
Chicago) and Alan B. Krueger (Princeton University). The paper analyzed the restructuring of General Motors and Chrysler. The inputs into the regression model used in the paper include:

- Real GDP Growth
- The unemployment rate
- Population growth
- The Federal Reserve's Senior Loan Officers' Survey (SLOOS) measuring willingness to lend to consumers
- Log of average real price of a gallon of gasoline (for the preceding quarter)
- Standard deviation of gas prices over the preceding four quarters

In every year since the paper was published, industry sales have surpassed 17 million, indicating the steady state may be biased upwards if rerun today. However, the data stops in 2007 just before the Great Recession, and because auto sales are procyclical, any increase in the steady state figure would likely be due in part to the longest economic expansion in the country's history over the past 11 years. Further, since vehicle sales are positively correlated with population growth, we would expect a long-term figure to be higher than early years and lower than more recent years. Ultimately, we find a steady state figure of 15.6 million to be reasonable for this analysis.

A Long Term View of SAAR

A long-term view of SAAR is presented in the graph below:



Source: FRED and Princeton University

When Might Things Return to Normal?

(continued)

The 1981 Recession

At the time, the 1981 recession was the worst economic downturn in the U.S. since the Great Depression. Triggered by a combination of monetary and global energy issues, unemployment reached 11%. While the effects of the recession were widespread, the manufacturing, construction, and auto industries were particularly affected. Auto manufacturers ended 1982 with **24% unemployment**. The industry saw 4 straight years of year-over-year declines in sales from 1979 to 1982 with the largest annual decline in 1980 at 19%. SAAR bottomed out in October 1981 with only 9,209,000 annualized vehicle sales; from there, SAAR increased 17% in both 1983 and 1984. SAAR reached over 15.6 million sales in August 1985, approximately 7 years after it first dropped below this threshold in September 1978.

As noted previously, population growth likely indicates the 15.6 million is a high threshold for this period, particularly since SAAR was only above this for a brief period in 1978. The precipitous decline at the beginning of 1980 appears to have been restored by the end of 1983, indicating just 4 years before recovery.

The Persian Gulf War

The Persian Gulf War, precipitated by Iraq's invasion of Kuwait, caused the oil shock of 1990. Though less severe than oil shocks that occurred in the 1970s, oil prices initially soared from a pre-invasion price of around $18 a barrel to above $40 in the late fall of 1990, leading to declining revenues for the auto industry. At the same time, the Fed was tight on interest rates, endangering an **already weak economy**. This combination of oil prices and economic policy brought the U.S. into a recession that hit the auto industry particularly hard. Vehicle sales declined each year from 1989 through 1991, with the biggest decrease in 1991 at 11%. It took until April 1994 for SAAR to reach 15.6 million again, about 4 years after it first began to drop.

The Great Recession

Arguably the most impactful event on the industry in recent history was the Great Recession (2007-2009). Precipitated by a financial crisis caused by a severe contraction of liquidity in global markets, businesses were forced to reduce their expenses and investments and layoffs resulted. From December 2007 to June 2009, real GDP declined by 4.3% and unemployment increased from 5% to 9.5%, **peaking at 10%** in October 2009.

The auto industry and other industries reliant on consumer loans (e.g., housing) suffered significant losses. In 2006 and 2007, vehicle sales volumes decreased about 2.5% consecutively, and the auto industry hourly workforce was reduced from over **90,000 to approximately 40,000.** Conditions worsened through 2008 and 2009, as sales declined 18% and 21%, which is the largest year-over-year decrease of any time period. SAAR dropped to just a little over 9 million in February 2009, 6.6 million below the steady state SAAR. However, through the assistance

When Might Things Return to Normal?

(continued)

of the government in the Troubled Asset Relief Program (TARP) and the end of the recession in 2009, the industry survived and returned to its steady state of 15.6 million vehicle sales in 2013, 5 years after it first dropped below that level in January 2008.

COVID-19

Although economic conditions currently point to a difficult period of uncertain length, there are some positive takeaways from looking at these past events. Periods of high growth have followed periods of low sales as consumers who delayed purchases in rough times returned to the market. SAAR increased 17% consecutively in both 1983-1984, following the 1981 recession. There were increases of 8% in both 1993 and 1994 following the Persian Gulf War. Finally, the auto industry experienced 5 years of expansion following the Great Recession, reaching similar sales as before the crisis and further set new highs in the 5 years after that.

Again, it may take a while to return to the 17 million in sales seen in the past few years, but that is above the long-term average and should not necessarily be the level from which we measure recovery. NADA expects it could take **three or more years** to return to this level, which would be reasonable given historical recovery times.

Conclusion

The auto dealer industry is resilient through tough times. We hope dealers are once again able to navigate both the known and unknown problems facing us today. Dealers must grapple with how to continue to pay their employees, alter their sales channels on the fly, and potentially even help teach their children at home.

Mercer Capital stands ready to partner with dealers in their time of need. Prior to the nationwide lockdowns, we were anxiously awaiting the NADC Conference in Florida at the end of April as well as the TAA/KYADA Conferences in June. We had hoped to launch this blog in happier times, but we still plan to offer our unique perspective as valuation experts as the pandemic impact unfolds. Working from home, we have more time to write these blogs, and we hope they are interesting to you. Feel free to reach out to us if you have valuation questions as to how your dealership may be affected.

Mercer Capital is a financial services firm specializing in business valuation. We also provide litigation support and transaction advisory services for clients big and small. Contact one of our professionals to discuss your needs in confidence. And stay safe.

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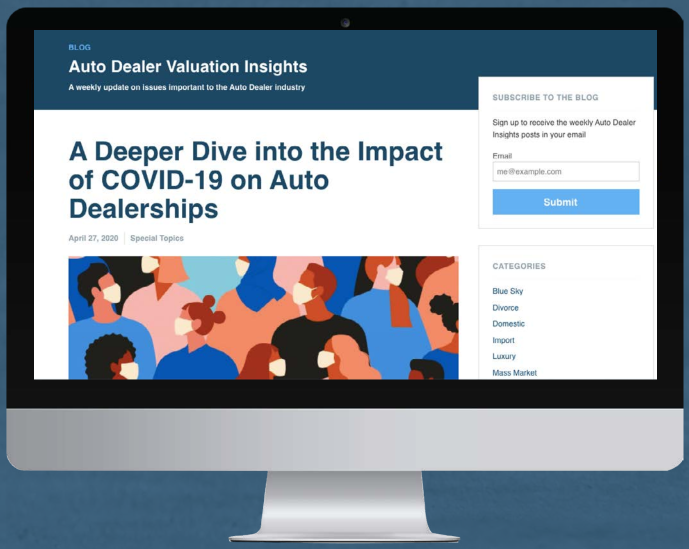

A Deeper Dive into the Impact of COVID-19 on Auto Dealerships

Auto dealers are in a unique situation. While technically categorized as consumer "discretionary" items, many people rely on their cars to navigate their busy daily lives. With activity grinding to a halt amidst stay-at-home orders, cars are tipping more towards discretionary items (despite many dealerships being deemed essential businesses).

While more practical than other expensive purchases, like a designer handbag, automobiles become less of a priority when budgets are trimmed, particularly when people are staying at home. All told, this will likely lead consumers to delay their purchases of cars, particularly those who want to peruse their options by walking a lot and test driving various makes and models.

While other retail industries have fallen prey to the "Amazon effect," auto dealers have avoided this fate because many consumers are not yet comfortable making such a significant investment without first getting behind the wheel. However, this means sales activity is even more adversely impacted by the current environment. Consumers with disposable income are more likely to spend it on other high-end items that require less personal inspection for style and feel before buying. As we'll discuss, this is just one of the impacts the coronavirus is having on the auto industry.

How Long Will COVID-19 Last?

The key questions for auto dealers, and all other business owners, are how long this period will last and how COVID-19 will impact consumer spending on the other side.

Buying a car is a significant investment that many consumers will simply delay as staying inside doesn't require much car travel. In fact, **some auto insurers will issue rebates** as they expect claims to decline during this period.

While lack of wear and tear will delay many timelines, people will still need cars. Significant mileage or a wreck are the most obvious reasons someone would require a new car, but not all purchases are necessitated by the status of a prior vehicle. Getting married, having a child, or turning 16 are life milestones that tend to increase car sales, and these are not necessarily going to be halted by the pandemic. However, if the economic reverberations cause consumers to forego rather than simply delay their automobile purchase as budgets are slashed on the backside of this, a permanent loss in demand would likely prove extremely detrimental to auto dealers.

How Will the Auto Industry Respond to COVID-19?

While the proliferation of the Internet may not have fully infiltrated the auto dealer business model before the pandemic, the impact of the coronavirus on the way people shop has likely forced dealers to reconsider their digital strategy. Tech-savvy consumers were already using services like TrueCar and Kelley Blue Book to increase price transparency and lower gross margins. While dealers have dipped into e-commerce to varying degrees, dealers have largely been thrust into it now.

A Deeper Dive into the Impact of COVID-19 on Auto Dealerships

(continued)

While dealers have dipped into e-commerce to varying degrees, dealers have largely been thrust into it now.

Aside from ramping up web presence, dealers must also consider how they will collectively respond to the reduced demand.

Contrast auto to another significantly impacted industry: restaurants. Restaurants can significantly decrease prices in order to keep customers coming through their doors. While they are sacrificing some profits by offering it cheaper, restaurants have plenty of turnover, and customers tend to return to their favorite places frequently. Auto dealers operate differently. Given the relatively long vehicle shelf life, dealers do not frequently experience near-term repeat customers (except for service and maintenance operations).

Dealers can **get creative with their inventory** to get cash infusions, though many will opt to offer increased incentives to boost sales. However, front-loading sales with incentives to make it through the tough times could have negative impacts on industry volumes as well as profits down the road. This pain will be particularly acute if some shoppers accelerate their purchases to take advantage of falling prices when they otherwise may have tried to delay a big expenditure by servicing their aging vehicle instead.

Incentive spending hit an all-time peak at $4,800 per vehicle in March, which supported the SAAR (a seasonally adjusted measure of Light-Weight Vehicle Sales) from dropping even further than it did. While annual sales have been above 17 million since 2014, this has included significant increases in incentives which come at the detriment of profitability. Gross profit is a much more relevant metric than revenue in the auto dealer industry, and revenues and volumes propped up by incentives that do not translate to improved gross profits will ultimately hurt dealership valuations as earnings deteriorate.

Government Response

Government response to this pandemic has come through both fiscal and monetary policy. Congress' efforts on the fiscal side have been more visible, culminating with President Trump signing a $2.2 trillion economic package (the "CARES" Act) into law on March 27. Stimulus checks have started to roll in and the small business loan program, Paycheck Protection Program or "PPP", **has already reached its $349 billion limit**. On Thursday, April 24th, **Congress passed an additional $484 billion economic package** with $320 billion replenishing the PPP, $60 billion in additional SBA disaster relief funds, and $100 billion to support hospitals and increased testing.

Government Response Impact on Dealerships

Many auto dealers, even those with significant top-line revenues, will qualify for small business grants and forgivable loans. For those on the fence about maintaining their workforce due to sharp decreases in demand for their ser-

A Deeper Dive into the Impact of COVID-19 on Auto Dealerships

(continued)

vices, these programs are structured to incentivize dealers to retain their staff.

The PPP is likely to boost morale for dealers able to retain their full staff during this time; this also saves future costs of having to train new staff when activity ramps back up. Still, tough decisions will have to be made, and auto dealers may be forced to cut costs they hadn't considered during the long bull market that categorized the past decade.

The auto industry isn't likely to receive the extensive aid being provided to airlines, but the small business loans won't be the only impact the CARES Act has on dealerships. The $1,200 payments to consumers are unlikely to motivate people to go out and buy a car, but it could provide enough money to make car payments and get tune-ups or other necessary maintenance.

Conclusion

At this point, there are likely more questions than answers. The first order and second order effects of the virus are being measured in real time, and we likely won't be able to fully understand its impacts until we have the benefit of hindsight. Government responses are likely to continue, though it is unclear the form of future actions.

What we do know is that many consumers are staying indoors, and odometers have slowed. Dealers must do what they can to maximize this downtime by increasing their digital presence and managing expenses and working capital. While dealers may need to sell at lower prices, they will have to balance near-term needs with long-term impacts. We have been impressed by the **outpouring of support dealers have shown for their communities**. We encourage everyone to continue checking in with family, friends, employees, customers, suppliers, and our local communities.

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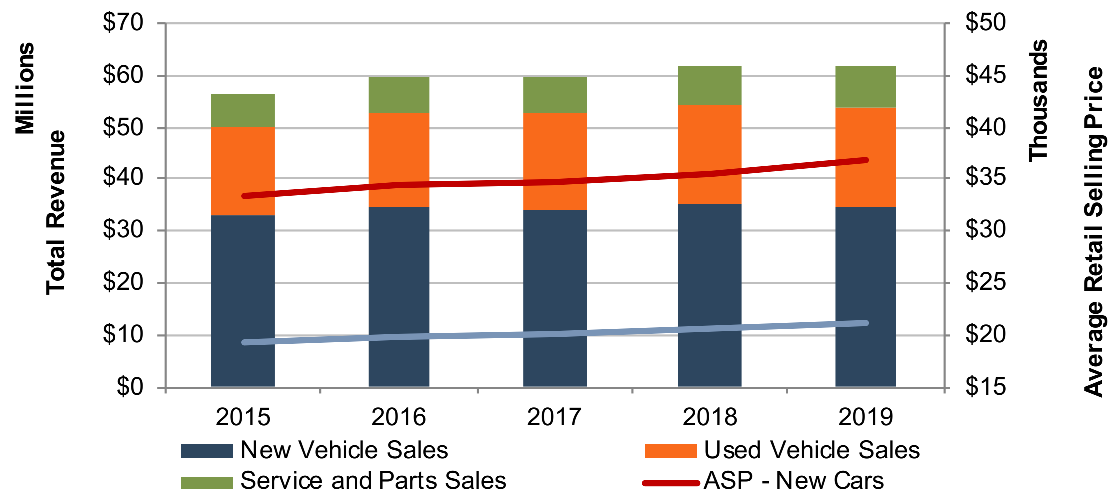
Average Annual Auto Dealer Profile

As of Year-End 2019

Average total sales per dealership increased 0.5% in 2019, driven primarily by increases in used car sales, which increased 3.3% or by $630 thousand per dealership. Service and parts departments increased 4.5%, but in dollar terms this was only $328 thousand. Revenue from new vehicles decreased 2.3%, though it continues to make up more than half of dealership revenues at 56%. Sales continued to march higher, despite declining volumes.

Combatting the 4.0% decline in average new vehicles sold, industry consolidation spreads lower volumes over fewer dealerships. The average retail selling price (ASP) of new cars and trucks also increased 3.4%. This accelerated in 2019, compared to a compound annual growth rate of 2.4% since 2015. In 2019, used vehicle sales increased both in price (2.5%) and quantity (2.1%), as the ASP of used cars increased to over $21 thousand, compared to nearly $37 thousand for new vehicles.

Total Sales and ASP for Average Light Vehicle Dealers



Source: NADA

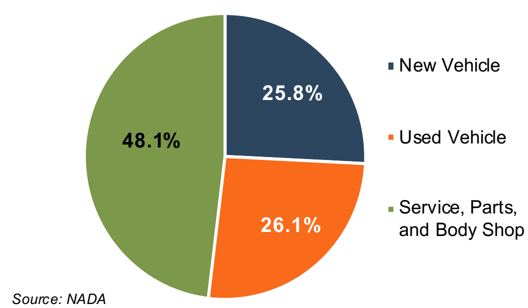
Domestic Dealerships

As of Year-End 2019

Gross Profit Trends

Gross profit increased 3.1% in 2019 for domestic dealerships, outpacing its compound annual growth of 2.7% since 2015. While achieving the highest level of gross profit ($6.3 million) in the past five years, domestic dealerships continue to earn the lowest gross profit compared to import, luxury, and mass market dealerships. Nearly half (48.1%) of gross profit in 2019 came from service and parts departments for domestic dealerships, up 46.2% from 2018. The remainder was relatively evenly split with used vehicle gross profit edging new vehicle gross profit, which declined from 27.8% in 2018 to 25.8% in 2019.

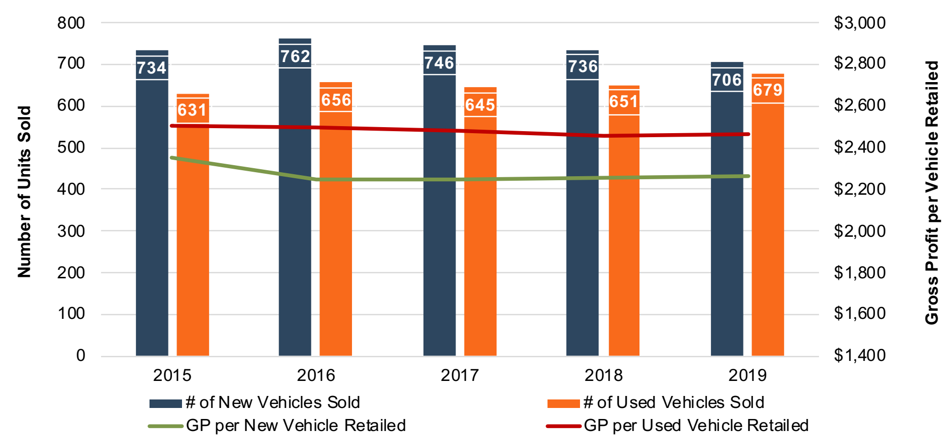
Gross Profit by Segment



Source: NADA

Domestic dealerships were the only category that did not see a decline in new vehicle revenues in 2019. However, the number of new cars sold dropped 4.1% in 2019, but used vehicle volumes increased 4.3% in 2019. Since 2015, the gap between new and used vehicles sold has declined from 103 units to just 27 more new than used. Gross profit per vehicle has trended downwards for domestic dealerships since 2015. However, gross profit per vehicle increased 0.1% in 2019 for both new and used vehicles, while these have declined 1.0% and 0.4% annually since 2015, respectively. In total, domestic dealerships have generally seen margin compression (GP per unit) and consumers have increasingly opted for used vehicles over new ones.

New and Used Vehicles Sold and Gross Profit per Unit



Source: NADA

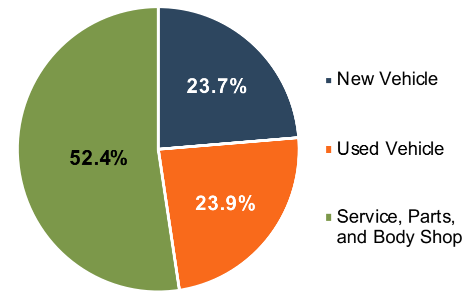
Import Dealerships

As of Year-End 2019

Gross Profit Trends

Gross profit increased 4.0% in 2019 for the average import dealership, led by a 5.0% increase in service and parts departments. This represented a rebound from a recent low of $7.5 million in 2018, down from a recent high of $7.8 million in 2016. More than half of gross profit in the first half of 2019 came from service and parts departments for import dealerships. This is similar to the breakdown seen for domestic dealerships with used vehicles making up a bit more of gross profit than new vehicles. Service and parts departments have considerably higher margins, which allows them to make up a significant portion of gross profit without being a large portion of the dealership's revenue.

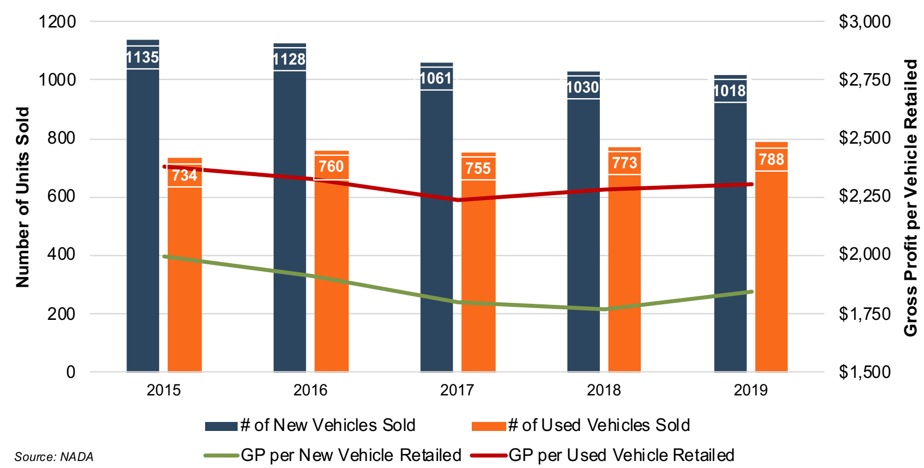
Gross Profit by Segment



Source: NADA

Import dealerships sold about the same number of vehicles in 2019 as the prior year, though the average number of new vehicles dropped by 12 units while used vehicles increased by 15. This represented a recent peak for used vehicles sold, which has increased 1.8% annually since 2015. This also represented a five-year low for new vehicle volumes. Still, import dealers sold 230 more new vehicles than used in 2019, the largest of all categories. While gross profit per vehicle is the lowest of all categories and has generally declined over the past five years, import dealers have seen a rebound of 4.2% from a recent low in 2018 for new vehicles and 2.8% from a recent low in 2017 for used vehicles.

New and Used Vehicles Sold and Gross Profit per Unit



Source: NADA

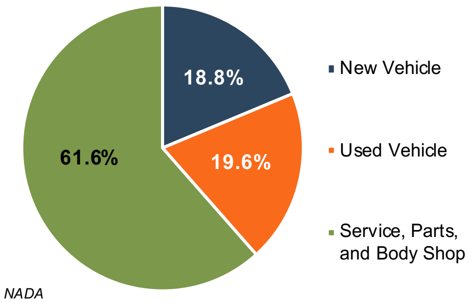
Luxury Dealerships

As of Year-End 2019

Gross Profit Trends

Average luxury dealership gross profit decreased 1.4% to $9.5 million in 2019, which was the lowest in recent history. These declines were broad based as used vehicle gross profit decreased the least, in percentage terms, by 1.2% while new vehicle GP declined the most at 2.1%. However, luxury dealerships continue to achieve the highest levels of gross profit, $1.7 million the next highest category which is imports. Luxury dealerships also receive the highest percentage of their gross profit from service and parts departments as consumers are more likely to go to a dealership for servicing when they purchase a more expensive vehicle.

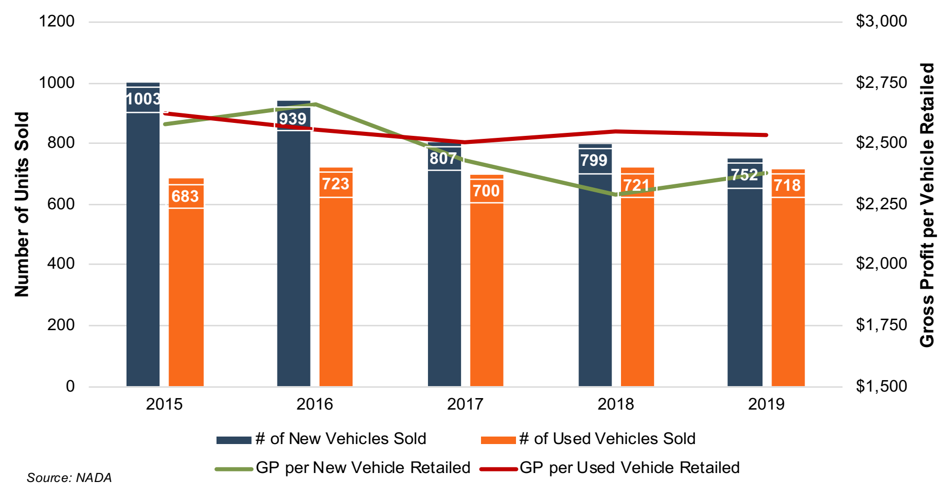
Gross Profit by Segment



Source: NADA

In 2019, new vehicle volumes declined 5.9% on average for luxury dealerships, but gross profit was supported by a 4.1% increase in GP per vehicle sold. The average number of new vehicles sold has declined 25% since 2015, while gross profit per vehicle has also declined 7.6%. While used vehicle volumes were essentially flat in 2019, gross profit per vehicle sold declined 0.7%. Gross profit per new vehicle rebounded from a recent low while GP per used vehicle modestly declined, narrowing the gap in GP earned per vehicle to $152, as luxury dealers earned $264 more per used vehicle in 2018.

New and Used Vehicles Sold and Gross Profit per Unit



Source: NADA

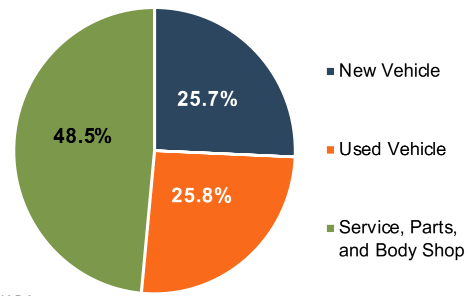
Mass Market Dealerships

As of Year-End 2019

Gross Profit Trends

Gross profit increased 3.8% in 2019 for mass market dealerships, reaching a recent peak of $6.7 million. Like most other types of dealerships, approximately half of gross profit in 2019 came from service and parts departments, with the remainder evenly split between new and used vehicles. Mass market dealers' gross profit increased due to 6.4% growth from the service and parts department which offset lower growth from used vehicles and declines from new vehicles. Service and parts gross profit has increased to 48.5% of total gross profit for mass market dealers, up from 42.8% in 2015, mirroring trends seen across all categories of dealerships.

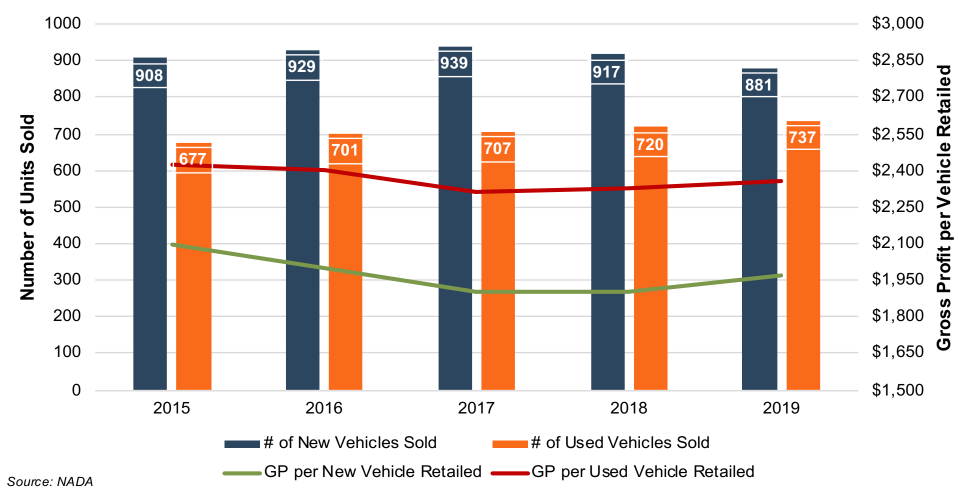
Gross Profit by Segment



Source: NADA

Mass market dealerships have seen declining new car sales as consumers increasingly choose used vehicles. However, these dealerships still sold 144 more new cars on average than used cars, despite earning $386 more in gross profit per used vehicle. Consumer's shifting towards used vehicles is not necessarily harmful to dealers, despite the lower sticker price, due to the pickup in gross profit. It remains unclear the degree to which dealerships may seek to shift this balance even further to enhance profitability. Gross profit per vehicle has picked up in each of the past two years for both new and used, though they remain below levels seen in 2015.

New and Used Vehicles Sold and Gross Profit per Unit



Source: NADA

Light Weight Vehicle Sales: Autos And Light Trucks (SAAR)

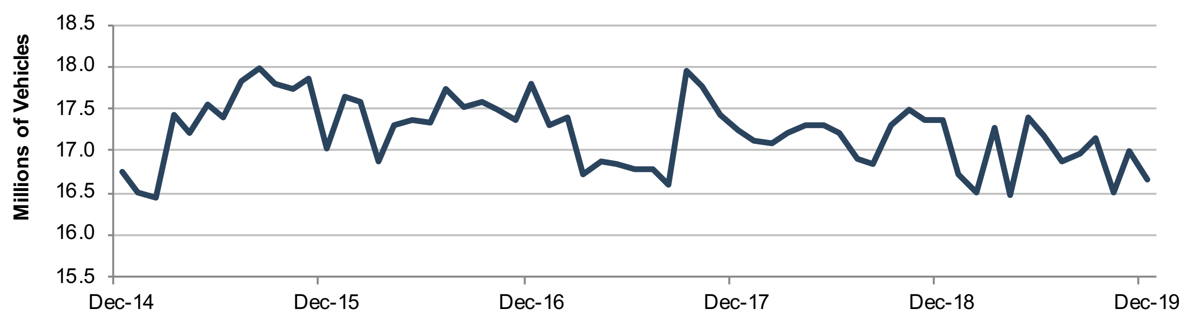
As of Year-End 2019

A Seasonally Adjusted Annual Rate (SAAR) is defined as a rate adjustment used for economic or business data, such as sales or employment figures that attempts to remove seasonal variations in the data. In the automotive space, it is understood to mean the number of light weight vehicles sales (autos and light trucks) sold in a given month, adjusted for seasonal factors and scaled up to a year's worth of sales based on that month.

SAAR came in at **16.70 million for December 2019**, as a shortened holiday season led to **volume declines of 5.8%.** However, **total volume was 17,047,725 for 2019**, the fifth straight year above the 17 million threshold. While volumes did decline, the drop was not as much as proffered at the beginning of the year as fears of a recession failed to materialize and the Fed cut interest rates three times to buoy affordability. As seen in the below graph, SAAR largely lagged its 5-year average in 2019.

NADA initially forecast U.S. light-vehicle **sales of 16.8 million in 2020**, which would represent a 1.2% decline and the second consecutive year-over-year decline. This would also be the first year under **17 million units sold since 2014**. SAAR came in at 16.922 in January (revised upward) and 16.833 in February, which does not materially belie expectations. However, while the fallout from COVID-19 is not fully known, sales will almost certainly decline below 17 million in 2020 as alluded to in the articles we feature in this newsletter.

Light Weight Vehicle Sales: Autos and Light Trucks, Seasonally Adjusted Annual Rate



Source: St. Louis Fed

Public Auto Dealers

As of Year-End 2019

Public auto dealers are some of the largest franchised dealers in terms of number of dealerships, ranging from AutoNation Inc. with 236 to Asbury Automotive Group with 88. This spread narrowed as AutoNation saw a net divestment of 3 dealerships in 2019 while Asbury finished with as many as it began, picking up two stores in the back half of the year. For the second year running, Penske Automotive Group Inc. divested dealerships, cutting its U.S. store count to 145; Penske remains the fourth largest dealer by store count and the largest by revenue. Lithia Motors Inc. added 7 locations while Sonic Automotive Inc. divested 9, further exemplifying how public dealers appeared to be motivated by company specific reasons as no clear trend of acquisition or divestiture emerged from these figures.

AutoNation was the only large public auto dealer to have negative revenue growth (for the second consecutive year) with a decline of 0.4%. Carmax revenues grew the most in 2019 at 9.9% followed by Lithia Motors with 7.7% growth. Sonic Automotive's revenue grew 5.1%, though it remains the smallest public dealership by revenue with $10.5 billion in sales. Penske remains the largest dealership with $23.2 billion in sales, followed by AutoNation, with CarMax nipping at its heels.

In terms of stock prices, all dealerships saw year over year increases after the stock market dropped considerably to finish out 2018. Sonic's market cap more than doubled while Penske grew the slowest at 19% in 2019. Carmax's stock price increased 33% in the first six months of 2019 then finished the year flat despite steady increases in revenue.

Public Auto Dealers	Ticker	Year-End Market Cap	6 Mo. Change in Market Cap	Y-o-Y Change in Market Cap	2019 Revenue	Y-o-Y Change in Revenue	Dealership Count	Y-o-Y Change in Dealerships	Y-o-Y Change in Dealerships	Revenue per Dealership
Asbury Automotive Group, Inc.	ABG	$2,163	31.4%	65.5%	$7,210	4.9%	88	0.0%	0	$82
AutoNation, Inc.	AN	4,338	16.0%	35.1%	21,336	-0.4%	236	-1.3%	-3	90
Group 1 Automotive, Inc.	GPI	1,791	22.8%	83.7%	12,044	3.8%	119	0.8%	1	101
Sonic Automotive, Inc.	SAH	1,337	32.9%	127.3%	10,454	5.1%	95	-8.7%	-9	110
Penske Automotive Group, Inc.	PAG	4,071	2.9%	19.0%	23,179	1.7%	145	-5.8%	-9	160
CarMax, Inc.	KMX	14,360	0.0%	33.3%	20,747	9.9%	215	7.5%	15	96
Lithia Motors, Inc.	LAD	3,417	24.3%	90.3%	12,673	7.2%	188	3.9%	7	67

Presented in $000,000s except dealership counts

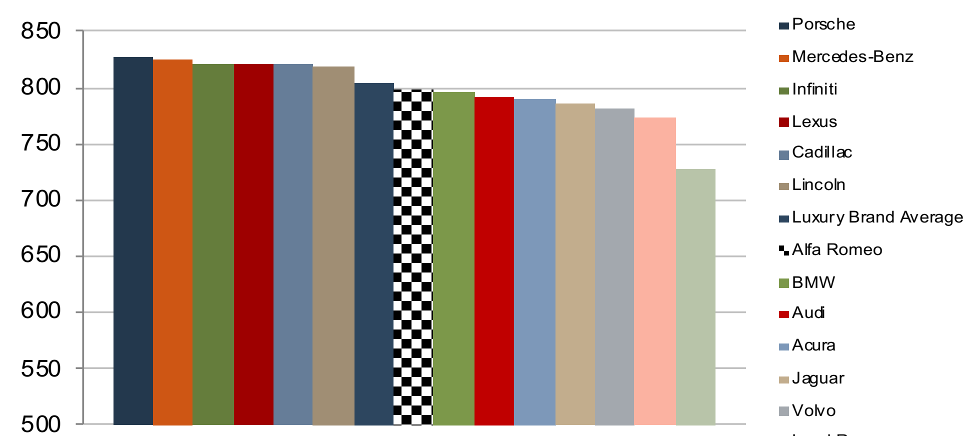
Public Auto Manufacturers

As of Year-End 2019

Every year, JD Power releases the Sales Satisfaction Index Study, measuring satisfaction with the sales experience among new-vehicle buyers and rejecters (defined as those who shop a dealership and purchase elsewhere). Buyer satisfaction is based on six measures: dealer personnel (28%), delivery process (21%), "working out the deal" (18%), paperwork completion (16%), dealership facility (13%), and dealership website (4%). Rejecter satisfaction is based on five measures: salesperson (40%); fairness of price (15%); experience negotiating (15%); variety of inventory (15%); and dealership facility (14%). Scoring is based on a 1000-point scale and is based on a survey of 28,867 participants.

Mercedes-Benz rebounded in 2019, gaining 10 points and jumping up to second place behind Porsche who remained at the top. The largest improvement came from Alfa Romeo, which at 798 was still below the luxury average of 805 but represents a 39-point increase from 14th place to 8th. Audi, on the other hand, dropped the most, from 804 to 791. Land Rover also dropped 7 points and Genesis continued to drop, distancing itself at the bottom of the group at just 728.

Sales Satisfaction Index (SSI) – Luxury



Source: JD Power

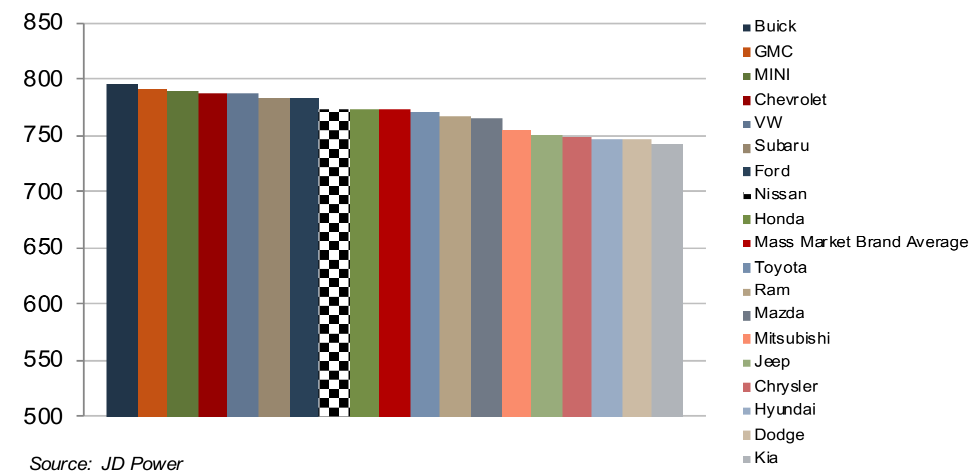
Public Auto Manufacturers

As of Year-End 2019

(continued)

Buick and MINI flip flopped first and third place with GMC remaining in second. Chevy and GMC each dropped 6 points while MINI dropped 8, showing some decline at the top end which again failed to crack 800. VW was the largest gainer, up 24 points from 14th place to 5th as it repairs its image coming out of Dieselgate. Honda also significantly improved, jumping 17 points to a notch above the mass market average of 772. Ram slipped below average in 2019 while Jeep improved marginally to 15th place at 750. Their counterparts in Chrysler-Dodge-Jeep-Ram did not fare as well, however, with declines of 14 and 17 dropping them from the middle of the pack to just above Kia and new entrant Fiat at the bottom.

Sales Satisfaction Index (SSI) – Mass Market



Source: JD Power

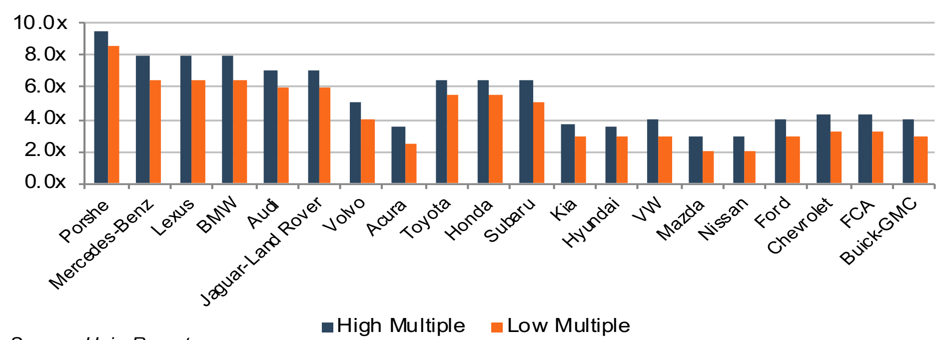
Blue Sky Multiples

As of Year-End 2019

Blue sky multiples come from the Haig Report and are calculated as a multiple of adjusted pre-tax profits. The ranges are an expression of what buyers in a competitive situation will pay for the goodwill of dealerships. Dealerships that are underperforming or in desirable markets will have high multiples while those that are over-performing, are in less desirable markets, or have significant real-estate issues will have lower multiples. In some cases, only a franchise value range is reported, indicating underperforming brands that potentially have negative earnings for which a pre-tax multiple would be non-meaningful.

With the exception of Porsche, Blue Sky Multiples for Q4 2019 were unchanged or down from midyear figures. Three out of four domestic brands declined while the remaining reductions for luxury and mid-line dealers were for brands that already commanded a lower multiple for their peer group, growing the chasm. Infiniti joined Cadillac/Lincoln with a dollar range of *$0-2 million.*

New and Used Vehicles Sold and Gross Profit per Unit



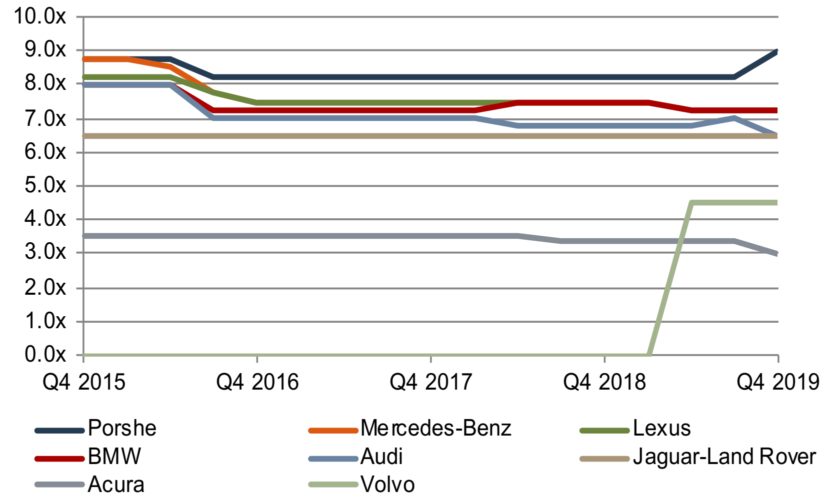
Source: Haig Report

Blue Sky Multiples History

As of Year-End 2019

Luxury Blue Sky History

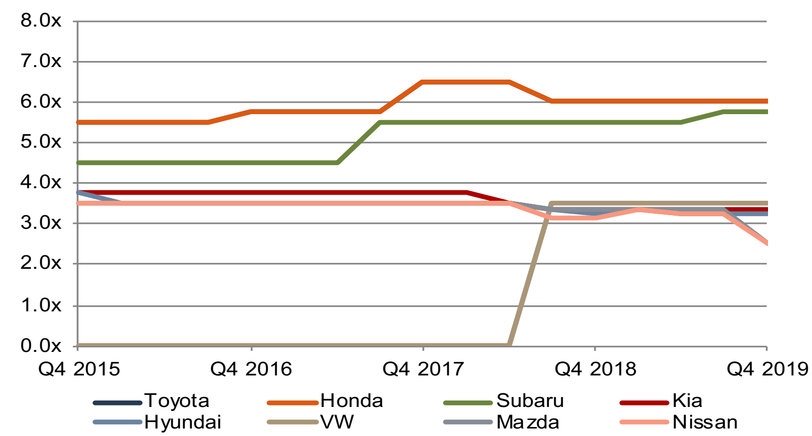
Luxury Blue Sky Multiples for Q4 2019 were mixed as Audi, Acura, and Infiniti declined and Porsche increased. Mercedes, Lexus, and BMW were unchanged from lowered mid-year figures. Infiniti joined Cadillac/Lincoln as the brands given just a franchise value. While historically reported along with Infiniti, Acura retained a multiple range, albeit lowered in Q4 to 2.5-3.5x, below the domestic franchises and trailing only Mazda and Nissan. Audi also fell in line with Jaguar in Q4 2019.



Source: Haig Report

Mid-Line Import Blue Sky History

Mid-Line imports generally receive lower multiples than high line, though Toyota, Honda, and Subaru do outpace some of the less popular luxury brands. Subaru edged up in Q3 2019 while Mazda and Nissan declined to a 2-3x range, which is the lowest reported since Haig began reporting in 2013, putting them in peril of potentially slipping to a franchise dollar value range.



Source: Haig Report

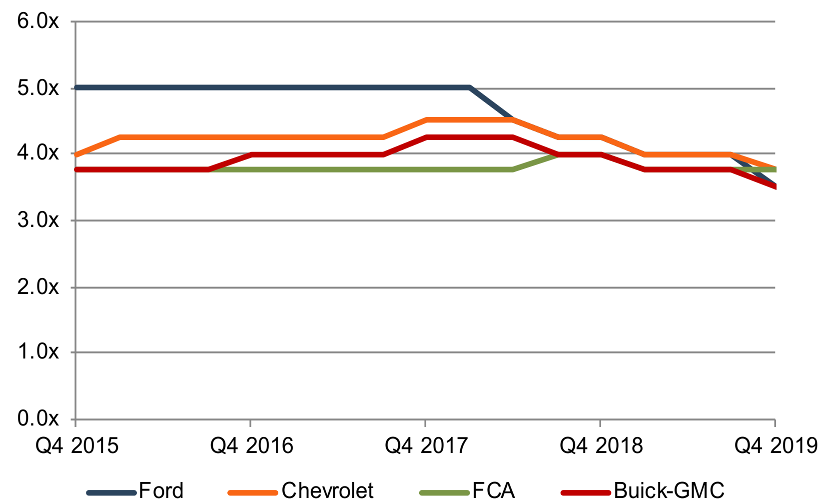
Blue Sky Multiples History

As of Year-End 2019

(continued)

Domestic Blue Sky History

All domestic franchises besides FCA declined in Q4 2019 with Ford falling the furthest. It now sits in the 3-4x range with similarly declining Buick-GMC. Chevy and FCA sit slightly above at 3.25x-4.25x. Buick-GMC sales were flat in 2019 whereas all the other domestic franchise brands declined in revenue driven by declining volumes.



Source: Haig Report

Auto Dealer Industry

Mercer Capital has expertise providing business valuation and financial advisory services to companies in the auto dealer industry.

Mercer Capital provides business valuation and financial advisory services to auto dealerships throughout the nation. We provide valuation services for tax purposes, buy-sell agreements, partner buyouts, and other corporate planning purposes. Mercer Capital also works with owners who are considering the sale of their dealership or the acquisition.

Services Provided

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- Transaction advisory for mergers, acquisitions and divestitures
- Valuations for purchase accounting and impairment testing
- Fairness and solvency opinions
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Contact a Mercer Capital professional to discuss your needs in confidence.

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