

## Exit Vertu Motors: Falling used car prices despite supply constraints

<b>Company:</b>	Vertu Motors (VTU LN)	<b>Market Cap:</b>	£186mio
<b>Industry:</b>	Car dealership	<b>Net current assets:</b>	£40mio
<b>Country:</b>	UK	<b>Revenue:</b>	£3.6bn
<b>Date:</b>	20 <sup>th</sup> June 2022	<b>Net Income:</b>	£60mio (1.6%)
<b>Dividend:</b>	3.21% (8% incl. share buybacks)	<b>Free Cash Flow:</b>	£70mio (2%)
<b>Entry:</b>	£229mio	<b>Exit:</b>	£190mio

### No takeover in sight

Having monitored UK car dealerships since the big jump in profits became present in the summer of 2021, I kept thinking that these profits are transitory, as supply constraints will ease. With the Ukraine invasion by Russia and renewed China Covid lockdowns these supply constraints began to worsen again, while at the same time an uptick in M&A activity started to sweep across the sector<sup>1</sup>. Vertu Motors, being priced as much as 1/3 cheaper than competitor Lookers, appeared cheap and an attractive takeover target. However, the M&A activity quickly became muted as the emerging online-only car dealers began to struggle with Carzam entering administration and Cazoo increasing cost cuts<sup>2</sup>.

### Falling used car prices

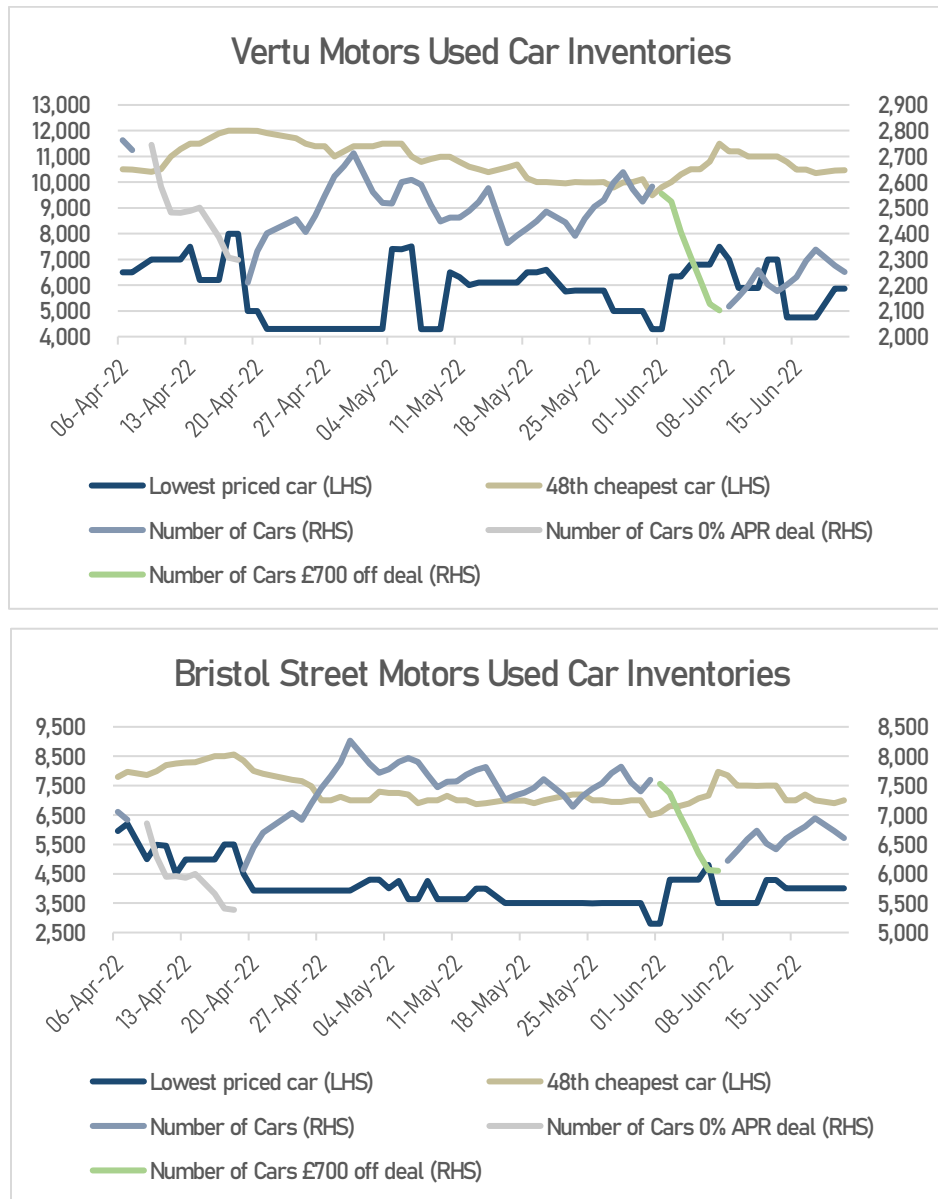
While new cars remain high in demand with most EV models having a waiting time of more than one year, new car prices continue to stay elevated. Used car prices, on the other hand, are seeing prices decline despite continued supply constraints, which signals rapidly waning demand. As Vertu Motors sells more low-cost cars than Lookers via its Bristol Street Motors brand, the discount of Vertu Motors market capitalization compared to Lookers begins to make more sense as the cost of living crisis intensifies with new record spikes in petrol and diesel prices in the UK. This can be further evidenced with Vertu Motors

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<sup>1</sup> <https://www.aozorastep.com/Vertu%20Motors.pdf>

<sup>2</sup> <https://www.am-online.com/news/dealer-news/2022/06/06/faltering-online-car-retailers-performance-blamed-for-carzam-s-failure>

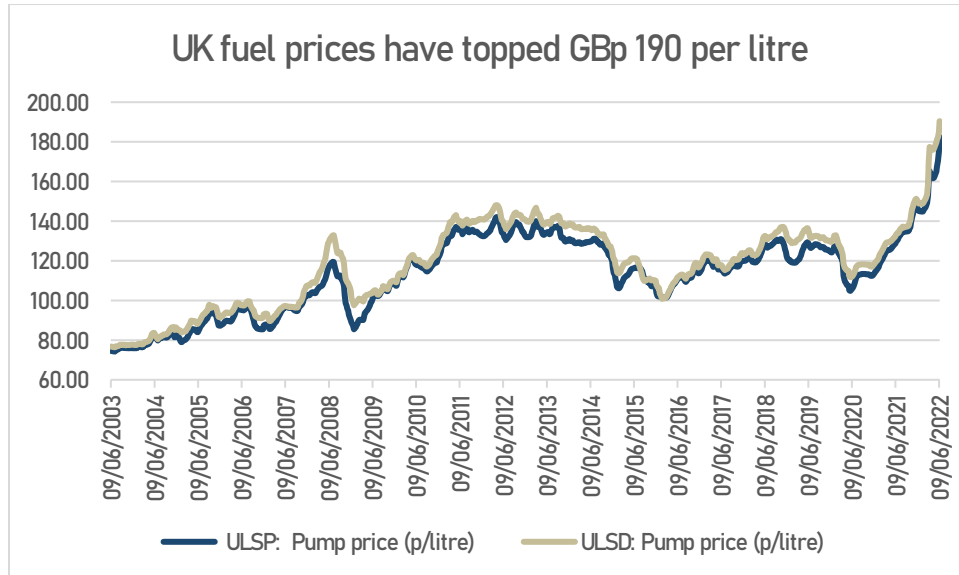
& Bristol Street Motors used car inventories declining only due to special offers and discounts. Halfords, a bicycle and motor equipment supplier, has also recently mentioned a decline in consumer demand for high ticket items<sup>3</sup>. Finally, last week the UK government announced to scrap the £1,500 EV grant one year early, which could potentially affect new EV sales negatively in the coming months<sup>4</sup>.



Source: Vertu Motors/Bristol Street Motors

<sup>3</sup> <https://www.halfordscompany.com/investors/rns/rns-announcements/4119797>

<sup>4</sup> <https://www.gov.uk/government/news/plug-in-grant-for-cars-to-end-as-focus-moves-to-improving-electric-vehicle-charging>



Source: Department for Business, Energy & Industrial Strategy

### No cars for sale & higher competition

2021 was about higher margins and fewer sales with margins outweighing the impact of lower sales, leading to record profitability. In 2022, I now believe that there is a risk of a reduction in sales that is outweighing the higher margins – this could be problematic for car dealerships as costs have generally risen, too. At the same time, every single dealership made record margins in 2021. This means every single dealership is investing, opening new dealerships, refurbishing, which will heat up competition and lower margins. Overall, these risks seem to be priced into the valuation of Vertu Motors, but there could be a deeper correction in valuation when the supply/demand balance shifts from -/+ to -/- in a more visible way. Having not foreseen this coming has been a big mistake on my end.



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