Lookers

Maintaining performance

Q3 trading update

Automotive retailers

Lookers maintained its outlook for the current year, notwithstanding supply-side disruption that created volatility in new car markets in Q318. Used car and aftersales activities remain healthy and Q318 trading was ahead against a strong Q317. There are signs of stabilisation in new car markets in Q418 and Lookers expects to deliver against market expectations for the full year. However, a more cautious view as Brexit looms leads us to reduce our FY19e EPS by 6%. Nevertheless, the undemanding rating remains supported by an attractive yield.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16	4,088.2	64.9	13.13	3.64	7.5	3.7
12/17	4,696.3	68.4	14.14	3.89	6.9	4.0
12/18e	4,835.4	67.7	13.70	4.08	7.2	4.2
12/19e	4,824.2	66.4	13.65	4.17	7.2	4.3

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Robust trading performance in volatile Q3

When considering motor retailers, investors' attention tends to be drawn towards New car performance, despite the fact that for Lookers two-thirds of gross profit is generated by the higher-margin Used and Aftersales segments. Both of these businesses continued to trade healthily through Q318. Margins in New cars actually improved, despite a sharp drop in sales and volumes. Q318 new car demand was highly volatile due to the introduction of the Worldwide Harmonised Light Vehicle Testing Procedure (WLTP) emission regime on 1 September. For the first nine months, Lookers saw new car revenues fall 7%, in line with the UK market, and gross profit fell by 5%. Used car revenues and gross profit grew 10%, and the high-margin Aftersales activity grew gross profit 6% on revenues up 5%.

More stable market conditions anticipated

As discussed in our last note, Lookers expected volatility in new car markets in H218 as initial supply constraints were worked through, but overall a neutral impact. The outcome seems increasingly likely as UK new car registrations showed a 2.9% decline in October, despite some clear ongoing effects from WLTP on a few manufacturers. The recently issued SMMT forecast now indicates a new car market down 6.3% in 2018, which compares to the year-to-date decline of 7.2%. With Brexit looming, the forecast is for a UK new car market of 2.325m cars, 2.7% below the July forecast. This has led us to reduce our FY19 earnings forecast by 6%. Used car and Aftersales trends remain supportive as we expect Lookers to outperform the underlying markets. The balance sheet continues to facilitate suitable acquisitions, as indicated by the £5.5m purchase of Jennings Group in September.

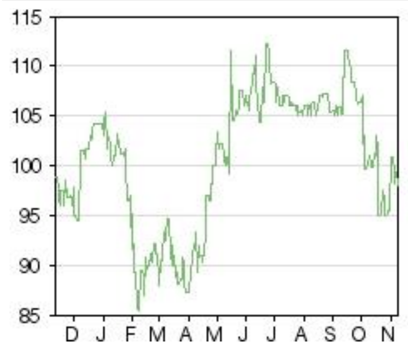
Valuation: Rating remains undemanding

Along with the other UK motor retailers, Lookers' share price performance has suffered since the interims as volatile new car data has remained the focus. The shares currently trade on an FY19e P/E of 7.2x, which remains undemanding.

9 November 2018

Price	**98p**
Market cap	**£384m**
Net debt (£m) at 30 June 2018	54.5
Shares in issue	392m
Free float	80%
Code	LOOK
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(2.0)	(6.7)	0.0
Rel (local)	(0.6)	1.4	5.5
52-week high/low		112.2p	82.0p

Business description

Lookers is vying to be the largest UK motor vehicle retailer, with its new car operations supported by the strength of used and aftersales activities. It now operates 155 franchises, representing 32 marques from 100 sites around the UK, with strong regional presences in Northern Ireland, Scotland, the South East and across northern England.

Next event

FY18 results	February 2019

Analysts

Andy Chambers +44 (0)20 3681 2525

Annabel Hewson +44 (0)20 3077 5700

industrials@edisongroup.com

Edison profile page

Lookers is a research client of Edison Investment Research Limited

Outlook

WLTP has caused major monthly volatility in the UK new car markets during both August and September, with pre-registrations boosting the former and a restricted supply of vehicles from several manufacturers depressing the latter. While October shows a more modest 2.9% decline, there are clearly some ongoing effects from WLTP affecting a few manufacturers. As a result, the SMMT now expects the 2018 UK new car market to decline 6.3% to 2.831m registrations.

While the trend is improving in Q4, few of the underlying issues affecting demand have been addressed. Consumers may be hearing of an end to austerity with almost full employment in the UK, but with Brexit looming in H119, and policies towards new cleaner diesels still failing to provide any support, the outlook for FY19 remains subdued

The SMMT forecast is now for further modest declines for 2019 (-2.4%) and 2020 (-1.0%) in UK new car sales. It should be noted that this still represents strong levels of demand compared to historic levels. We also expect to see a more normal seasonal trading pattern compared to this year and last. We expect some effects to used car and aftersales trends but we believe remain more supportive

While our FY18 numbers remain as previously, we have reduced our FY19 PBT and EPS forecasts to reflect the more subdued markets, as shown below:

Exhibit 1: Lookers revisions to earnings estimates

Year to December (£m)	2018e			2019e		
	Prior	New	% change	Prior	New	% change
New	2,446.8	2,446.8	0.0%	2,486.0	2,412.6	-3.0%
Used	1,873.0	1,873.0	0.0%	1,966.6	1,891.7	-3.8%
Aftersales	429.2	429.2	0.0%	446.4	429.2	-3.8%
Leasing	86.4	86.4	0.0%	90.7	90.7	0.0%
Total sales	4,835.4	4,835.4	0.0%	4,989.7	4,824.2	-3.3%
EBITDA	105.2	105.2	0.0%	107.9	103.3	-4.3%
Underlying EBITA	84.3	84.3	0.0%	86.8	82.8	-4.6%
Underlying PBT	67.7	67.7	0.0%	70.4	66.4	-5.6%
EPS - underlying continuing (p)	13.7	13.7	0.0%	14.5	13.7	-5.6%
DPS (p)	4.08	4.08	0.0%	4.29	4.17	-2.9%
Net debt/(cash)	66.7	66.7	0.0%	56.5	57.3	1.4%

Source: Edison Investment Research estimates

We have also reduced our expectation for the FY19 dividend to an inflationary 2% increase that maintains earnings cover at over 3x, but still provides a healthy yield for investors.

EDISON

Exhibit 2: Financial summary

£m	2016	2017	2018e	2019e
Year end 31 December	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS				
Revenue	4,088.2	4,696.3	4,835.4	4,824.2
Cost of Sales	(3,638.7)	(4,192.2)	(4,327.7)	(4,317.7)
Gross Profit	449.5	504.1	507.7	506.5
EBITDA	97.6	105.4	105.2	103.3
Operating Profit (before amort. and except.)	82.5	84.7	84.3	82.8
Intangible Amortisation	0.0	0.0	0.0	0.0
Exceptionals	14.7	(10.0)	(4.5)	(12.1)
Other	0.0	0.0	0.0	0.0
Operating Profit	97.2	74.7	79.8	70.7
Net Interest	(17.6)	(16.3)	(16.6)	(16.4)
Profit Before Tax (norm)	64.9	68.4	67.7	66.4
Profit Before Tax (FRS 3)	79.6	58.4	63.2	54.3
Tax	(7.9)	(10.5)	(12.7)	(11.1)
Profit After Tax (norm)	53.3	57.9	55.5	54.5
Profit After Tax (FRS 3)	71.7	47.9	50.4	43.2
Average Number of Shares Outstanding (m)	396.4	397.3	393.2	386.9
EPS	13.4	14.6	14.1	14.1
EPS - normalised fully diluted (p)	13.13	14.14	13.70	13.65
EPS - (IFRS) (p)	18.1	12.1	12.8	11.2
Dividend per share (p)	3.6	3.9	4.1	4.2
Gross Margin (%)	11.0	10.7	10.5	10.5
EBITDA Margin (%)	2.4	2.2	2.2	2.1
Operating Margin (before GW and except.) (%)	2.0	1.8	1.7	1.7
BALANCE SHEET				
Fixed Assets	536.5	563.2	572.6	596.1
Intangible Assets	217.4	221.2	220.5	219.8
Tangible Assets	319.1	342.0	352.2	376.3
Investments	0.0	0.0	0.0	0.0
Current Assets	1,171.3	1,332.4	1,344.8	1,345.9
Stocks	839.4	984.1	967.1	945.6
Debtors	292.1	303.0	322.4	325.1
Cash	39.8	45.3	55.3	75.3
Other	0.0	0.0	0.0	0.0
Current Liabilities	(1,130.3)	(1,294.2)	(1,251.8)	(1,236.5)
Creditors	(1,105.2)	(1,228.1)	(1,251.8)	(1,236.5)
Short term borrowings	(25.1)	(66.1)	0.0	0.0
Long Term Liabilities	(235.8)	(216.4)	(263.6)	(276.4)
Long term borrowings	(88.8)	(77.0)	(122.0)	(132.6)
Other long term liabilities	(147.0)	(139.4)	(141.6)	(143.8)
Net Assets	341.7	385.0	402.0	429.1
CASH FLOW				
Operating Cash Flow	130.5	65.9	121.9	102.7
Net Interest	(13.8)	(17.6)	(16.3)	(16.6)
Tax	(17.3)	(10.5)	(12.7)	(11.1)
Capex	(45.5)	(54.2)	(51.0)	(49.6)
Acquisitions/disposals	18.9	0.0	0.0	0.0
Financing	0.0	0.0	(10.0)	0.0
Dividends	(13.2)	(15.0)	(15.7)	(16.1)
Other	28.0	7.7	15.0	0.0
Net Cash Flow	87.6	(23.7)	31.1	9.4
Opening net debt/(cash)	161.7	74.1	97.8	66.7
HP finance leases initiated	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Closing net debt/(cash)	74.1	97.8	66.7	57.3

Source: Company reports, Edison Investment Research estimates

Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
295 Madison Avenue, 18th Floor
10017, New York
US

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia