Student Investment Fund

Consumer Discretionary Group

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Trade Recommendation for Group 1 Automotive, Inc. (NYS: GPI)

The Consumer Discretionary group for the University of Oklahoma is writing this document to recommend that the fund purchase 600 shares of Group 1 Automotive, Inc. stock. The shares are trading for $121.52 as of the end of day November 17, 2020. The group analyst report on Group 1 Automotive, Inc. is located on the next page.



Date: November 18, 2020 Forward P/E: 6.56

Company Ticker: GPI Sector Forward P/E: 9.70

Sector: Consumer Discretionary Market Price: $121.40

Industry: Automotive Retail Forecasted Price: $141.35

**Recommendation: Buy**

**Company Summary**

Group 1 Automotive is an automotive retailer that offers new and used cars and light trucks, arranges related vehicle financing, and service and insurance contracts. It also provides automotive maintenance and repair services and sells vehicle parts. They operate out of three main geographical segments: Brazil, the United Kingdom, and the United States. Group 1 owns and operates 238 franchises offering 30 brands of automobiles at 186 dealership locations and 49 collision centers worldwide.

**Industry Outlook**

Group 1 operates in the industry known as “New Car Dealers in the US”, as they sell new and used vehicles. Industry revenue will likely increase over time, due to an increase in consumer confidence and the current low interest rate levels due to the coronavirus pandemic. IBISWorld predicts that revenues in the industry will rise at an annualized rate of 5.1% to $1.0 trillion over the five years. These predictions obviously hinge on how the economy and the greater World recovers from the recent coronavirus pandemic. Higher (or lower) consumer confidence levels will lead to higher (or lower) revenues for the industry. The same statement can be said for disposable income.

**Earnings Forecast**



Our earnings forecast for Group 1 Automotive, Inc. is based on numerous drivers such as itemized revenue growth year over year, and other costs as a percentage of their relative dependencies, etc. (see our earnings forecast to review all drivers used). Some of these drivers are based on empirical data, but some are industry-specific. Our earnings forecast uses data from as far back as Q1 2016 and forecasts all the way out to Q3 2021. Almost all line entries are based on the drivers mentioned above, which are based on historical averages or regression analysis.

**Valuation**





A standard long-term growth rate of 3.50% is used, while the short-term growth rate comes from historical trends (averages) year over year. The short-term growth rate we calculated was 1.28%. The cost of equity we calculated was 13.81%. The Cost of equity is dependent on the long-term growth rate and the sector forward P/E ratio. Additionally, the Q3 Earnings Call revealed that management did not plan to aggressively service existing debt. Although the cost of equity may seem relatively high, we believe these factors and forward P/E ratios among comparable firms justifies this decision. The sector forward P/E ratio was pulled from Yardeni Research’s November 11th, 2020 report.

**Sensitivity Analysis**

While we have an idea of what the most likely equity value, and subsequently, the equity value per share is, we have also modeled other equity values and the probabilities of these values. The model predicts that the most probabilistic equity value per share is $141.35.



**Conclusion**

Based on the analysis provided above, we recommend buying equity in Group 1 Automotive, Inc. Based on our modeling, it appears that Group 1 Automotive, Inc. is undervalued by 16.4%, with a target price of $141.35.

