GROUP 1 AUTOMOTIVE

Driving Value in an Inflated Market

June 24, 2015

VALUE x VAIL

MOON CAPITAL MANAGEMENT

Group 1 Automotive

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Ticker: GPI
Stock Price: $82.53 *

- Group 1 owns and operates auto dealerships
  - Third largest dealership group in the U.S. retailing 275,000 new and used vehicles annually
  - 104 US dealerships, 17 UK dealerships, 17 Brazil dealerships
  - Market capitalization of $2.0 billion

- Recent valuation multiples
  - ’15e P/E: 11.5x

* All financials assume June 1, 2015 share price of $82.53

Local Monopolies

- Dealers provided a great deal of protection in different states (receive long-term operating agreements because they are independently owned and capitalized)
- Franchise agreements provide geographic exclusivity in densely populated areas
- Law requires that the sales channel for new cars must be directed through the dealer network
- Manufacture paid maintenance service required to be completed at dealership
- Expensive OEM specific tools and diagnostics provide barriers to entry for service techs at independent shops

Economic Moat

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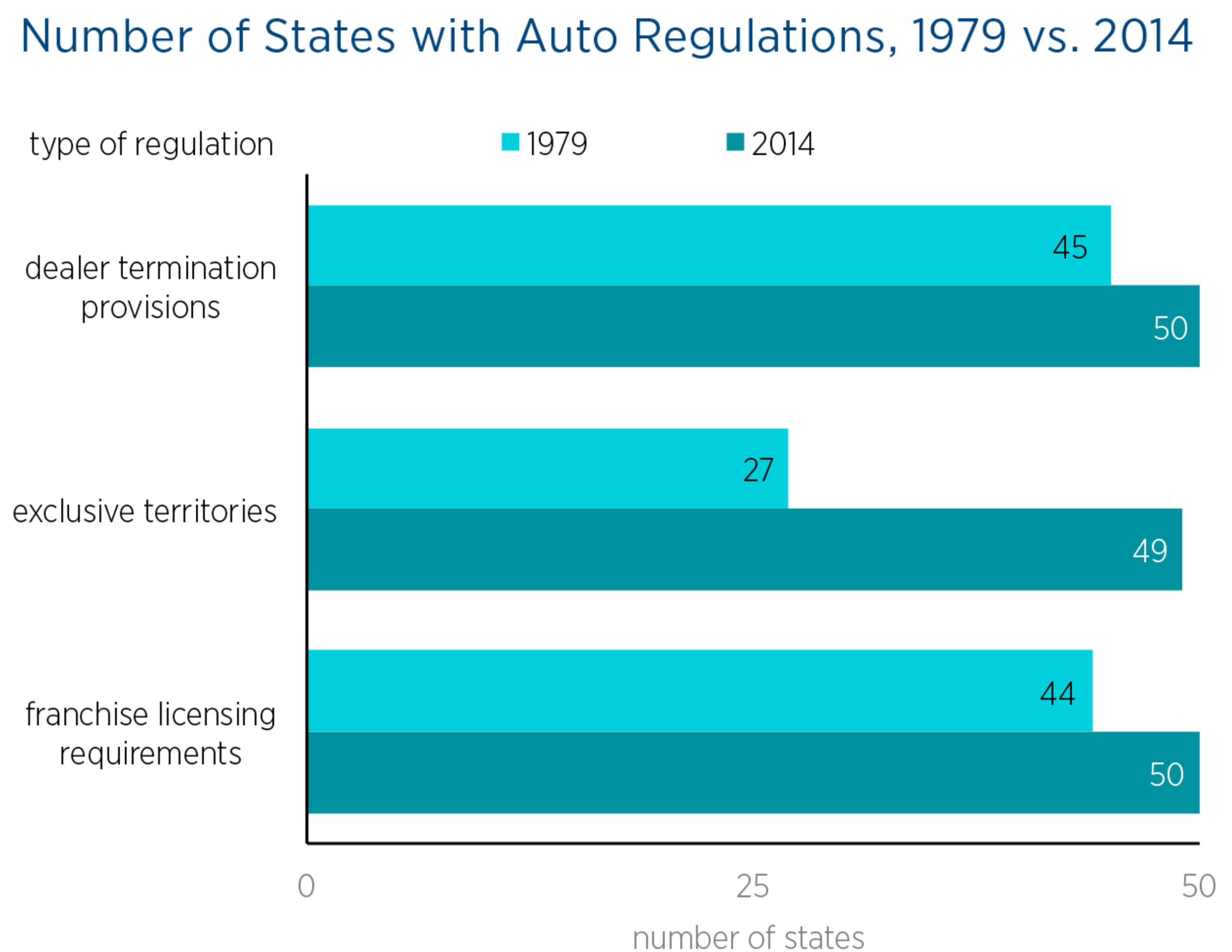


Deceptively High-Quality Business

- Inventory is financed through vehicle floorplan notes payable from various OEMs
  - Notes accrue like other types of borrowing, but OEMs extend "floorplan assistance" to offset the expense
  - Little inventory risk as the OEMs provide retailers with significant incentives to move inventory and dealers are often *paid to carry*
- Dealership decline has improved the competitive environment
  - Dealers down 20% over the past seven years
  - GM allowed to rationalize its dealer network during bankruptcy (cut network by 30%)

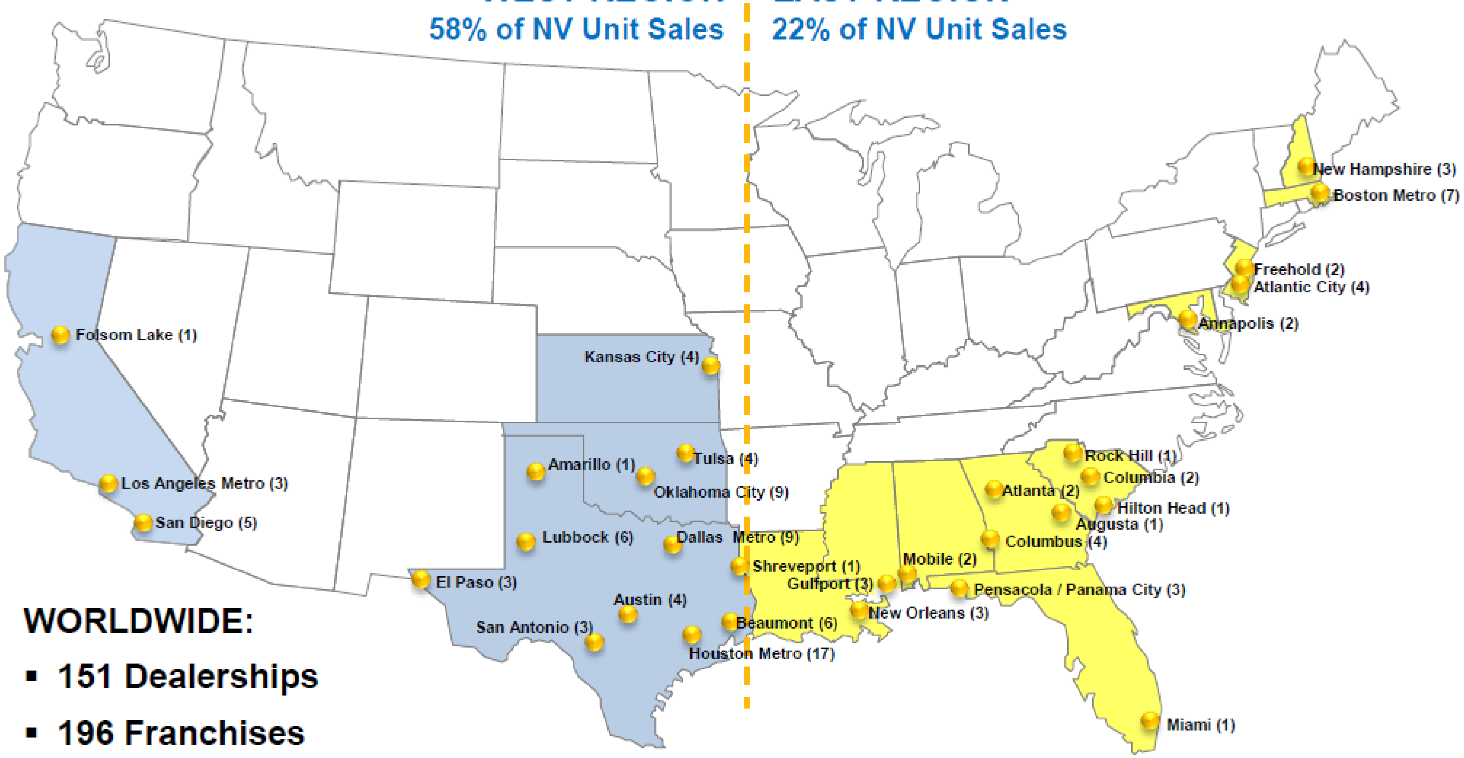
Strong National Footprint

UNITED STATES – 14 States

117 Dealerships

WEST REGION
58% of NV Unit Sales

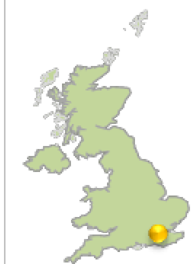
EAST REGION
22% of NV Unit Sales



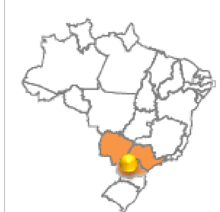
WORLDWIDE:

- 151 Dealerships
- 196 Franchises
- 38 Collision Centers
- 32 Brands

U.K.
England:
- 17 Dealerships
- 12% of NV Unit Sales



BRAZIL
Mato Grosso do Sul, Sao Paulo & Parana:
- 17 Dealerships
- 8% of NV Unit Sales



Business Mix

- New Vehicle- 54% of sales, 20% of gross profit
  - Roughly $1,850 in gross profit per vehicle, with certain luxury vehicles bringing in more than twice this amount.
  - These per car margins are lower than historical norms
- Used Vehicle- 30% of sales, 13% of gross profit
  - Roughly $1,600 in gross profit per vehicle
  - Unwanted cars sold at breakeven into the wholesale market
- Finance & Insurance- 4% of sales, 26% of gross profit
  - Fees and spreads on car loans and leases
  - Purely a fee-based earnings stream for arranging third-party financing, insurance, etc.
- Parts & Service- 12% of sales, 41% of gross profit
  - The real profit center of the dealership

Finance & Insurance

- Pure margin business– GPI receives roughly $1,350 per unit for arranging financing, service, and insurance contracts
  - **Financing:** 1/3 of F&I ($450) comes in the form of flat fees or financing spreads paid to arrange a loan
  - **Vehicle Warranty and Protection:** 2/3 of F&I comes from fees earned from selling third-party extended warranty, vehicle service, and insurance products

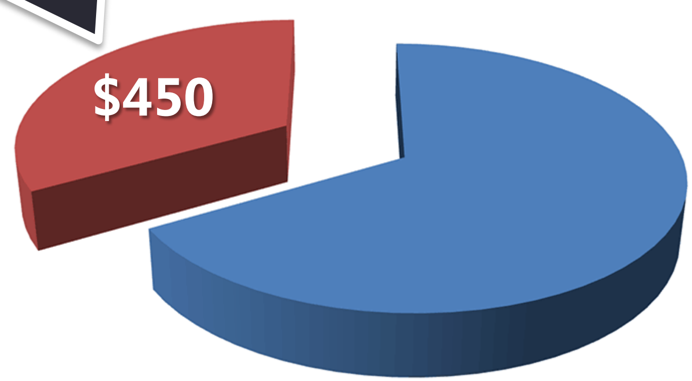
Financing

Buyer qualifies for a lender offered 3.5% 60-month amortizing loan

Dealership tells the buyer that 5.5% is the best available rate

The difference between the buy rate and the dealer rate known as the **yield spread premium** is calculated and capitalized

The dealer receives the majority of this markup as a kick-back from the lender



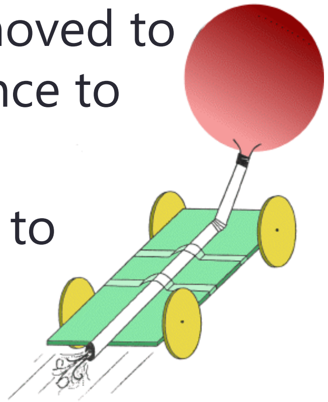
CFPB- Headline Risk

The **Consumer Financial Protection Bureau** believes dealer discretion in setting interest rates can potentially lead to discrimination in the form of higher prices for certain groups

Implication: The extremely profitable F&I segment for auto dealers is set to be impacted.

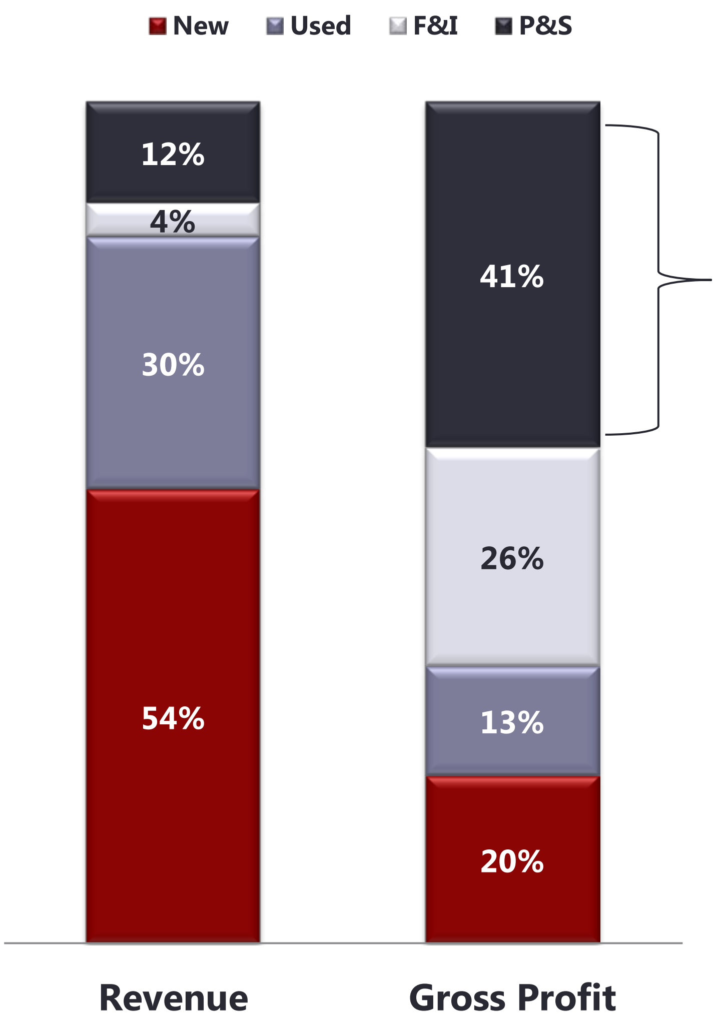
CFPB- Headline Risk

- The CFPB's intent is to monitor discrimination practices not set pricing—the ***CFPB agrees that dealers should be compensated for processing financing***
- Any impact is ***limited to financing***—dealer markups represent 1/3 or less of F&I income
- The expectation is that lenders will be forced to move from dealer reserves (interest rate markups) to flat fees
- Certain lenders including BMO Harris Bank in Chicago have moved to flat fees (3% of finance amount) with no change of consequence to dealer economics
- Dealer economics are unlikely to change as they will continue to choose which lenders get the financing business



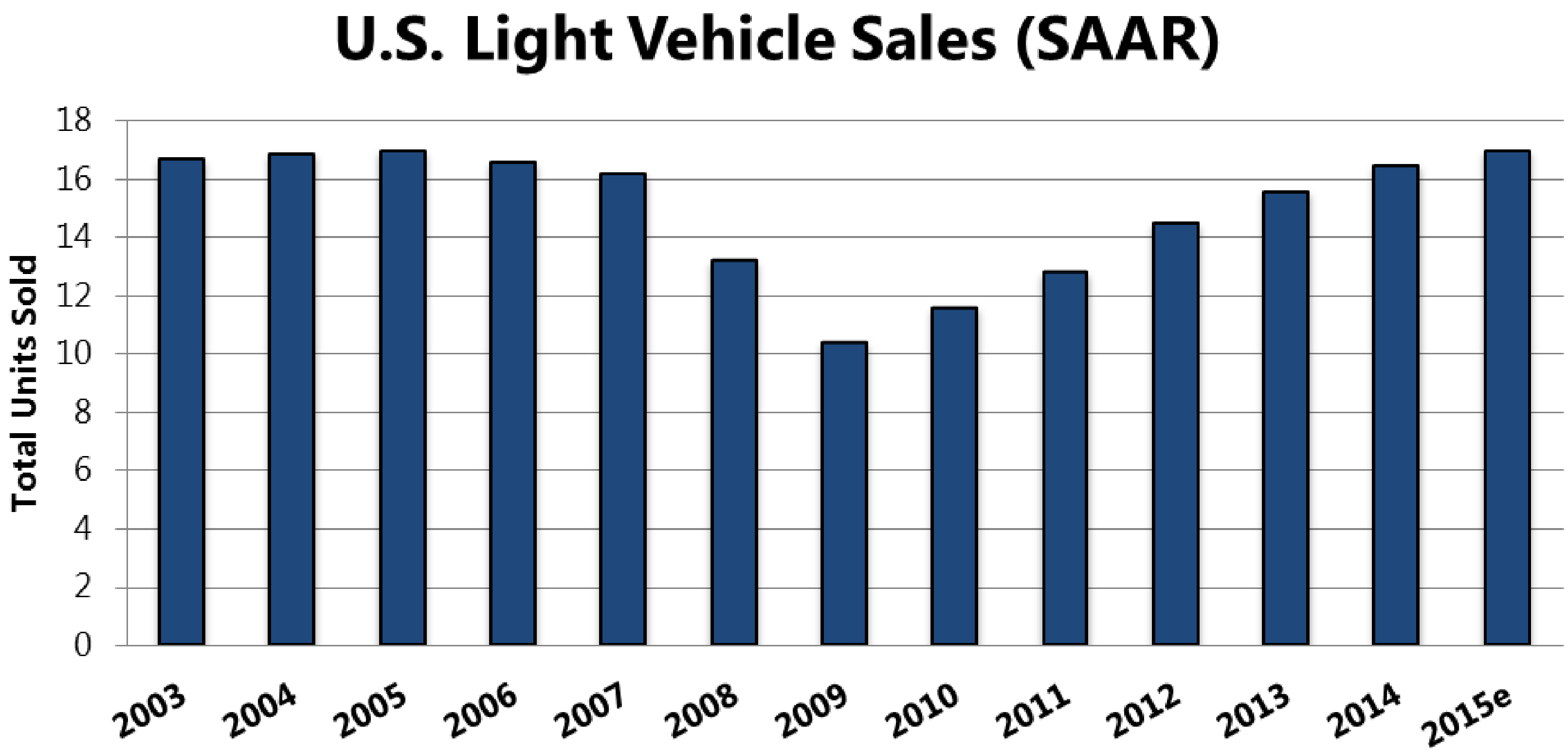
"Spread and yield is like a balloon in our mind, you can push in one place and it will expand in another place" - Craig Monaghan CEO Asbury Automotive

Parts & Service (The Real Profit Driver)



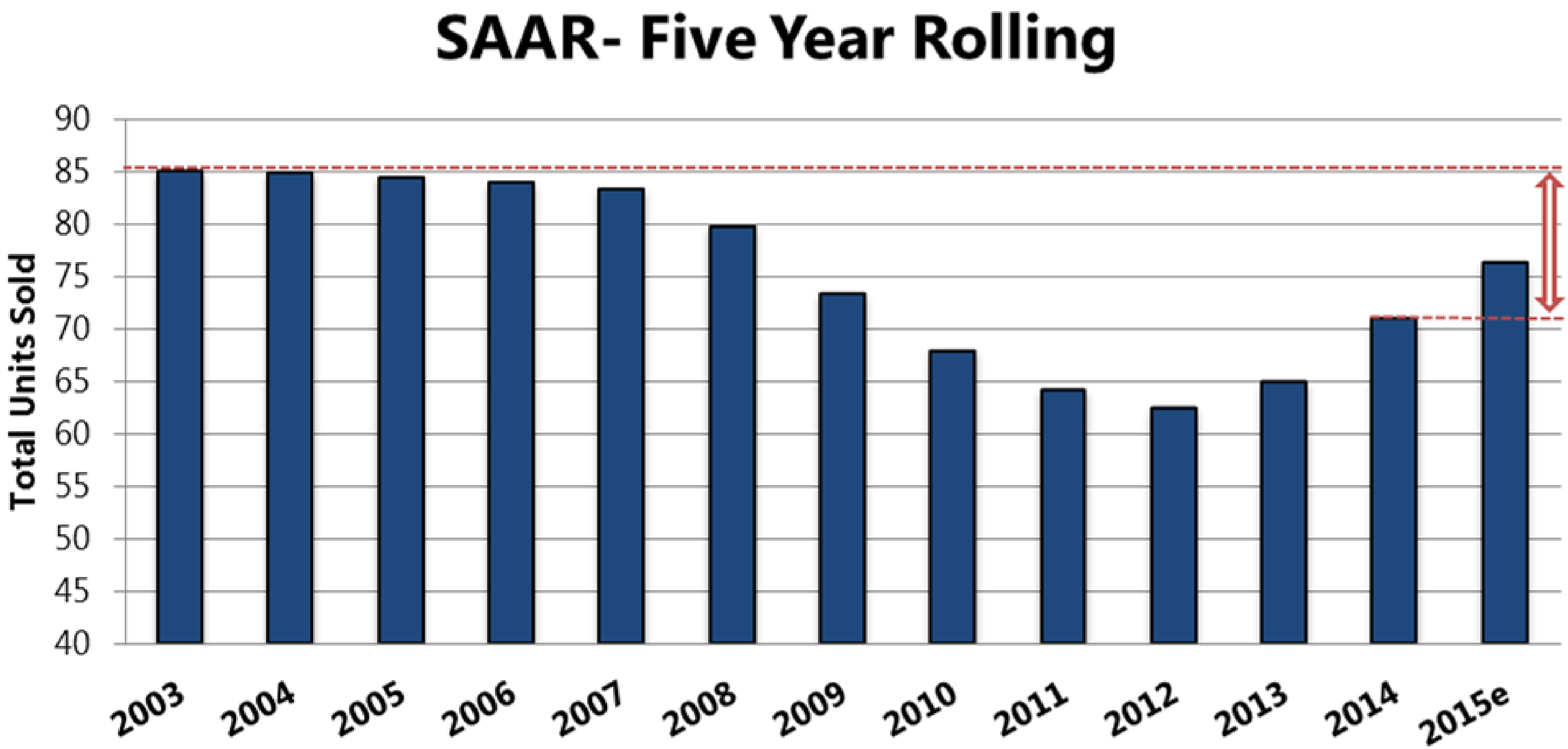
- Gross margins run at 52% (half is service at 70-80% margin, half is parts at 35% margin)
- Trends in manufacture-paid maintenance have improved economics for dealers—since service is free to customers, the dealer retains the entire service stream
- Customers may look outside hometown for a new car purchase, but they are a captive customer for car servicing
- Price & Servicing is driven by the servicing base (0-5 year fleet)

Near-Term Catalysts: SAAR Rebound



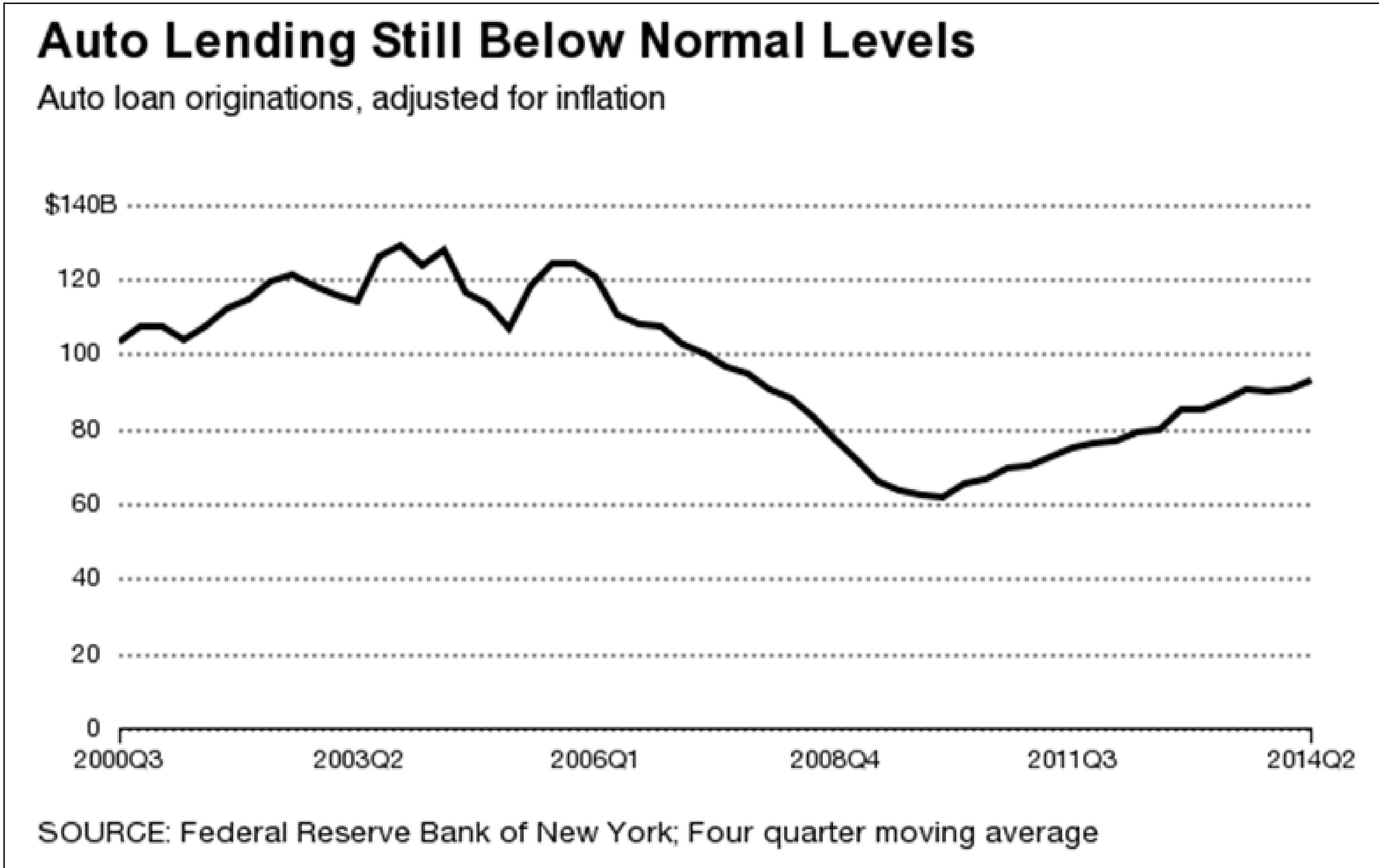
US auto sales have now fully recovered from the last financial crisis

Auto Recovery Tailwind



Parts & service sales base of 0-5 year old vehicles is still more than 15% below its pre-2008 average, providing a mult-year tailwind for the business

Auto Lending—Is there a Bubble?



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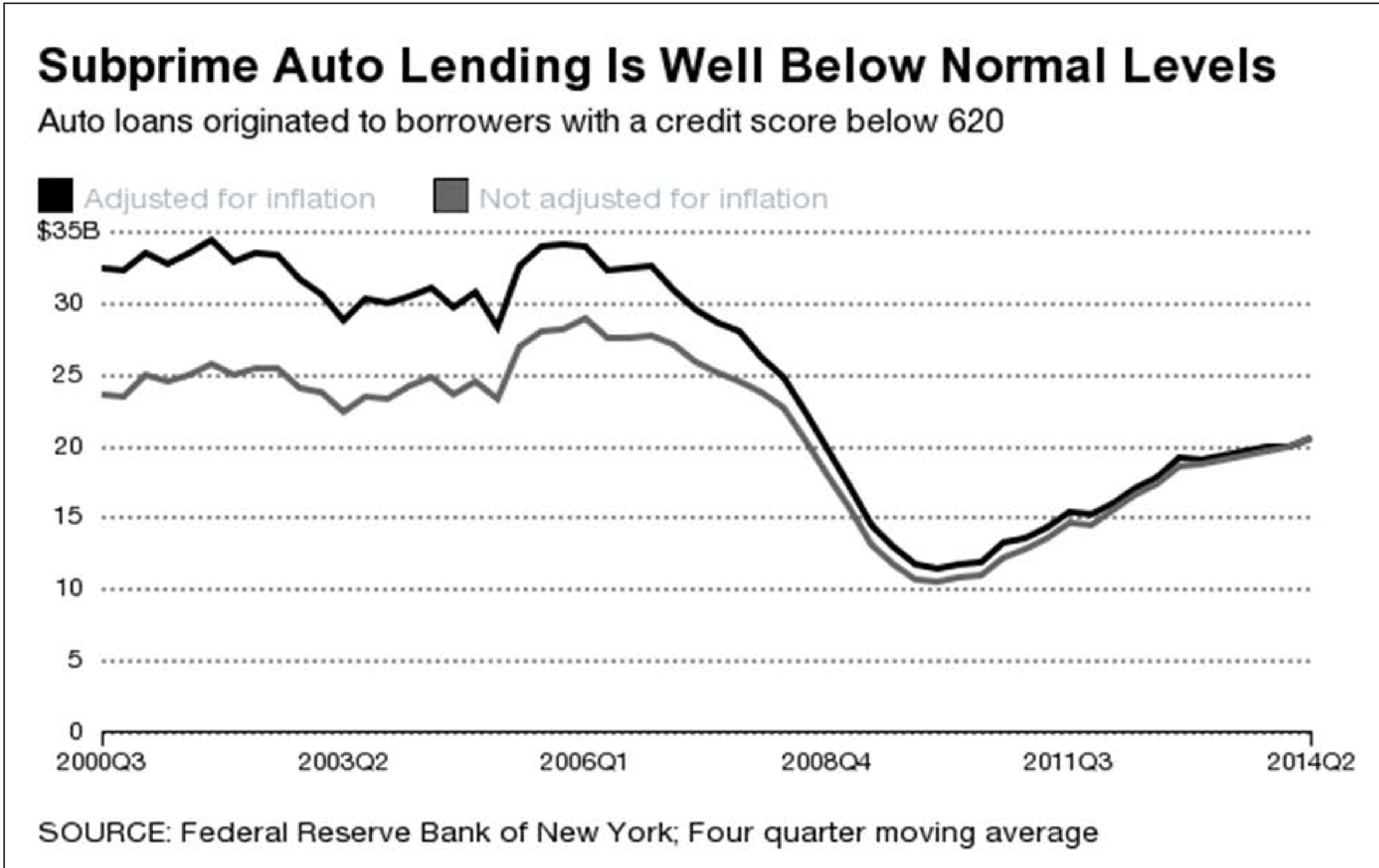
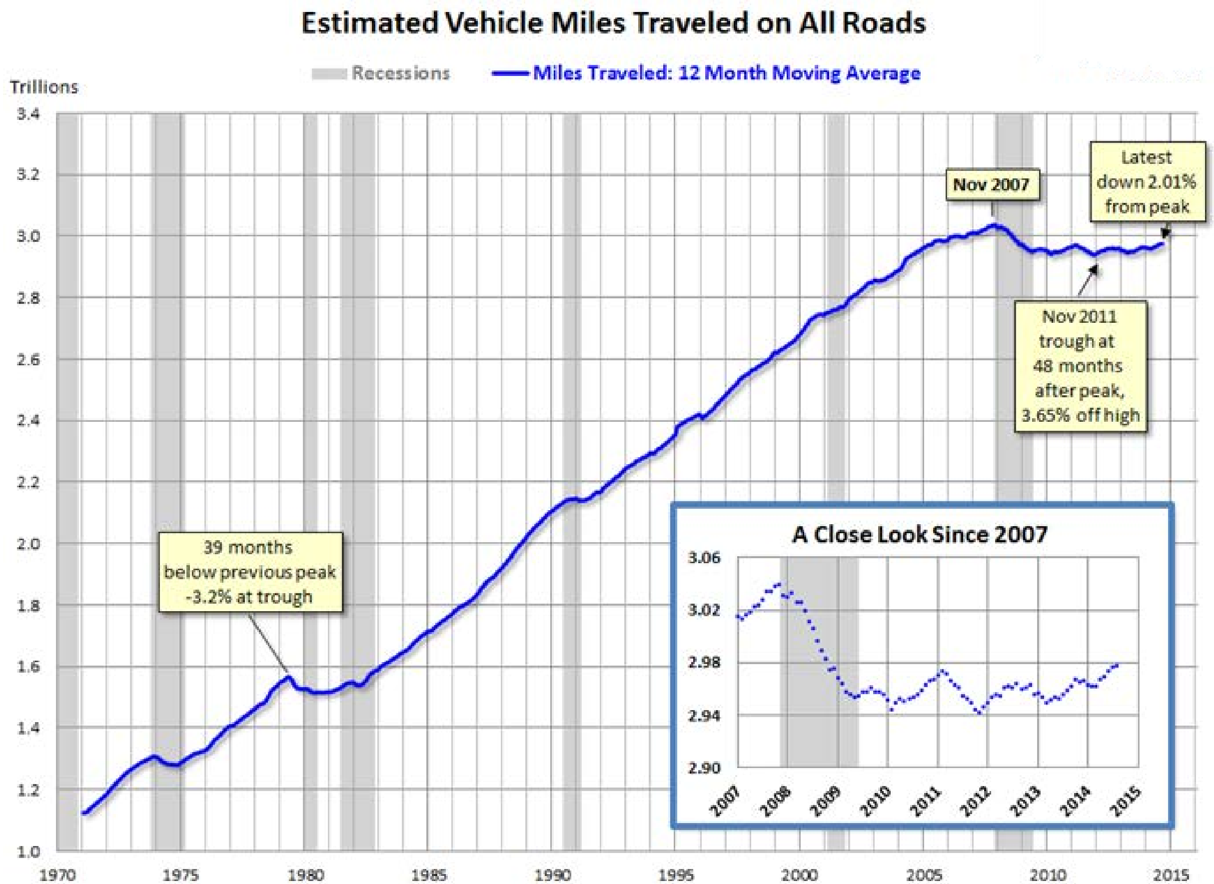


Normalized SAAR



Total vehicles miles traveled remains remarkably steady and suggests a replacement rate similar to the early 2000's

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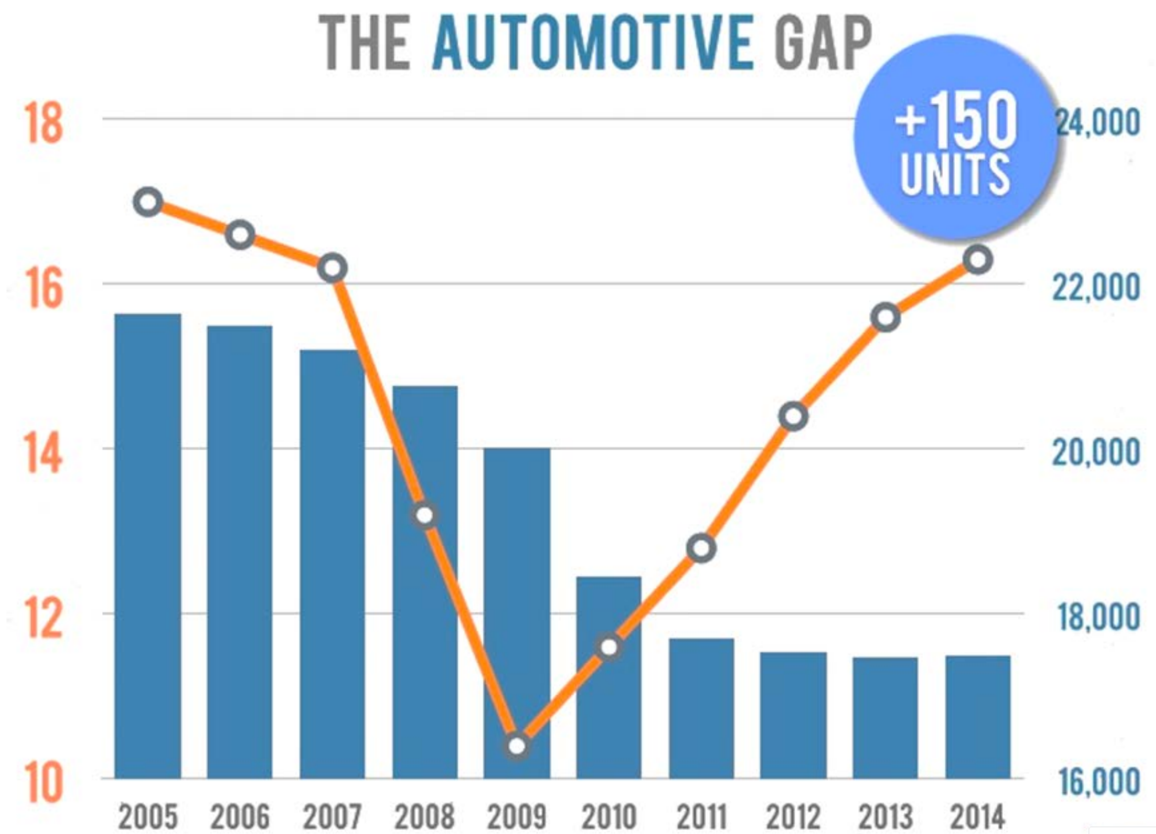
Normalized SAAR

Replacement SAAR		
Annual miles driven (in millions)	3,000,000	(3 trillion)
Average vehicle scrap mileage	180,000	(includes totalled vehicles)
Implied average life	14.4	years
Normalized replacement demand	**16.7**	**million cars**
Current fleet size	250	million cars
Mileage consumption	12,500	yearly miles per car
Average fleet age	11.4	years

The Automotive Gap



Then (2008)		Now (2015)	
Total Dealerships	20,000+	Total Dealerships	16,400
New Vehicle Sales	16,000,000	New Vehicle Sales	16,000,000
Units Per Dealer	**800**	**Units Per Dealer**	**976**

GPI Acquisition Strategy

- Over the past five years, GPI has purchased 89 franchises with expected annual revenues of $3.6 billion
- Purchase dealerships at 15-20% of revenues (excluding real estate and floorplan liabilities)
- Increase operating efficiency in areas such as used vehicle sourcing, advertising, purchasing, data processing, personnel utilization, and cost of floorplan financing
- Improving pre-tax margins to 2.5% results in an unlevered return of 10%
- Target 15% returns on acquisitions

Less than 10% of US dealerships are held by publicly traded companies, leaving a huge opportunity for dealership consolidation

Comparables

Comparables					
Company Name	**Enterprise Value To EBITDA**	**EBITDA Margin (3-Year Average)**	**EBITDA Growth**	**Price/ Earnings**	**Total Debt to EBITDA**
Group 1 Automotive	7.9	3.7%	22.5%	11.5	6.2
AutoNation	9.9	4.7%	11.1%	17.8	5.6
Carmax	10.0	5.1%	19.9%	26.2	8.6
Asbury Automotive Group	10.6	4.7%	17.7%	18.0	5.0
Pensky Automotive Group	10.6	3.3%	16.7%	15.1	7.1
Sonic Automotive	6.9	3.4%	1.3%	13.3	6.8

Valuation

	2012	2013	2014	2015	2016	2017
Revenue	**$ 7,476,100**	**$ 8,918,581**	**$ 9,937,889**	**$ 10,387,363**	**$ 10,857,889**	**$ 11,267,050**
Cost of Sales	**$ 6,358,848**	**$ 7,626,035**	**$ 8,489,951**	**$ 8,871,099**	**$ 9,271,204**	**$ 9,619,675**
Gross Margin	**$ 1,117,252**	**$ 1,292,546**	**$ 1,447,938**	**$ 1,516,265**	**$ 1,586,685**	**$ 1,647,375**
	14.94%	14.49%	14.57%	14.60%	14.61%	14.62%
Same Store Sales Growth	13.7%	6.2%	5.6%	4.5%	4.5%	3.8%
Total Expenses	**879,980**	**1,012,752**	**1,104,308**	**1,167,524**	**1,221,747**	**1,268,479**
Tax %	25.5%	27.8%	23.6%	25.0%	25.0%	25.0%
EPS	**$ 4.53**	**$ 4.96**	**$ 5.87**	**$ 7.05**	**$ 7.48**	**$ 7.85**
(+) Improved of Brazilian Ops				0.05	0.25	0.50
(+) Addt. Acquisition Accetion				0.42	0.84	1.26
PF Cash EPS				**$ 7.52**	**$ 8.57**	**$ 9.61**
P/E Multiple				**15.0x**	**15.0x**	**15.0x**
Value Per Share				**$ 112.86**	**$ 128.61**	**$ 144.20**
(+) Cumulative Dividend				0.60	1.40	2.20
Adj. Value Per Share				**$ 113.46**	**$ 130.01**	**$ 146.40**
% Premium to Current				**37%**	**58%**	**77%**

Group 1 trades at 12x earnings, a substantial discount to the current market multiple

Conclusion

Competition for Existing Units	Local Monopoly
Barriers to Entry	High
Maintenance CAPEX	.2% of Revenue
Returns on Capital	High

Group 1 is a high quality business selling at a significant discount to intrinsic value

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