Vertu Motors plc

Analyst Q&A

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Transcript

Scott: Welcome to the Vertu Motors Interim Results Q&A. We're joined by Robert Forster, Karen Anderson, and Phil Clark. Phil will be moderating the Q&A and if you would like to ask a question, please raise your hand. When asking a question please ensure that you unmute yourself. Phil, I'll hand over to yourself.

Phil Clark: Great. Thank you, Scott. Good morning, everybody. As Scott said, if you could just raise your hand and I will ask the questions as we go through one by one. Sanjay, would you like to go first, please?

Sanjay Vidyarth: Morning, all. Can you hear me okay?

Robert Forreste...: Yeah, fine.

Karen Anderson: Yes, clearly

Sanjay Vidyarth: Great, thanks. Three areas of questioning if I can. First one, you talked a little in the presentation about multi-franchise sites. Could you remind us now how many multi-franchise sites you have and what the potential for them is and the opportunities and challenges that you see with them?

Robert Forreste...: Yeah, I think we've got around 130 physical locations and 190 sales outlets. I think that tells you the level of multi-franchising because some of our sites now have three or four franchises in. I think this will continue to evolve. There are some manufacturers who don't want to do multi-franchising or know that the need to do it, but aren't quite ready to take the step.

Interestingly, Mercedes-Benz, and you'd have never have thought this would happen, are actually quite open to multi-franchising now. And quite a number of Mercedes dealerships, not ours actually, have gone down that path though at Beaconsfield, we have got MG adjacent to Mercedes-Benz.

I think this is all part of the network restructuring, which has been going on for decades, and will continue to go on, where smaller outlets probably cease. You've seen us do some of that, Stroud and Moldan. There are a small number of partners who have a bigger scale with each manufacturer and there is a reduction in retail sales outlets. Multi-franchising complicates that equation mathematically, but that's broadly the direction of travel.

Sanjay Vidyarth: Okay, thanks for that. Next question is, obviously we've seen the growth in the fleet market. How do you think that will play out into mainly new cars into used? Do you think daily rentals, etc, will be holding cars for longer now than they have done historically? And that you might see a more orderly shift into the used car market?

Robert Forreste...: Yeah, I mean the growth of fleet is complicated. It's largely a story at the moment of pent-up demand. Post-pandemic the manufacturers didn't have a lot of supply, prioritized the retail market, which is higher margin for them. And left the fleet operators and indeed, Motability was very short of new vehicles. Everything was extended out, which actually exacerbated then the shortage of used cars. In fact, that was pivotal to the short used cars.

I don't think we're going to get into too much short cycle. Let's hold the car for three months and flood the used car market. I don't sense that actually. I think people will keep it for longer than historically. There are some interesting dynamics. Clearly Motability has been a massive increase. That's pent-up demand and actually that's a useful outlook for the manufacturers. But another growth area, and you could argue this is actually substitutional for retail, is the supply into salary sacrifice schemes via the fleet channel, particularly of battery electric vehicles.

I think that has taken some volume out of retail. You'll see that our fleet gross profits are 1,100 pounds in fleet and vans, so it's actually not bad business for us. And we are doing quite a lot of supply into salary sacrifice, which you could argue was really retail demand but now switched into fleet.

I'm not too concerned that we're going to head back into 2015, '16, '17 levels of fleet supply into used and undermining residuals on an heroic scale. But I think that as the new car supply comes up, you would see an easing over time in used vehicle supply. But I think from the modeling we've done of past issues in used vehicle supply coming out of new car market takes four or five years. And what are we, probably in year two?

Sanjay Vidyarth: Okay. Understood. Last question is just in terms of, obviously you've talked about consumer environment being stable at best in terms of demand on the retail side. But what are you seeing in terms of web traffic or footfall into dealerships? Is it lower and that you are working harder to convert or actually, is the footfall there and it's just that they're buying lower value cars?

Robert Forreste...: Yeah, I perceive my issue isn't necessarily footfall actually. I think there's a lot... It's a complicated area, Sanjay. I will try and simplify it. We've had a period coming out of the pandemic when we had more customers than supply, when sales teams didn't need to do too much of the selling because the customers wanted the car and were going to buy it.

We're now in a position where there is more supply, but I actually think, and I think this is an industry issue rather than a Vertu specific issue, the actual selling skills of our sales teams are rusty or at a lower level than they were pre pandemic. Personal view. Closing skills, objection handling. And you've got issues now about does somebody buy an electric vehicle? Overcoming the objections. You've got higher APRs. Overcoming the objections.

I think we've got two things to do in sales. One, actually we need more salespeople because as volumes come back post pandemic and as everybody curtail resource, I think we'll actually need more resource to handle the opportunities we've got. But we also need to increase conversion. And I think that's about upskilling and drilling our salespeople on how to sell and how to close. And that is a total number one focus for us as a business alongside continued increased recruitment of technicians. They are the things I incessantly talk about.

Sanjay Vidyarth: Understood. That's great. Thanks very much.

Karen Anderson: Thanks.

Phil Clark: Thanks, Sanjay. Just a reminder to everyone, if you can put your hand up for questions and we'll just take them in order. Next up, we've got Carl from Zeus.

Carl Smith: Hi. Morning. Can you hear me okay?

Karen Anderson: Yes.

Robert Forreste...: Yeah.

Carl Smith: I just got three questions. The first of all is what have you seen the impact on consumer behavior from higher APRs? Are fewer people choosing to take out finance and just buying outright or are people extending the length of PCP deals in response to higher interest rates?

Robert Forreste...: I don't think really they're extending too much actually. I don't think that's a phenomena. I think given the fact used car value are 20%, 25% higher probably than Jan '21, the impact of higher interest rates is probably more modest. And you're looking at 11.9, 13.9 actually, even in some premium franchises.

I think there is an impact and I think the impact is as follows. Affordability means they probably want to get something cheaper because when you apply the finance rate, the payment's still high. There's definitely more demand for cheaper cars rather than more expensive cars. I think that talks to some of the residual value pressure we're seeing in higher end products at the moment.

We're not seeing a reduction in finance penetration. There has been some turbulence actually over the last 12 months as those interest rates come through but I think customers have broadly got their minds around that actually. I don't think we're seeing lower finance penetration. I think again at the higher end there might be a propensity to try and seek personal loans and things like that, but I think we need to continue to monitor that. We've a lot of work to do on finance and we're very good at selling finance.

The other thing is that it goes back to my answer to Sanjay, I think it produces a reticence so people inquire, but our conversion is down on where it was I think previously. Now it might be skewed by the excellent conversion we had in the pandemic, but I think that higher finance rate gives pause for thought when people are looking because the cost of change has gone up. I think it's actually around objection handling and skill of sales team and management in actually converting people. That's where I see the biggest impact.

Carl Smith: Okay, thank you. Hiring technicians is a key focus. Why would the technicians want to choose Vertu to come work for? Besides pay or maybe pay is the main reason now.

Robert Forreste...: Oh no, there's a variety of reasons. Pay is critical. You've got to be competitive. I think we are competitive, we're at the top end I believe now. But we've introduced across the country in different places, different flexible working patterns. Some of our technicians work four days, long shifts of four days, three days off. We have recruited a lot of apprentices and continue to recruit more apprentices than we've historically done so.

We have in other benefits over the last few years, increased actually other benefits to our workforce, extended holidays for long service, etc. I think we are in a very good place and the proof is in the eating. We have 50 more technicians in the core group than we had six months ago. That should generate an extra £5 million of gross profit annualized and there's more to come. And the strategies we've put in place have worked and continue to work and I think that's a very good thing. I think we're winning that one.

Carl Smith: Okay. Thank you. And then finally, we saw announced maybe six months ago that Arnold Clark was starting to provide charging as a service across 100 of its dealerships. Partnering with a ChargePoint operator to put EV chargers at some of its high traffic locations. Is that an opportunity that you've looked into at all? Or is it-

Robert Forreste...: I mean, well, they didn't partner with an electric vehicle charging company. They bought it actually. This is something that we will not intend to have an independent strategy on. We will work closely with the manufacturers to make sure that in each of our franchise dealerships we're offering the franchised preferred system. It is potentially in the future a revenue opportunity, but I think got to bear in mind, electric vehicle sales, certainly in used, is relatively low level at the moment.

I personally don't see it as a massive opportunity. It's not in my top 10 of things to do, if I'm honest. Partly because actually from personal experience it's an absolute pain having a charging point fitted and I don't want the customer complaints.

Carl Smith: Yeah, makes sense. Thank you.

Phil Clark: Great. Thanks a lot, Carl. Next question, we're going to go to John Stevenson at Peel Hunt. John.

John Stevenson: Okay, perfect.. Good morning, everybody. Couple of questions again, go for the standard three if I can. Just interesting actually, you're talking about selling skills and conversion. Are you seeing that come through in other things when you look at, I don't know, used finance penetration, when you're looking at service pack sales, all the add-ons? And also just how that fits with agencies well in terms of selling skills when it's not your sale to convert almost? I don't know if you want all three in one go or-

Robert Forreste...: All right. Well, I'll try and coalesce.

John Stevenson: Go on.

Robert Forreste...: Don't think that agency means we don't sell. We still sell. The only thing agency does is the invoice goes to the manufacturer, to the customer. We still have to sell the car. Don't get in your head that we don't sell new cars under agency. We have to sell. You have to do a test drive, objection handle and close. Actually, we've done a full analysis of the differences between the two models and my overall summary was not much. Absolutely.

John Stevenson: The lowest stock loan I guess, but yeah.

Robert Forreste...: Yeah, not much different. Now, it's a very interesting point you make about finance and add-ons. And I've got a bit of a bee in my bonnet about this because we do a lot of training on making sure we're selling finance, making sure it's compliant, making sure we've got good finance penetration, make sure you've got add-on products.

But I do keep telling people that unless you actually sell the car, you can't actually sell the add-ons. I'm trying to move people into some fundamental areas like how do you close a deal to buy a car? Which might sound like real basic stuff, but bear in mind we've just gone through two years where customers came in, put their hand up and were desperate to get the car. And I think we're into a more normal environment now.

You're right, all those areas are important. And I'm not actually seeing lower penetration in those areas. I am more concerned about actually selling the car.

John Stevenson: Fair enough. Okay, perfect. Very clear. Just in terms of used stock levels, obviously you've been building up for the opportunity. Has there been much of a change instead of the holding time turnover rate of the car? How are you doing on that front now we're back to depreciating stock values? How good are you at getting stuff out on the lot and out the door?

Robert Forreste...: Well, look, I think you've got to go back to why did we increase our stock levels fundamentally. And we increased our stock levels because used car demand was pretty stable, continues to be so. And that's because we were getting into older cars, and this is the problem the used car supermarkets have got. The cars need more preparation time mechanically, they need more cosmetic work because they're older cars because we have to shift into older cars. And we've had a shortage of technicians.

The time it was taking us to prepare the cars was elongated. Which means the amount of retail cars we actually had on the websites to draw inquiries in was reduced. We took the decision to actually increase our stock to make sure that we had more cars on the web. And that's certainly been the case and it has, in our view, worked. You'll have noticed the relatively subtle wording in the current trading outlook section that talked about our volume trends in used cars were ahead of the reported period. I think there's two reasons for that.

One, reported period had 0% in the prior year. But two, we got more stock. You make a very valid point though that in a period of depreciation of cars, which clearly I think we aren't entering. In fact, we have entered. Stock turn and everything else has to be absolutely bang on. We continually monitor that and I'll probably turn to Karen in terms of what our plans are for used car stock levels in H2 because I think that's quite pertinent actually.

Karen Anderson: I think the answer there is we'll end up probably, given that we are been successful in recruiting extra technicians as well, we should be able to shorten that prep time down. And actually, I think we'll see us unwind at least partially the working capital absorption we've seen in the first half. But I mean it is a constant evaluation of supply, demand and market conditions that we do in order to assess that stock level. And we've obviously got the systems enabled to track that very, very closely as well.

Robert Forreste...: I would say it's that, if we are into a period of vehicle depreciation, and certainly CAP indicates we are, interestingly I'm sure you've picked this up as analysts, but CAP said that the depreciation in news vehicles was 1.9% in

September, which was actually the highest September 4th since September 2008.

But anyway, if you play that out, if we had the same number of vehicles in six months time, we would've less cash absorbed in working capital because the average value would be down. There's lots going on, but I actually think we'll get our unit numbers down as well, which is what Karen really just alluded to. We are quite optimistic in terms of working capital into the full year-end.

John Stevenson: Okay, brilliant. Very clear. And last question, I guess just on the portfolio developments, just stepping back. I don't know how you see things evolving over the next few years, whether there are opportunities with specific OEMs, obviously opportunities with some of the new EV brands coming in. And I guess acquisition, I don't know if there are more independent ready to come to market.

Robert Forreste...: Yeah. All the above. All the above. Yes.

John Stevenson: Any color in terms of specific OEMs or from new EVs you can talk of?

Robert Forreste...: Not really, no.

John Stevenson: No. Fair enough.

Robert Forreste...: I mean MG will do 80,000 units this year. Chinese, a lot of EV, very well priced. That seems to be a winner. We're quite keen on Geely. We are looking at some of the others, but I think it's too early to comment really.

And in terms of where our core focus is, the core focus is clearly on the established brands that we've got. We think we've got strong relationships. We think we will be able to grow with quite a lot of our current manufacturers and that's a judgment on us and it's a judgment by us, isn't it? You've got to assess long-term prospects. But I think we're in a good position to continue to grow.

We have got, as we alluded to in the statement, some bolt-on acquisitions we're progressing. We've got some other growth opportunities. For example, been awarded Tyne-and-Wear for Ford, Newcastle Ford should open by Christmas. Big operation, big operation there.

Yeah, no, we're quite happy actually with portfolio development and also making logical decisions to take assets that might be underperforming, free up the cash, get the cash back in, invest it somewhere else, strengthen the dealerships around them. And I think that's working well.

John Stevenson: Okay, fine. I mean on that last point, I don't know if you're willing to comment on, I suppose the optimization point, isn't it? To what extent there is the scope going to churn and within the existing portfolio?

Robert Forreste...: There's always scope, isn't there? I mean I think our portfolio is in pretty good nick. But you can bet your bottom dollar, we're continually evaluating it. You've got to make long-term judgements, not short-term judgments. You've got to take account of leases coming to an end. Is it freehold? What's the alternative use? It's complex, but we do actively manage our portfolio and you can see that in the cash that comes through from divestments.

John Stevenson: Okay, brilliant. Great stuff. Okay, thank you.

Karen Anderson: Thanks, John.

Phil Clark: Thanks John. I think yellow card there for more than three questions, but maybe we'll...

John Stevenson: I've got my 26 so I stopped short.

Phil Clark: Exactly.

Robert Forreste...: Lop one off next year.

Phil Clark: Exactly. Next question. We were going to go to Sam from Stifel. Sam.

Samuel Dindol: Morning, guys. Congratulations on the results. Three questions from me please. Firstly, do you anticipate any change in the competitive environment from the likely change in ownership of some key competitors?

Robert Forreste...: Interesting question. Interesting question. Yes.

Karen Anderson: [inaudible 00:20:02].

Robert Forreste...: I think our competitors will be better probably. I think they'll go through a period of uncertainty and maybe reorganization, which will be to our benefit. But let's be honest, having strong competitors is actually not a bad thing because it forces us to get better. Will there be opportunities coming out where manufacturers take different views on portfolios? Possibly. It's something we're cognizant of.

Samuel Dindol: Great. Secondly, on the bolt on M&A, is there opportunities in the ancillary area where you'd like a bit more capability, which could be of interest? And is it easier to buy that capability in some instances rather than to build it yourselves organically?

Robert Forreste...: Yes, it is. And we are continually looking. We'd definitely like some more accident repair centers. There are some specifically different businesses that we are looking at. Whether we'll pull it off or not, I don't know. We have very strong pricing disciplines in those areas. I think we've been successful to date in that action. But yeah, I mean they've got to compliment the core group is the critical point.

Karen Anderson: I think one of the opportunities we're focused on at the moment is the expansion of our smart repair business to retail customers, to our own retail customers. And that'll be us generating as opposed to going out and buying.

Samuel Dindol: Got it, thank you. And then lastly, on the service side, appreciate the attractive gross margins from growing that technician base and how you can attract more. But do you have a number in mind in terms of what would be the optimal number of technicians in the group at this sort of scale versus the nearly 900 you have?

Robert Forreste...: Well, I think that's a bit of a moving feast, but if I recruited another 50 to 75, I'd be happy.

Samuel Dindol: Great. Thank you very much.

Karen Anderson: Thanks.

Phil Clark: Great, thanks. Sam. We seem to have a follow-up question from Sanjay. And then I'll just remind everyone if they want to find a question if they put their hands up.

Robert Forreste...: Hi, Sanjay.

Karen Anderson: Sanjay?

Robert Forreste...: No, he is gone.

Sanjay Vidyarth: Sorry, there was no follow-up question. I was just, I hadn't lowered the hand.

Phil Clark: So sorry, Sanjay. Great. I think that's probably all the questions covered, Robert, so maybe back to you.

Robert Forreste...: No, that's super. Well, thank you very much for your time.

Karen Anderson: Thank you.

Robert Forreste...: This is a bit of a novelty for us. We haven't done an analyst Q&A for quite a long time. Hopefully if you provide Phil with feedback as to whether you felt it helpful or not, that will be handy. And we look forward to reading your scribbles. Okay. Thank you.

Karen Anderson: Thank you.

Phil Clark: Thanks, everyone.