Economic conditions have bottomed out and are now recovering

Dealership profits exploded in recent months

Buy-sells are down 16% in H1 2020

Blue sky values have recovered to an estimated 95% of their 2019 levels

Public equity valuations are 25% higher than they were before the pandemic

Buy-sells resumed in June and public companies are buying

SEE PAGES 4 AND 17 FOR OUR OUTLOOK ON THE INDUSTRY AND BUY-SHEELS
The pandemic has proven the strength of the auto retail business model. Despite massive shocks to both the demand for vehicles as customers were forced to stay home and to the supply of vehicles as plants were closed, dealers have rebounded and generated record-high levels of profits over the past couple of months. A banker recently told us he has never seen more cash and less debt on the balance sheets of dealers. Few people would have predicted that dealers would have big smiles on their faces just a few months after one of the most damaging events in our lifetime.

Just think about the list of obstacles that dealers have had to overcome. When customers couldn’t come into showrooms, dealers responded by selling vehicles online. When inventory levels for new vehicles fell, dealers focused on used car sales and were able to hold for more gross on both new and used vehicles. While waiting for the recovery, dealers reduced advertising, personnel and floorplan expenses significantly. The pandemic forced dealers to adopt new technologies and leaner business practices sooner than they otherwise might have. The result is that most dealers have become stronger during this time of crisis, not weaker. Investors have noticed. The publicly traded franchised groups have higher values today than before COVID, and we have seen the values of private retailers rebound as well. Dealership buyers are betting that the future of auto retail is bright, even when the lift from trillions of dollars of government stimulus spending wears off.
Buy-Sell Activity Fell, But Has Now Begun To Rebound

COVID had a big impact on the buy-sell market in the first half of 2020. Over the past few years, buyers purchased an average of 25 to 30 dealerships per month. The market was at the same pace in January and February and then the numbers dropped sharply from March through May. Buyers were concerned about the potential decline in earnings caused by the pandemic. Transactions that had been in the works for many months, even years, were scrapped or postponed. The result is that the number of dealerships acquired in the first half of 2020 has declined by 16% from the first half of 2019.

The good news is the buy-sell market has already started rebounding. There were 33 dealerships sold in June, above the monthly average we have seen over the past few years, and many more are coming. Our firm, for instance, expects to close on the sale of more than 20 rooftops by the end of Q3 2020.

**U.S. DEALERSHIPS BOUGHT/SOLD**

**Q2 U.S. DEALERSHIPS BOUGHT/SOLD**

<table>
<thead>
<tr>
<th>Year</th>
<th>Berkshire Hathaway</th>
<th>Public Acquisitions</th>
<th>Private Acquisitions</th>
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<tr>
<td>YTD Q2 2020</td>
<td>127</td>
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<td>122</td>
</tr>
</tbody>
</table>

Source: The Banks Report and Haig Partners
Public Company Acquisition Spending Has Been Flat, But Will Soon Be Increasing

During the first half of 2019, the publics bought relatively few dealerships. Their stock prices had been low due to investor concerns about tariffs, trade wars, rising interest rates, a declining SAAR, and fears caused by some of the tech disruptors. We saw the same moderate acquisition pace in the first half of 2020. Lithia and Asbury, however, are eager to grow now. Each company has announced sizeable acquisitions that will be closing in Q3 and we expect spending on these deals will exceed $1B. The amount spent by these two groups in just Q3 will far exceed the amounts spent on average for a full year from 2015-2019 for all the public companies, combined.

Buy-Sell Outlook for the Remainder of 2020

There are many buyers looking to acquire dealerships at the moment. This is a big change from the last recession when few dealers would even consider acquisitions. They were focused on improving the dealerships they owned. The pandemic and all the stimulus spending are taking today’s buy-sell market in a different direction. Dealers are excited that despite the pandemic, or perhaps because of it, dealerships are producing impressive profits. They are asking for more cake, please.

As discussed above, there are a couple of large transactions that two of the public retailers will be closing in Q3. In addition, there are a good number of acquisitions being conducted by private dealers. We expect that by the 4th quarter the market will be back to closing 20+ transactions per month.

Dealership Values Rebound

We carefully track the buy-sell market to assess the value of auto dealerships. We analyze offers for the transactions that we are involved in and regularly speak with leading buyers and many attorneys and CPAs who are involved in other acquisitions. Prior to the coronavirus, we reported that the value of dealerships increased slightly from 2018 to 2019 as dealership profits rose modestly. But when COVID arrived, it quickly had an impact on the buy-sell market. Some buyers pulled their offers, while others demanded price concessions. We reported in our Q1 2020 report that for those transactions that survived, we estimated that blue sky values declined by about 10% from 2019 levels. Over the past 60 days, however, we have seen an increase in interest in buying dealerships and a willingness to pay more for them. While every transaction varies, we estimate now that dealership values have rebounded and are now just 5% below their values at the end of 2019.
The table below provides our estimate of what multiple a motivated buyer participating in a competitive sales process (i.e., not the only buyer at the table) would be willing to pay for the blue sky of a franchise, in addition to the other dealership assets. In our Q1 Haig Report, we had reduced the average estimated blue sky multiple for most franchises by 0.5x at the top and bottom of their ranges. But due to recent buy-sell activity and our research, we have increased the multiples for most franchises by 0.25x–0.5x. At current levels, blue sky multiples are equal to about 95% of the year-end 2019 multiples. The franchises on the right side of the graph are usually nominally profitable or lose money and we often see buyers put a dollar value on them since there are no earnings and therefore a blue sky multiple is not applicable. Given the limited buyer appetite for these franchises, we have not seen their values increase from their values in Q1 2020.

The chart above is a guide for many dealerships, but multiples or prices paid by buyers for dealerships will vary depending upon a number of factors and they can be higher or lower than the ranges we indicate. This is particularly true during this period where coronavirus is impacting some areas more than others. Cities like Las Vegas that are based on tourism, travel and gaming have suffered severe job losses so dealership valuations in those cities may have fallen by much more than 5% from 2019. Dealerships in cities like Austin or Salt Lake City that have maintained much of their employment may not have suffered any loss in value. The table below provides a list of some qualifying factors that could impact the value paid for a dealership.

**FACTORS IMPACTING MULTIPLES**

- Underperforming
- Metro Markets
- Rapid Growth Markets
- Low Tax Markets
- Low Real Estate Cost
- Geography Well Suited to Franchise
- Not Marketed Properly
- Facility Issues
- Rural Areas
- Slow/Negative Growth Markets
- High Tax Markets
- Add-Point Risk
- High Real Estate Cost
- Over-Dealeded Markets
New Unit Sales Begin To Rebound As The Country Opens Up

Overall sales for the year have declined 24% from the same period last year. This decline is comprised of a fall in sales of 18.1% at retail and 43.5% for fleet. The bigger decline in fleet came as rental car companies stopped buying vehicles as travelers stayed home and municipalities also reduced their purchases.

The good news is that auto sales have begun rising again. June sales increased 7% from May and we are back to a SAAR of 12.8 million units. Retail sales are likely performing better since much of the contraction has come from fleet sales to rental companies which are now selling their inventories. For the rest of 2020, many experts are projecting continued growth in new vehicle sales and that the industry will end up selling 13.5 million light vehicles. At this level, the total new unit sales would be 21% less than what the industry sold in 2019, but a greater proportion of the decline will come from fleet vs. retail, making the picture less bleak.

If there is a silver lining from COVID-19, it may be that the pandemic forced retailers to revise their sales operations. Dealers have installed new digital sales tools and retrained their staff to serve customers who want to handle part or all of sales or service transactions online or over the phone. Customer satisfaction may also improve thanks to greater transparency, shortened transaction times, and increased convenience. Also, dealers have discovered that they are able to significantly reduce the number of people they need to operate the stores. This may allow them to maintain strong profit levels even in the face of a smaller new-vehicle market.
Changes in Sales for Individual Franchises

The following chart sets forth the change in new unit sales among the major franchises in Q2 2020 compared to Q2 2019. All franchises saw declining sales, with Mazda being the only franchise whose sales did not fall double digits. Both Nissan and Infiniti saw sales drop more than 33%. Note, this data reflects changes in total sales per franchise, so it includes fleet sales that can cloud results at the retail level.

YEAR/YEAR SALES PERFORMANCE – YTD Q2 2020

Source: Automotive News (June 2020 Data)

MACROECONOMIC INDICATORS ARE MIXED

GDP Fell Sharply, But Has Begun to Rebound

The coronavirus is a worse shock than the Great Recession in terms of its impact on the economy and employment. The good news is that the worst is behind us and the economy has started growing again. The Congressional Budget Office predicts GDP will be 5.6% lower than it was in 2019 but will grow in 2021 by 4.2%. This means it will likely take at least two years before our economy returns to 2019 levels. If these predictions are correct, the pandemic will be both more severe and shorter than the Great Recession.

Unemployment Is Falling

The unemployment rate has steadily improved since it spiked to 14.7% in April. It fell to 13.3% in May, 11.1% in June and 10.2% in July. We still have a long way to go as overall employment is down by almost 13 million jobs since February. And while we are adding jobs, 1.8M in July alone, there is a chance the recovery will slow when companies are no longer required to retain most of their employees in order to have their PPP loans forgiven. If each of the estimated 650,000 companies who took PPP loans were to lay off a handful of their employees, unemployment would rise again.

Fuel Prices Are Low

The national average price per gallon of gas at the pump was $2.19 by the end of July 2020, 20% below the level at the same time last year. These low gas prices can be beneficial to dealers as consumers have more discretionary income with which to make auto purchases. Fuel prices will likely remain low for the near future as demand remains depressed worldwide due to the pandemic.
Sharp Decline in Miles Driven

The number of miles driven on an annual basis is a key driver for our industry as it heavily influences the replacement rate for vehicles. More miles driven equals more vehicles needed. As people stayed home due to the pandemic, travel on all roads and streets plummeted 41.4% in April 2020 as compared to April 2019. Travel then increased 24.1% from April to May 2020 as some states began to reopen but we are still driving a lot less than we used to. It’s unclear how the countervailing trends of working from home, which would imply less driving, and the move away from public transportation, which would imply more driving, will impact the total number of miles driven in the US. Rising employment and a return to school would certainly lift the number of miles driven.

Interest Rates Are at Rock Bottom

The Federal discount rate has been reduced to just 0.25% and most analysts expect it to remain at this level for years. Low-interest rates help to stimulate auto purchases and leases since they reduce the monthly payments for consumers. Low rates will also continue to boost dealer profits by reducing floorplan expense and mortgage payments. However, unlike the Great Recession, this time around many banks are instituting LIBOR floors which are resulting in less interest savings to the dealer.

Consumer Confidence Is Fluctuating

The Consumer Confidence Index plummeted from a near historic high of 101.0 in February 2020 to 71.8 in April 2020. The index rebounded to 78.1 in June, but gains were reversed to 72.5 in July as infection numbers increased and fears of a second pandemic peak worsened. Any future stimulus package will likely see a decrease in Federal benefits, which has resulted in a decrease in the Expectations Index. This means that consumers’ short-term outlook on income is worsening. The latest report reads, “Declines were experienced in Michigan, Florida, Texas and California … Such uncertainty about the short-term future does not bode well for the recovery, nor for consumer spending.” The latest report indicated consumers saw “… gains in the outlook for personal finances and more favorable prospects for the national economy due to the reopening.” However, it also warned that nearly half of consumers still expect a renewed downturn due to a resurgence of coronavirus and slow employment recovery.

The Lowest Inventory Levels Since The Great Recession

While demand from consumers has rebounded strongly, supply from the OEMs is still low due to COVID related production shortfalls. The result is that inventory levels have fallen precipitously in just a few months. As shown in the table on the following page, new vehicle inventory levels are down 35% from 3.58 million units at the beginning of March to 2.33 million units at the beginning of August. This marks the lowest inventory levels since 2011 as the auto retail industry began to recover from the Great Recession. Dealers tell us that many new vehicles are being sold off the car carriers as soon as they arrive at dealerships, at full sticker. Even aged units are finally moving off dealers’ lots without the need for heavy discounts. Some CPAs are concerned their clients will sell so deep into their inventory levels that they may trigger LIFO recapture taxes.

While dealers wish for more supply, they are taking advantage of their pricing power to increase their gross profits. See Page 10 for a graph depicting the lift in new vehicle profits. Popular mid-size trucks and SUVs are facing the tightest inventory levels, while the smallest, cheapest vehicles have the biggest supply. Toyota had the lowest inventory of all major brands but Buick, Fiat, and Mitsubishi still have plenty of inventory. Get your Fiat 500L while they last!

In fact, in this current environment of rapid turnover of inventory, dealers who own franchises that provide floorplan credits are likely generating hundreds of dollars of profits per unit retailed since the cars are moving so quickly. Please see Page 12 for data on this subject.
Used Vehicle Values Hit A Record During A Pandemic

The used vehicle market has confounded dealers and analysts over the past few months. When the pandemic hit and consumers were forced to stay home, many fleets and dealers attempted to sell down their inventories. But with lots of sellers and few buyers, wholesale values plummeted. The large majority of vehicles taken to auction simply did not sell. The market began to turn in May, however, perhaps as consumers received their stimulus checks. A lack of new vehicle supply likely also increased demand for used vehicles. And there are new buyers in the market like Carvana and Vroom that are growing aggressively and so they are making strong bids for used units. Wholesale used vehicle prices have been climbing ever since and now stand 11% over where they were a year ago, according to Manheim’s Used Vehicle Value Index, setting a new record high level.

Used Vehicles Are Increasingly Important

Franchised dealers are increasingly focused on selling more used cars for several reasons. First, as new vehicle sales began to decline over the past years, dealers sought to offset these losses with higher volumes in the used vehicle department. Second, there is a higher supply of attractive used vehicles since many vehicles sold during 2016-2018 are coming off lease and they are the right mix of trucks and SUVs that consumers are seeking. Third, many dealers find they are making more money off the sale of used vehicles than they are from the sale of new ones. Overall used unit sales are down so far in 2020 given the shut-down of many stores in March and April, but June and July have seen an explosion in sales. Privately owned franchised dealers had a used-to-new ratio of 1.02:1.0 for YTD June 2020. This ratio is up substantially from the 0.85:1.0 average in 2019. We expect this ratio to continue to grow as new inventory is supply-constrained and the lower prices of used vehicles remain a draw for cash strapped consumers.
New Vehicle Grosses Have Passed Pre–COVID Levels

The Japanese tsunami and Thai floods of 2011 created the last supply shock in auto retail. During this period, dealers compensated for a lack of inventory by raising prices. But after production returned, dealers saw their new vehicle gross profits per vehicle fall for seven years until they managed a slight increase in 2019. The second quarter of 2020 provided a big increase, up $377 per vehicle from the second quarter of 2019. The grosses were likely even higher in July as consumers were hungry to buy, but the limited inventory they found meant dealers had significant pricing power. It is unlikely these gross profits will last long as factories are rapidly increasing production and shipping it to dealers.

Used Vehicle Grosses Have Passed Pre–COVID Levels

Given the strong demand for used vehicles, the average gross profit per used vehicle increased by $110 for the public retailers from Q2 2020 compared to Q2 2019. Prices are up sharply as we reported earlier in this report, and these increases are beginning to create some concern. Dealers are telling us they are worried about the possibility that these buyers will suffer significant negative equity in their vehicles when new vehicle supply returns to normal, which should push down the value of used vehicles. A large amount of negative equity will take these consumers out of the market for years. As a result, dealers may be earning record profits today but suffer in the future.
Finance & Insurance Departments Are Generating Record Profits

F&I profits per vehicle continue to increase as transaction values go up and retailers do a better job on product penetration. The public companies earned $1,756 per vehicle retailed in F&I gross profit in Q2 2020, up an impressive $169 (10.6%) from Q2 2019. AutoNation has set the pace for the rest of the publics, generating F&I income of $2,172 per vehicle retailed. Private dealers also enjoy substantial profits made through reinsurance companies that do not run through dealer statements. For instance, a Toyota dealer making $2M at his store is likely making another several hundred thousand dollars per year in the reinsurance company.

PUBLIC COMPANY F&I PER UNIT RETAILED

**PUBLIC COMPANY VEHICLE GROSS + F&I PVR**

*Weighted Average Same Store Performance – In Current Dollars*

Combined Front and Back Profits per Vehicle Retailed Continue to Increase

The tables below track combined front and back end profits per vehicle retailed data back to 2010. They show that on a combined basis, profits have trended up slightly in absolute dollar terms as the gains in F&I have more than offset the declines in front-end gross.

**Note:** Front end gross profit includes manufacturer incentives and other income.

*Source: SEC filings*
Fixed Operations Declined

According to NADA, fixed operations fell 16.7% for the average dealer for the first six months of 2020 compared to the same period in 2019. Fixed operations had been growing consistently since the Great Recession ended in 2009, but widespread job losses, stay-at-home orders, and the reemergence of rising COVID-19 rates have kept people from servicing their vehicles. People are also driving less due to the pandemic, which has decreased demand for maintenance, repairs, and parts. We have heard from some dealers that their fixed operations have returned to pre-COVID levels in July, which is an encouraging trend that we hope will continue. But we are also hearing concerns that the OEMs are having parts shortages due to plant closures that will limit dealers’ ability to perform service work in the short term.

Dealerships Are Reducing Expenses

The average privately-owned dealership’s total gross profit from all departments (including other vehicle income) declined 12.8% YTD for June 2020 compared to 2019, while operating expenses shrank by just 10.9% compared to the same period last year. Most dealers have eliminated an estimated 20% of their staff and have discovered they can service the current demand with far fewer people. Advertising expenses are down 22.3% YoY (0.7% of gross) as dealers move more to digital. Floorplan interest is down 87.8% (1.3% of gross), coinciding with an overall drop in inventory and low-interest rates. Some expenses that are fixed or semi-fixed cannot be reduced even though there are fewer customers. As a result, expenses increased as a percentage of gross profit from 83.4% in January-June 2019 to 85.1% in January-June 2020.

As stated above, the reduction in floorplan expense has been much welcomed by dealers in recent months. Net average floorplan expense per vehicle retailed decreased from $155 for the six-month period January-June in 2019 to an expense of just $24 for the same period in 2020. If we look at just the month of June, we see that floorplan expense flipped from an $82 expense in June 2019 to a $122 credit in June 2020. We expect to see even bigger credits in August before dropping back later in the year as inventory begins to build again.
Dealership Profits Are Declining

Average profits at privately owned dealerships decreased 21.8% for the first half of 2020 compared to the same period in 2019. Many dealerships were closed or had limited operations in March and April. Operations began to rebound in May before exploding in June and July. And for the 88% of the dealerships that received Payroll Protection Program loans, they have been incurring additional personnel expense but have not yet taken the PPP funds into income. When that happens, we expect a significant lift to dealer profits. The table below shows the annual profits at privately owned dealerships since 2010.

While dealers are pinching themselves with their good fortunes in June and July, many are wondering what the rest of the year will bring. Will COVID be contained? Will employment rise? What will stimulus spending look like? How will consumers respond to the upcoming election? When will the supply of new units pick up? Will the OEMs produce too many? There are many more questions at the moment about our industry than we normally have, making it difficult to predict dealership profits for the balance of the year.
Private Dealership Values Are Recovering

There are many factors that drive the blue sky value of dealerships. A buyer’s expectations of future profits is an important one, as are interest rates, the amount of debt a buyer can deploy, and tax rates. All of these are now in flux which makes it more challenging than normal for buyers to value dealerships.

Let’s start first with a buyer’s expectations of future profits. For the past several years we have enjoyed annual sales of over 17M new units and average dealership profits between $1.4M and $1.5M — remarkably consistent. Due to the pandemic, analysts predict it will be at least two years before new vehicle sales return to these levels, which implies lower dealership profits. Average monthly profits since the pandemic hit have been highly variable. Many dealers were forced to shut down or severely restrict their operations in March and April. As a result, their profits plunged and many incurred significant losses. But thanks to pent up demand and stimulus dollars, traffic rebounded in June and July and many dealers reported record-high levels of income. Dealers know these record profits are not sustainable, but they don’t know what the new “normal” will look like. Based on what we have seen in the market, we believe many buyers are using 2019 results as a baseline of what profits could be in the future. As the months pass by we expect buyers to begin using the last twelve-month period again as the basis for making their offers.

In our Q1 2020 Haig Report, we estimated that blue sky multiples had fallen about 0.50x from 2019 levels, which equated to a 10% reduction in average estimated blue sky multiples, from 4.75x to 4.25x. We are now increasing our estimated blue sky multiples by 0.25x-0.5x from Q1 2020 levels, leaving them about 5% below our estimates at year-end 2019. As the chart below shows, we estimate the average blue sky value per dealership has fallen 5% from $6.7M at year-end 2019 to $6.4M as of June 2020.
Public Dealership Values Fell Sharply But Have Rebounded Higher

The share prices of the public franchised retailers declined sharply in March 2020 as investors became more concerned about the impact of COVID-19. Fortunately, we have seen a steady recovery for these share prices since the end of March as data emerged about the return of sales and service business. Their prices are now up 25% since the beginning of the year, compared to the S&P 500, which is up 5% year to date. Investors have become more bullish on our industry as they are seeing that the public companies are generating large amounts of profit even with a lower SAAR thanks to reduced personnel expenses, a bigger focus on used vehicle sales, and the possibility that technology will help these larger groups take share from smaller dealers. Lithia is driving a big part of the increase in the average stock price. This is partly due to their growth strategy that we outline on Page 17. The chart below shows how the franchised retailers have performed compared to the used retailers (CarMax and Carvana) and the S&P 500. Note that the used retailers have performed best thanks largely due to Carvana’s explosion in market value to over $35B at the time of this writing – more than all the franchised retailers combined.

Real Estate Values May Be Declining

From 2010-2019 we saw dealership real estate values steadily rise. Escalating values helped transactions to come together since the appraisals we obtained on our client’s real estate before going to market were met or exceeded by the appraisals that buyers obtained when they went for financing. Buyers, sellers and lenders were all happy. Unfortunately, we are now beginning to run into issues where some of the new appraisals ordered by banks are lower than those we sourced just a few months ago. This seems incorrect since there have been very few dealerships sold during this period. What evidence is there that valuations have fallen? It’s as if these appraisers are anticipating a decline in value due to the COVID, so they are creating the decline due to COVID.

Whatever the reasons, some recent appraisals are coming in 5%-10% less than our pre-pandemic appraisals. Others are unchanged. This decline is meaningful to dealers since their real estate values constitute a big portion of the total value of their stores. Hopefully, this decline is temporary and will be reversed when appraisers see the resilience of auto retailers. Plus, lower interest rates should support higher real estate values.
The Buy-Sell Market Declined March – May

COVID had a negative impact on the buy-sell market in the first half of 2020. Our data shows that 16% fewer rooftops traded hands January–June 2020 compared to the same period in 2019. The market had been relatively strong in January and February, but deals began to be put on hold or canceled in March when COVID began leading to deaths, business closures, and the loss of so many jobs. Dealership sales remained well below average levels for March-May before rebounding in June.

The Buy-Sell Market Is Rebounding Quickly

The last shock to the buy-sell market was the Great Recession. Dealership profits fell significantly and so did the buy-sell market. Buyers had less access to capital and were worried about preserving their own businesses, not expanding. The public companies had been spending $500M to $1B a year on purchasing dealerships before the Great Recession, but this figure dropped to just $14M in 2009, down 97%! When sales rebounded, so did dealership profits and acquisition spending. In 2011, just two years after the bottom of the cycle, the public companies spent $500M on dealerships. We are seeing a far faster rebound to the buy-sell market today. Many transactions that were due to close in Q1 or Q2 but were postponed are now back on track. And some transactions that were terminated, such as Asbury’s acquisitions of Park Place Dealerships, have been resurrected and are due to close in Q3. Lithia has announced several major acquisitions recently, including the purchase of BMW San Francisco, a Haig Partners client. These transactions will push the amount spent by the public auto retailers to the highest level in many years, well over $1B. Further, Lithia has announced its intention to quadruple in size over the next five years, much of the growth coming from acquisitions. The stock prices for Lithia and Asbury jumped on the announcement of their acquisitions.

The table at right illustrates the slow down and then the acceleration of the buy-sell market. It shows the number of dealerships bought/sold during each of the past six months.

Overview of the Park Place
Dealerships Acquisitions

Asbury’s purchase of Park Place Dealerships is the most money spent on a dealership group since 2014 when Berkshire Hathaway acquired the Van Tuyl group for several billion dollars. The purchase included three Mercedes-Benz/Sprinter stores, two Lexus stores, a Jaguar-Land Rover store, a Porsche store and a Volvo store. Also included are two collision centers and an auto auction. All of the dealerships are located in the high-growth Dallas-Ft. Worth market. The price was $685M in goodwill plus $50M for parts, fixed assets, leaseholds, but excluding vehicle inventories. Asbury is leasing the dealership real estate. Asbury announced, “the purchase price [for blue sky and the other assets] reflects a 7.7x multiple on targeted EBITDA of $95M, including run-rate synergies of at least $20M, expected to be realized over the next three years.” If we try to calculate the effective blue sky multiple on this transaction, including the synergies, we get a blue sky multiple of 7.2x. Without any of these synergies, the goodwill reflects a 9.1x multiple of EBITDA. Since some of these synergies are likely customary add-backs that we see in buy-sells (elimination of unneeded corporate overhead, etc.), we estimate that Asbury is paying a blue sky multiple of around 8.2x EBITDA, the mid-point between the amount with all synergies/add-backs and no synergies/add-backs. Since auto dealers often purchase on the basis of pre-tax income, which is after depreciation, the effective blue sky multiple would have been slightly higher than the estimated 8.2x after the “expected synergies” are factored in. If our estimates are correct, we believe that Asbury paid a fair price for these assets. The overall blue sky multiple is near the top of the range for luxury stores, but we would expect this since the stores are located in Dallas – Ft. Worth.
which we believe is among the most desirable markets in the country. Dealers have historically paid premium prices to purchase stores in the market.

**Lithia’s Expansion Plans**

Lithia’s CEO, Bryan DeBoer, announced plans last month to quadruple the revenue of his company over a five-year period. This is a stunning plan, unlike anything our industry has ever seen before, even during the late 1990s, when AutoNation was acquiring hundreds of dealerships using its high stock price as its currency. Wayne Huizenga, the legendary entrepreneur who helped to build AutoNation along with five other NYSE listed companies, would be tipping his hat at the boldness of this plan. The growth is projected to come from a combination of:

- Approximately 50% higher revenue from existing dealerships – this implies Lithia believes it can take market share from surrounding dealers;
- Acquisitions of hundreds of additional dealerships – this means Lithia believes it will have the support of the OEMs and its lenders; and
- A push into online retailing under the “Driveway” brand – which states Lithia is embracing a one-price sales model that may become the norm for its traditional customers who call or walk-in.

From the charts presented by Lithia, Lithia intends to acquire enough dealerships to generate $20B in incremental annual revenue – roughly the size of AutoNation today. To meet these growth targets, Lithia will need to acquire about $4B in revenue per year. These acquisitions could easily cost $1B per year for goodwill, real estate and other assets. Sellers will benefit by having such a well-capitalized and hungry buyer in the market. If Lithia executes on this plan, it will likely become, by far, the largest of the franchised retailers. The investor community reacted with great enthusiasm as Lithia’s stock has jumped from about $180 per share prior to the announcement to over $240 per share. Lithia had been steadily gaining ground on what has been for over 20 years the most valuable of the publicly traded retailers, AutoNation, but Lithia’s market capitalization of $6.0B has now surpassed AutoNation’s $5.0B even though AutoNation is a far larger company. Investors like growth. We look forward to Lithia continuing the success it has enjoyed over the past decade.

**The Current Perspectives of Buyers and Sellers**

We have been speaking with many leading dealership groups, attorneys who conduct buy-sell work, lenders who provide capital for acquisitions, and CPAs who provide due diligence and closing services for buy-sells. This is what we are hearing in most parts of the country.

**The buyer’s perspective:**
- They have been pleasantly surprised by how strong the past couple of months have been.
- They have a lot of cash on their balance sheets and want to invest it.
- They are open to all brands.
- They expect some discount from previous values to move forward on transactions.

**The seller’s perspective:**
- Their high profits are giving them leverage in terms of pricing.
- They are willing to take a slight discount from 2019 values to sell today, but would rather wait for conditions to improve than take a significantly lower price.
- They are increasingly worried about higher capital gains taxes that could take effect in a new administration.

**The Outlook for Buy–Sells for the Remainder of 2020**

Dealership buy-sell activity came back to life in June with 33 dealerships trading hands. Some of these were transactions that were delayed earlier in the year, due to COVID. That said, we doubt there will be 25-30 closings per month in the back half of the year which has been the rate in recent years. Fewer new deals were put together in recent months and it typically takes 90-150 days after reaching agreement on a price for closings to happen because of the time it takes to complete due diligence, document negotiations and the OEM approval process. We are starting several new transactions now which will not likely close until Q1 2021. At the risk of “jinxing” transactions in our pipeline, we expect to close on transactions representing more than 20 rooftops between now and the end of Q3 2020. We estimate the total market will see about 20 rooftops acquired per month for the balance of 2020.
Dealership Valuation Methods

There are various ways to value dealerships. Since many dealers employ it, we will refer to the traditional method of combining blue sky (calculated as a multiple of the adjusted pre-tax profits), plus the value of other assets acquired. Adjusted pre-tax income excludes non-recurring income or expenses. Note, the significant change we see at present is that buyers are tending to put less emphasis on the most recent months as a guide for making their offers since there is so much noise in the numbers. Instead, many buyers are basing their offers on 2019 (pre-COVID) adjusted pre-tax profits. They assume that future profits are going to be slightly lower. In our Q1 Haig Report, we had reduced the average estimated blue sky multiple for most franchises by 0.5x at the top and bottom of their ranges. But due to recent buy-sell activity and our research, we have increased the multiples for most franchises by 0.25x-0.5x. At current levels, blue sky multiples are equal to about 95% of the year-end 2019 multiples.

The blue sky multiple ranges for various franchises that we set forth in this report reflect our expectations of what motivated buyers in competitive situations will pay for the goodwill of average dealerships in the current marketplace. We remind the reader that each transaction is unique, and dealerships may trade above or below the ranges we describe in this report. See page 5 for factors that could increase or decrease the multiples paid by buyers from what we estimate here.

Luxury Franchise Blue Sky Multiples

Porsche
Porsche sales were down 20.1% in the first half of 2020 compared to the same time last year, a little better than the average franchise. Porsche finished atop the 2020 J.D. Power APEAL Study that measures the excitement and attachment to new luxury vehicles for the second year in a row. It also set a certified pre-owned sales record in June, selling nearly 3,000 CPOs vs. 5,000 new vehicles. Demand for the upcoming electric Taycan is high, which should further improve sales. Due to their rarity and high profitability, Porsche stores bring the highest blue sky multiples of any franchise other than Ferrari. Higher multiple range on 2019 adjusted pre-tax profit: 8.25x–9.25x.

Mercedes-Benz
Mercedes-Benz saw sales decrease by 13.4% in the first half of 2020 compared to Q2 2019, better than the average. MB recently announced plans to cut seven car models from its U.S. product lineup, which would reduce costs and complexity. MB Financial Services can provide lots of attractive debt capital to dealership buyers which helps their returns on investment. Dealer profits remain among the highest of any franchise, and buyers are highly interested in these dealerships. Higher multiple range on 2019 adjusted pre-tax profit: 6.5x–7.75x.

Lexus
Sales at Lexus were down 21.3% in the first half of 2020, a little better than average. Lexus topped luxury brands in the 2020 J.D. Power Brand Loyalty Study. Consumers love the quality, high resale value, and cheap leasing options of Lexus vehicles. Dealer profits continue to remain healthy even amidst an aging product catalog due to excellent fixed operations. Current margins remain low per unit retailed, but the upcoming LQ SUV should provide dealers with a higher-margin model in the expanding full-size SUV segment. Additionally, the newly re-engineered IS Sedan aims to attract younger buyers. Higher multiple range on 2019 adjusted pre-tax profit: 6.5x–7.75x.

BMW
BMW saw sales drop 28.4% in the first half of 2020 compared to the same period last year, worse than the average franchise. We are hearing its SUVs are almost impossible to keep in stock right now although some of its other models are cold. BMW’s well-balanced product line and high front-end gross profits have kept dealer profits high in recent years so it remains one of the most lucrative franchises. Higher multiple range on 2019 adjusted pre-tax profit: 6.5x–7.75x.
Audi
Audi sales are down 24.9% in the first half of 2020 compared to the first half of 2019. Audi recently stated that they expect sales to reach pre-pandemic levels by 2022-2023. Consumers enjoy Audi's well-balanced product line-up, but dealers grumble about its profitability being much lower than competitive brands. And they complain about Audi management being difficult to work with, even during the pandemic. Until Audi can help dealers with low new vehicle gross margins (due to difficult to attain incentive structure), costly facilities, and its expensive loaner program, the franchise will remain less desirable than BMW, Lexus, or Mercedes-Benz. **Higher multiple range on 2019 adjusted pre-tax profit: 5.75x–6.75x.**

JLR / Land Rover
JLR reported a 23.1% decline in sales through the first half of 2020 compared to the same period last year. Combined sales in North America for both brands had grown for ten consecutive years, and the launch of the new Defender was expected to extend this streak, but the pandemic may have ended it. Land Rover’s premium SUVs continue to carry the company as Jaguar struggles to find buyers. JLR trades at a lower range from other luxury brands due to its expensive facilities, the drag of Jaguar, and incoming add points. **Higher multiple range on 2019 adjusted pre-tax profit: 5.75x–6.75x.**

Volvo
Volvo saw sales decrease just 13.7% during the first half of 2020 compared to the same period last year, better than most franchises. Volvo CUVs are doing well but dealers need more volume and fixed operations to help them cover overhead costs so they can generate attractive profits. **Higher multiple range on 2019 adjusted pre-tax profit: 3.75x–4.75x.**

Acura
Acura’s sales fell 24.1% in the first half of 2020 compared to the same period in 2019. With many dealers suffering from low sales and low margins, Acura is looking for a strong turnaround with its fresh lineup of models. Currently, demand is low for Acura dealerships. **Higher multiple range on 2019 adjusted pre-tax profit: 2.5x–3.25x.**

Infiniti
Infiniti sales dropped a whopping 33.9% in the first half of 2020 compared to the same period in 2019. The product line continues to age. We expect some dealerships to close as dealers aim to mitigate losses and monetize dealership properties. Many have become glorified used car lots. Infiniti’s parent company, Nissan, is losing billions as it begins a painful restructuring. Some good news is that Infiniti officials have said that the company sees the U.S. as a core market and plans to release five new vehicles over the next three years to help rebuild sales. The demand for Infiniti stores is very low. **Same value range: $0–$1,500,000.**

Cadillac
Cadillac saw sales decrease by 29.2% in the first half of 2020 compared to the same period last year. Cadillac dealers are looking forward to the redesigned Escalade’s release later this year. There are also a couple of electric vehicles coming, although we wonder how the Cadillac brand fits with consumers who want to purchase “green” vehicles. The oversaturation of Cadillac dealerships throughout the US prevents most dealers from being very profitable. **Same value range: $0–$1,500,000.**

Lincoln
Lincoln sales were down 8% in the first half of 2020 compared to the same period in 2019. Dealers are irritated that Lincoln is pushing them to build free standing, costly facilities. There is not enough volume and gross profit per Lincoln franchise to support many stand-alone facilities. We wish Lincoln execs would speak with their colleagues at BMW/MINI about their experience in separating those brands many years ago. They have now reconsidered and are allowing both brands back into the same buildings. Lincoln’s portfolio will soon be 100% CUVs and SUVs. Despite attractive new products, Lincoln also suffers from dealership oversaturation so profits per store are generally very low. **Same value range: $0–$1,500,000.**

Mid-Line Import Franchise Blue Sky Multiples

**Toyota**
Toyota announced a 22.6% sales decrease in the first half of 2020 compared to last year, about average for the industry. Toyota has the widest product mix in the industry with sedans, CUVs and trucks in small, medium and large sizes. Toyota dealerships remain in high demand due to their high-volume new vehicle sales, strong fixed operations, and customer loyalty. Dealers also commend Toyota Financial Services for its aggressiveness in the market. We are marketing several Toyota dealerships currently and there is broad and strong interest in the franchise. Dealers believe Toyota/ Lexus is the best OEM partner. **Higher multiple range on 2019 adjusted pre-tax profit: 5.5x–6.5x.**

**Honda**
Honda sales were down 23.7% in the first half of 2020 compared to the same period last year. Honda produces excellent products that are consistent sales leaders in their segments, but some dealers wish its incentives were more competitive. Demand for these dealerships remains high as dealers continue to realize consistent, strong profits. **Higher multiple range on 2019 adjusted pre-tax profit: 5.25x–6.25x.**

**Subaru**
Subaru sales decreased 21.3% for the first half of 2020 compared to the same period in 2019, the first time Subaru has not grown in about a decade. Customer brand loyalty remains unsurpassed according to J.D. Power, and dealers can never seem to maintain enough inventory. Plants have reopened, but are still in very short supply. These dealerships remain in high demand as both current Subaru dealers and dealers of other brands continue to seek these franchises. **Higher multiple range on 2019 adjusted pre-tax profit: 5.0x–6.0x.**

**VW**
Volkswagen saw sales drop 21.5% for the first half of 2020 compared to last year, about the same as the overall market. Dieselgate is fading from consumers’ minds, but the franchise is stuck in a low volume – low gross position. As a result, dealer profits remain lower than most other franchises. Tesla CEO Elon Musk has noted that VW is doing more than any other automaker to go electric and that could help it to take share in markets like CA that will have tougher emissions standards. **Higher multiple range on 2019 adjusted pre-tax profit: 2.75x–3.5x.**
**Kia**

Kia sales fell just 13.6% so far in 2020 compared to 2019, far better than most other franchises. Since South Korea handled the pandemic well its plants were able to reopen faster so supply has not been as badly impacted as other brands. The Telluride was recently named Car of the Year at the 2020 World Car Awards and continues to maintain high consumer demand and impressive margins. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x–3.75x.

**Hyundai**

Sales decreased by 18.4% so far in 2020 compared to last year. Like Kia, Hyundai is in a good position regarding vehicle supply so we expect it will perform better than most other brands over the next few months. Palisade remains in high demand and is bringing luxury vehicle grosses. Many dealers in the US are watching what effect Jose Munoz, hired about a year ago as Global COO and President and CEO of Hyundai Motor North America, will have on the franchise. Some Nissan dealers blame him for the policies he enforced when he was a senior executive there that led to major problems at Nissan dealerships. So far, his leadership seems to be working out well. Dealers are pleased with the higher profits they were seeing prior to the pandemic. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x–3.75x.

**Mazda**

Mazda sales were only down 7% so far in 2020 compared to the same period in 2019, making Mazda the best performing franchise of 2020 so far. Mazda had been on a bit of a roll with strong sales of its CUVs. The construction of a US plant in conjunction with Toyota should help boost its position in the US. Mazda dealers can benefit from gross profit margins over 12% on new units by hitting some achievable metrics. Mazda’s new image requirements bother some dealers and potential buyers who do not see the cost is worth the benefit. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x–3.5x.

**Nissan**

Nissan reported a 39.9% decline so far in 2020 compared to last year. The Q2 numbers were even worse, down 50% from Q2 2019. The brand continues to struggle with restructuring efforts and fallout associated with the Ghosn scandal. Nissan lost $6B in the most recent fiscal year, about the same as the year before. There are some signs of hope for US dealers as the brand works through its “Nissan Next” restructuring plan to improve incentives and marketing. While some stores are nicely profitable, many dealers are reluctant to give the brand another chance. Higher multiple range on 2019 adjusted pre-tax profit: 2.0x–2.75x.

**Domestic Franchise Blue Sky Multiples**

**Ford**

Ford sales fell by 23.8% in the first half of 2020 compared to the same period last year. Ford opted to replace CEO Jim Hackett with Jim Farley who is liked by many dealers. US vehicle production has returned to pre-pandemic levels, and the company is excited for the upcoming launch of the redesigned F-150, the return of the Bronco, and the new Mach-E electric SUV. Ford has been a relatively cold brand for the past few years. Perhaps the CEO change will inspire dealers to call us to buy these stores again. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x–4.0x.

**Chevrolet**

Chevrolet saw sales drop by 19.4% in the first half of 2020 compared to the same period in 2019. In terms of new products, the demand for the 2020 Corvette far exceeded demand. The new Silverado got good reviews in terms of how it performs, but its interior falls short compared to the Ram and F-150, in the minds of some. The new Tahoe and Suburban should further boost sales. Dealers can do very well with Chevrolet stores in markets that are not overdealered since they can generate healthy grosses on new and used units and fixed operations are strong. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x–4.0x

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**THANK YOU!**

The team at Haig Partners would like to thank our clients, buyers, industry partners and associates as we celebrate these milestones.
FCA (Chrysler-Jeep-Dodge-Ram-Fiat)
Collectively, FCA saw sales decrease by 25.7% for the first six months of 2020 compared to last year. The Ram and Jeep brands continue to lead the group, with Ram making consistent moves ahead of the competition with regard to infotainment, interior design, and driving assistance. Dodge was the first domestic brand to top J.D. Power’s quality scorecard, which is a notable achievement since FCA’s brands have not ranked highly in the past. The FCA-PSA merger is still on track and, if approved, it would create the fourth-largest automaker in the world. These dealerships can also offer healthy profits in areas where they are not overdealed. This multiple range excludes the Fiat brand. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x-4.0x.

Buick-GMC
Buick-GMC sales fell 24.6% in the first half of 2020 compared to the same period last year. Buick is now only offering CUVs. The era of Skylarks, LeSabres, Rivieras, and Regals is over. The GMC Sierra continues to be a strong seller at healthy gross profits and dealers are optimistic about the upcoming release of the redesigned Yukon and Yukon XL. GMC will be also launching the Hummer sub-brand in 2022 that will offer electric-powered SUVs and trucks. Higher multiple range on 2019 adjusted pre-tax profit: 3.0x-3.75x.

Haig Partners is not a traditional dealership brokerage firm. We combine the skills gained during our years in investment and commercial banking with experience of buying and selling dealerships for AutoNation and Asbury. We do not seek “listings” of many dealerships. Instead, we provide the best possible advice and service to a limited number of clients, helping optimize the sale of their most valuable asset in a highly confidential process. We spend a tremendous amount of time and energy on each engagement. Emphasizing quality over quantity to best serve our clients’ interests.

Higher Prices
We create offering materials that provide buyers with a compelling investment thesis about why they should acquire our client’s business instead of other opportunities. We then run a sales process that creates competition to generate highly attractive offers from buyers.

Relationships with Buyers
We know and are respected by many of the best buyers across the U.S. We understand what they want to acquire and how they negotiate. By targeting specific buyers instead of running ads, we preserve confidentiality and close transactions more efficiently.

Experience
Since we have been involved in more than 180 transactions for over 360 dealerships with over $5.4 billion in value, we know how to respond to issues that can arise in a buy-sell process.

Speed
We focus on the transaction every day, allowing our clients to focus on dealership operations.
The auto industry is rapidly recovering from the initial hit from the pandemic. Many dealers enjoyed record levels of profits in June and July due to pent up demand and limited inventory that helped to boost margins. Most dealers have been pushed by the pandemic to restructure their operations. They added digital retailing, reduced expenses with outside vendors, and streamlined their staffing models. Lower interest rates are reducing floorplan and mortgage costs. What remains unknown is how long it will take to rebuild our economy. No one can predict the effects of countervailing trends like rising vehicle production, falling stimulus spending, low-interest rates, reduced employment, an election year, work-from-home initiatives and other forces that are usually at work. Dealers tell us they expect monthly profits will fluctuate for some time.

The buy-sell market took a hit in the first half of the year but is now also recovering. The number of dealerships sold in the US in Q1 and Q2 2020 fell 16% from the same period in 2019. Sales in the second half of the year are increasing as buyers return to the table, eager to invest their substantial amounts of excess cash. At the risk of “jinxing” transactions in our pipeline, we expect to close on transactions representing more than 20 rooftops in Q3 2020. Based on our experience and the information we have gathered from others, we believe blue sky values have fallen about 5% from year-end 2019 to the end of Q2 2020 because of declining earnings. Many private groups are looking to buy and Lithia has stated it will be purchasing about $1B worth of dealerships each year over the next five year period to hit its growth targets. These acquisitions demonstrate that dealership buyers remain excited about the future of auto retail and have plenty of capital for acquiring businesses that are fairly priced.

**KEY TAKEAWAYS**

Having been involved in over 180 transactions for more than 360 dealerships, no other firm has a better understanding of the perspectives of both buyers and sellers of dealerships across the U.S. We use this expertise to create highly informative and compelling offering materials that help buyers to focus on our clients instead of other opportunities. We listen to our clients to create a customized marketing process that carefully balances their priorities of maximizing price, preserving confidentiality, and time to closing. Through our unmatched expertise, deep relationships with buyers, and well-honed processes, Haig Partners is able to produce highly desirable outcomes for our clients.
Contact Us Today To Learn More About Your Dealership’s Potential Value

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HAIG PARTNERS LATEST TRANSACTIONS

**VIRGINIA**

Haig Partners represented the sale of Southern Auto Group

**CALIFORNIA**

Has been acquired by BMW

**CALIFORNIA**

Has been acquired by Hatom Automotive

**ILLINOIS**

Has been acquired by Zeigler

**MISSISSIPPI**

Has been acquired by Mclarty Automotive Group

**FLORIDA**

Has been acquired by Morgan Automotive Group