

Sonic Automotive

Lighter results, but heavy EchoPark lift may ultimately resonate – 4Q first take

Maintain Rating: UNDERPERFORM | PO: 60.00 USD | Price: 57.45 USD

4Q:23 results light

Sonic Automotive (SAH) reported 4Q:23 adj. EPS from cont. ops. of \$1.63, below our estimate of \$1.78 and Bloomberg consensus of \$1.82. On an operating basis, the miss was primarily driven by weaker used vehicles and F&I. The US auto market continues to recover with total industry unit sales up 7% YoY in 4Q to 3.8mm or 15.5mm on a SAAR basis, but SAH faces micro issues in its used vehicles segment EchoPark. We therefore maintain our Underperform rating.

FY 2024 Outlook below expectations

Sonic released a broad 2024 outlook with many moving parts, but the balance appears to be lower than expectations. In total SAH expects lower Franchised Dealership segment earnings to be partially mitigated by stronger Powersport and Echopark (should reach EBITDA breakeven in 1Q24 and be positive for FY24). Specifically on Franchised Dealerships, SAH sees New vehicle GPUs approaching ~\$3,000 at year-end, low single digit growth in New & Used volumes, mid single digit growth in fixed ops, and low single F&I gross profit growth, which combines for a mid-single digit gross profit decline. SG&A as a percentage of gross profit is expected to be in the low 70% range. SAH also expects floor plan interest expense to increase due to higher inventory and higher average interest rates versus 2023.

Same-store sales (franchised)

Total same-store sales increased 2.0% YoY (BofAe -1.1%), driven primarily by strong New vehicle sales. New SSS increased 8.7% YoY, much stronger than BofAe of a +2.5% increase, driven by a 0.4% decline in revenue per unit and +9.1% unit volumes YoY. Used retail same-store sales were down 10.6% YoY (BofAe -10.9% YoY), with Franchised unit volumes down -7.1% YoY. SSS F&I sales declined 1.3% YoY (BofAe -3.3% YoY), while SSS Parts & Service was +6.2% YoY, below BofAe of +7.0% YoY.

Gross margins and GPUs mixed results

Total consolidated gross margin of 15.1% was below our 15.3% estimate. New vehicle gross margin of 7.4% (BofAe 7.7%) declined 310bps YoY, while SSS Franchised Retail New gross profit per unit (GPU) of \$4,236 was down \$1,831 YoY. Consolidated Used retail gross margin of 3.1% was softer than BofAe of 3.3% but up 40bps YoY. SSS Franchised Used retail GPU of \$1,433 was down \$14 YoY, while SSS EchoPark Used/F&I GPU of \$2,338 was up \$28 YoY. SSS Franchised F&I per vehicle of \$2,334 declined \$62 YoY. Lastly, total P&S margin of 49.9% was above BofAe of 49.5%, and up 20bps YoY.

EchoPark losses shrink, EBITDA breakeven in sight

Recall during 2Q:23 SAH announced the indefinite suspension of 8 EchoPark locations. In 4Q:23 EchoPark reported segment loss of \$15.9mm down from \$33.3mm in 4Q:22. Encouragingly, the company announced that it expects to achieve breakeven at the EBITDA level in 1Q24. Note that in January 2024, Sonic closed additional stores.

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Stock Data

Price	57.45 USD
Price Objective	60.00 USD
Date Established	28-Nov-2023
Investment Opinion	C-3-7
52-Week Range	39.02 USD - 62.26 USD
Mkt Val (mn) / Shares Out (mn)	2,055 USD / 35.8
Free Float	62.1%
Average Daily Value (mn)	10.57 USD
BofA Ticker / Exchange	SAH / NYS
Bloomberg / Reuters	SAH US / SAH.N
ROE (2023E)	27.3%
Net Dbt to Eqty (Dec-2022A)	170.1%
ESGMeter™	Medium

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SAH = Sonic

F&I = Finance & Insurance

FIPVR = Finance & Insurance per vehicle retailed

P&S = Parts & Service

GPU = Gross profit per unit

SSS = Same-store sales

SAAR = Seasonally adjusted annual rate

Cost execution softer than expected

Adj. SG&A as a % of gross profit of 71.4% deteriorated 620bps YoY and was 80bps worse than BofAe of 70.6%. Dollar gross profit and SG&A declined respectively \$35mm YoY and \$10mm YoY. With gross profit declining faster than SG&A, the ratio of SG&A to gross worsened showing deleveraging. We expect some improvement as EchoPark improves through 2024, which may ultimately provide upside to the bottom line.

Exhibit 1: Quarterly results YoY and versus BofAe

SAH reported 4Q:23 adjusted EPS of \$1.63 versus BofAe of \$1.78

	YoY Change			Variance		
	4Q:23	4Q:22	% Δ	4Q Actual	4Q BofAe	% Δ
Operating Items:						
New vehicles - total	1,702,000	1,584,700	7.4%	1,702,000	1,644,350	3.5%
Used vehicles - total	1,285,000	1,421,000	-9.6%	1,285,000	1,437,501	-10.6%
Parts and services	431,900	411,100	5.1%	431,900	447,936	-3.6%
Finance and insurance	166,000	173,800	-4.5%	166,000	173,736	-4.5%
Total Revenue	3,584,900	3,590,600	-0.2%	3,584,900	3,703,523	-3.2%
COGS	3,043,800	3,014,400	1.0%	3,043,800	3,136,834	-3.0%
Gross Profit	541,100	576,200	-6.1%	541,100	566,689	-4.5%
SG&A	386,300	375,400	2.9%	386,300	400,082	-3.4%
D&A	36,600	33,500	9.3%	36,600	36,000	1.7%
Operating Profit	118,200	167,200	-29.3%	118,200	130,607	-9.5%
FP Interest Expense	18,400	13,600	35.3%	18,400	18,000	2.2%
Other Interest Expense	28,300	24,900	13.7%	28,300	30,000	-5.7%
Other Income	(100)	100	n/a	(100)	-	n/a
Pre-tax Income	71,400	128,800	-44.6%	71,400	82,607	-13.6%
Taxes	14,500	31,000	-53.2%	14,500	21,065	-31.2%
Adjusted Net Income Reported	56,900	97,800	-41.8%	56,900	61,542	-7.5%
Adjusted EPS - Cont. Ops	\$1.63	\$2.61	-37.5%	\$1.63	\$1.78	-8.1%
Diluted Share Count	34,802	37,400	-6.9%	34,802	34,600	0.6%
Gross Margin Detail:	4Q:23	4Q:22	Bps Δ	4Q Actual	4Q BofAe	Bps Δ
New Vehicle Retail	7.4%	10.5%	(313)	7.4%	7.7%	(31)
Used Vehicle Retail - Franchised	4.8%	4.7%	16	4.8%	5.0%	(18)
Used Vehicle Retail - EchoPark	0.3%	-0.7%	104	0.3%	1.0%	(65)
Used Vehicle Retail Total	3.1%	2.6%	42	3.1%	3.3%	(23)
Parts & Service	49.9%	49.6%	25	49.9%	49.5%	37
Finance & Insurance	100.0%	100.0%	-	100.0%	100.0%	-
Total Gross Margin	15.1%	16.0%	(95)	15.1%	15.3%	(21)
Adjusted SG&A as % of Gross	71.4%	65.2%	624	71.4%	70.6%	79
Same-Store Sales:	4Q:23	4Q:22	Bps Δ	4Q Actual	4Q BofAe	Bps Δ
New Vehicles Retail	8.8%	16.2%	(734)	8.8%	2.5%	636
Used Vehicle Retail - Franchised	-10.6%	7.1%	(1,768)	-10.6%	-10.9%	30
Used Vehicle Retail - EchoPark	39.5%	-13.8%	5,336	39.5%	67.2%	(2,768)
Used Vehicles Retail Total	3.1%	-1.3%	443	3.1%	10.4%	(729)
Parts & Service	6.2%	12.1%	(589)	6.2%	7.0%	(76)
Finance & Insurance	4.8%	3.1%	167	4.8%	7.8%	(304)
Total	6.0%	7.0%	(103)	6.0%	6.1%	(11)

Source: Company filings, BofA Global Research estimates

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Price objective basis & risk

Sonic Automotive (SAH)

Our price objective of \$60 is based on a P/E multiple of roughly 9x on our 2024 estimates, which is just below an average dealer through-cycle multiple. We believe this is appropriate in light of the somewhat stalled recovery in the US/NA automotive cycle following the COVID-induced trough in 2020, as well as SAH's over exposure to the Used market via its standalone EchoPark stores.

Upside risks are 1) prolonged upside in the US cycle beyond our forecasts, 2) material accretive M&A activity, 3) market share gains as a result of successful initiatives. 4) interest rates decline quicker than expected, stimulating demand in 2H23.

Downside risks are 1) a swift and/or material downturn in US sales, 2) higher interest rate environment causes material demand deterioration and/or repossessions, 3) consumer dissatisfaction with auto retailing, and 4) the potential for franchise law and/or consumer finance law changes.

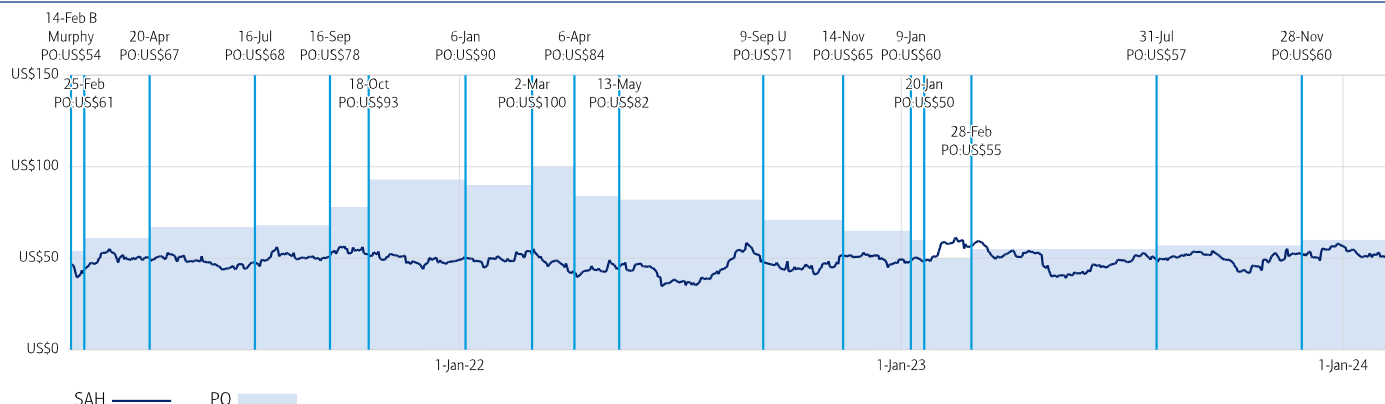
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Sonic Automotive (SAH) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Distributors Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	5	71.43%	Buy	2	40.00%
Hold	0	0.00%	Hold	0	0.00%
Sell	2	28.57%	Sell	1	50.00%

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Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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