Truist Dealer Insider

The Automotive Retail Newsletter

Volume 1, Winter 2021

BB&T | SunTrust
Now Truist

Truist Securities

Welcome to the Truist Dealer Insider

Dear Friends,

Undoubtedly, 2020 was an unprecedented year on many levels. There aren't enough words to describe the events that have shaped our lives and businesses during these past months. The adage, "the more things change, the more things stay the same," has proven its wisdom once again. Throughout this cycle, auto dealers have demonstrated their resiliency and effectiveness at embracing economic and societal disruption. They are leading the U.S. economy into another era of potential prosperity despite headwinds never before encountered. The ongoing efforts and admirable results being generated by auto retailers is why our automotive team at Truist believe that U.S. car dealers are the fabric of American entrepreneurialism. They deserve our thanks and encouragement.

You are reading the inaugural issue of a publication we hope will become a valued resource you look forward to receiving. The Truist Dealer Insider will provide auto retail industry stakeholders reliable market information, contemporary updates to the M&A and lending environments, and views from professionals and other entrepreneurs who are influencing the future of auto retail. The continued focus will be to provide you with timely information that you can trust and use in developing strategies and tactics to make your businesses more valuable.

A benefit of having the resources of one of the largest commercial banks (Truist), and a full-service investment bank (Truist Securities), is the large volume of dealership transactions that we are involved in on an ongoing basis. The auto team at Truist Securities has taken years' worth of transaction data, a survey of 1,200 dealership owners and public information regarding dealership transactions to develop a robust confidential database of deal information called the Truist Blue Sky Index (page 9). We then compiled the data and produced thoughtful analysis on what buyers are paying for car dealerships, how dealers value brands when pursuing acquisitions, and the capital structures employed to consummate the transactions. We have identified desirable franchises and geographies currently being pursued by growth-minded dealers. You can count on us to update the Truist Blue Sky Index regularly and we'll do our best to make it relatable to the marketplace.

Inside you will also find content from dealers, legal experts, auto tech company founders, commercial and consumer lending leaders, marketing professionals, and financial advisors that will give you a contemporary viewpoint on issues facing the industry today and tomorrow. We hope you enjoy this first issue of the Truist Dealer Insider, and we look forward to bringing you more insightful content throughout the year.

JT Taylor*
Head of Automotive
Truist Securities

David Stevens
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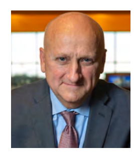
Dealer Commercial Services



Bill Jones
Head of Truist
Dealer Retail Services

Denotes licensed with FINRA

We are Truist Financial Corporation

Closed merger of equals between BB&T and SunTrust on December 6, 2019

275+ combined years of serving our clients and communities

$500 billion in assets

Headquartered in Charlotte, N.C.

Serving automotive dealers with focus and commitment

- ~$15 billion of capital committed to dealers
- 500+ commercial dealer clients and 15,000+ retail dealer clients
- Dedicated resources to support dealers throughout their entrepreneurial lifecycle, including automotive retail investment banking through Truist Securities, dealer commercial and retail services, business transitions advisory, and insurance and risk management

Inside this issue

2020 Dealership M&A and Valuation Overview

Recent noteworthy deals in automotive retail M&A

Lithia Motors, Inc. acquires Sterling

- **Announced:** November 18, 2020
- **Transaction value:** Undisclosed

"Sterling Motorcars is a high-performing fixture in the Washington D.C./Beltway corridor and is well-respected for the exceptional customer service and attention to detail they provide their clientele. This is a very important milestone for Lithia and expands our national footprint in the mid-Atlantic."

– Lithia CEO Bryan DeBoer

Recent transactions

Date	Target	Headquarters
Dec-20	Ramsey Subaru & Mazda	Des Moines, IA
Nov-20	Keyes Automotive	Los Angeles, CA
Oct-20	Latham Ford	Latham, NY

Observations and takeaways

- Dense populations and a remarkable per capita income make Northern Virginia a high demand area
  - Acquisition in the Mid-Atlantic region is geographically strategic for Lithia, with Sterling's location residing in a Top 10 metropolitan area in the U.S.
  - Sterling's brands include BMW, MINI, Rolls-Royce, Lamborghini and McLaren, with the latter 3 introducing exotic brands to Lithia's portfolio
- Lithia expects the new dealerships to add $225MM in annual sales
- Founded in 2001, Sterling is headquartered in Loudoun County, VA

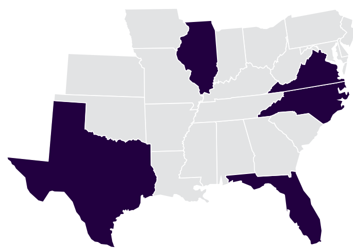
Acamar Partners to acquire carlotz

- **Announced:** October 22, 2020
- **Proceeds:** $321MM
- **Pending Investors:** Fidelity, KAR Auction Services, McLarty Diversified Holdings
- **Sponsor:** TRP Capital Partners

"On top of this great combination of attractive market dynamics and a differentiated business model, CarLotz benefits from multiple short and long-term growth opportunities driven by its ongoing nationwide expansion."

– Acamar Partners CEO Luis Solorzano

Geographies supported



CarLotz currently has eight locations, mostly concentrated in the Mid-Atlantic; competitors Vroom and Shift, recent public filers in the space, operate in TX and CA, respectively.

Observations and takeaways

- Focus on technology has allowed CarLotz to decrease inventory needs and sell vehicles direct-to-consumer, similar to a consignment versus retail
- Thesis for explosive growth in the coming years
  - Purchase price of $827MM represents 7.5x and 0.9x 2020E and 2022E revenue, respectively
  - Transaction proceeds to fully fund additional investment in technology and distribution hubs nationwide
- The deal is expected to close in early 2021 and represents the exit opportunity for TRP Capital Partners who initially invested in the company in 2017
- Founded in 2011, the company is headquartered in Richmond, VA.

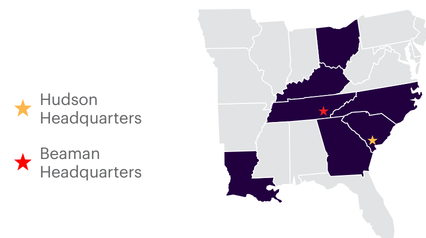
Hudson Automotive acquires Beaman Automotive Group

- **Announced:** July 30, 2020
- **Transaction value:** Undisclosed
- **Sponsor:** Redwood Capital Investments

"Nashville is booming right now so we were excited to expand our footprint in middle Tennessee with great brands. Beaman Auto Group has been an institution in Nashville for 75 years and we're delighted to add it to our group."

– Hudson President David Hudson

Geographic overlap



Transaction included 4 dealerships in TN, with brands including Toyota, Buick-GMC, CDJR, Fiat and Ford, as well as a parts warehouse and collision center.

Observations and takeaways

- Deal closed in November 2020 and epitomizes growing trends for owners to exit due to absences of succession and legacy
- Beaman Automotive generated $414MM in revenue last year and represents Hudson's 7th dealership in the Nashville area
- Hudson has seen tremendous expansion since it was backed by Redwood Capital in 2018
  - Acquired a Honda and Chevrolet dealership in February and June of 2020, in addition to 6 other dealerships
  - Upon closing of the transaction, Hudson will become a leading retailer in the Southeast, with 31 dealerships
- Founded in 1955, Beaman is headquartered in Nashville, TN

Source: Capital IQ, Industry News

Overview of automotive dealership M&A activity

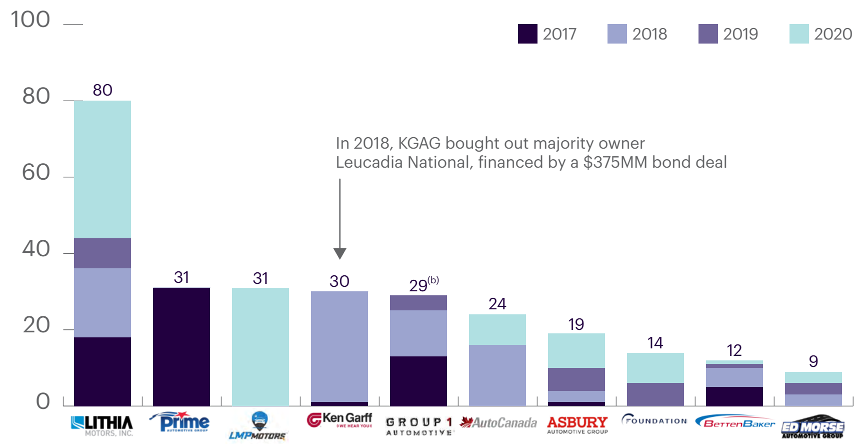
M&A commentary

- Number of annual transactions has trended higher in recent years, with 2020's transactional pace on par with the previous year
- Dealership buy-sell activity rebounded after 1Q20, with 1H20 transactions on par with 1H19 and accelerating through the year-end
- Dealership profitability significantly outperformed expectations through the downturn – leading many potential buyers to re-engage toward the end of May
  - Lithia has continued its acquisition plans, closing on 24 stores since September
  - During July, Asbury Automotive returned to the negotiating table, revising its offer in March to acquire certain assets of Park Place Dealerships
- Outside investors are expressing increased interest in automotive dealerships, but remain cautious with respect to economic uncertainty

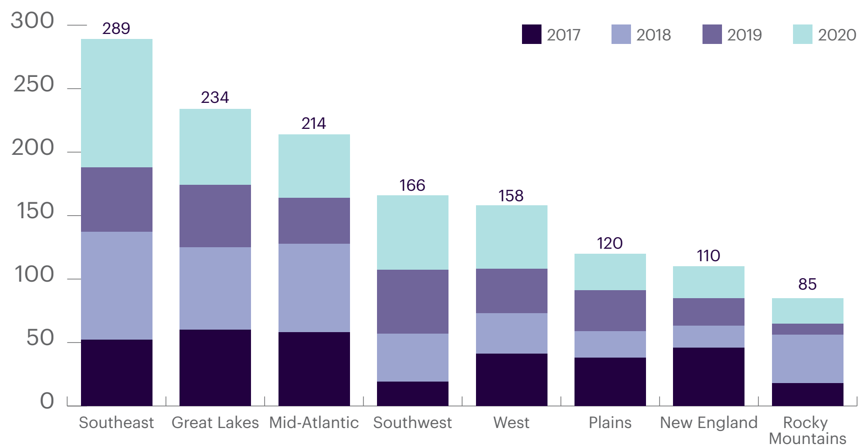
"Larger dealerships generally post profit far higher and more stable than smaller operators. Increased profit and advantageous cost structures will likely propel additional growth of large dealer groups because they can spread fixed costs over many dealerships and can centrally coordinate marketing, purchasing and labor activities, which reduces expenses. While consolidation continues, though, the industry will likely remain highly fragmented, as small, localized players will likely continue to dominate the industry."

– IBIS World, August 2020

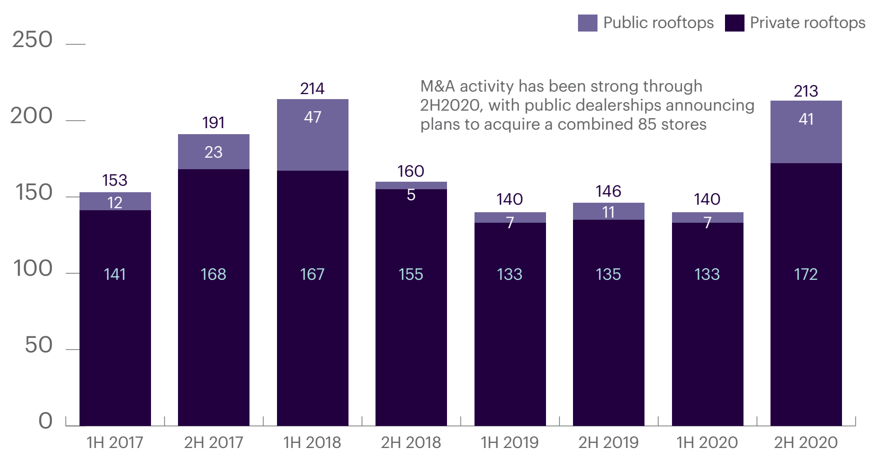
Most active acquirers[a]



M&A activity by region[a]



Historical private / public M&A activity



Source: The Banks Report, Industry News; (a) Includes announced transactions in addition to closed transactions (b) Includes 20 international acquisitions
Note: Chart figures account for the number of rooftops acquired.

Summary of recent transactions in the auto dealership space

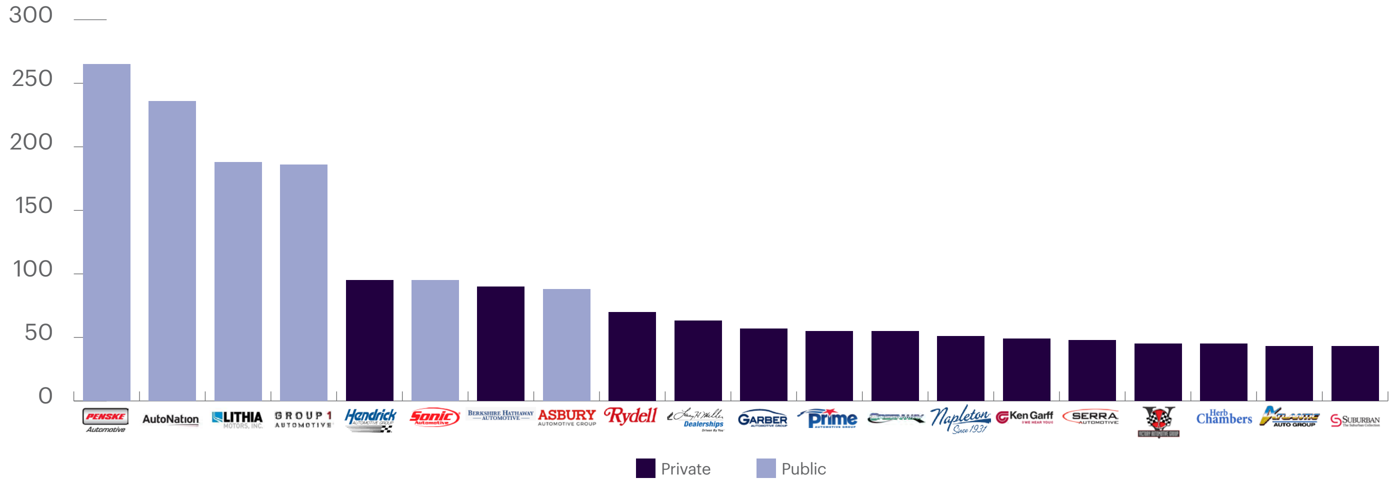
Announced date	Acquirer	Target	Region	TEV ($mm)	Target stores	Transaction commentary
12/15/20	Redwood Automotive	Pendragon (PDG)	West	$22	1	Pendragon has agreed to sell the assets of its Jaguar and Land Rover motor vehicle dealership located in Santa Monica, California, to Redwood Automotive for around $22MM
12/1/20	Lithia Motors	Ramsey Subaru & Mazda	Plains	-	2	Lithia Motors acquired Ramsey Subaru & Mazda in Iowa. The dealership is expected to add $225MM to Lithia's annual sales, totaling $3.5BN during YTD November of 2020
12/1/20	AutoCanada	Haldimand Motors	Canada	-	8	AutoCanada acquired Haldimand Motors, a used car retailer based in Ontario. The acquired operations will be at the center of AutoCanada's new initiative, Used Digital Retail Division
11/18/20	Lithia Motors	Sterling Motorcars	Southeast	-	5	Lithia Motors acquired Sterling Motorcars based in Virginia. The new dealership marks Lithia's entry into the Mid-Atlantic region. The dealership is expected to add $225MM to Lithia's annual sales
11/12/20	Victory Automotive Group	Midtown Toyota (Resnick Auto Group)	Great Lakes	-	1	Victory Auto further expands into California with the announced acquisition of Midtown Toyota from Resnick Auto Group. The acquisition puts the Michigan-based retailer at 26 franchises
11/10/20	Lithia Motors	Keyes Automotive Group	Southwest	-	9	Lithia Motors acquired a total of 9 dealerships from Keyes automotive group, expanding the Company's presence in Los Angeles and Phoenix. The new dealerships under Lithia's ownership will add $1.4BN of annualized revenue
10/21/20	Acamar Partners (ACAM)	CarLotz (LOTZ)	-	827	8	CarLotz is going public through a merger with a special-purpose acquisition company. CarLotz will be the 3rd largest national online retailer after Vroom and Shift Technologies. Unlike its peers who buy and sell used cars, CarLotz operates a consignment store
10/13/20	Lehman Autoworld	Largo Honda	Southeast	17	1	Lehman Autoworld acquired Largo Honda, a South Florida retailer. Lehman also operates brands including Hyundai, Subaru, Mitsubishi, Buick, GMC, Genesis and Kia
10/9/20	LMP Automotive	Atlantic Automotive Group & Atlantic Central Storage	Mid-Atlantic	608	17	LMP Automotive announced its acquisition of 70% interest of Atlantic Automotive Group and its vehicle storage company, Atlantic Central Storage. The closing of LMP's pending acquisitions will put the retailer at 33 franchises
10/6/20	Gossett Motor Cars Dealership Group	Infiniti of Memphis	Southeast	-	1	Gossett Motor Cars, a Memphis-based dealership group, acquired Infiniti of Memphis. The acquisition extends Gossett's positioning as one of the largest automotive groups in the Mid-South region
10/5/20	Lithia Motors	Latham Ford	Mid-Atlantic	-	1	Lithia Motors expands its portfolio through its acquisition of Latham Ford based in New York. Latham Ford is expected to contribute $55MM in annual sales to the combined company
10/2/20	ZT Motors	Ron Carter Autoland	Southwest	-	3	ZT Motors, a Texas-based retailer with dealerships in Atlanta and Florida and backed by private equity firm ZT Corporate, acquired Ron Carter Autoland. The locations are being divested by GPB Capital. The acquisition expands ZT Motors' presence in Texas
9/22/20	Lithia Motors	Jim Cogdill CDJR	Southeast	-	1	Lithia Motors acquired Jim Cogdill CJDR, marking the Company's first dealership in Tennessee. The new dealerships include Chrysler, Dodge, Jeep and Ram brands, and is expected to contribute $90MM to Lithia's annual sales
9/11/20	Elway Dealership Group & Schomp Automotive Group	Strong Auto Group (Porsche Dealership)	Rocky Mountains	-	1	Elway Dealership Group & Schomp Automotive Group acquired Porsche Salt Lake City from Strong Automotive Group. The deal gives Elway Dealership entry into the high-end luxury space
9/7/20	Triunity Automotive Group	Pendragon (LSE:PDG) JLR Dealership	West	21	1	Triunity Automotive Group acquired the JLR dealerships located in California from Pendragon, a U.K. retailer. Pendragon is restructuring due to heavy losses in 2019. Pendragon is targeting a "fulfilment hub" model for its remaining locations
9/3/20	LMP Automotive	Fuccillo Kia Dealerships	Southeast	69	2	LMP Automotive announced its acquisition of 2 Florida-based Kia dealerships from Fuccillo Automotive. Fuccillo is one of New York's largest dealers and continues to operate 3 Nissan dealerships in Florida

Source: Industry News

Consolidation in the automotive retail space

Landscape remains eventful for industry consolidation with only 10% of dealerships operated by the 20 largest groups

Top 20 dealership platforms by store count

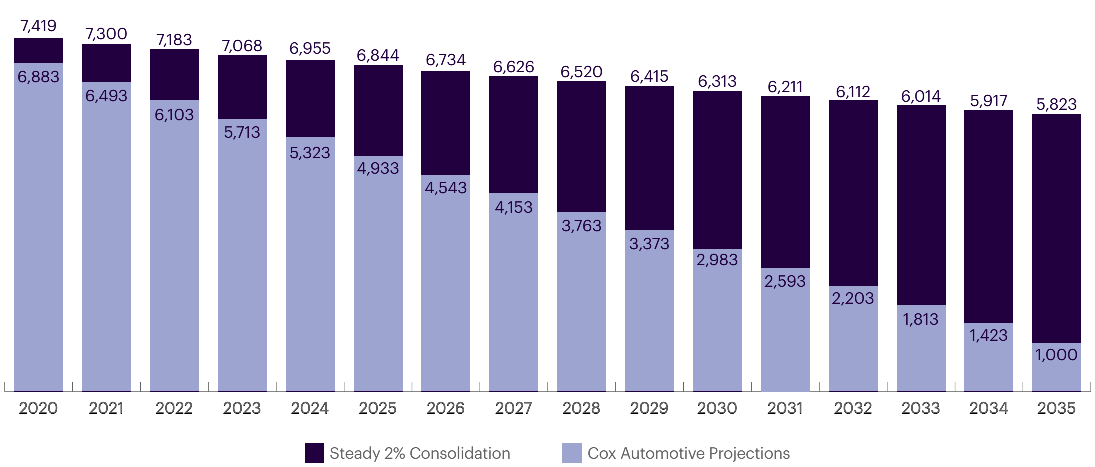


Industry commentary

Automotive retail remains a fragmented industry, with the top 20 dealership platforms accounting for only ~10% of the 18,000+ dealership locations, fueling an expectation for abundant "grow or go" strategic opportunities. Consolidation trends within the industry will continue as groups look to pursue growth through acquisitions and outside investors begin to deploy currently-sidelined capital, seeking both minority & majority positions in strong dealership acquisition platforms. The number of dealership owners has historically consolidated at a rate of nearly 2.0%, equating to ~225 M&A transactions or ~480 franchises trading annually, and may accelerate through the next decade as dealership platform scale becomes a key competitive advantage.

Historical 2% consolidation trend expected to accelerate with outside capital fueling growth

Projected number of dealership owners (2020 – 2035)

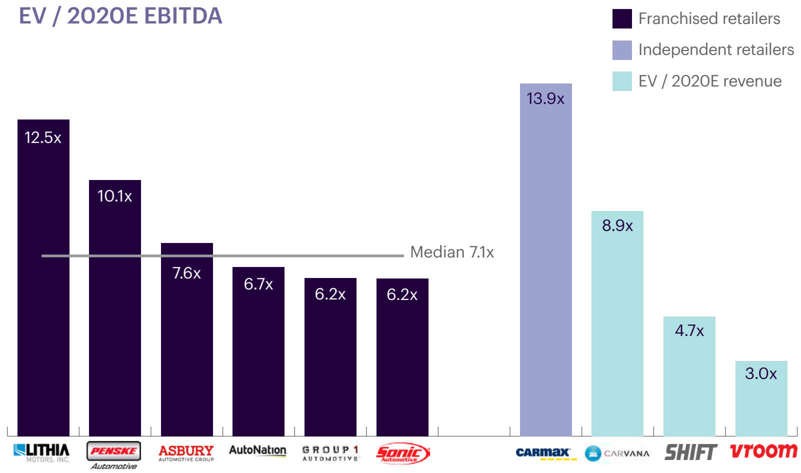


Public dealership valuation and performance

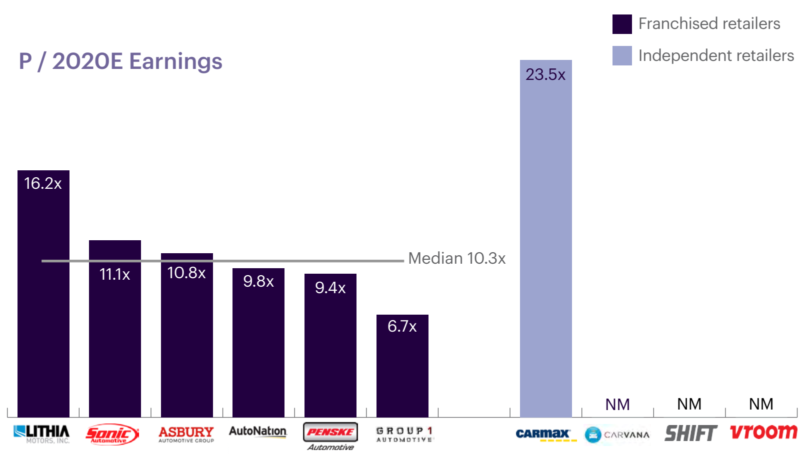
Market commentary

- Shares of automotive retailers have historically led changes in market valuations in both timing and magnitude through recessions while outperforming the broader market over the last decade
- Uncertainty surrounding consumer demand for automobiles historically leads shares of automotive retailers to both trade sharply lower at the onset of recessions as well as higher towards market recovery and stabilization
- Positive market sentiment has formed around expectations for pent-up demand for vehicle purchases on the heels of macroeconomic tailwinds, increased personal savings and renewed consumer demand for private transportation caused by the global pandemic
- Headwinds experienced in the wholesale market in March that put significant pressure on used vehicle prices have dissipated as physical auto auctions began reopening, supported by an increased use of digital auction forums COVID Impact
- Record number of off-lease vehicles coming to market are high quality, low-price alternatives that will support the already resilient used car market

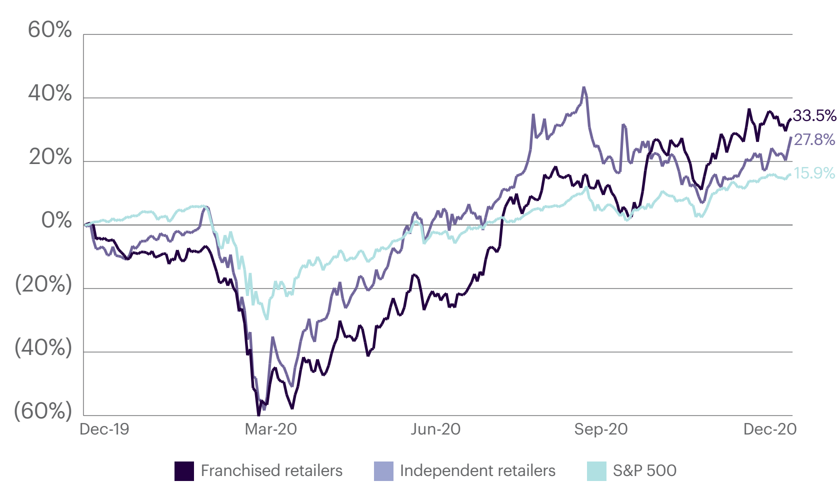
EV / 2020E EBITDA



P / 2020E Earnings



1-Year stock performance



Source: Capital IQ; Market Data as of 12/16/20

Truist Blue Sky Index

Truist estimates for brand valuation include a mix of precedent transactions, Truist State of the Market Survey results, and industry observations

The table below represents our estimate of the multiple of adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) a motivated buyer participating in a competitive sales process would pay to acquire the goodwill or "blue sky" portion of a franchised dealership. Public and private transaction data was supplemented with a survey of Truist's dealership clients to inform the valuation ranges. The multiples reflect the estimated standalone value of a brand and are not inclusive of a dealer group "consolidation premium," which typically adds an incremental 0.5x – 1.0x the implied blue sky value of the group. Our inaugural Truist **Blue Sky Index (TBI)** shows the continued trend of higher valuations for Premium franchise brands relative to those categorized as Mainstream, with domestic premium brands trading at a discount to the market. Additionally, sales volume significantly influences brand value – with Leading Premium & Mainstream brands trading above their counterparts. In general, import brands are favored relative to domestic brands, and buyers are supportive of longer payback periods following their acquisition. We expect these trends to continue: Premium franchises trading higher than Mainstream, sales volume to drive desirability, and import franchises preferred to domestic counterparts. Brands trading at discounts to their peers traditionally struggle with OEM-dealer relationships (VW), low service absorption rates (Hyundai / Kia), or a lack of vehicle diversity relative its competitors (Mazda).

Brand		Payback (YR)	TBI Brand Multiple of Adjusted EBITDA (low)	TBI Brand Multiple of Adjusted EBITDA (high)
Leading Premium	Lexus	5.9	7.5x	9.0x
	BMW	5.5	7.3x	8.8x
	Mercedes-Benz	5.3	6.3x	7.8x
	Audi	5.4	4.8x	6.3x
Premium	Porsche	5.2	7.0x	8.5x
	Jaguar Land Rover	4.9	5.8x	7.3x
	Volvo	4.1	4.0x	5.5x
	Infiniti	8.0	3.0x	4.3x
	Lincoln	4.8	2.8x	4.3x
	Acura	5.6	3.0x	4.0x
	Cadillac	5.5	2.0x	3.5x
Leading Mainstream	Toyota	5.1	5.3x	6.8x
	Honda	4.9	5.0x	6.5x
	Chevrolet	4.5	3.5x	5.0x
	Ford	4.5	3.3x	4.8x
Mainstream	Subaru	4.8	4.3x	5.8x
	Chrysler Dodge Jeep Ram	4.6	3.5x	5.0x
	Nissan	5.0	3.8x	5.0x
	Buick GMC	5.0	3.5x	5.0x
	VW	4.4	3.5x	5.0x
	Hyundai	4.5	3.0x	4.5x
	Kia	3.4	2.5x	4.0x
	Mazda	5.9	2.5x	4.0x

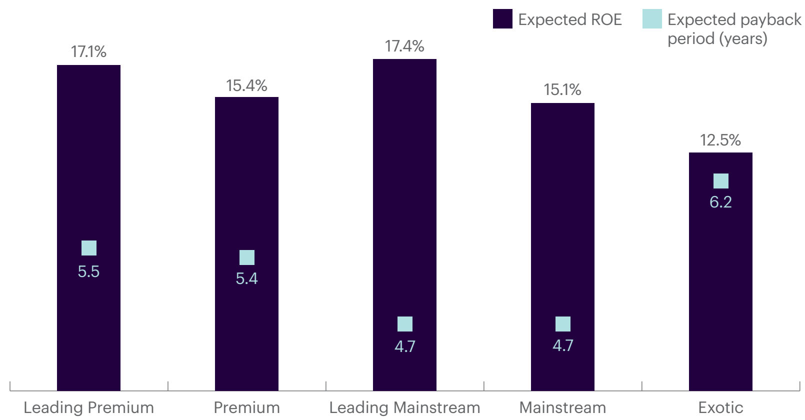
Source: The Banks Report, Cox Automotive, Industry News

Truist State of the Market survey results

Factors influencing acquisitions

- Buyers willing to accept a longer payback period when investing in premium segments
- Respondents were twice as likely to cite OEM Relationship as a rationale for acquisition of an import versus domestic brand
- Investment in Leading Premium and Mainstream brands is expected to provided a higher return on equity in the first year of operations
- Exotic brands lag in both expected ROE and payback period – indicating non-financial motives when adding to a portfolio

Expected returns by brand category

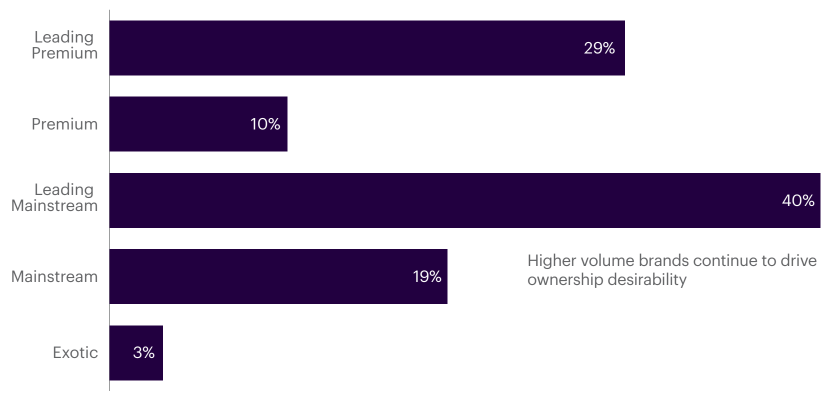


When asked to select the top five brands on their "Shopping List" if they were seeking to grow their current portfolio, respondents chose:

1. Toyota
2. Honda
3. BMW
4. Mercedes-Benz
5. Lexus

- Cash flow / profitability and ROE were the primary driver for inclusion on the Shopping List
- 74% cited financial returns (Profitability / ROE) as a rationale for inclusion
- Strategic Fit and OEM Relationship were also considerations for inclusion, but with significantly less impact
- Respondents were twice as likely to cite OEM Relationship as a rationale for acquisition of an import versus domestic brand

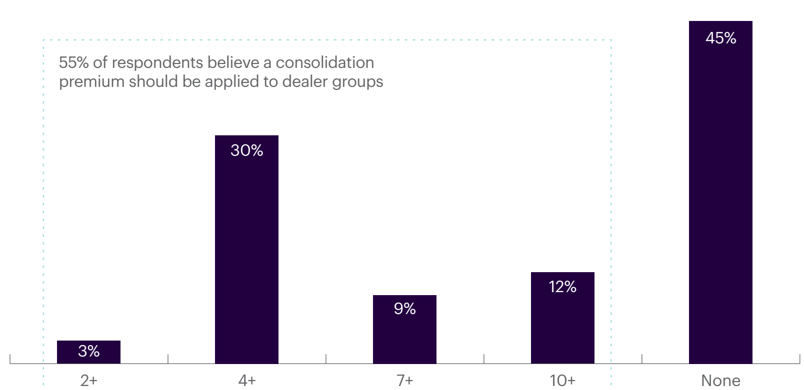
Brand categories included on Shopping List



Dealers pursuing acquisition opportunities

- 87% of those surveyed have looked to acquire dealerships in the past 24 months
- 37% are willing to pursue acquisitions > 200 miles outside their current geography
- 54% would consider a minority equity partner

Minimum group size to receive consolidation premium



The consolidation premium assigned ranged from 0.7x – 1.2x and averaged 0.9x

Source: 4Q20 Truist Dealership State of the Market Survey

Truist Securities' automotive capabilities

Sell-side advisory

- Exclusive sell-side advisory role
- Evaluation of potential or existing unsolicited offers
- Negotiation of terms and conditions
- Manage an organized and competitive marketing process in either a targeted or broad auction format depending on client concerns and objectives
- Broad access to financial sponsor/ family office investors interested in automotive retail

Buy-side advisory

- Advisory role for buyer when evaluating an identified and actionable acquisition
- Valuation analysis to support the acquisition
- Negotiation of deal structure and key terms
- Coordinated effort with financing team to evaluate optimal pro forma capital structure

Financial advisory/capital raising

- Advisory services to determine best strategic alternative
- Private capital raising initiations to support growth or selling minority holders
- Recapitalizations to facilitate management buyouts or succession planning
- Leading equity platform provides a breadth of experience to advise on any equity offering

Select recent automotive transactions

Project Permian	**Project Vail**	**Project Balboa**	**Project Catawba**	**$805MM / $550MM**	**$250,000,000**	**$1,800,000,000**
				LITHIA MOTORS, INC.	ASBURY AUTOMOTIVE GROUP	AutoNation
Franchised Car Dealership	Auto Technology	Auto Technology	RV Dealership	Follow-on Offering Senior Notes	Hy Notes Add-on	Senior Credit Facility
Sell-Side M&A Advisor	**Sell-Side M&A Advisor**	**Strategic Advisor**	**Sell-Side M&A Advisor**	**Co-manager**	**Co-manager**	**Joint Lead Arranger**
In-Market	In-Market	In-Market	In-Market	October 2020	September 2020	February 2020

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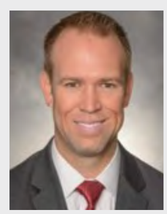

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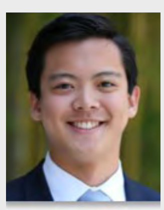

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Automotive Commercial Market Update

David Stevens
Head of Truist Dealer Commercial Services

COVID-19 response and what we learned

Looking back at 2020, it is difficult to imagine all that we have been through and learned since the pandemic began in the U.S. To recollect back to March, we would be reliving emotions of confusion, uncertainty for the future, and fear of the unknown. However, in the face of economic downturns and government mandated shutdowns, the auto dealer industry has once again proven its resiliency and strength during this historic year. Across the country, Truist saw dealers take the obstacles set out by COVID-19 and turn them into catalysts for innovation and growth.

From the very beginning, Truist Dealer Commercial Services (DCS) knew that protecting our clients in the face of economic uncertainty was of the upmost importance. We supported our dealer clients by proactively offering deferrals on principal and interest payments, helped them secure PPP funds, and had deep conversations with every client to offer our assistance and gauge financial health.

Truist dealer COVID-19 response

During the onset of the pandemic, we embarked on a mission to deeply connect with every commercial dealer client to assess their financial health and gauge their ability to pivot effectively in the face of a global pandemic. Topics of conversation included how Truist can assist dealers in managing the pandemic, what cost reduction initiatives were being implemented, what measures were being taken to ensure the safety of clients, what measures were being taken to minimize the economic effects of the pandemic, and how the dealerships were performing in the midst of a global pandemic. The results were astonishing. After having in-depth dialogue with our entire client base, we were able to asses the health of our dealer clients and their ability to weather the early impacts of COVID-19. Our dealer portfolio, and the industry as a whole, continue to show strong performance and unwavering economic fundamentals despite the pandemic.

To further assist our clients, Truist funded $13.1 billion in Paycheck Protection Program (PPP) proceeds across our footprint, saving an estimated 1.7 million jobs. Truist was among the top 3 largest participants in the Paycheck Protection Program, and we helped our dealer clients defer billions of exposure.

What we heard in our conversations with dealers

The impact varied widely depending on the state, region, or sub-geography, but experienced management teams across all regions consistently took decisive actions within their operations, including:

- Participating in deferral programs
- Participating in PPP and are now focused on the forgiveness portion
- Focusing on cash and cash management practices
- Furloughing staff and reducing variable expenses
- Executing digital, online, and virtual programs as well as contactless sales, service, and delivery methods
- Leaning in on data to drive the sales process
- Building inventory of low mileage, late model used vehicles, anticipating the new vehicle inventory shortage
- Implementing COVID-19 social distancing and other client/employee safety programs
- Significantly increasing vehicle grosses

Short term results

- Most dealerships have remained profitable or cash flow positive throughout the COVID-19 crisis
- Dealers are maintaining significant cash balances/reserves
- Dealerships have hired back staff as their state/region reopened and sales volume returned
- Dealers with deep inventory reserves were able to capitalize on vehicle shortages and increase gross profits

Ongoing dealer concerns

- Attaining PPP forgiveness
- Obtaining and managing new car inventory
- Elevated used car prices
- A second COVID-19 shutdown
- The health of the consumer

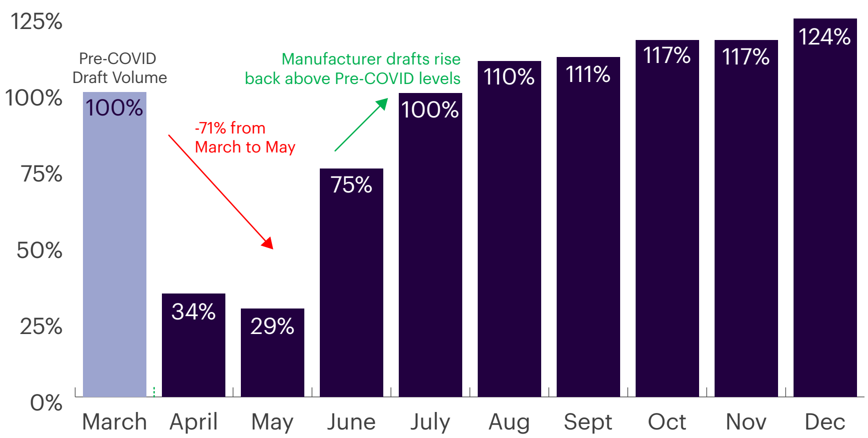
The slow recovery for supply chain and inventory challenges

Continued month-over-month improvement in new vehicle manufacturer draft orders

Following the early months of the pandemic, all automotive manufacturers faced the massive problem of operating their supply chains against the widespread disruption that COVID-19 caused within their facilities. With production plants and supply chain facilities essentially shuttered during these early months, delivery of new vehicle inventory plummeted, and dealers were forced to learn how to operate their businesses with dramatically thinner inventory levels. In order to correct the inventory levels for a supply chain as large and complex as the automotive industry, it takes significant time for manufacturers' production volume to catch up to dealer demand. This is especially true given the automotive market dynamics during the summer of 2020, as consumer demand remained consistently strong despite the pandemic. Manufacturers began to ramp up production volume in June and July to rebuild inventory levels for their dealers by significantly increasing their draft orders for new vehicle inventory. Since July, Truist has seen higher manufacturer draft orders month-over-month for new inventory compared to the pre-pandemic volume. Looking forward, Truist Dealer Commercial Services believes we're beginning to see these efforts pay off as inventory among many of our dealers showed hopeful signs of making a recovery into Q4 2020. Although inventory levels continue to rebound, there is some industry sentiment that we may see a permanent reduction in the inventory level that dealers carry – some predicting a reduction by as much as 25%.

Pre-COVID "Normal" Draft Volume vs. Post-Lockdown Draft Volume

Source: Truist Dealer Commercial Services



Beginning in June 2020, Truist has seen a dramatic increase in manufacturer draft orders and inventory flow as OEMs continually work to increase new inventory deliveries and re-normalize inventory levels across their supply chain

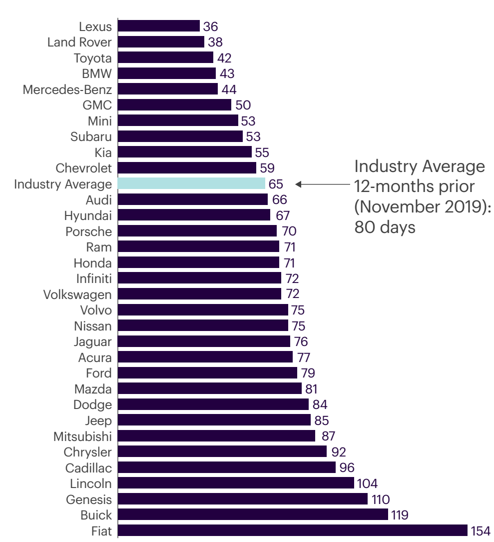
Hopeful progress in new vehicle inventory seen among franchises

As previously mentioned, Truist Dealer Commercial Services is hopeful the worst days of the new inventory shortages among dealers is behind us. Following recent market data, it appears that the progress of the automotive manufacturers' efforts were finally being realized into Q4 2020. According to a report released by Cox Automotive, the total U.S. supply of available unsold new vehicles was recorded at 2.67 million on November 2, 2020, with the industry average days' supply at 65. While these metrics fall below the 3.39 million vehicles and 80 days' supply in November 2019, this represents a hopeful improvement from the 2.54 million vehicles and 58 days' supply recorded at the beginning of October 2020.

Among the data recorded in the report, luxury-import brands led the franchise mix with lowest supplies seen among Lexus, Land Rover, BMW and Mercedes-Benz – all brands showing less than 45 days' supply. In recent months, Toyota and Subaru have consistently remained among the lowest supplies of non-luxury brands. However, the aforementioned luxury and non-luxury brands are still improving compared to previous months' performances. Full- and mid-sized pickup truck inventories remain lower than the industry average among Toyota, Chevrolet, and GMC, while Ford, Ram, and Honda all showed healthier levels.

National Days' Supply by Brand

Source: Cox Automotive



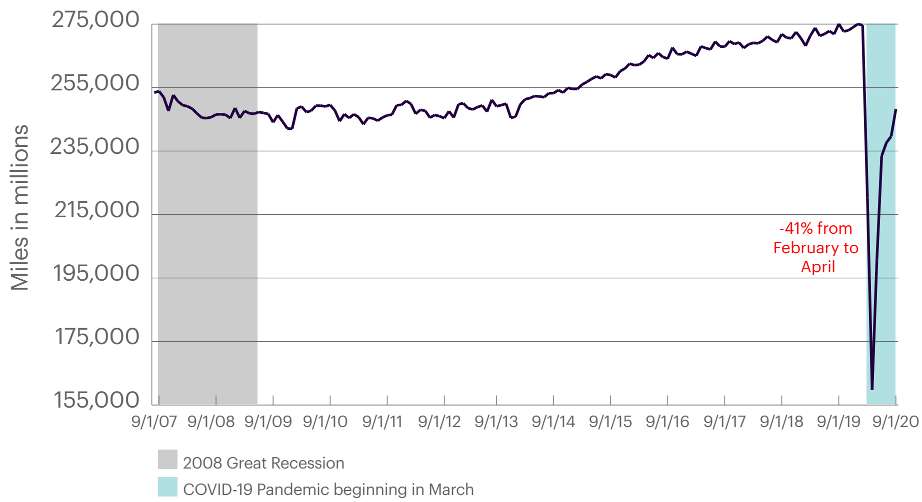
Rebound in consumer travel after historic lows

Every month since January 1, 2000, the U.S. Bureau of Transportation Statistics has published the vehicle miles traveled throughout the U.S. Following the early waves of the pandemic, April showed the lowest travel activity ever since the Bureau began publishing the data, dropping over 41% from February to April. After the historic free-fall in transportation, the metric made a sharp V-shaped recovery in the early months of summer, and has continued to move back to normalized levels, according to the most recent available public data.

A dramatic reduction in Vehicle Miles Traveled has a short-term impact on fixed operations and consumer vehicle maintenance demand. This will ultimately impact a dealership's revenue and overall profitability; however, this demand is expected to bounce back and potentially exceed historic levels due to potential pent up demand and the return of more normal travel. Truist Dealer Commercial Services anticipates transportation to return to historical levels and the normalization of demand in fixed operations.

Vehicle Miles Traveled

Source: U.S. Bureau of Transportation Statistics



Key takeaways

The auto industry has shown incredible resiliency during past recessions and its ability to quickly adapt when needed. By furloughing staff and reducing variable expenses, participating in federal aid programs, implementing strict cash management practices, leaning in on data, and implementing proper COVID-19 safety protocols, dealers were able to successfully navigate through the early phases of a global pandemic. The future looks bright for the retail automotive industry. With historic low borrowing costs, improved inventory flow/management, and elevated grosses, the industry is poised for growth in the upcoming years.

Truist continues its commitment to growth within the automotive industry by leveraging its leadership and community, scale and technology, dedicated relationship managers, world class investment bank, indirect capabilities and strategic partners to deliver the whole bank to every dealership across the country.

Sources: St. Louis Federal Reserve FRED Economic Data, U.S. Bureau of Transportation Statistics

If you have any questions or wish to discuss this information in more detail, please contact:

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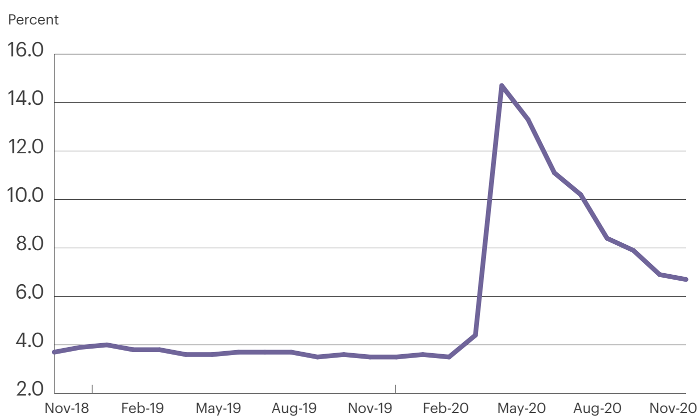
Retail Financing Update

Bill Jones
Head of Truist Dealer Retail Services
and CEO/President of Regional Acceptance Corporation

Economic volatility and challenge disrupts and redirects the retail auto industry

From a macro-economic perspective, we entered 2020 with a particularly strong economic environment characterized by an unemployment rate just below 4% and quarter over quarter average growth in GDP at approximately 2.5% in 2019. Between March and April, unemployment increased on an unprecedented basis by over 10 percentage points to just over 14% and GDP plummeted by approximately 30%. Since that time period, as the country has begun to get back to work, we've seen unemployment improve to just below 7% and GDP turn positive. Unfortunately, part of the drop in unemployment has been the result of people leaving the work force as evidenced in the labor participation rate dropping from approximately 63.5% pre-COVID to approximately 61.5% in November.

Unemployment rate, seasonally adjusted November 2018-November 2020
Source: Bureau of Labor Statistics



New vehicle sales recovery

New vehicle sales for 2020 were originally projected to continue to be relatively strong and flat compared to 2019 coming in around 16.8mm units. In late February, when actions began to be taken to slow the spread of the virus, we saw auto application volumes drop almost immediately by approximately 20% from our 15,000 dealers across the country within Truist Dealer Retail Services. The drop occurred in both our prime Dealer Financial Services business as well as in our non-prime Regional Acceptance business. State level mandates for dealer operations created immediate challenges in terms of the normal sales process. Additionally, some reluctance from consumers to leave their "shelter from home" situations further contributed to the substantial decrease. As a result, initial adjusted forecasts around annual sales were fairly bleak. Some projections had the level dropping to below 12.0mm units. Not surprisingly, our dealer clients delivered a strong response and clearly demonstrated resiliency by quickly adjusting operations by both instituting protocols to protect consumer clients as well as moving more rapidly toward digitizing portions of their sales and financing processes. While annual new vehicles sales for 2020 are projected to come in just under 14.0mm units due to the pandemic challenges described above, this strong reaction by dealers has shown up more recently in quarterly annualized new vehicle sales improving to just below 16.0mm units on a run rate basis.

Higher risk application flow and growth has been more challenged

On the prime side of our business, we enjoyed a rapid recovery in application flow in May back to pre-COVID levels and that strength in application flow continues to today. On the non-prime end of the credit spectrum, Regional Acceptance Corporation, our non-prime operating unit within Truist Dealer Retail Services, we have observed a more sustained drop in applications at around the 20 to 30% level when compared to January and February of 2020. A modest portion of the drop is attributable to tightening certain credit risk parameters which is typical for lenders during challenging economic time periods, particularly on the higher risk end of the spectrum. More recently, we have begun to resume our normal credit approach within Regional Acceptance Corporation. All this said, we continued to deliver uninterrupted service throughout 2020.

Technology transformation accelerates the rate of automation within the industry

In January 2020, we began a project focused on transformation in the auto industry and how we needed to position ourselves for success in the future. What we didn't know at the time was that the work we were embarking on would coincide with the COVID-19 pandemic. As a result, we quickly became aware

that technology advancements would become even more critically important in dealing with the rapidly changing external environment.

While there are a number of trends occurring that will likely impact our industry such as: shifting consumer demographics and preferences, electrification of vehicles, ride sharing, access versus ownership, and mobility, one initiative that has already been underway at Truist relates to the digital transformation currently occurring in the industry. Fundamentally, we believe lenders will need to integrate with dealer clients more seamlessly to provide the digital experience that consumers are demanding. As this digital transformation continues, lenders will be required to integrate with dealer API's during a consumer's online shopping experience. We believe functionality will be required to include consumer pre-qualification for financing, configuring financing to include the purchase of products, applying for credit, and ultimately being directed to the dealer's finance department for closing. The net benefit of these process improvements will be reduced costs as well as transaction friction for the consumers, dealers, and financial institutions.

If you have any questions or wish to discuss this information in more detail, please contact:

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Exploring the benefits of a multi-lender credit facility

Rick Schmersal
Senior Vice President, Truist Corporate Finance Group

Truist has been expanding its presence in the auto dealer industry by helping growth-minded dealer groups establish an efficient source of capital to seamlessly execute on strategic initiatives.

Traditional dealer financing

A single point dealership is typically financed by a single bank and/or captive finance company. The structure and needs may be slightly less complex and therefore served by a vanilla financing structure. The dealer principal may have growth objectives to build out a platform of dealerships, which would necessitate additional capital considerations to scale the business.

Similarly, a multi-point dealership group may have a single banking relationship or multiple financing relationships via bi-lateral agreements. Each bi-lateral agreement may be bespoke to each lender but serve as a way to diversify financing sources and award various bank/captive partners. This increases the complexity of the financing structure and may not offer the flexibility or capacity needed to leverage the entire platform.

Current evolution of dealer financing

The trend of continued consolidation in the automotive dealer space has facilitated the need for more flexible capital structures that allow dealers to efficiently grow their business and reach new milestones. Large consolidators in today's industry continue to develop highly sophisticated management teams charged with growing the enterprise and finding new avenues to improve margin. To support this growth and help the business hit a new gear, operators need a scalable financing structure that offers a cost efficient source of capital while optimizing the balance sheet. A multi-lender credit facility delivers on this critical financing need and is a growing trend utilized by many best-in-class consolidators.

Benefits of a multi-lender credit facility

1 Streamlined capital structure to facilitate future growth

- Consolidates the primary components of the capital structure (Floor Plan, Real Estate, and Blue Sky loans) into a single credit agreement shared on a pro-rata basis with multiple lenders
- Multi-year capital commitment
- Lead lender arranges the transaction
- Increased access to capital from both banks and captives
- Bolsters liquidity prospects
- Enhances operational efficiency
- No personal guarantees typically required
- Risk based pricing

2 Uncommitted capital via accordion

- Additional uncommitted capacity to fund growth initiatives
- Flexibility to scale any tranche of the facility (Floor Plan, Real Estate, or Blue Sky) as needed
- Market, industry or company tailwinds could increase access to capital and improve facility terms
- No additional costs associated with the accordion - pay for it only when and if you need it

3 Committed capital via Delayed Draw Term Loan (DDTL)

- Additional committed capacity to fund growth initiatives
- Capital is pre-approved by lender group
- Multi-year facility with negotiated draw period(s)
- Locked-in pricing grid for duration of facility tenor

A multi-lender credit facility provides dealer groups with a committed source of capital, enabling them to pursue a variety of strategic initiatives.

Capital structure optimization

Acquisitions & add points

Organic growth

Construction & image compliance

Wealth diversification

Truist Securities helps automotive dealer groups establish efficient capital structures via multi-lender credit facilities

Project Road

Truist Securities acted as Sole Lead Arranger and Sole Bookrunner

In April 2020, Truist Securities acted as Sole Lead Arranger and Sole Bookrunner on a $594.6 million multi-lender credit facility for Project Road. Proceeds of the transaction were used to support a refinance, fund a buy-sell, and provide growth capital to support the company's future strategic initiatives.

As Project Road continued to grow through its acquisitive strategy, shortly after closing on the multi-lender credit facility, the company began to add incremental credit facilities to support the organic and inorganic growth needs of the business.

In November 2020, Truist Securities acted as Sole Lead Arranger and Sole Bookrunner on $156.9 million of incremental senior credit facilities. The transaction supported Project Road's acquisition of a multi-store platform with a complementary footprint to the existing business. The acquisition diversified the company's flags and expanded market share in its underlying markets, positioning Project Road for accelerated growth.

The existing lender group continues to be supportive of Project Road's acquisitive strategy by providing incremental financing commitments at attractive terms. Additionally, new lenders were added to the bank group in support of the ongoing capital needs of the business.

Representative Truist private auto dealer multi-lender transactions

Private Auto Dealer
(LBO)
$202,589,090
Senior Credit Facilities
Joint Lead Arranger
November 2020

Project Road
(Growth Capital)
$156,889,475
Incremental Senior Credit Facilities
Sole Lead Arranger
Sole Bookrunner
November 2020

Project Road
(Refinance & Growth Capital)
$594,562,500
Senior Credit Facilities
Sole Lead Arranger
Sole Bookrunner
April 2020

Private Auto Dealer
(Growth Capital)
$380,290,000
Senior Credit Facilities
Sole Lead Arranger
Sole Bookrunner
March 2020

Private Auto Dealer
(LBO)
$1,130,600,000
Senior Credit Facilities
Joint Lead Arranger
Joint Bookrunner
August 2019

Private Auto Dealer
(Refinance & Growth Capital)
$1,006,000,000
Senior Credit Facilities
Syndication Agent
Joint Bookrunner
December 2018

Private Auto Dealer
(LBO & Growth Capital)
$321,800,000
Senior Credit Facilities
Sole Lead Arranger
Sole Bookrunner
April 2018

Private Auto Dealer
(Change of Control)
$679,158,500
Senior Credit Facilities
Co-lead Arranger
October 2017

If you have any questions or wish to discuss multi-lender credit facilities in more detail, please contact:

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Utilizing lease capital to access liquidity and expand real estate footprint

Justin Wilde, Head of Truist Structured Real Estate Group

Throughout the post-Great Recession economic cycle, and the ongoing COVID-19 pandemic, many corporate users of real estate have continued to utilize lease capital as an efficient means to monetize owned assets as well as expand an organization's real estate network.

Amidst the COVID-19 pandemic, net lease commercial real estate transaction volume continued to decline in third quarter 2020 across all property sectors. Transaction volume declined by 53% quarter-over-quarter ($11.1 billion compared to $23.6 billion last year) and by 36% year-over-year ($37.6 billion compared to $58.1 billion last year). But in light of all the uncertainty, the market has not grinded to a halt. Instead, the market is projected to meet or exceed $50 billion in transaction volume this year, with the fourth quarter anticipated to be the strongest quarter of 2020 as investors execute transactions at year end. Cap rates in the net lease sector compressed across the retail, office, and industrial asset classes in Q3 2020 when compared to Q2 2020. The cap rate compression in the third quarter can be primarily attributed to the late-September announcement by the Federal Reserve which suggested interest rates will remain near zero through at least 2023. This announcement along with a "flight to quality" by real estate investors has led to moderate cap rate compression, especially for strong credit and essential net leased assets.

As the global pandemic continues to impact all sectors of the economy including the real estate market, investors continue to be selective in the type of assets they are looking to acquire or sell. Net-lease property supply saw an approximate 10% drop in Q3 2020, and as supply decreased, investors continued to seek assets with high quality tenants in conjunction with long term leases. As a result, properties with long term leases to investment grade tenants continue to have the greatest demand in the marketplace. The retail sector experienced its largest cap rate tightening since 2014, with an average Q3 2020 retail cap rate of 6.15%. This cap rate movement was largely fueled by private and 1031 exchange buyers seeking lower-priced assets typical of the retail sector. While transaction volume is down overall, the aggressive nature of buyers in some asset classes have led sellers of high-quality net lease properties to price assets at historically high levels to take advantage of investors in search of quality.

While the structured real estate market has been available to auto dealers for several decades, it is still somewhat nascent given dealer principals desire to own their real estate outright. Historically owning real estate is thought to provide dealers with more flexibility as well as potentially tax advantageous corporate structures. The preference towards owning real property is beginning to shift given several changing dynamics associated with auto dealership ownership. One issue that is on the forefront of most dealers minds is the increased capital that is required to finance the higher costs from 1) building an open point dealership, 2) acquiring an existing dealership, 3) bringing a dealership up to OEM image compliance standards, and 4) investing in new technology. The amount of capital that is going to be required to operate a competitive dealership will continue to rise. Facilities may continue to get larger and more complex with the further electrification of fleets. Dealer Principals have begun to analyze the return on capital for these increased capital expenditures and some have come to determine that it doesn't make sense to keep so much capital trapped within their RealCo.

Consolidation and the entrance of financial investors into the auto retail sector is another factor that is beginning to spur the use of structured real estate products like sale leasebacks and build-to-suits. While some dealer principals view themselves as savvy real estate investors, the majority pride themselves on their dealership operations. This is particularly evident with financial investors who are attracted to the high free cash flow generating characteristics of dealerships, as well as the consolidating nature of the auto retail industry. These investors typically target higher returns than what a real estate investment offers and prefer to focus on the OpCo where higher returns are achievable.

As these trends continue to proliferate within the automotive retail market, the use of structured real estate products will garner more mind share from dealer principals.

Transparent and low cost solutions for client development projects and real estate monetization

Truist Securities' Structured Real Estate Group provides strategic real estate solutions as part of an overall banking relationship with our clients. We are uniquely positioned as the only bank in the U.S. with principal real estate investing capabilities for leasing transactions. Compared to more traditional real estate investors, Truist Securities can provide competitive pricing with greater certainty of execution because of our broad access to financial alternatives as a financial institution.

Truist has established a strong transactional record with structured leases on more than 4,200 properties for an aggregate value of over $22 billion.

Build-to-suit transaction highlight

Murfreesboro, TN
RV Dealer Build-to-Suit

$18,000,000
Truist Securities acted as principal

In March 2020, Truist Securities closed on a build-to-suit transaction providing capital for the construction of a new RV dealership in Murfreesboro, TN. The $18 million project is being constructed over the course of 12 months and when complete, will strengthen the tenant's grasp on a high demand market for RV sales.

Truist is funding the construction of the project, while the company has hired a developer on a fee basis to complete the project. Interest will be capitalized into the total lease amount during the construction period and the company will enter into a long-term, triple-net lease on the asset with Truist when construction is complete.

The primary reason Truist was awarded the transaction was due to our relationship focus, ability to provide a flexible lease/funding structure, ability to provide certainty of execution (Truist will use its own capital to close/fund the transaction), and attractive pricing.

We continue to focus on acquiring and developing real estate assets in order to support our clients' real estate strategies through two main product suites:

Sale/leaseback acquisition

In a sale-leaseback transaction, a company sells its property to Truist and simultaneously executes a lease agreement with Truist. A sale/leaseback is a strategic real estate transaction offering a number of benefits:

- **Capital optimization** – Access hidden capital from non-earning assets and re-deploy proceeds into higher yielding activities, boost liquidity, or use for more strategic purposes.
- **Alternative capital** – Long-term source of capital with no principal repayment, no refinancing risk, and no financial covenants.

Build-to-suit financing

In a build-to-suit transaction, Truist funds 100% of the project cost for the company's new real estate facility or growth project. At project completion, a lease agreement commences between the company and Truist. Benefits include:

- **Growth capital** - Allows the company to fund its growth through construction of new real estate facility/project.
- **Capital preservation** – 100% financing solution with no capital required from the company preserves capital for more strategic purposes.
- **Optimize development process** – The company maintains control of the construction/development process with transparent capital solution with no hidden equity/debt or project fees.

If you have any questions or wish to speak to someone about this information, please contact:

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**Denotes licensed with FINRA*

Automotive tech perspectives

Steve Greenfield
CEO & Founder, Automotive Ventures LLC

The auto industry has to be thankful for the resiliency of the U.S. Consumer.

If you roll back the clock to April, I would have bet that consumer demand for both auto sales and service would have dried up over the course of the year, and that we would have seen thousands of dealers go out of business.

I don't think anyone would have imagined that in Q3 2020, amidst a global pandemic, automakers and dealers would experience their most profitable quarters of all time.

Combined, General Motors, Ford and FCA delivered a total of more than $10 billion in earnings in North America during the latest quarter, versus losing a combined $1 billion in the same quarter a year before.

Coupled with strong performance from the automakers, the public dealer groups also all reported record profitability, as consumer demand remained strong, pared with healthy expense discipline by dealerships.

Despite the virus, high unemployment, and the financial downturn, it's turned out to be a great year to be in automotive retail. When we have healthy dealers and OEMs, we have happy vendors, and we tend to have strong interest in physical dealership buy/sell activity.

Most importantly, in terms of the pandemic, there's light at the end of the tunnel.

In early November, we received great vaccine news from Pfizer, BioNTech, and Moderna. Moderna's coronavirus vaccine was shown to be 94.5 percent effective in a large, late-stage clinical trial. It — as well as Pfizer's vaccine — could receive initial government approval in December, but will probably not be widely available until the spring.

The Dow Jones Industrial Average and the S&P 500 closed at all-time highs on the news, with the Dow approaching 30k points.

The IPO market has been busy this year, despite the COVID-19 pandemic. To date, there have been 371 IPOs in 2020, a record that was only bested by the 397 IPOs back in 2000, the height of the dot.com era.

Many are saying that the first quarter of 2021 could set a new record for tech IPOs, if markets hold, seeing a lot of activity due to the low interest rate environment, businesses benefiting from digital transformation, and a pipeline of strong venture-backed businesses that have been built over the last decade.

There's still a lot of capital sitting on the sidelines waiting to get deployed, and for much of 2020 the holders of this capital have been cautious. We could see that change as investors- sitting on piles of cash - get more bullish.

2020 automotive technology themes

As we look back on 2020 there have been a number of themes in the auto tech space:

- **Online retailers**: Buoyed by Carvana's impressive market cap, and Covid forcing dealers to adopt digital retailing experiences, both Vroom and Shift Technologies came to market via special purpose acquisition corporations (SPACs). The theme wasn't limited to the U.S., as Cazoo in the U.K. raised money at a $2B valuation, just 10 months after launching. And consignment dealership CarLotz is planning to go public via SPAC, with an investment from ADESA parent KAR Global.

- **The year of the SPAC**. We also saw many Electric Vehicle (EV) automakers plan to go public via SPAC, including Fisker, Canoo, Arrival and Lordstown Motors. Tesla's large market cap is helping pave the way for these EV manufacturers to command lofty valuations.
- **Online marketplaces**: Another area of interest this year was marketplaces. In terms of consumer marketplaces, CarGurus acquired Autolist early in the year, and Hearst Autos acquired Bring A Trailer during the summer. If you're an auto enthusiast, you probably spend far too much time on BAT. If you don't, beware; it's addictive.
- **Dealer-to-dealer B2B marketplaces**: BackLot Cars was acquired by KAR Global for $525 million. And rumor has it that ACV Auctions will IPO sometime in early 2021.
- **Disruption of giants**: No article on the automotive tech space would be complete without a few words on Tekion, which is attempting to attack the two DMS companies with the most entrenched market share, Reynolds & Reynolds and CDK Global. Reynolds and CDK each have more than $2 billion in annual revenues, high margins and together probably comprise ~80%+ of the franchised dealer count. They've both built very nice, defensible businesses.

Late this year, Tekion, a cloud technology company and provider of a software-as-a-service DMS, announced its Series C financing round of $150 million at over a $1 billion valuation. The funding round was led by global Private Equity firm Advent International.

Tekion hopes to solve the issue of technology fragmentation that has plagued the industry for decades. With its modern cloud-based platform, complete with a centralized accounting system built on a secure data platform, Tekion says dealers can access their company's data from anywhere while also providing seamless access to vendors via its set of APIs.

Tekion will definitely be a company to watch, as it attempts to attack the two largest software providers in the automotive technology space.

Strong M&A Pipeline

Not dissimilar to the robust physical buy/sell market, we are experiencing a very strong pipeline of M&A deals in the auto tech space.

Fear of possible increasing tax rates, the strong stock market, uncertainty around policy from a new administration, and strategic acquirers wanting to take advantage of COVID weakness has meant a flurry of companies rushing to either become public, or get their companies sold. This trend will continue into 2021.

It's an exciting time to be in the automotive space. Grab your popcorn, and get prepared for a lot of action.

Special thanks to Steve Greenfield, CEO and Founder of Automotive Ventures LLC, for this special contribution. If you have questions about the material covered in this article, please contact Steve at 678-576-9972 or steve@automotiveventures.com.

Auto tech vendor spotlight

Automotive digital retailing: yesterday a concept – today a reality

Tom Murray, CEO, WebBuy

Automotive digital retailing is not just a concept; it is a necessary reality. Given the COVID crisis and its lasting impact, dealers are in a position where they need to pivot to survive. Consumer feedback confirms that buying cars online is the new normal. The pandemic has also impacted the growth of Carvana and Vroom, and dealers should be ready to defend their share of the used vehicle market.

Amazon customers have embraced the experience and transformation of not only shopping online but also completing their transaction and taking delivery of their purchase. No lines. No hassles. No heavy sales pressures. This transformation has been hyper-accelerated with the onset of COVID. One only needs to go to Walmart or Target to find self-service checkout kiosks and parking lots with drive-up lanes for items pre-ordered online.

Digital retailing is the new business reality of meeting consumer expectations. The auto industry is now moving toward providing a revolutionary, easy-to-navigate process that takes consumers from the idea of "hey, I want to buy a vehicle in less than five hours in a showroom and not take the unnecessary risk of infection, to "hooray, I just bought a car online!"

CarMax figured this out 25 years ago by recognizing that there was a base of consumers who were frustrated with the traditional buying experience. Two years ago, CarMax exceeded 1 million sales in a calendar year. It leveraged a niche that franchised dealers ignored.

What's occurred in the last 25 years is that the constituent group of people that CarMax originally targeted, people who are negotiation averse, who say "my time is too valuable," or "I buy everything with two thumbs on my phone," has exploded in size and importance. The critical mass of this consumer group is too large to ignore any longer.

The fear many dealers face on this new horizon stems primarily from their expectations. Many see digital retailing as a threat to their very existence. In reality, the opposite is true. The savvy and visionary dealers, and great businesspeople in general, see an opportunity and exploit it in their market to augment their growth and profitability. Now, consumers demand an online option.

Just one year ago it was thought that automotive digital retailing would never be the majority of a dealer's sales volume, but today this idea is not far from reality. Early adopters who

now see digital retailing as the opportunity that it is – a chance to engage with a new customer base that they have never interacted with before. The chance to grow their business with a new subset of consumers yearning for a self-directed, easier, and less time-consuming way to buy a car. And, by the way, dealers make higher profits on this constituent group.

Many dealers think they are already in the digital-retailing marketplace but they are mistaken. What is digital retailing? Here is what it is not:

- It is not just having a dealership website and listing inventory
- It is not merely a lead generator
- It is not to provide a trade-in "ballpark" value
- It is not just offering an app, in-store kiosk, or touch-screen tool to see what vehicles are available
- It is not letting customers start the car-buying process online and not allowing them to finish online. It is not gaining a loan pre-approval, or simply setting the stage for financing to be arranged at the store

Intuitive, consumer-friendly technology facilitates the entire sale. From identifying the vehicle, setting a price, locking in a firm trade-in value, digitally auto-decisioning loan approvals, facilitating an "Amazon-like" checkout and taking possession of the new car.

Some dealers are also using digital-retailing apps in their showrooms, walking customers step by step through a very transparent process. Every dealership in America could use additional salespeople.

What if dealer advertising made a shift and promoted the idea of consumers going to their website and just buying their next ride online versus the showroom? Or, when we get back to normal, allowing a self-guided process in the showroom and give that customer a chance to begin the purchase process at a desk with a monitor or a kiosk.

As forward-thinking dealers embrace the new normal world we live in, they will foster new relationships with customers they likely would never have met. The relationships will begin with letting a customer take ownership of the process and continue through repeat and referral business in the future. Dealerships who truly engage in digital retailing may see CSI scores soar, and lead-closing rate growth and profitability rise.

Special thanks to Tom Murray, CEO of WebBuy, for this special contribution article. If you have questions about the material covered in this article, please contact Tom at 312-852-4000 or t@webbuy.com.

The fiction – and fact – of the "Carvana advantage"

John Possumato, Founder & CEO, DriveItAway

The new stars of Wall Street in automotive retail, Carvana, Vroom and Shift, are gaining value and market share despite historic losses and only recent breakeven results. So what defendable market advantage do they have over traditional car dealers? Nothing more or less than a new way of thinking about the customer.

As the market value of Carvana, and its newer rivals Vroom and Shift, soar into the stratosphere compared to the traditional valuation of public and private dealer groups, while just now achieving some break even numbers, car industry veterans like myself have to ask, why?

The last research report I read about Carvana, from a very respected Wall Street investment firm, said the usual things about growing sales and market share, and how increased growth will bring the reconditioning costs and SG&A down. Indeed, this is a new dawn for in-app car sales, marking a revolution similar to the Amazon effect (losing money initially, but owning the market in the future). It went on to say that Carvana sold 9 times as many retail vehicles online as the second largest operator, and that online sales in the U.S. used vehicle industry represent less than 1.0% of the $841B market compared to broader U.S. retail which is approximately 16% penetrated online (pre-COVID).

What is market defensible advantage?

Is there anything that Carvana is doing now or plans to do that is unique or couldn't easily be duplicated? That is, if it turns out a larger group of folks are willing to buy a used vehicle, sight unseen, with no test drive, inside an app (with a limited return policy).

Yes, they have an app driven purchase system, but who doesn't see this capability coming to dealers soon through many vendors in many variations. The thing about app technology is that developments and processes inevitably get better, faster, cheaper with time. Therefore, coming in later, for a dealer, may well be an advantage as opposed to a disadvantage.

These in-app purchase providers, like Carvana, have spent a lot to build a first mover advantage in their brand. However, all dealers that I know also have built up a local personal presence, and, with many more face-to-face customers, they are the incumbents in their neighborhoods.

Physical plant is where traditional dealers win hands-down. Although they don't have car "elevators" (at $5m cap cost per copy), dealers have physical facilities that invite used car buyers in for test drives, personal interaction, and, retail service facilities that allow for lifetime customer service as well as initial used vehicle reconditioning. All of this is paid out, or will be paid out, from current business activity, which is why most dealers make a profit per unit sold versus the in-app new guys who are just now reaching some level of break even, counting on the day when they get their volume up, and their reconditioning and SG&A down, to the point where a substantial profit is in sight.

Why Wall Street investor love?

The reason why Wall Street has embraced the Carvana and in-app sales story for used cars, I think, has far less to do with a physical plant or technology advantage, and far more to do with dealer culture. That is, these new entrants gain market share specifically because investors believe they are reading customer wants and needs directly and are adapting their process accordingly.

Wall Street is betting that these new folks will do it better for the changing customer on the horizon, and by the time the traditional auto retailers are willing to change, the market will already be owned by them.

This is not as farfetched as it seems at first glance. Let me give you some well-known recent real-world examples of culture blocks devastating entire traditional industries.

If the taxi industry had united to offer an easy, in-app booking and payment experience, Uber & Lyft probably would not have dealt the industry such a blow over the last decade. My DriveItAway fellow founder knows this first hand. He offered taxi companies the "Uber killer app" to use and unite with in 2009 in New York City and had virtually no takers. Now all are too broke to participate. A taxi medallion's value went from $1.4M to less than $150k roughly during the same period.

If the larger hotel chains had organized their own platform for AirBnB type room sharing, would that company be in the position it's in today?

Again, nothing was stopping either of these things from giving the market to the much better (at least initially) positioned incumbents, except that it required a culture change, which, although much depended upon it, didn't happen in time.

Of course, some out there will point out, correctly, that none of the new folks are yet making any real money, so the jury might still be out to some degree on valuation, but does anyone really see Uber or AirBnB going away completely? They have reached critical mass in market capitalization, brand equity and customer base to be able to survive and lead, in all probability.

This is precisely why Carvana has the valuation it has, because it is approaching that point of market cap, customer momentum and acceptance that it will survive into the future as a big market share consolidator. The only questions: how much consolidation, and at what time/growth curve?

What do we make of all this?

While many more dealers have embraced some form of online sales, or a hybrid model where much of the transaction happens before the prospect gets to the dealership, especially with the "accelerated evolution" prompted by COVID-19, many still resist or completely refuse to allow the entire purchase transaction to happen online or in-app (in states that allow it). The old mantra "get them into the store" may not be followed quite as strictly as it was in our industry a few years ago, but still prevails from what I can see, especially for used vehicles.

This is not like the old days where most dealers used the Internet as a floor traffic generator. More dealers are using online tools to get further down the transaction funnel (financing, even trade evaluations, etc.). It's more of a "I have to see the customer first to write-up the deal" kind of mentality that's still the norm among even the most progressive dealers I observe, especially for subprime used car prospects.

I've seen many recent studies worldwide that indicate lots of folks will never completely transact a used car deal online or in an app, without even a test drive or visiting a dealership, and even among those who do, there will be plenty deal "breakage" or returns (with the generous return policies coaxing prospects to do the entire deal digitally). However, there will be a new generation of consumers who will do the entire transaction online. Carvana, Vroom and Shift are proving it right before our eyes, and this, plus the traditional dealer's failure to embrace and accommodate this change (even in the areas most affected by these new entrants where these digital-only sales are happening now), is what's powering the positive vibes of Wall Street for these Carvana "disruptors."

I think the good news is the ability to compete and prosper right now against the new entrants is available to almost every dealer. The bad news is most dealers tend not to go "all the way" for an online, in app type sale, particularly for used vehicle prospects, where these new companies are taking significant market share and building traction. Although this is entirely in a traditional dealer's power to do so. It's a culture blockage more than any resource or technology "defendable moat" for the new folks, at least right now.

It is actually much easier to write-up a deal (and scale volume sales) from a digital perspective, in that all the stipulations can be captured and verified within the app process (pay stubs, bank account balances, etc.), without a lot of human intervention. You don't have to see the customer to write-up and consummate a deal. Technology can take over, if only for a minority of buyers that prefer this method, but who may be the majority of buyers in the future.

I note here the recent EY 2020 Mobility Consumer Index that tells us that Millennials will lead the next car-buying boom. Shoppers ages 24 to 39 will represent 45 percent of the nearly one-third of people without a vehicle who intend to buy one in the next six months. I also note that Millennials, saddled by student loans and other debt, make the single highest demographic of subprime buyers.

Open up to new ways of thinking. That's the only constraint here for dealers to compete and close deals in new ways - free of the constraints currently in the market. Get that incremental sale today that might be mainstream tomorrow.

This does present the classic "innovators dilemma," set out by Clayton Christensen in his classic book of the same name. No one feels the pressing need to do what is clearly "on the fringe" today with a few early adopters, so they miss out on what might be a tidal wave of "mainstream" just over the horizon. Just look at digital photography - Kodak invented it, then dismissed it as a tiny presence in the market. Compact disk drives are another tale - the mainframe drive folks completely missed the market, as compact disk drives could never do the work of the big guys.

The retail battle here is truly won or lost in the willingness and ability to change and accommodate, or lack of it, for dealer culture – a confirmation of the quote of Sun Tzu's seminal work, "The Art of War," that "Every battle is won or lost before it's ever fought."

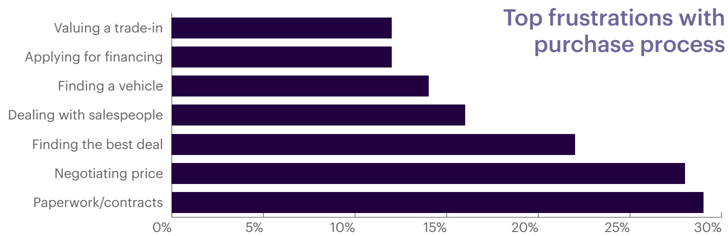
Special thanks to John F. Possumato, founder of DriveItAway, for this special contribution article. John's company enables automotive retailers to offer app-enabled remote rental and rent-to-purchase options. He is active in the Drive For Freedom Foundation, the nonprofit driving out the "Poverty of the Carless." If you have questions about the material covered in this article, please contact John at 856-577-2763 or john@possumato.com.

Side by side comparison of automotive dealerships

	Carvana	Vroom	CarMax	Average Dealership
Revenue	$3.9BN	$1.2BN	$20.3BN	$61.5MM
Used vehicle GPU	$2,883	$1,696	$3,898	$2,374
Retail unit sales	$117.5BN	$18.9BN	$832.6BN	$735.0MM
Locations	Free delivery in 261 markets (73% us population)	Flat $599 delivery fee nationwide	216 stores	Typically 1-5
Average days to sale	$62.0BN	$52.0BN	$55.0BN	$74.0MM
Financing method	Vertically Integrated	Indirect	Hybrid	Indirect
Used car finance attach rate	$0.8BN	NA	$0.8BN	$0.8MM
Net promoter score	$82	$52	$81	$39
Delivery?	Yes	Yes	Testing in select locations	Very few offering delivery
Time for delivery	Less than 7 days	Less than 7 days	1-28 days to ship to another location	N/A

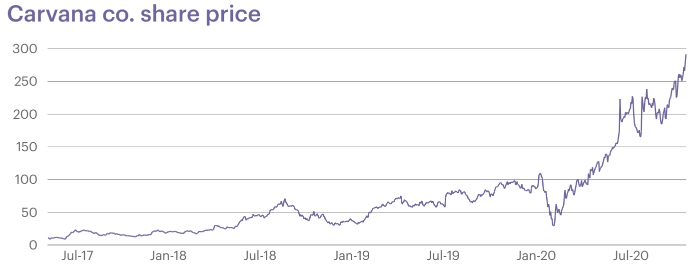
Sources for above: Company documents, NADA | Notes: CarMax sales are for fiscal 2020.

Top frustrations with purchase process



Low category ecommerce penetration

Carvana co. share price



Sources for charts to right: Company documents, Gallup, Cox Automotive, Dealersocket 2016 report. Notes: Cox Automotive was conducted in May 2020.

Alignment of strategy and tactics:
Rewards, motivation, productivity and achievement

Author: Sean Ugrin, CEO & Founder, Spiffit

In automotive retail we have two consistent profit centers: Fixed Operations (service & parts) and F&I (finance & insurance). Success depends on front-line staff to drive revenue in these areas of the business. Incentives (recognition, bonuses, commissions, Spiffs) are the catalyst. Modifying and reinforcing desired behavior is the key to unlocking potential. This applies to any business or industry.

Warren Buffett's business partner Charlie Munger, Vice Charmain of Berkshire Hathaway, has long been aware of the power of incentives to motivate staff:

> *"Show me the incentive and I will show you the outcome. Never, ever, think about something else when you should be thinking about the power of incentives."*
>
> *"I think I've been in the top 5 percent of my age cohort all my life in understanding the power of incentives, and all my life I've underestimated it." If you're trying to change a behavior, reason will take you only so far. Reflecting on an example where misaligned incentives hampered the sales of a superior product, Munger said:*

"Early in the history of Xerox, founder Joe Wilson, who was then in the government, had to go back to Xerox because he couldn't understand how their better, new machine was selling so poorly in relation to their older and inferior machine. When he got there, he found out that the commission arrangement with the salesmen gave a tremendous incentive to the inferior machine."

The science of reinforcement

B.F. Skinner, a Harvard professor of psychology, promoted Reinforcement Theory. He is famous for developing "Skinner's Box" to train laboratory rats in operant behavior.

Skinner states that the best way for us to learn new and/or complex behaviors is through **continuous reinforcement**, in which the desired behavior is reinforced every time it's performed.
If your team is not selling a specific, valuable service or product, use continuous reinforcement to re-focus them and drive volume.

Scaled reinforcement is an efficient way to improve and/or maintain an already learnt behavior, **providing a greater reward for achieving more of the highlighted activity**. By enticing your audience to reach for a higher level of performance, you trigger excitement and competition - aka "Gamification". **If your team is under-selling a specific, valuable service or product, try using scaled reinforcement to lift performance**.

Think of physical training as a form of scaled reinforcement. **The harder and longer a climber trains, the greater the mountain he or she can scale**. The more feet/meters conquered, the greater the reward. Sir Edmund Hillary's incentive for scaling Mt. Everest was "being first." As a reward, he lived his life as he chose, through a lifetime of exploration.

What about reprimand and disincentives?

Reprimand can also be powerful, if used in a fair, targeted manner. When applied sparingly it can "correct" behavior. Forgiveness and course correction provides a return to the path of reward. The reprimand is temporary; it is a reminder not a sentence.

Continuous reprimand inhibits the ability to learn new and better behavior. It triggers a number of responses — flight, resistance, and checking out. Reprimand focuses on what not to do rather than reinforcing desired behavior. **Innovative and high-performing cultures forgive failure**. They don't apply disincentives; they apply positive reinforcement and fine-tune or re-focus the incentives **rather than cancel them**.

The role of Gamification

Gamification powers the motivations and desires that exist in all of us for community, helpful feedback, accomplishment, and reward.

The goal is to effectively engage with employees, to move them to participate, collaborate, share and interact in activities. The interaction strengthens company culture and employee longevity, two key bottom-line contributors.

The genius in gamification strategies is that they're addictive.

Gamification principles are easy to grasp. They tap into basic human needs fed by dopamine, which controls the brain's reward and pleasure centers. Healthy competition follows.

One of the most appealing aspects of gamification is that it compels people to recognize each other's contributions, enhancing the organization's social bond.

What makes a program work are the game points and/or cash rewards applied to each user every time they achieve a clearly stated directive. The leaderboard automatically updates achievements and can be viewed at a glance. People like seeing themselves atop the leaderboard. They also know that their peers and superiors view their achievements, which further reinforces the social bond.

This basic human science also gives leaders powerful levers. Managers rely heavily on training and process execution. Gamification provides the reinforcement that makes training "stick" because of the obvious relationship between execution and reward. Mastering the process increases personal return.

Aligning strategy and tactics – pulling it all together

Take a moment to reflect, adjust and align your team's daily behaviors with your desired strategy:

- Did you provide the right incentives? Is your team engaged?
- Are the rules of the game clear and simple to understand?
- Are you training for new behaviors while reinforcing desired learnt ones?
- Are you acting transparently and honorably when distributing rewards?
- Are you publicly recognizing individual achievement?
- Is your feedback loop timely?

Incentives are powerful forces shaping the way we and others behave. They are strong levers that can move mountains. When applied correctly **incentives align staff tactics with management's strategy, resulting in reduced friction while unleashing greater performance**.

Special thanks to Sean Ugrin, CEO & Founder of Spiffit, a data-driven employee recognition and revenue generation platform that motivates staff and increases productivity. Sean's automotive roots come from working globally with Robert Bosch. As an adviser and e-commerce consultant, he designed and developed business solutions that tracked automotive production and drove sales efforts worldwide. If you have questions about the material covered in this article, please contact Sean at 720-220-1711 or sean.ugrin@spiffit.com.

PE, FA, SPAC, IPO and JV's: What does this alphabet soup mean to auto retail M&A?

Stephen J. Dietrich
Partner, Holland & Knight

At the risk of sounding as if I have time-travelled back to the early 2000s, the focus of this article is the reality of what I refer to as "non-car" money coming into the auto retail industry. While the influx of such investment has been heralded during several economic cycles in the last twenty years, significant and consistent influx of such capital has not occurred. Every one of us can point to two or three examples where a family office or private equity shop worked an investment in auto retail, some of which are sizable and noteworthy. But, the systematic and routine investment by these sorts of investors has not materialized to the point where it has become commonplace or a clear and competitive alternative to dealers. It continues to be noteworthy when one of these transactions occurs. In looking at this issue I think it makes sense to include potential new public company efforts (IPO or SPAC), as well as creative deal structures that may not be driven only by the performance of the core business, but more by location of a dealer group or technology opportunities.

The resilience of the auto retail industry is undeniable. Over the past twenty-five+ years, there have been multiple economic, geographic, cultural and even biological challenges to the industry, and in each instance, auto retail has proven to be nimble, reflective and tenacious. This is important to understand because these characteristics are key foundational attractants to capital investment in the space. There are sharp people who spend vast amounts of time analyzing data, trends and fortitude of businesses and industries. Many of these people see auto retail as a solid investment and a business to be in based upon investment metrics and desired return on capital deployment. This is not a surprise to hear, but what is surprising is how difficult it has been to effectively and efficiently enter the industry from the outside. This is not because the business is too complex to understand or because there are limited opportunities. While an auto, truck or RV business is in reality several business units in one, and therefore by definition, complex, it is not necessary to be a savant to understand how to operate one well. Not everyone could operate a dealership or dealership group well, but many people can. With respect to opportunities, there are over 15,000 dealerships in the United States, and even factoring in groupings of dealerships as potentially limiting opportunities, there are plenty of dealership investment opportunities.

The most significant challenge has been the effective barrier to entry related to being approved by the OEMs to become an investor in a dealership. This relates to the well-known policies of the OEM community relating to day-to-day operational control of the dealership assets being vested in an individual with meaningful operational experience in the auto retail industry and dealership operations. These policies differ in how they are implemented or structured, but generally focus on brand preservation, customer experience and operational integrity.

The drivers behind the policies make sense and are understandable. What has been a challenge is to create ownership structures and related investments that comply with the OEM policies while also providing for investment protections many third party and passive investors believe are reasonable in the marketplace. Adding to some of this tension are the size of some of the investments, which drive an investor to want to be more involved in the use of their investment dollars.

With current dealers pushing for various types of monetization events for any number of reasons, and the increasing valuation for dealerships, the reality of non individual investors or purchasers has become a reality that must be dealt with. Narrowing the pool of approvable investors to already approved operators or owners will not suffice for the volume or size

of transactions. While there has been an appetite to invest by outsiders for some time one of the largest impediments to these new investors being able to engage with dealers has been perceived deal risk. Meaning a seller or potential dealership owner/operator partner would shy away from these non-traditional participants because the risk of rejection or deal termination due to attrition was too great. The likelihood of approval was not great or the time it may take to work through a curated approval from an OEM was too long for a deal to survive.

Over the past several years we have seen these outside potential investors educate themselves on the OEM policies and the operations of dealerships to understand the foundation of these policies, and how to balance investor needs with OEM and operational realities. These investors have also invested heavily in relationship building with potential dealer owners/partners or with dealership operators who will spearhead the operational aspects of the new investment. As part of this education and evolution, investors have internally reviewed their investment models and operational governance to determine if compliance with the OEM realities will work. Some investors have opted out while others have doubled efforts to invest and become involved in the industry. These instances of investment decision often boil down to the culture of the investor, so conclusions run the gamut.

While the investors have been evaluating investment and governance models, we have seen many OEMs work to understand various investment structures and ownership groups in efforts to address the increasing demand by their dealer constituents of new entrants to the M&A marketplace in the auto retail industry. Much of this effort by the OEMs relates to deeper diligence on proposed ownership structures as well as interviews with representatives of investors. We see both objective education and diligence, as well as relational and emotional diligence, being conducted. With these efforts to understand the investment structure, motivations and realities of governance in new ownership structures, it appears that a foundation of institutional knowledge and fledgling comfort with a broader range of investment possibilities is occurring. With this knowledge and comfort comes the potential for a more routine and knowable process to achieve OEM approval. Ultimately, the process relates to the OEM's becoming comfortable that their policy objectives are achieved while balancing the demands of their current dealers. As there becomes more certainty in the process, the likelihood of additional investors being willing to engage in the approval effort increases.

With this backdrop, now more than ever, we are seeing a diversity of new entrants to the auto retail space. There are traditional private equity and family offices, and added to these stalwarts are new public companies, the potential use of SPAC (Special Purpose Acquisition Company) entities and complementary businesses looking to joint venture with auto dealers. The capital focused activities are variations on understanding and investing in the value of the operations. Potential joint ventures are a different type of entrant and it will be interesting to see if and how these develop in the coming years. These joint ventures may come from technology providers to the industry or other periphery businesses. The vast number of ways that auto dealerships may change operations or morph in the coming years, along with the accelerated technology and business model changes that COVID-19 has forced, makes the auto dealership an attractive target for acquisition or for co-investment by ancillary businesses that see opportunity.

From an observational standpoint, it appears that more non-auto related investments are moving forward and being completed. A process and path appears to be developing that will create some predictability to investors. Therefore more sellers or dealers looking for investment will be more likely to engage in serious conversations with these non-traditional investors.

Special thanks to Stephen J. Dietrich, partner at Holland & Knight, for this special contribution article.
If you have questions about the material covered in this article, please contact Stephen at 303-974-6550 or stephen.dietrich@hklaw.com.

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