

# Marshall Motor Holdings

FY17 results

Outperforming its markets

Marshall Motor Holdings (MMH) delivered FY17 results that exceeded our earnings estimates despite the challenges of softer UK car markets that are persisting into FY18. The dilutive disposal of the leasing activity leaves MMH effectively ungeared and in a strong position to pursue its growth strategy. As previously, we forecast a modest organic earnings decline for FY18, which may be augmented by value-adding M&A if suitable opportunities arise.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16	1,899.4	25.4	26.2	5.5	6.4	3.3
12/17	2,268.9	29.1	30.8	6.4	5.4	3.8
12/18e	2,283.9	23.5	24.1	6.9	6.9	4.1
12/19e	2,334.4	24.0	24.6	7.1	6.8	4.3

Note: \*PBT and EPS are normalised, excluding amortisation of acquired intangibles and exceptional items.

## Robust like-for-like performance

In the ongoing retail segments, FY17 saw solid like-for-like sales performances despite softer new and used car markets. Gross profit rose 22% for the continuing activities with a margin expanded to 11.6%, up around 17bp for the full year and increasing sequentially in H217. This implies a successful integration of the Ridgeway business acquired in H116. The FY17 dividend was increased 16% to 6.4p and was covered 4.2x by adjusted EPS of the continuing activities that grew 26% to 26.9p. The disposal of the leasing business in November left year-end net debt of just £2.2m. Having guided the company through the float and the transformational acquisition of Ridgeway, the chairman is stepping down, but the senior executive team remains in place to pursue development of the group.

## Outlook remains challenging

Both new and used car sales fell in the UK, although overall volumes remain high in comparison to history. MMH faces FY18 without the significant benefit from M&A that boosted FY17 performance. The Society of Motor Manufacturers & Traders (SMMT) is forecasting 5.6% decline in FY18 new car sales, with the first half comparing to a record level in Q117. Used car market volume trend is also likely to remain modestly down. We take encouragement from H217 performance when an essentially like-for-like improvement in gross profits was achieved by all three of the retail segments; new, used and aftersales. If this continues in FY18, then the continuing business should deliver a resilient profit performance.

## Valuation: Rating gap to peers has closed

The share price has proved quite resilient over the last 12 months, while some of its immediate peers have faced a further de-rating. The FY19e P/E of 6.8x compares to our auto retailer peer group multiple of 7.1x, which still represents a discount, albeit lower than a year ago. The sector rating also remains exceedingly cautious at a discount of around 37% to the broader FTSE All-Share General Retail Index. While not surprising given a softer sales environment, we feel the larger dealership groups can outperform what are still historically high market demand levels.

Automotive retailers

14 March 2018

**Price** 167p  
**Market cap** £129m

Net debt (£m) at 31 December 2017	2.2
Shares in issue	77.4m
Free float	34.9%
Code	MMH
Primary exchange	AIM
Secondary exchange	N/A

### Share price performance



%	1m	3m	12m
Abs	10.6	1.8	1.5
Rel (local)	10.4	6.0	3.1
52-week high/low	178.5p	134.5p	

### Business description

Marshall Motor is the seventh largest UK motor retailer, operating 101 franchises spread across 23 brands at 86 locations. It is one of six UK dealership groups that represent each of the top five volume and premium brands. The group has a strong presence in eastern and southern England.

### Next events

AGM	22 May 2018
Interim results	August 2018

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## FY17 results summary

Despite a market that remained less favourable throughout the second half of the year, MMH has announced FY17 results that were broadly in line with expectations. The main highlights are summarised below:

### Exhibit 1: Marshall Motor Holdings FY17 key data

Year to December (£m)	2016	2017	% change
Revenues	1,899.4	2,268.9	19.5%
EBITDA	38.4	46.4	%
EBIT (underlying)	32.3	37.2	%
Profit before tax (underlying)	25.4	29.1	14.4%
Profit before tax (underlying continuing)	20.5	25.4	23.7%
EPS (p) – (underlying)	26.2	30.8	17.6%
EPS (p) – (underlying continuing)	21.3	26.9	26.3%
DPS (p)	5.5	6.4	16.4%
Net debt	119.0	2.2	
Adjusted net debt	54.5	2.2	
<b>NAV per share (p)</b>	<b>188</b>	<b>248</b>	

Source: Company reports

The disposal of the leasing business was completed in the final quarter, essentially eliminating net debt of the ongoing operations, which are now focused on the retail operations of the group. The company also boosted net assets, which stood at 248p per share at the end of 2017, up by 32% and supported by the large portfolio of long leasehold and freehold property.

In terms of trading, the Retail operations generated an overall increase in gross profit in H217, which was essentially a like-for-like comparison against a tougher new car market backdrop. The first half had benefited from the additional contribution from Ridgeway, which was acquired during H116. All three of the subsegments (new car sales, used car sales and aftersales services) improved gross contributions in the second half over the prior year. Retail gross margins finished some 17bp up for the year, mainly due to an improvement in the high margin aftersales activity.

### Exhibit 2: Marshall Motor Holdings gross profit analysis

Year to December (£m)	2016			2017			% change		
	H116	H216	FY16	H117	H217	FY17	H1	H2	FY
New	30.8	38.1	68.9	45.1	39.0	84.1	46.4%	2.3%	22.0%
Used	22.8	27.9	50.7	31.2	28.7	59.9	36.8%	2.9%	18.2%
Aftersales	39.7	52.6	92.3	57.3	56.7	114.0	44.3%	7.7%	23.5%
<b>Retail (continuing businesses)</b>	<b>93.3</b>	<b>118.6</b>	<b>211.9</b>	<b>133.6</b>	<b>124.4</b>	<b>258.0</b>	<b>43.2%</b>	<b>4.9%</b>	<b>21.7%</b>
Leasing (discontinued)	4.9	3.7	8.6	4.0	3.1	7.1	-16.8%	-16.4%	-16.6%
<b>Group gross profit</b>	<b>98.2</b>	<b>122.3</b>	<b>220.5</b>	<b>137.6</b>	<b>127.5</b>	<b>265.1</b>	<b>40.2%</b>	<b>4.2%</b>	<b>20.3%</b>
New	7.1%	6.9%	7.0%	7.4%	7.0%	7.2%			
Used	7.4%	6.8%	7.1%	6.8%	7.0%	6.9%			
Aftersales	46.1%	45.2%	45.6%	46.5%	47.3%	46.9%			
<b>Retail (continuing businesses)</b>	<b>11.6%</b>	<b>11.3%</b>	<b>11.4%</b>	<b>11.4%</b>	<b>11.7%</b>	<b>11.6%</b>			
Leasing (discontinued)	24.0%	19.3%	21.7%	20.7%	17.8%	19.3%			
<b>Group</b>	<b>11.9%</b>	<b>11.4%</b>	<b>11.6%</b>	<b>11.6%</b>	<b>11.8%</b>	<b>11.7%</b>			

Source: Company reports

In new car markets, after reaching a record level in the first quarter, registrations fell significantly and persistently as confidence from consumers ebbed away in the face of political and Brexit uncertainties. The situation was further exacerbated by the pull forward of sales into the first quarter resulting from the introduction of new vehicle excise duty (VED) rates from the beginning of April. In addition, adverse publicity with respect to personal contract plan (PCP) finance and diesel engine emissions severely affected buyers' choice of the fuel.

Against this market environment, MMH recorded a new vehicle unit sales increase of 9% to 53,308 cars (FY16 48,884), which represented a like-for-like decline of 7.5%. Interestingly, while the retail segment of the market showed a sharper decline in 2017, MMH actually outperformed with a like-for-like decrease of just 2.8% in retail units. The balanced portfolio of volume, alternate premium and premium brands provided a supportive platform. Alternate premium and premium brands account for 75% of sales and outperformed the market trend. Boosted by the full year from Ridgeway, the overall improvement in retail demand was 12.3%, accounting for around 60% of overall group new car sales.

By contrast, fleet sales dropped 13.9% against a market decline of 4.7%. The performance reflected the already announced decision to withdraw from some lower-margin activities.

In common with other large motor dealership groups, the use of PCPs remains an important tool in the affordability of new cars for buyers. 83% of customers buying new cars on finance from MMH utilised PCPs in 2017, and it had almost 67.5k customer PCP contracts in force at the end of 2017. The concerns over PCP utilisation appear to be abating, with an awaited report from the FCA towards the end of this month, and management expects to give them a largely clean bill of health. It is also anticipated that while monitoring of credit risk and regulatory requirements may be stepped up, the larger dealership groups such as MMH already apply rigorous standards to any offer.

PCPs are regarded as beneficial in retaining customer engagement when renewals are due. In addition, PCPs provide a forecastable and high quality source of vehicles for used car operations, as well as supporting aftersales service volumes.

MMH's performance in the used car segment was impressive in what was a slightly softer market. Volumes grew by 17.1% to 44,237 units, up 5.2% like-for-like. In turn, this drove revenues up by 21.1% (7% like for like), and while gross margin slipped modestly to 6.9% (FY16 7.1%), the gross profit contribution was also up almost 20%.

Again PCPs play an increasingly important role in the used segment with 58% of the group's 2017 sales utilising the product. As with new cars and the ability to offer service plans to customers on quality vehicles, the use of PCPs provides support for the aftersales operations.

Aftersales is a very high gross margin activity operating in the more mature growth environment of the overall car parc, and MMH's position within that. The addition of Ridgeway drove sales up 20.0%, 2.3% on a like-for-like basis. The customer base has continued to grow in recent years thanks to strong new and used vehicle sales, as well as the penetration of the aforementioned PCPs and service plans. The group had over 77K service plans in force at the end of 2017. Customer service and experience remains of paramount importance in client retention. Gross margin increase by some 130bps to 46.9% in 2017, and the contribution to gross profit increased 23% to £114m, or 44% of the total for the continuing Retail business.

The Leasing business was sold on 24 November 2017 for a gross consideration of £42.5m. Its contribution was down slightly on the prior year during its period of consolidation. Management also closed six subscale loss-making businesses during 2017.

## Outlook

The trends apparent through the second half of 2017 have persisted into the current year. The SMMT forecast for the current year is for a 5.6% decline in new cars, which still implies a strong market in an historical context. At 2.56m units 2017 was still the third-best selling year ever following the record 2.69m units in 2016. The first-quarter comparisons will be the toughest but these should progressively ease as the year progresses.

Operating in this environment management has indicated no change in its expectations for FY18 after considering year-to-date trading. We have tweaked our numbers modestly following the

confirmation of FY17 performance, but essentially we leave our FY18 earnings estimates are unchanged.

It shows modest year-on-year decline which we expect to start to reverse in our 2019 estimates which we introduce for the first time.

<b>Exhibit 3: Earnings estimates revisions</b>						
Year to December (£m)	2017e	2017a		2018e		
	Prior	Actual	% change	Prior	New	% change
New Car	1,199.6	1,166.5	-2.8%	1,164.6	1,154.0	-0.9%
Used Car	855.2	869.7	1.7%	867.3	925.6	6.7%
Aftersales	234.4	243.1	3.7%	243.7	252.8	3.7%
Intra group	-55.6	-47.6	-14.4%	-57.0	-48.8	-14.4%
<b>Retail</b>	<b>2,233.5</b>	<b>2,231.7</b>	<b>-0.1%</b>	<b>2,218.6</b>	<b>2,283.6</b>	<b>2.9%</b>
Leasing	37.2	37.0	-0.6%	0.0		
Unallocated	0.4	0.3	-23.6%	0.4	0.3	-23.6%
<b>Group revenues</b>	<b>2,271.1</b>	<b>2,268.9</b>	<b>-0.1%</b>	<b>2,219.0</b>	<b>2,283.9</b>	<b>2.9%</b>
<b>EBITDA</b>	<b>44.8</b>	<b>46.4</b>	<b>3.5%</b>	<b>38.7</b>	<b>38.8</b>	<b>0.3%</b>
Retail	41.9	41.5	-0.9%	41.4	40.5	-2.3%
Leasing	5.2	4.3	-17.7%	0.0	0.0	
Unallocated	-9.5	-8.6	-9.3%	-9.7	-8.8	-9.3%
<b>Underlying EBITA</b>	<b>37.6</b>	<b>37.2</b>	<b>-1.1%</b>	<b>31.7</b>	<b>31.7</b>	<b>-0.2%</b>
<b>Underlying PBT</b>	<b>28.8</b>	<b>29.1</b>	<b>1.0%</b>	<b>23.5</b>	<b>23.5</b>	<b>0.0%</b>
<b>EPS - underlying continuing (p)</b>	<b>29.1</b>	<b>30.8</b>	<b>6.0%</b>	<b>23.8</b>	<b>24.1</b>	<b>1.3%</b>
DPS (p)	6.5	6.4	-0.8%	6.9	6.9	0.0%
Net debt / (cash)	1.6	2.2	n.m.	-9.8	6.1	-165.2%
Source: Company reports, Edison Investment Research estimates						

The balance sheet is now essentially ungeared with net debt of just £2.2m at the year end, following the disposal of Leasing and its associated asset-backed debt. Together with its significant banking facilities the group is well positioned to pursue value creating opportunities in the sector as they arise, with the softer market environment anecdotally starting to lower vendor expectations.

In addition to £6.8m of restructuring costs and the £36.9m profit on the leasing disposal, the company took a £6.0m provision in FY17 included in non-underlying items that is the estimate of the cost of withdrawal from the Marshall Group Executive Pension Plan. MMH has no active members of the scheme and it is the last defined benefit pension scheme exposure for MMH.

The dividend increase of 16% to 6.4p for 2017 provides an attractive yield of 3.8% that remains covered 4.2x by underlying earnings of the continuing businesses. We feel this has played an important role in providing share price resilience for MMH, which has allowed it to close the rating gap to some of its peers. Auto retailers remain cautiously rated by the market compared to the more general retail sector, but we think as the larger groups continue to display resilience in tepid markets, the market should start to increasingly respect the value afforded.

<b>Exhibit 4: Peer group comparison</b>					
	Price	Market cap	FY17 revenue	P/E (x)	P/E (x)
	(p)	(£m)	(£m)	2018e	2019e
Cambria Auto	63.0	62	644	8.3	7.8
Lookers	93.5	372	4,766	6.4	6.0
Marshall Motor Holdings	165.0	140	2,269	7.0	6.9
Pendragon	27.9	397	4,739	8.0	7.3
Vertu Motors	43.0	165	2,818*	7.3	7.4
<b>Simple average</b>				<b>7.4</b>	<b>7.1</b>
<b>FTSE All-Share General Retailers Index</b>				<b>12.1</b>	<b>11.2</b>
Source: Bloomberg, Edison Investment Research. Note: Prices at 12 March 2018. *Bloomberg estimate.					

**Exhibit 5: Financial summary**

	£m	2015	2016	2017	2018e	2019e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>						
Revenue		1,232.8	1,899.4	2,268.9	2,283.9	2,334.4
Cost of Sales		(1,087.5)	(1,678.9)	(2,003.8)	(2,015.6)	(2,060.1)
Gross Profit		145.3	220.5	265.1	268.4	274.3
EBITDA		22.5	38.4	46.4	38.8	39.2
Operating Profit (before amort. and except.)		18.7	32.3	37.2	31.7	32.0
Intangible Amortisation		(0.2)	(0.3)	(0.3)	(0.4)	(0.5)
Exceptionals		(0.5)	(3.2)	24.1	0.0	0.0
Other		0.0	0.0	0.0	0.0	0.0
Operating Profit		18.0	28.8	60.9	31.3	31.6
Net Interest		(2.9)	(6.9)	(8.1)	(8.2)	(8.0)
Profit Before Tax (norm)		15.8	25.4	29.1	23.5	24.0
Profit Before Tax (FRS 3)		15.1	21.9	52.8	23.1	23.6
Tax		(3.6)	(4.4)	(3.8)	(4.9)	(5.0)
Profit After Tax (norm)		9.4	20.3	23.8	18.6	19.0
Profit After Tax (FRS 3)		11.5	17.5	49.0	18.2	18.5
Average Number of Shares Outstanding (m)		59.4	77.3	77.4	77.2	77.2
EPS - normalised (p)		15.8	26.2	30.8	24.1	24.6
EP		15.3	25.4	29.8	23.3	23.8
EPS - (IFRS) (p)		19.3	22.6	63.4	23.6	24.0
Dividend per share (p)		2.98	5.50	6.40	6.90	7.11
Gross Margin (%)		11.8	11.6	11.7	11.8	11.8
EBITDA Margin (%)		1.8	2.0	2.0	1.7	1.7
Operating Margin (before GW and except.) (%)		1.5	1.7	1.6	1.4	1.4
<b>BALANCE SHEET</b>						
Fixed Assets		150.0	326.4	266.6	286.0	295.6
Intangible Assets		40.8	122.0	121.6	121.7	121.7
Tangible Assets		109.2	204.4	145.0	164.3	173.9
Investments		0.0	0.0	0.0	0.0	0.0
Current Assets		307.5	475.2	499.1	488.1	504.7
Stocks		240.6	380.0	401.3	388.3	396.9
Debtors		28.9	71.0	64.1	63.9	65.4
Cash		24.1	0.1	4.9	6.9	12.9
Other		13.9	24.1	28.8	29.0	29.6
Current Liabilities		(290.1)	(584.9)	(539.3)	(527.9)	(539.6)
Creditors		(263.4)	(507.2)	(538.6)	(527.9)	(539.6)
Short term borrowings		(26.7)	(77.7)	(0.6)	0.0	0.0
Long Term Liabilities		(37.6)	(71.1)	(35.2)	(41.6)	(42.8)
Long term borrowings		(24.7)	(41.4)	(6.5)	(13.0)	(14.2)
Other long term liabilities		(12.9)	(29.7)	(28.7)	(28.6)	(28.5)
Net Assets		129.9	145.7	191.2	204.5	218.0
<b>CASH FLOW</b>						
Operating Cash Flow		29.6	98.9	60.8	35.4	34.7
Net Interest		(1.1)	(1.4)	(2.9)	(2.7)	(2.7)
Tax		(3.0)	(17.3)	(3.8)	(4.9)	(5.0)
Capex		(39.6)	(61.9)	(57.5)	(26.5)	(16.8)
Acquisitions/disposals		(21.5)	(91.4)	44.6	0.0	0.0
Financing		66.9	0.0	0.0	0.0	0.0
Dividends		(15.4)	(3.3)	(4.5)	(5.1)	(5.4)
Other		8.6	(15.5)	80.2	0.0	0.0
Net Cash Flow		24.5	(91.8)	116.8	(3.9)	4.8
Opening net debt/(cash)		51.7	27.2	119.0	2.2	6.1
HP finance leases initiated		0.0	0.0	0.0	0.0	0.0
Other		0.0	0.0	0.0	0.0	0.0
Closing net debt/(cash)		27.2	119.0	2.2	6.1	1.3

Source: Company reports, Edison Investment Research estimates

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