EDISON

Stern Groep

Optionality in a perfect storm

Initiation of coverage

Automotive retail

Downturns tend to be opportunities to invest in car dealerships, especially those that are likely to emerge stronger. Stern is well positioned to weather the current storm with its significantly restructured organisation. Its valuation is undemanding at 9.8x 2021e P/E and there is additional optionality in light of a potential merger with much larger Swedish automotive group Hedin.

Year end	Revenue (€m)	EBIT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/18	989	(1.7)	(0.73)	0.00	N/A	N/A
12/19	989	5.5	0.29	3.50	N/A	28.9
12/20e	816	7.5	1.31	0.58	9.2	3.3
12/21e	923	12.3	1.23	0.52	9.8	4.1

Note: *EBIT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Weathering a perfect storm

While Stern has to deal with market-wide structural changes such as the transition from combustion engines to hybrid/EVs, a higher proportion of less profitable lease clients and shared car concepts, all of which are having a profound impact on the market, COVID-19 has presented another big challenge to car dealerships. Flexibility is what is required in this environment, and fortunately Stern has already started optimising its dealer network by reducing geographical overlap and moving out of unattractive car brands, while eyeing new network additions like the recently announced ambition to expand in Renault and executing stringent cost controls.

From bricks to clicks

Late 2019, Stern launched its 2020-2022 Focus on Value strategy. It aims to complete the company's transformation from a traditional bricks and mortar car dealership into an integrated automotive service platform with a strong digital offering. Stern has made much progress in its digitization efforts this year and together with the optimisation of the dealer network, this places the company in a relatively strong position for the coming years. We forecast Stern to achieve adjusted EBIT of €7.5m in FY20 (up 35% y-o-y), generating a margin of 0.9% and expect this margin to improve to 1.9% by FY23e on the back of a global economic recovery and ongoing corporate restructuring.

Valuation: Attractive and supported by Hedin talks

Stern is trading at an FY21e P/E of 9.8x compared to the peer group average of 10.9x. Applying the average multiple and adding the market value of the stake in insurer Bovemij (€3.17 per Stern share) results in an implied valuation of €16.6/share. Scale is becoming even more important in light of the structural market changes and Stern and Hedin, a much larger Swedish automotive group, recently restarted their merger talks. Although no details have been released so far, we note that most of the company's recent divestments were made at a price to book value in excess of 1x. With Stern's reasonably well impaired book value of €23.54/share at H120, we believe this could provide some support in the ongoing merger discussions with Hedin.

13 October 2020

Price	**€12.1**
Market cap	**€69m**
Net debt (€m) at H120, pre-IFRS 16	82
Shares in issue	5.7m
Free float	29.5%
Code	STRN
Primary exchange	Euronext
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	12.9	28.4	(14.6)
Rel (local)	8.9	28.0	(13.9)
52-week high/low		€17.90	€7.92

Business description

Stern Groep is one of the largest automotive groups in the Netherlands. With 75 locations and revenues of almost €1bn it is the second largest car retailer group in the Netherlands. The company has over 1,850 employees.

Next event

FY20 results	4 March 2021

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Investment summary

Well-positioned car dealership defying a perfect storm

As the Netherlands second largest automotive dealership group, Stern has already had to cope with structural changes to its markets like the transition from combustion engines to hybrid/electric vehicles (EVs), new accessibility methods including private lease and shared car concepts, such as Car2Go or SnappCar (rent from your neighbours). While these trends have had a profound impact on the market environment already, COVID-19 has presented another big challenge to car dealerships. Consumer confidence declined rapidly in lockdown and new car sales dropped double digit percentages. Used car sales were strong despite working from home trends, as public transport was not an option for many commuters in the context of COVID-19. Car maintenance activities were lower than usual, as staff availability was limited due to COVID-19.

Flexibility is what is required in this environment, and fortunately Stern had already started downsizing its dealer network, optimising its car repair network and adjusting to the market trends years ago. For instance, the position in attractive car brand Kia was expanded, while the positions in Fiat (relatively unattractive) and Volkswagen (not able to get to desired market share) were reduced. Scale, the optimised network and the new Focus on Value strategy aimed at optimising platform efficiency and transactions place the company in a relatively strong position for the coming years. Stern’s efforts are now directed at channelling as many services as possible through its physical dealership and car services sales network, instead of the traditional sales only focus. This is done for instance through the service level agreement (SLA) that was closed with lease company ALD, to which Stern sold off its leasing activities in 2019 (for €88m).

Financials: Potential to improve medium-term profitability

We expect Stern to report revenues of €816m in FY20, a 17% y-o-y reduction, driven by the sharp reduction in new car sales in H120 due to COVID-19 and the divestment of Heron, offset by some normalisation of revenues in H220 on the back of improving economic activity. We forecast FY20 adjusted EBIT of €7.5m compared to €5.5m in 2019 (H120: €4.8m), a visible improvement thanks to the cost control and government support. The main one-off items so far in 2020 include the write down of goodwill for dealerships of €20m and appreciation in the book value of Bovemij of €4m. We expect a reported net loss of €10.6m in FY20 (adjusted net profit €7.4m).

2021 should mark a rebound of revenues to €0.9bn, as the effects of COVID-19 reverse, with the subsequent anticipated return to the pre COVID-19 revenue level of €1bn revenues by 2023. We believe that EBITDA and EBIT should benefit significantly from the ongoing improvements in the dealer model and we expect that a 1.3% EBIT margin should be achievable in 2021 rising to 1.9% by 2023. We note, however, that our forecasts are made against a weaker historical performance, with an FY19 adjusted EBIT margin of only 0.6%.

Valuation: Undemanding compared to European peers

After the cyclical trough in 2016, Dutch new car sales started to pick up again in 2017 and 2018, which were followed by a difficult 2019. 2020 was looking better again driven by a better consumer confidence until COVID-19 hit. Valuations dropped fast in the face of the pandemic and Stern's share price declined from around €17 to a low of €7.9, but has since recovered to €12.1 at the time of writing. Stern is currently trading at a 10% discount to the European peer group on FY21e P/E and a 23% premium on FY21e EV/EBITDA (excluding its stake in Bovemij). However, noting the difference in capital structures and quality of the balance sheets of the peer group companies, we see P/E as a more relevant valuation metric for the sector. As such, applying the average peer group multiple of 10.9x to Stern's FY21e normalised EPS estimate of €1.23, we arrive at an implied value of €13.4/share. Adding to this the market value of Stern's stake in car insurer Bovemij of €3.17 per share results in a value of €16.6. Nordic peers trade at FY19 P/B of more than 3x and UK peers at 0.4–0.6x versus Stern's 0.5x. We believe Stern is conservatively valued given its transparent and significantly impaired balance sheet.

Hedin merger talks add optionality

Given the ongoing structural industry changes, scale is getting more important and the restarted merger discussions between Stern and much larger (~3x turnover) Swedish automotive group Hedin Automotive, which were suspended after the coronavirus outbreak in March, could result in a combination of the two companies. The potential deal would bring economies of scale, geographical diversification and a platform for further growth with Stern's stock listing. In addition, Hedin would add complementary car brands in several smaller countries to the Stern brand portfolio.

We note that Stern's CEO, who also is a 12% shareholder, has always focused on realising at least the intrinsic or book value for the divested assets. For example, the real estate and lease activities were sold last year for €89m, achieving a book profit of €31m. As such, Stern's well impaired H120 NAV of €23.54/share could represent a support in the ongoing discussions with Hedin.

Strong balance sheet

At H120, Stern had net debt of €82m on a pre-IFRS 16 basis, including €12.5m in cash. In addition, the company had €112m in lease liabilities on its balance sheet. The reported net debt position was complemented by the largely undrawn bank facility of €60m. However, given that Stern made use of the option to postpone tax payments for €29.2m in H120 and by July these have been paid, part of this bank facility has likely been drawn down. Our model suggests FY20 net debt of €128m, excluding leases (vs €139m in 2019), driven by positive working capital movements, amongst others as a result of the sale of Heron.

Stern has always targeted a solvency ratio of 12.5% for its lease activities, 20% for the rent activities and 30% for its other activities and at 28.4% solvency this is still in range (adjusted for goodwill impairment 32.2%). Stern's policy has been to pay out any amount of solvency that is not required in the targets and we expect it to continue on this path, which means that a large part of profits will be paid out to shareholders. Stern paid out an extraordinary €3.50 cash dividend in 2019 and we also expect dividends to be paid in 2020, although at a lower rate of €0.6/share.

Risks and sensitivities

Generally, **automotive retail** is not a structurally growing business, which faces a number of structural challenges. These were amplified by the coronavirus in 2020. All this points to the need of consolidation in the Dutch market and Stern is playing its part in this.

In the short term, **Consumer confidence** has always been an important driver and dynamics have been very volatile this year against the backdrop of COVID-19. In the longer term, **EV/hybrid/shared cars** represent a risk for traditional dealerships like Stern, as they either require less cars (shared) or less maintenance (EVs). Furthermore, there is always balance sheet risk, as dealerships are highly leveraged. Despite a strong balance sheet and liquidity compared to peers, Stern still has a large **debt position** of €100m at the end of June 2020 (FY19: €140m including Heron). Stern's track record in **profitability** of the dealer and car service activities is relatively weak and **lease companies** are becoming a more important client group, and with the larger volumes involved they have a strong bargaining position. The ongoing restructuring should partly offset this effect.

Stern: A dealership with national coverage

With sales of around €1bn, Stern is the second largest car dealership in the Netherlands after Van Mossel Groep. In 2019, it also sold fewer cars than Tesla, whose sales were mostly fiscal incentive driven, including many Model 3. The company has been a strong consolidator in a shrinking dealership landscape and is now optimising its network with 57 dealer locations in 2019, compared to 85 in 2015. In addition to car dealerships, Stern has a network of 15 Stern Points, which provide car aftermarket services (Car Services), and offers rental services (Mobility Services). Stern works closely with French lease company ALD, which bought Stern's lease activities in 2019. The companies signed an SLA for the servicing of running and future lease contracts. The group has over 1,850 employees. The key benefits of a large-scale dealership include:

- With near-national coverage, Dealergroup Stern and the Stern Points are able to service clients nationwide and Stern also has a strong position towards importers.
- Stern can offer third-party financing (including lease and private lease), insurance and fleet management services to clients and fleet owners like lease companies.
- With the sale of the lease activities to ALD in 2019, Stern also signed an SLA to service both existing and new lease contracts.

Stern is a market leader in the Netherlands for major car brands like Mercedes, Renault and Ford. Up and coming Korean car brand Kia is also getting more and more important. In addition to these four, Stern also represents 14 other leading car brands in its 57 franchise locations, of which Nissan, Volvo, Land Rover and Opel are the most important ones (see Exhibit 1). Maintenance, used car sales and parts are also important contributors to the Dealership business.

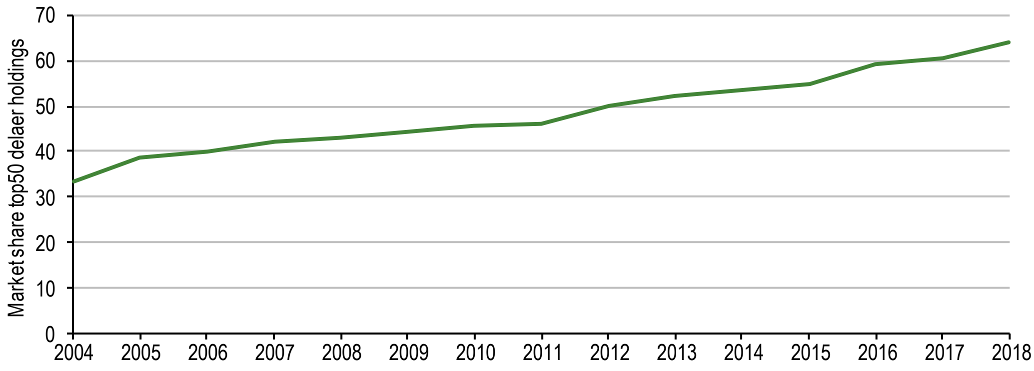
Exhibit 1: Car sales in Netherlands and Stern's market share

	Car sales 2019	Stern sales 2019	Stern's market share
Netherlands total new	446,114	20,862	4.7%
Netherlands used	1195,348	20,480	1.7%
Ford	25,295	5,950	23.5%
Mercedes	19,125	2,667	13.9%
Renault	26,207	2,647	10.1%
Kia	25,260	2,269	9.0%
Volkswagen	47,452	1,671	3.5%
Opel	32,324	1,578	4.9%
Volvo	16,316	1,057	6.5%
Audi	15,827	433	2.7%
Fiat	4,025	276	6.9%
Land Rover	1,325	78	5.9%

Source: Bovag

Stern's total sales of new and used passenger cars and light commercial vehicles amounted to nearly 47,500 units in 2019, of which 20,862 were new cars, 20,480 used cars and the remainder new light commercial vehicles. Stern has a share of 4.7% in the new passenger car market in the Netherlands, which shows there is still room for further consolidation despite the consolidation trend that has been occurring for years. In light commercial vehicles, Stern's market share is higher (7.3%). The market share in the much more fragmented used car market is roughly 1.7%. In 2004, the top 50 dealership companies in the Netherlands had a market share of 33.5% of the new passenger car market and that increased to 64% by 2018 (see Exhibit 2).

Exhibit 2: Development market share top 50 dealers



Source: Aumacon

Like everywhere in Europe, gross margins on the sale of new and used cars are very thin, usually 4–5%, somewhat higher for used than for new cars. The majority of profit stems from maintenance, selling spare parts, changing oil and sales bonuses from the importers and OEMs. We believe that a well-executed dealership business should be able to make EBIT margins of 2–3% in the Netherlands. We note that Stern has reported EBIT margins of up to 1.6% over the last 10 years in its dealer division, well below this threshold. This was partly caused by the fact that lease car sales were reported within Mobility Services, which had relatively high margins compared to peers.

Making optimal use of the network

With 75 locations (including Stern Points), Stern has near nationwide coverage and is therefore able to service clients operating nationally. Making optimal use of this network is crucial to get to at least the 2% EBIT margins that Stern targets.

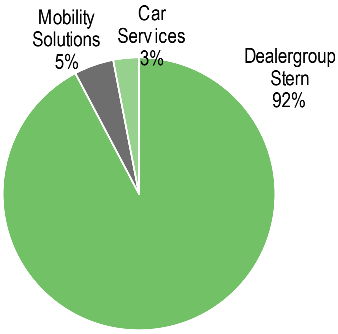
Within Car Services, the 15 locations of Stern Point handle body repair works, services like winter/summer tyre change, oil change and light commercial vehicle interior building and lettering. Furthermore, there is a small operation in electric vehicles for urban mobility.

Mobility Services handles rental and fleet management services. In 2019, Stern had 2,574 rental cars in its fleet and serviced 57,560 mobility contracts (car park, financial lease, rent, warranty). COVID-19 has had a devastating effect on rental companies and Stern reduced its fleet to 1,800, but after markets stabilised the fleet is at 1,916 again on 30 June.

Stern also offers leasing in cooperation with ALD, which acquired Stern's leasing activities in 2019 for €88.6m (book profit of €30.5m). Stern now offers ALD lease contracts and gets a commission for each contract closed. Furthermore, there is an SLA in place for maintenance services and the remarketing of former lease cars. The benefits of this SLA will gradually start to become visible as of this year and are an important contributor to the expected margin recovery.

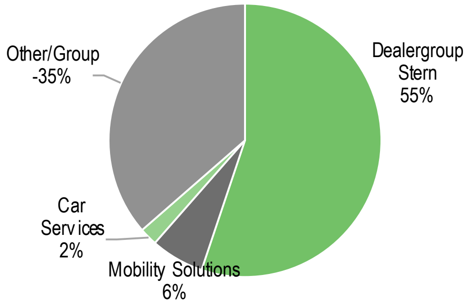
Other financing options are offered, like private loans through OEMs (captive financing), as well as insurance and extended warranty (brand-certified). Stern earns a commission on these transactions. Furthermore, Stern has a valuable 5% participation in car insurance group Bovemij.

Exhibit 3: Revenue segmentation 2019



Source: Stern Groep

Exhibit 4: EBIT segmentation 2019



Source: Stern Groep

Focus on Value strategy

After the sale of the lease activities in 2019, Stern launched its 2020–22 Focus on Value strategy, put in place to complete the transformation of Stern from a traditional bricks and mortar car dealership into an integrated automotive service platform with a strong digital offering.

Consolidating all car brands on the www.stern.nl website and rebranding to the single brand name Stern have been steps in realising this strategy. Digitalisation of client contact points, tracking preferences through customer behaviour on the site and business after sales (such as service appointments/material logistics) are being implemented to optimise platform efficiency and increase the number of platform transactions. Network optimisation, loading Stern Point with external services from ALD and possibly other fleet owners and increasing efficiency of workshops also continues.

In 2019, 10 dealer locations were closed or combined, 104 staff reductions were realised through restructuring and rental and purchase agreements were renegotiated, resulting in an overall reduction of operating costs by 7%. In H120 this trend continued with a staff reduction of 77. This all adds to optimising the network. We would not rule out further network optimisation, both in terms of addition and closure of dealer locations, and see the recent announcement about the sale of the Renault location in Zaandam and the desired expansion of Renault exposure in the south of the Netherlands as next steps in this strategy.

Financial targets have not been communicated after the sale of the lease activities to ALD, which signalled Stern's focus on the dealerships. In its 2018–20 strategic plan, Stern targeted an EBITDA improvement to €48m by 2020 from €24.5m in 2016. €3.9m of this improvement were from improving efficiencies at the dealers and €11.8m from organically growing the parts business and expanding the number of car service locations of Stern Point to 25 (H120: 15). Of course, these targets are not realistic now due to the impact of COVID-19, but it gives a sense of how the targeted improvement in profitability could look as markets recover and the company expands value-added services. According to the company, an EBIT margin of at least 2% should be feasible (compared to 0.6% in adjusted EBIT margin in 2019).

The potential merger with Hedin Automotive of Sweden also fits into the company's strategy of network optimisation (see page 8 for more details on the potential Hedin/Stern combination).

Exhibit 5: Focus on Value strategy

Source: Stern presentation

Road to a more predictive model, increasing value-add services

Stern's focus is on making optimal use of its physical dealer network, while also making the car offering more accessible and visible online. The improvement of the website has been impressive in the last years and Stern's complete offering is now visible on the centralised platform, as well as through leading used car sales platforms in the Netherlands such as Autoscout and Autotrader

Initiatives to make best use of the existing network and to improve predictability include:

- making **optimal use of online potential** through its own and third-party websites and **physical locations** through national coverage;
- the **SLA** with ALD should lead to a larger number of car services per Stern location and higher visibility, and
- the **Stern Point** network adds to the dealer network and can be used for car repair and relatively simply maintenance jobs (oil renewal/tyre changes).

Car sales are only part of the story for car dealers. Gross margins on the sale of a new or used car are normally 4–6% in the Netherlands, higher for used cars and lower for new, and that is not enough to keep a large dealer network afloat. The higher gross margins are made on maintenance, car repair, oil and part sales. Therefore, optimising Stern Point and better utilisation of engineers is key to further increasing margins and Stern is gradually improving on this through clearer KPIs for workshop mechanics and management as well as sharing best practices through the organisation. Further digitisation and more work for ALD should push the 2020 results further.

Stern's efforts on digitalisation have been strong in recent years and we believe that it has regained territory compared to competition. Data is collected from everything the (potential) customer does and is consequently analysed and routed to parts of the organisation for which it is useful. Lead generation and processing has become much more centralised in Stern's head office.

Another important element in getting to a more predictive model is Stern's recently initiated cooperation with ALD. With the sale of its Lease division, Stern signed an SLA that should lead to higher maintenance and repair volumes through Stern's dealer distribution channels. We believe that this cooperation could be a game changer for Stern. An increasing proportion of ALD's lease car fleet (c 65,000) should now be routed through Stern's dealer network and that should lead to much higher visibility of maintenance work, but also for instance to better utilisation of the rental fleet. Visibility is also higher because maintenance patterns of leased fleet cars are more predictable, driven by contract requirements to support resale values.

Successful execution of this more predictable business model with the larger volume of higher value-added services should help the company to improve margins, potentially achieving its profitability target of 2% in adjusted EBIT in the longer term. According to Dutch industry organisation Bovag, the average Dutch dealership made a net profit margin of 0.6% in 2019. Given its scale and the potential to attract more nationwide operating clients like lease companies, Stern should be in a position to outperform the sector. That said, in 2019 the company achieved profitability below this level on an adjusted basis. We forecast adjusted EBIT margin to recover to 1.9% by FY23.

Potential merger with Hedin

In January 2020, the much larger Swedish group Hedin Automotive and Stern announced merger talks. After several divestments over the last year by Stern, a merger with Hedin would be a decisive step to become one of the European leaders in automotive retail. The combined group would have a turnover of roughly €3.5bn and, given Hedin's aggressive acquisition strategy, we would expect it to have ambitious further growth plans. With that, the combined entity could become a top five European automotive dealer. Details of the potential transaction are not available yet, but the way that Stern is valued in the combination will be key for shareholders. The enlarged group would certainly lead to a higher liquidity of the shares on Euronext.

The combination, through a reverse takeover, intends to retain and use the Euronext Amsterdam listing as a platform for further growth. In March after COVID-19 hit, the merger talks were suspended, but the talks have been resumed. Important conditions like the proposed exchange ratio have not been disclosed. The combination of Stern and Hedin Automotive would be complementary in terms of geographic focus with strong positions in the Netherlands, Norway, Sweden, Switzerland and Belgium, and also in represented car brands (it would add BMW and Porsche for instance). By forming a large combination with leading positions, especially in smaller countries, Hedin and Stern would be better positioned to play into the numerous trends and developments that are shaking up the automotive retailer world. One of these is the ongoing globalisation of the automotive market.

Management

The management board currently only consists of CEO Van der Kwast. We believe that the financial director, Mr Finus Porsius, who has been in this position at Stern Groep for many years now, is as close to a CFO as can be.

After a career in banking and corporate finance, Mr van der Kwast became an entrepreneur in 1993, when he acquired loss-making Opel dealership Riva. In the following years, the former rower (he participated in a number of world championships) gradually built out into a leading nationwide multi brand dealership and got access to the stock exchange through a reverse takeover of AIR (Auto Industrie Rotterdam) in 2000. He still is a major shareholder with a >12% stake.

Stern Groep is effectively led by Mr van der Kwast, advised by the 12-person strong Group Council. The council consists of the company's CEO (who is a chairman of the council), Mr Porsius, all the car franchise heads (five, ranging from Mercedes to Ford), the product group heads (Mobility Solutions and Stern Point) and group functions (HR, corporate affairs, controlling).

Although we believe that Stern is effectively led, a more balanced management board would be a positive in terms of corporate governance.

Exhibit 6: Management and supervisory board

Mr Henk van de Kwast	CEO of the management board
Mr B Goeminne	Chairman of the supervisory board
Mrs MEP Sanders	Supervisory board member
Mr P Nielen	Supervisory board member

Source: Stern Groep

COVID-19 adding to an already disrupted environment

The car dealership business is already undergoing major disruption from established trends like the move to cleaner fuels (electrification) and a tendency to lower car ownership by leasing or shared car concepts. COVID-19 just exacerbated the already harsh market environment, resulting in a collapse of new car sales, lower utilisation of the rental fleet and decreasing workshop revenues, although interestingly used car sales were comparatively robust. Many car dealerships in the Netherlands, Stern included, have made use of the Dutch government support programs for companies suffering a >20% revenue collapse after COVID-19 and with a robust balance sheet and stringent cost cutting, Stern continues to proactively manage cash flow.

EVs and other attitudes to car ownership

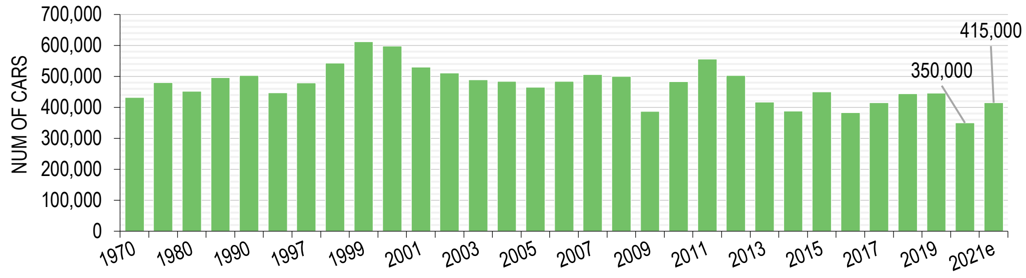
COVID-19 has had a profound impact on the Dutch car market, which was already going through disruptive changes:

- **New car sales collapsed:** Over the first six months of the year, new passenger car registrations fell by 30% to 158,150, mostly driven by lower consumer confidence caused by COVID-19. For the full year, sector organisations Bovag and Aumacon expect a 22% decrease to 350,000 new passenger car sales and Aumacon expects a rebound to 415,000 new passenger cars by 2021 (Exhibit 7).
- **Rental services and Maintenance** were hit severely by the lower mobility needs driven by working at home and less business travel due to COVID-19.

Longer-term trends affecting the car market include:

- **The way people buy new and used cars continues to shift** towards primarily online identification and specification with dealership visits becoming rarer and shorter.
- There is a continuing transition to **EVs,** which will most likely reshape the current automotive landscape in the medium to long term. EVs require much less maintenance, which is the current profit driver of dealerships.
- New generations care less about **car ownership**. In particular, private leases have become popular in the Netherlands. Leases lead to margin pressure due to the better bargaining position of lease companies compared to individuals, and shared car concepts lead to market pressure as fewer cars are needed when they are shared.

Exhibit 7: New passenger car sales in the Netherlands



Source: CBS, Aumacon, Bovag

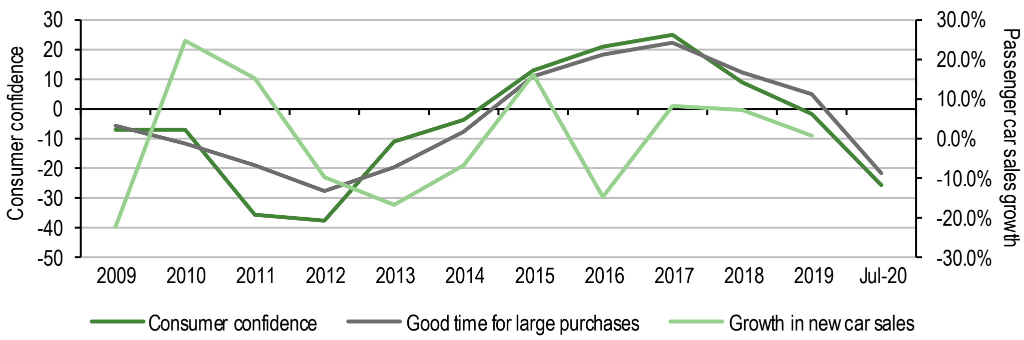
New and used car sales

New and used car sales are mostly driven by consumer confidence for large purchases, as measured by the Dutch statistics office Centraal Bureau voor de Statistiek (CBS, see graph below). Consumer confidence collapsed on the back of COVID-19, which has resulted in much lower new car sales. On top of that, people started working from home on a large scale, however this effect was partly mitigated by people not being willing to use public transport and therefore switching to cars.

In the first six months of 2020, only one brand reported growth and that was Kia, with its success model the Kia Niro, available in (plug-in) hybrid or EV cross over. For Stern, sales of the important brands such as Mercedes (-27%), Renault (-30%) and Ford (-33%) fell significantly.

On the other hand, the used car market was much more resilient in H120, with sales falling only 1.6% in the first six months to 664,000, according to sector data supplier VWE. In June, the number of used car sales actually increased by 15.5% y-o-y, as consumers looked for alternatives to public transport. However, it is currently unclear if this is a sustainable longer-term trend.

Exhibit 8: Consumer confidence and growth in new car sales



Source: CBS, Bovag, Aumacon

Rental market

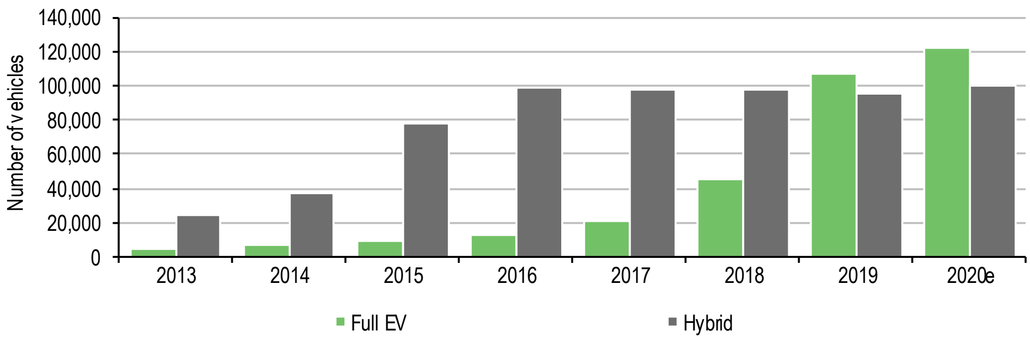
The utilisation of the rental car fleet diminished as well, as mobility decreased in the Netherlands. Up to 50% declines in revenues have been seen in the Dutch rental sector according to sector organisation Bovag. Unlike pure car rental companies such as Hertz, which filed for bankruptcy, Stern can be much more flexible and it has been able to reduce its rental fleet to 1,916 cars by the end of Q2 from 2,574 at the start of the year. Maintenance was also hit due to a lower utilisation of staff, as disease rates were higher.

Electric car market

Internal combustion engines fuelled by gasoline or diesel will probably reach the end of their lives in the coming decades, now that the economics of **electric powered cars** are getting more attractive every year, in a society that in general is becoming more focused on environmentally friendly energy solutions. The Dutch government started to incentivise EVs after the pandemic was declared, with large subsidies (€4,000 for a new car and €2,000 for a used car) and Stern has limited exposure to fully electrical powered cars. In the top selling ranks, electrical and hybrid car models are being introduced and that will have a gradual impact on all segments of the value chain, from a changing dealer landscape to parts selling to maintenance, as EVs require different service for power units and batteries as well as running gear wear parts.

Despite the momentum and noise around these new developments, EV/hybrid car penetration in the Netherlands is still relatively low, at only 222,102 according to Nederlandelectrisch.nl compared a total fleet of roughly 8.7m passenger cars (CBS.nl), or only 2.6%.

Exhibit 9: EV and Hybrid fleet development in the Netherlands



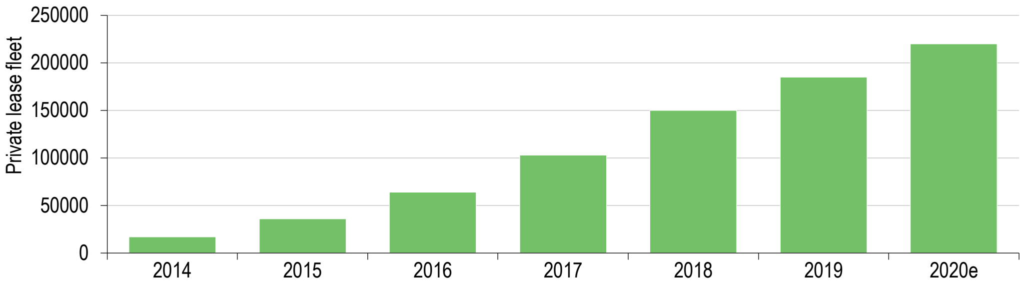
Source: nederlandelectrisch.nl

Lease and car sharing

In a world in which car ownership is becoming less important, especially for the younger population, car sharing concepts and leased cars are getting more popular. Leases already account for over 60% of all new car sales in the Netherlands and margins on lease cars for dealerships are typically lower, as lease companies are able to negotiate large discounts. At the same time, servicing lease cars can be more attractive and that is why having a national coverage network is so important. From the total leased car fleet in the Netherlands of around 1m cars, according to lease company sector organisation Vereniging van Nederlandse Autoleasemaatschappijen (VNA) (of a total passenger car fleet of 8.7m and 915k light commercial vehicles according to CBS), 68% are company leased passenger cars, 15% private leased company cars and 17% light commercial vehicles. While corporate leases have always been dominant in the lease market, private leases are growing fast (see Exhibit 12), driven by low interest rates, which result in the attractive rates that are offered. Lease contracts are based on a fixed duration, a maximum number of kilometres a year and include service at predefined service stations, taxes and insurance and can include fuel as well.

We see car sharing as the smallest of the trends mentioned, as it will be probably more limited to the more urban areas, where availability of shared cars is much higher. Nevertheless, new car buyers are getting older, as younger generations do not really attach value to owning a car and are happy to make use of car share concepts like Car2Go, Greenwheels or even the neighbour’s car (SnappCar).

Exhibit 10: Development of the private lease fleet in the Netherlands



Source: VNA-Lease, ING estimate

H120 results: Weathering the storm

2020 has become an especially challenging year for car dealerships in the Netherlands. Overall, the Dutch new passenger car market showed a decrease of 30% to 158,000 units in H120 compared to H119, while the light commercial vehicle segment recorded a 31% drop in sales to 30,000. On the other hand, used passenger car sales only declined 1.6% to 664,000 vehicles but ended the half year on a much more positive note with a rise of 15.5% to more than 126,000 in June. For the full year, the new passenger car market is expected to decline 21.5% to 350,000 vehicles, according to sector organisations Aumacon and RAI, which implies a year-on-year decrease of 20% in H220.

In these difficult market conditions, Stern surprised positively with an estimated c 19% decrease in new passenger car sales and 33% lower light commercial vehicle sales, despite a dealer network that has closed 10 branches in H219. Nevertheless, the impact from COVID-19 was still very pronounced. All in all, overall revenues declined 12.5% to €382m in H120.

To weather this operational storm, Stern made use of the subsidies the Dutch government supplied for companies with >20% sales impact from COVID-19 under the so-called NOW legislation, which lasts up to October 2020. In total almost €4.9m was provided to Stern, mostly in its Mercedes and Ford dealerships. The government facilities for the later payment of VAT and income tax on wages were also used.

As a result of the use of the government support, operational cash flow has been strong at €46m in H120 (compared to €4.6m in H119). Part of this will reverse in H220 when postponed taxes, of which €29.2m was outstanding at H120, will have to be paid. This is something we see at many Dutch companies.

Maintenance revenues in the Dealergroup segment were lower in H120 as a result of 5% lower staff numbers compared to H119 and COVID-19 related health implications on staff. Nevertheless, efficiency of the workshops, measured in billable hours per available employee, was better and also higher rates for mechanics helped to smooth the decrease. In all, EBIT for the Dealergroup business decreased to €2.6m (excluding goodwill impairment) compared to €5.8m in H119, which we believe is a very strong performance given the top-line decrease.

Mobility Services, mostly rental business, counterintuitively had higher revenues in H1, due to remarketing of cars removed from the rental fleet (from 2,574 at end 2019 to 1,916 at the end of June 2020) being sold within the car dealerships, which offset the large decline in rental activities. As a result of the decline in rent activity, the division reported an EBIT loss of €0.7m compared to a small profit in H119.

The Car Services segment posted 11% lower revenues in H120 and a negative EBIT of €0.4m on the back of the lower car body repair works during the coronavirus outbreak.

At the consolidated level, EBIT from continued activities came in at €4.0m, compared to €4.8m in H119, which we believe is an impressive performance given the market environment, albeit achieved with the government support. In addition, this result was somewhat distorted by a one-off benefit on the revaluation of the 5% stake in car insurer Bovemij of around €4m to €18.5m we expect, partly offset by restructuring costs. In the first six months Stern reduced its staff by 77 from 1,858 full-time equivalent employees at year end 2019.

Stern took an impairment of €20m for all the dealer related goodwill on the balance sheet and also wrote down €1m on used cars. This resulted in Stern posting its biggest reported half year loss of €19m in H120. In the 2019 annual report Stern had mentioned that the headroom in testing the value of goodwill was already limited. The current situation has prompted management to impair goodwill based on more conservative assumptions (a higher WACC and lower results), making the balance sheet more transparent and realistic.

Sensitivities: Consumer behaviour and profitability

Generally speaking, automotive retail is not a structurally growing business in the Netherlands, with an ageing population (older people represent a larger share of new cars) and a relatively well-equipped public transport system. That is also why the market is consolidating and Stern is playing its part in this. Below we discuss a number of risks and sensitivities that the company if facing at the corporate and macro levels.

Consumer confidence dynamics have been very volatile this year against the backdrop of COVID-19. It has always been the most important feature of consumer behaviour, driving large purchases like new cars in the short term. As such, new economic headwinds and prolonged COVID-19 related issues continue to present a significant risk for the industry.

The long-term **EV/hybrid/shared cars** trends that we described above represent a risk for traditional dealerships like Stern. Government incentives, especially related to the pace of the transition towards EVs, but also hybrids, affect the new car market. Furthermore, EVs require less maintenance compared to a regular combustion engine powered car. The shift towards EVs could also lead to a shift towards new car brands that are less covered by dealerships.

Despite a strong balance sheet compared to peers, Stern still has a large **debt position** of €100m at the end of June 2020 (FY19: €140m including Heron). Covenants are related to solvency (>30%, before the impairment on dealer goodwill) and interest cover (EBITDA based interest coverage ratio (ICR) >3) for the €57m bank facilities (not completely drawn), as well as captive financing, which has other terms (more and more related to the loan production of the related car brand at the dealers). The lending rates are mostly based on Euribor with a margin (undisclosed). We see most risk in the interest cover, which could be breached in difficult times like this year. In case of a breach this year we would expect a small waiver fee, given the exceptional environment.

Stern's track record in **profitability** (EBIT margin not exceeding 1.6% in the last 10 years) of the dealer and car service activities is relatively weak. The company's ability to execute on the new strategy, getting to EBIT margins of more than 2%, especially in the current market conditions, represents a challenge. There is a significant element of execution risk attached to a people business like the dealerships. We do believe that risks have come down though, as cost control has been tightened and more centralised.

Lease companies are becoming a more important client group, and with the larger volumes involved they have a strong bargaining position. They are operating in an increasingly competitive environment and will attempt to pass through costs to car dealerships. That said, dealerships like

Stern, which operate on a national scale, should be in a better positioned compared to smaller players.

Valuation

COVID-19 has had a pronounced negative effect on the results and share prices of car dealerships and rental companies worldwide. Combined with the megatrends that we described earlier in the report, such as a growing share of electrical vehicles and more lease and shared car concepts, this would suggest that this is not a very obvious sector to invest in.

Nevertheless, we believe that there clearly is value in the Stern Groep stock. Combustion engine cars will continue to represent the vast majority of the global car fleet at least for the coming decade and car dealerships should have enough time to adapt to the growing share of EVs. A higher share of lease contracts in the market will lead to an intensified need for consolidation on an international basis, as lease companies are already multinational and the possible merger of Hedin and Stern plays well into that.

Given the longer-term forecasting difficulties due to these trends, we believe that a discounted cash flow model is not the right way to reflect the value of a dealership like Stern. We prefer to look at peer multiples and book value. Stern's management has always been focused on realising above book value prices on the divested parts of the portfolio (lease, Heron, buildings) and we expect this approach to remain intact now that Stern is engaged in merger talks with Hedin again. The write-down of the goodwill in the dealerships in H120 has contributed to a more realistic book value of €23.54.

Peer valuation suggests a share price value of €16.6

After the cyclical trough in 2016, Dutch new car sales started to pick up again in 2017 and 2018, followed by a difficult 2019. 2020 was looking better again driven by better consumer confidence until COVID-19 hit. Valuations dropped fast in the face of the pandemic and Stern's share price declined from around €17 to a low of €7.92, but has since recovered to €12.10 at the time of writing.

Looking at Stern's valuation compared to international peers, the stock is trading at a discount on an adjusted P/E ratio with a much larger discount on the price to book ratio. Among other things this could be explained by the fact that Stern's profitability is lower compared to the international peers, especially the Scandinavian peers. However, it should be possible for Stern to achieve or exceed EBIT margins of about 2% if the company successfully implements the restructuring outlined in its Focus on Value strategy. We have not included the full potential effect of this restructuring in our estimates and currently model EBIT margins to gradually recover to 1.9% by 2023 (vs adjusted 0.4% and international peers at about 2% in 2019), therefore remaining below the 2% level.

At the same time, Stern is trading at a 23% premium to peers on FY21e EV/EBITDA (excluding its stake in Bovemij at c €18.5m). That said, while the stock trades at a premium to more geared peers, it is valued at a 18% discount to Kamux, which has a broadly similar conservative balance sheet gearing. Overall, noting the difference in capital structures and quality of the balance sheets of the peer group companies, we consider P/E as a more relevant valuation metric for the sector. As such, applying the average FY21e P/E of the comparable European dealership holdings to our FY21 adjusted net profit estimate of €7.0m and adding the market value of the Bovemij stake (we estimate at €3.17 per Stern share), we arrive at an implied value for Stern of €16.6.

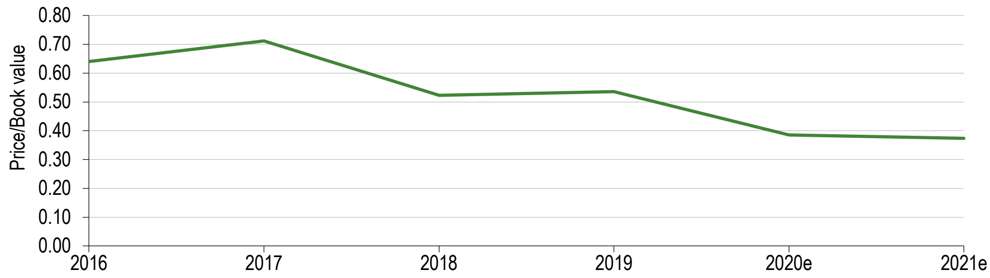
Exhibit 11: Peer group valuation

	Market cap	EV	P/E (x)			P/B (x)			EV/EBITDA (x)		
Company	**€m**	**€m**	**2019**	**2020e**	**2021e**	**2019**	**2020e**	**2021e**	**2019**	**2020e**	**2021e**
Bilia	1,091.1	1,559.0	12.7	12.1	12.4	3.6	3.0	2.7	6.8	7.6	7.7
Kamux	410.2	440.9	21.0	21.6	16.4	4.9	4.4	3.7	12.9	12.4	10.3
Marshall Motors	108.2	272.2	5.1	N/A	8.4	0.4	0.5	0.5	4.5	7.2	5.2
Pendragon	127.5	578.6	N/A	188.0	6.4	0.7	N/A	N/A	4.9	5.5	4.2
Peer average			**12.9**	**73.9**	**10.9**	**2.4**	**2.6**	**2.3**	**7.3**	**8.2**	**6.9**
Stern	68.3	150.3	2.8	9.2	9.8	0.4	0.5	0.5	4.7	10.4	8.4
Premium/(discount)			-78%	-88%	-10%	-81%	-81%	-79%	-35%	27%	23%

Source: Refinitiv Edison Investment Research. Note: Prices at 11 October. Stern's P/E based on adjusted EPS. Stern's net debt is at H120 to account for the recent divestments and does not include the Bovemij stake and leases.

Stern's FY19 P/B amounts to only 0.4x versus 2.4x for the peer group. Compared to the hard-hit UK-listed car retailers Pendragon and Marshall Motors, the P/B ratio of more resilient Stern looks somewhat low. At the same time, the P/B ratios for the Scandinavian car retailers are above 3x. We note that the company has historically been trading at a discount to its book value (see Exhibit 12) and that this discount has been gradually widening over the years. Given the current stage of the economic cycle and the company's relatively conservative and already impaired balance sheet, we believe that the current forward-looking P/BV of around 0.5x might already discount the near-term earnings weakness.

Exhibit 12: P/B values for Stern Groep



Source: Stern Groep, Edison Investment Research

Optionality in Hedin deal

The merger talks between Stern and Hedin Automotive started in January of this year, then were suspended because of COVID-19 and they have restarted recently. The combination, through a reverse takeover, intends to retain and use the Euronext Amsterdam listing as a platform for further growth. Important conditions, like the proposed exchange ratio, are not disclosed yet.

We see added value in this deal for Stern shareholders. Stern is relatively conservatively financed (Stern's solvency ratio is 27% vs 11% for Hedin in FY19) and has the stock exchange listing that can be used for further growth, while Hedin has much bigger scale (roughly 2.5x Stern's sales), an attractive position in smaller countries in Europe (Sweden, Norway, Belgium and Switzerland) and could potentially add complementary brands like BMW and Porsche. By forming a large combination with leading positions, especially in smaller countries, Hedin and Stern should be better positioned to play into the numerous trends and developments that are shaking up the automotive retailer world. Moreover, the car market is becoming an international market.

We note that Stern's CEO, Mr. van der Kwast, who also is a 12% shareholder, has always focused on realising at least the intrinsic or book value for the assets that the company divests. For example, the real estate and lease activities were sold last year for €89m, realising a book profit of

€31m. As such, Stern's well impaired net asset value per share of €23.54 at H120 could represent a support in the ongoing discussions with Hedin.

Financials

The most important factor in Stern's profit and loss accounts are **Dealergroup** results, as they also carry the bulk (~95%) of revenues. As we have explained before, achieving 2% EBIT margins should be possible in this division, but due to a variety of reasons, ranging from WLTP related issues to the Diesel scandal and internal reasons like a structurally loss making Mobility business that now has been sold and also an end market that has not been supportive, this margin has been out of reach recently (2019: 0.6%).

Gross margins on new and used cars are very tight (4–6%) and with a large network in place, operating costs are relatively high. Stern does not disclose gross margins per division and we have therefore had to make our own assumptions. Getting operating costs down and increasing utilisation rates of the mechanics in the workshops are key to achieving higher margins in the Dealergroup division and we have seen a lot of work in the last two years to improve on both accounts. We estimate that operating expenses have come down from over €140m in 2018 to around €110m this year, although that is of course also due to the divestment of Heron (roughly €100m turnover) and the help of government support (emergency law to help COVID-19 affected companies).

For **Mobility Solutions**, the track record in the new formation without the lease business is limited, but we do believe that EBIT margins of c 5% should be possible in this part of business. For Stern, we have pencilled in 3% margins in 2022 compared to a slightly negative EBIT in 2020, due to the large COVID-19 related decrease in revenues. In our estimates for this segment we assume gross margins of c 10% and a decreasing opex percentage on revenues as costs are expected to be relatively stable while revenues should gradually increase from the low level of FY20. For **Car Services**, we estimate EBIT margins of 3% as well, with a lower result this year.

Group costs (labelled other) are pretty stable at around €2m, but includes one offs and revaluations of Bovemij, which makes the final results very volatile. For this year we expect a positive result due to the revaluation of Bovemij, partly offset by some one-off costs related to restructuring.

All in all, we expect Stern to report 18% lower revenues of €816m in FY20, driven by lower new car sales in H120 and some normalisation of revenues in H220. Adjusted EBIT before one-off items is forecast to come in at €7.5m, compared to €5.5m in 2019 (H120: €4.8m), thanks to the implemented restructuring measures, government support and cost control. One-off items in 2020 include the write down of all goodwill from the dealerships of €20m, €1m on used cars, an appreciation in the book value of Bovemij by €4m and one-off costs that we estimate at around €1m related to restructuring. We expect a reported net loss of €11m.

For 2021, we expect a rebound in group revenues to €0.9bn, as the effects of COVID-19 reverse and a return to €1bn revenues by 2023. EBITDA and EBIT should benefit significantly from the improvements in the dealer model and we expect that a 1.3% EBIT margin should be possible by 2021, increasing to 1.9%, or €18m in normalised EBIT, by 2023. Reported net profit should be able to increase to €11.6m by 2023, reversing a forecast net loss of €11m in 2020.

Exhibit 13: Consolidated Stern P&L

Year end 31 December, €m	FY16	FY17	FY18	FY19	FY20e	FY21e	FY22e	FY23e
Revenue	1,096.9	1,124.5	988.7	989.3	815.5	922.8	955.9	987.9
Cost of Sales	(907.9)	(934.2)	(812.3)	(816.5)	(681.8)	(770.3)	(795.8)	(819.9)
Gross Profit	189.0	190.3	176.4	172.8	133.7	152.5	160.1	167.9
EBITDA	26.7	20.5	6.1	48.9	14.4	17.8	21.0	24.3
Normalised operating profit	16.5	11.4	(1.7)	4.0	7.5	12.3	15.3	18.3
Amortisation of acquired intangibles	0.0	0.0	(0.1)	(0.1)	-20.1	0.0	0.0	0.0
Reported operating profit	18.7	12.7	(1.5)	2.7	(10.5)	12.3	15.3	18.3
Net Interest	(3.4)	(3.3)	(4.1)	(6.9)	(4.5)	(4.5)	(4.5)	(4.5)
Net Interest	(3.4)	(3.3)	(4.1)	(6.9)	(10.5)	12.3	15.3	18.3
Profit Before Tax (norm)	13.1	8.1	(5.8)	(1.4)	3.0	7.8	10.8	13.8
Profit Before Tax (reported)	15.3	9.4	(5.6)	(4.2)	(15.0)	7.8	10.8	13.8
Reported tax	(4.0)	(1.9)	1.7	3.0	4.4	(0.8)	(1.5)	(2.2)
Profit After Tax (norm)	9.1	6.2	(4.1)	1.6	7.4	7.0	9.3	11.6
Profit After Tax (reported)	11.3	7.5	(4.0)	(1.2)	(10.6)	7.0	9.3	11.6
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	4.5	22.6	0.0	0.0	0.0	0.0
Net income (normalised)	9.1	6.2	0.4	24.2	7.4	7.0	9.3	11.6

Source: Stern Groep, Edison Investment Research

Dealer division almost back to 2019 revenues by 2023

In the Dealer division, we expect new passenger car sales to rebound 19% to €370m in 2021 following a 21.5% decline in 2020, which is broadly in line with the market estimates of sector organisations RAI and Aumacon for these years. Light commercial vehicles are expected to rebound more moderately following the 25% decrease that we factored in for 2020 (31% drop in H120) and in light of the still fragile economic environment. We expect a more moderate recovery in revenues of 10% in 2021 for this division. Overall, we expect used car sales to be more resilient with an expected decrease of 5% in 2020 and an expected 4.5% increase in 2021. For the years ahead we expect moderate growth towards the 2019 level of €1bn sales again.

Maintenance/workshop results have taken a hit from high sickness leave levels of staff in H1 and we estimate this will lead to a 5% decrease in FY20 revenues. Next year, we expect a return to the 2019 revenue levels, as we do not expect Stern to further reduce workshop staff and demand is more stable in this part of the business. We expect a similar performance in the Parts business.

In terms of gross margins we estimate a somewhat lower profitability in 2020 compared to 2019, as the effects of remarketing of former rental cars were not fully offset by the mix effect of relatively higher workshop revenues. In 2021, we expect an increase in gross margins due to these mix effects. Operating expenditures are expected to come down to €110m from the estimated €135m in 2019, driven by restructuring and the NOW government support. All in all, adjusted EBIT for the dealer division is expected to be €7.3m in 2020, before the amortisation of goodwill, gradually increasing to €17m by 2023.

Exhibit 14: Dealer results

Dealers (€m)	FY17	FY18	FY19	FY20e	FY21e	FY22e	FY23e
Gross Revenues	1119	1113	1075	806	907	932	958
Growth	12%	8%	-3%	-25%	12%	3%	3%
Gross margin	145	145	141	105	120	124	128
Opex estimate	-141	-141	-135	-98	-107	-109	-111
EBIT	4.9	3.2	5.5	7.3	12.7	14.9	17.2
EBIT margin	0.4%	0.3%	0.5%	0.9%	1.4%	1.6%	1.8%
Revenue segmentation							
Passenger cars	493	482	443	311*	370	377	385
- growth	10.3%	-2.1%	-8.2%	-21.5%	19.0%	2.0%	2.0%
Company vehicles	151	154	175	118*	138	142	146
-Growth	0.2%	2.3%	13.2%	-25.0%	17.0%	3.0%	3.0%
-Used cars	277	273	257	213*	222	229	236
-Growth	-4.8%	-1.5%	-5.7%	-5.0%	4.5%	3.0%	3.0%
Total cars	921	910	875	641	730	748	767
-Growth	3.6%	-1.2%	-3.8%	-26.7%	13.8%	2.5%	2.5%
-Maintenance	86	90	89	74*	81	85	90
-Growth	3.5%	4.4%	-1.3%	-5.0%	10.0%	5.0%	5.0%
-Parts	112	113	111	91*	96	99	102
-Growth	0.3%	0.7%	-1.6%	-7.0%	5.0%	3.0%	3.0%
Total revenues	1119	1113	1075	806	907	932	958

Source: Stern Groep Edison Investment Research; *FY19 numbers adjusted for Heron divestment

Mobility Solutions

After the divestment of the lease activities in 2019, rental services are the bulk of revenues in Mobility Solutions. As such we only present the adjusted numbers from 2018 in Exhibit 18.

In 2019, revenues in this division increased almost 20% to €55m, based on a higher number of sold rental days per car and a higher number of rental cars. In H120 revenues increased 4% to €29.2m, much better than the Dutch rental market, which collapsed by roughly 50% according to sector organisation Bovag. As a combined rental/dealership company, Stern's top line in this division benefited from the effect of vehicle remarketing: over 600 cars were taken out of the rental fleet (fleet went down from 2,574 in FY19 to 1,916 cars at H120) and sold through the Dealergroup division. The rental fleet will increase again in H220 according to the company, but the effect of remarketing will disappear.

We expect Stern Rent to start to reap the benefits from its SLA agreement with ALD in H220, in the shape of replacement transport for lease contracts. Pure rental activities had roughly €10m turnover in H120 and we expect a somewhat higher number for H220 now the market is normalising and assuming there are no further effects from remarketing. By 2021, the rental fleet should be getting back to normal levels on the back of the economic recovery and we have therefore pencilled in a recovery of revenues, which should continue in 2022, when we expect the rental fleet to return to pre COVID-19 levels again.

We assume a gross margin at around 10% in this segment and lower opex mostly driven by the restructuring and cost control. We do not expect capacity expansions in the coming years for this division, as we assume that there is enough capacity to absorb growth in the coming years. As a result of forecast stable gross margins and opex of about €4.4–4.6m per annum, EBIT margins should be able to recover to 3% by 2022 from 1.2% in 2019.

Exhibit 15: Mobility Solutions	FY18	FY19	FY20e	FY21e	FY22e	FY23e
Rental cars fleet (x)	2,638	2,767	2,075	2,594	2,853	2,996
Revenue per car (€)	17,266	19,693	20,332	20,738	21,153	21,576
Sold rental days (x)	728,151	756,000	567,000	708,750	779,625	818,606
Rental revs per day (€)	33	33	33	34	35	36
Total revenues (€m)	45.5	54.5	42.2	53.8	60.4	64.6
- growth (%)	-29.5%	19.6%	-22.6%	27.5%	12.2%	7.1%
EBIT (€m)	0.2	0.6	-0.2	0.8	1.8	1.9
EBIT margin (%)	0.5%	1.2%	-0.5%	1.5%	3.0%	3.0%

Source: Stern Groep, Edison Investment Research

Car Services & Group

Car Services, the smallest division in Stern's operations, has undergone a significant transformation in recent years. The restructuring from a general maintenance group towards a network of car repair locations (working for lease companies and insurers) has resulted in losses in 2017–18.

In the coming years, we expect turnover growth due to the network expansion and a stable cost base thanks to the cost cutting. However, 2020 will be affected by COVID-19 as lower population mobility (fewer kilometres driven in the Netherlands) results in a smaller number of accidents. After a turnover decrease of 10% in H120 we expect a slightly more pronounced reduction in H220 (as January and February were still relatively strong). For 2021 and 2022, we expect growth to accelerate, partly driven by the SLA with ALD (oil refreshing, winter/summer tyre changes, bodywork repairs for lease cars) but also market recovery as much repair work has been postponed in the current economic environment.

Exhibit 16: Car Services and Group

Car Services (€m)	FY17	FY18	FY19	FY20e	FY21e	FY22e	FY23e
Gross revenues	33	36	35	31	35	38	42
- growth (%)	-9.3%	8.7%	-0.5%	-11.0%	10.0%	10.0%	10.0%
EBIT	-1.0	-0.7	0.2	-0.3	1.0	1.1	1.3
EBIT margin (%)	-3.1%	-1.9%	0.6%	-1.0%	3.0%	3.0%	3.2%
Group costs	-3.2	-4.4	-3.7	1.1	-2.2	-2.2	-2.2

Source: Stern Groep and Edison Investment Research

Cash flows affected by COVID-19 related items

After the divestment of the lease activities in 2019, Stern's cash flow profile has changed dramatically in terms of financing and investment cash flows as lease fleet expansion was financed through loans, as well as operational cash flows through the relatively high lease margins and depreciation of lease cars.

On top of that, COVID-19 distorts the 2020 cash flow performance significantly with negative COVID-19 effects in car sales and rental revenues partly offset by the positive effects from deferred VAT and income tax payments and other government support. However, visibility is low because of the changing business model and the ongoing coronavirus impact on the economy and business.

For this year, we expect a large positive operating cash inflow of €35m due to positive working capital movements, government support and positive cash flow generation from operating activities (the expected reported net loss for this year is caused by the impairment on the dealer group assets). In FY21, we expect a reversal with a slightly negative operational cash flow (€2m) as working capital reverts to more normal levels. We expect the company to pay out c €5m in dividends in the coming two years. After paying out €3.50 interim dividend per share in 2019, we expect a reduced dividend of €0.39 per share to be paid for 2020, rising to €0.49 in 2021.

Overall, based on our operating and financial assumptions, we expect cash flows to recover gradually in the next few years, driven by the improving operating margins, which will be partly offset by negative working capital effects as the tax benefits from government support measures

A smaller and simplified balance sheet

Stern's balance sheet has decreased significantly in size in the last few years, mostly driven by the divestment of the lease activities and the accompanying lease financing, as well as the much smaller divestment of Heron this year. At the end of 2018, Stern's total assets on the balance sheet were €675m and by H120 this fell to €470m.

Goodwill has disappeared almost completely with the impairment of all goodwill of previously acquired dealerships. Together with the divestment of the lease business, this makes the balance sheet much more simple and easier to interpret.

At H120, Stern's fixed assets on the balance sheet are tangible fixed assets of €108m (buildings owned and rental cars mostly) and of course stock of €165m (cars). Furthermore, there is a tax asset of around €11m, related to losses in the past that can be offset against future taxable income and a mark-to-market value of over €18m of the 5% stake in insurer Bovemij. The (rental) cars and buildings are financed by interest bearing debt of €99.7m and captive financing of €97m (under creditors). The working capital position is more or less neutral. Furthermore, there are now lease assets of €106m (mostly rented buildings under IFRS 16), which are almost fully offset by €112m lease liabilities (also IFRS 16).

All this results in a book value of equity after the recent reduction of goodwill of €23.54 per share, compared to €26.90 at FY19. We believe this book value is a pretty fair reflection of the value, as it is just cars and buildings on the asset side of the balance sheet.

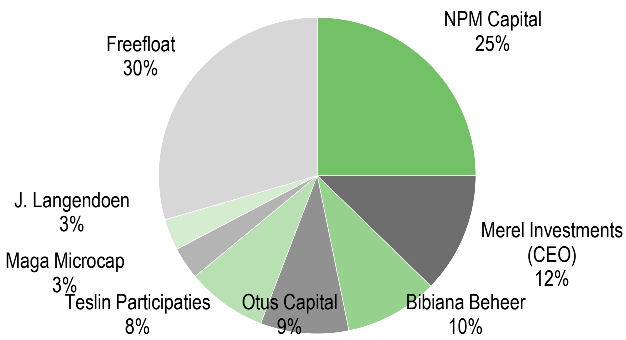
At H120, Stern had net debt of €82m on a pre-IFRS 16 basis, including €12.5m in cash. In addition, the company had €112m in lease liabilities on its balance sheet. The reported net debt position was complemented by the largely undrawn bank facility of €60m. However, given that Stern has made use of the option to postpone tax payments for €29.2m in H120 and by July these have been paid, part of this bank facility has likely been drawn down.

Covenants for the bank facilities are related to solvency (>30%, before the impairment on dealer goodwill) and interest cover (EBITDA based ICR >3). The captive financing has other terms (more and more related to the loan production of the related car brand at the dealers). The lending rates are mostly based on Euribor with a margin (undisclosed). We see most risk in the interest cover, which could be breached in difficult times like this year. In the case of a breach, we would expect a small waiver fee, given the current exceptional economic environment.

Shareholders

Stern has had a very stable shareholder base in the last years and the free float is only 29.5%. Private equity company NPM Capital has been a longstanding shareholder, as well as family office Teslin Participaties and Mr Frits van Delft (Bibiana Beheer). Otus Capital and Maga Microcap are more recent major shareholders. Otus Capital also manages Maga Microcap fund and is a London-based investment house, specialised in small caps.

Exhibit 17: Stern's shareholders

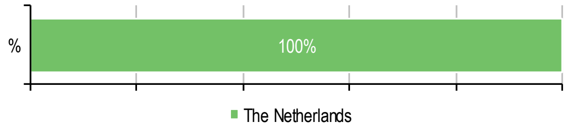


Source: Autoriteit Financiele Markten (AFM)

Exhibit 18: Financial summary

	2018	2019	2020e	2021e
Year end 31 December	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT				
Revenue	988.7	989.3	815.5	922.8
Cost of Sales	(812.3)	(816.5)	(681.8)	(770.3)
Gross Profit	176.4	172.8	133.7	152.5
EBITDA	6.1	47.4	14.4	17.8
Normalised operating profit	(1.7)	5.5	7.5	12.3
Amortisation of acquired intangibles	(0.1)	(0.1)	0.0	0.0
Exceptionals	0.2	(1.3)	(18.0)	0.0
Reported operating profit	(1.5)	2.7	(10.5)	12.3
Net Interest	(4.1)	(6.9)	(4.5)	(4.5)
Profit Before Tax (norm)	(5.8)	(2.9)	3.0	7.8
Profit Before Tax (reported)	(5.6)	(4.2)	(15.0)	7.8
Reported tax	1.7	3.0	4.4	(0.8)
Profit After Tax (norm)	(4.1)	1.6	7.4	7.0
Profit After Tax (reported)	(4.0)	(1.2)	(10.6)	7.0
Minority interests	0.0	0.0	0.0	0.0
Discontinued operations	4.5	22.6	0.0	0.0
Net income (normalised)	0.4	24.2	7.4	7.0
Net income (reported)	0.5	21.3	(10.6)	7.0
Average number of shares outstanding (m)	5.68	5.68	5.68	5.68
EPS	0.09	3.76	(1.86)	1.23
Normalised EPS	(0.73)	0.29	1.31	1.23
DPS	0.00	3.50	0.39	0.49
Revenue growth (%)	-12.1	0.1	-17.6	13.2
Gross Margin (%)	17.8	17.5	16.4	16.5
EBITDA Margin (%)	0.6	4.9	1.8	1.9
Normalised Operating Margin	-0.2	0.4	0.9	1.3
BALANCE SHEET	**2018**	**2019**	2020	2021
Fixed Assets	391.8	278.6	285.9	287.7
Intangible Assets	30.6	22.4	22.3	22.3
Tangible Assets	343.1	243.5	250.9	252.7
Investments & other	18.1	12.7	12.7	12.7
Current Assets	283.6	294.8	223.9	234.0
Stocks	237.6	201.4	163.1	184.6
Debtors	35.3	41.7	32.6	32.3
Cash & cash equivalents	0.7	0.7	20.8	8.8
Other	10.0	51.0	7.3	8.3
Current Liabilities	272.6	271.7	223.5	230.9
Creditors	139.9	97.4	100.9	104.0
Short term borrowings	93.9	90.0	90.0	90.0
Other	38.8	84.3	32.6	36.9
Long Term Liabilities	247.6	149.1	146.5	146.8
Long term borrowings	244.0	49.7	49.7	49.7
Other long term liabilities	3.6	99.4	96.8	97.1
Net Assets	155.2	152.6	139.8	144.0
Minority interests	0.0	0.0	0.0	0.0
Shareholders' equity	155.2	152.6	139.8	144.0
CASH FLOW				
Op Cash Flow before WC and tax	52.6	11.9	(8.2)	12.9
Working capital	(0.9)	(8.3)	42.9	(14.7)
Net operating cash flow	51.6	3.6	34.6	(1.9)
Capex	(81.6)	26.6	(12.2)	(7.4)
Dividends	(4.3)	(19.9)	(2.2)	(2.8)
Other	33.7	(10.4)	0.0	0.0
Net Cash Flow	(0.5)	(0.1)	20.2	(12.0)
Opening net debt/(cash)	302.9	337.1	139.0	118.9
Closing net debt/(cash)	337.1	139.0	118.9	130.9

Source: Stern Groep, Edison Investment Research

Contact details	Revenue by geography
Pieter Braaijweg 6 1114 AJ Amsterdam Netherlands +31-882929701 www.stern.nl	

Management team

CEO: Henk van der Kwast

After a career in banking and corporate finance, Mr van der Kwast became an entrepreneur in 1993, with the acquisition of a loss-making Opel dealer. Over the years, he has built the company to the second largest car dealership in the Netherlands.

Principal shareholders	(%)
NPM Capital	25.0
Merel Investments	12.3
Bibliana Beheer	9.5
Teslin	8.2
Otus	9.0
Maga Microcap	3.3
J.Langendoen	3.2

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