VIEWPOINT

Northmarq

Bonus Round for the Car Wash Sector?

How Bonus Depreciation and Interest Rates Could Impact Deal Making After a Wild Start to 2025

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After a recent whirlwind of news including a major bankruptcy, a large M&A transaction and meaningful guidance from POTUS regarding the future of bonus depreciation, investors are gearing up for what could be an active year ahead in the car wash space.

In the four weeks between February 5 and March 4, 2025, the car wash market was rocked by these and other notable events that will shape the landscape for deal making in 2025. In this analysis, we break down each of these events and provide our outlook for transaction activity and pricing in the merger and acquisition (M&A), net lease real estate and sale-leaseback markets.

Recent Car Wash News

- **February 5, 2025:** ZIPS Car Wash, the fifth largest car wash operator in the U.S. with more than 260 units, filed for voluntary Chapter 11 bankruptcy protection. This marks the first major bankruptcy in the car wash space and has materially impacted ZIPS' landlords.

- **February 19, 2025:** Mister Car Wash (NASDAQ: MCW) held their fourth quarter earnings call. Notably, MCW announced they will only seek to raise around $50 million from sale-leaseback transactions this year, down from nearly $130 million raised in 2024. Given this guidance, we expect to see roughly 10 new sale-leasebacks offered from MCW this year.

- **February 25, 2025:** Driven Brands (NASDAQ: DRVN) announced the sale of their U.S. car wash platform, Take 5 Car Wash with 385 units, to Whistle Express Car Wash for $385 million. The sale price represents a multiple of about 8x on more than $50 million of EBITDA.

- **March 4, 2025:** In a joint address to Congress, President Trump announced his desire to reinstate "100% expensing" – also known as 100% bonus depreciation – as a part of his tax plan. Bonus depreciation benefits have historically provided a key tailwind for car wash investors since 2017.

Bonus Depreciation Outlook

On March 4, President Trump announced his desire to reinstate 100% bonus depreciation in his tax plan. He also proposed a retroactive application of 100% bonus depreciation benefits to January 20, 2025. This would make any car wash purchased after that date eligible for 100% bonus depreciation if the plan is implemented as proposed.

The car wash community breathed a collective sigh of relief upon this announcement. Bonus depreciation benefits have provided an extraordinary tailwind for both car wash operators and real estate investors since the passing of the Tax Cuts and Jobs Act (TCJA) in 2017.

The comprehensive tax plan still needs to be passed by Congress but given that the reinstatement of 100% bonus depreciation is a top presidential priority, and with the Republican-controlled Congress remaining highly supportive of the administration's agenda, we expect that the return of 100% bonus depreciation is very likely in 2025. Speaker of the House, Mike Johnson, is pushing Congress to pass a broad reconciliation bill that includes direction on tax policy by late spring. We will be keeping a keen eye on Congress in anticipation that a formal announcement about 100% bonus depreciation will be coming soon.

If 100% bonus depreciation returns, it will have a measurable impact on the car wash market. M&A and greenfield development opportunities will start to make more economic sense for operators, and real estate investors searching for net lease car wash investments to offset tax liabilities will have further motivation to enter the market. We have already seen heightened demand from real estate investors looking for net lease car wash assets in anticipation of 100% bonus depreciation's return. If a formal announcement is made, we expect real estate investor demand to skyrocket in the second half of the year, which already tends to be the most active season for tax-motivated car wash buyers. Historically, nearly 70% of all net lease car wash transactions have occurred in third and fourth quarters.

Overall, this is a very positive development for sellers. A larger and more motivated pool of tax-driven buyers should improve liquidity for both M&A and net lease deals and could help drive cap rates lower and multiples higher. The direction of interest rates and the inventory of available car wash deals will also impact cap rates and multiples, but the return of 100% bonus depreciation will undoubtedly contribute to overall market health if it is ultimately reinstated.

TCJA Bonus Depreciation Schedule

Year Placed in Service	Bonus Depreciation Rate
2018-2022	100%
2023	80%
2024	60%
2025	40%
2026	20%
2027 and Beyond	0% or TBD

*As tax code is currently written. If implemented, President Trump's proposal would make all car washes purchased after January 20, 2025 eligible for 100% bonus depreciation for at least the remainder of 2025.

Interest Rate Outlook

The second key factor that will impact the direction of both cap rates and multiples is interest rates. As of April 1, the U.S. 10-year Treasury note reflected a yield of 4.17%, down 62 basis points from its 2025 high of 4.79% in early January. There is no broad consensus among economists and rate watchers about the ultimate direction of interest rates given the extreme uncertainty around how President Trump's broader economic policies will impact things like inflation and economic growth.

However, one thing is certain. President Trump and Treasury Secretary Scott Bessent are deeply concerned with the 10-year rate and have explicitly stated in recent speeches and interviews that they want to see lower rates in the immediate term.

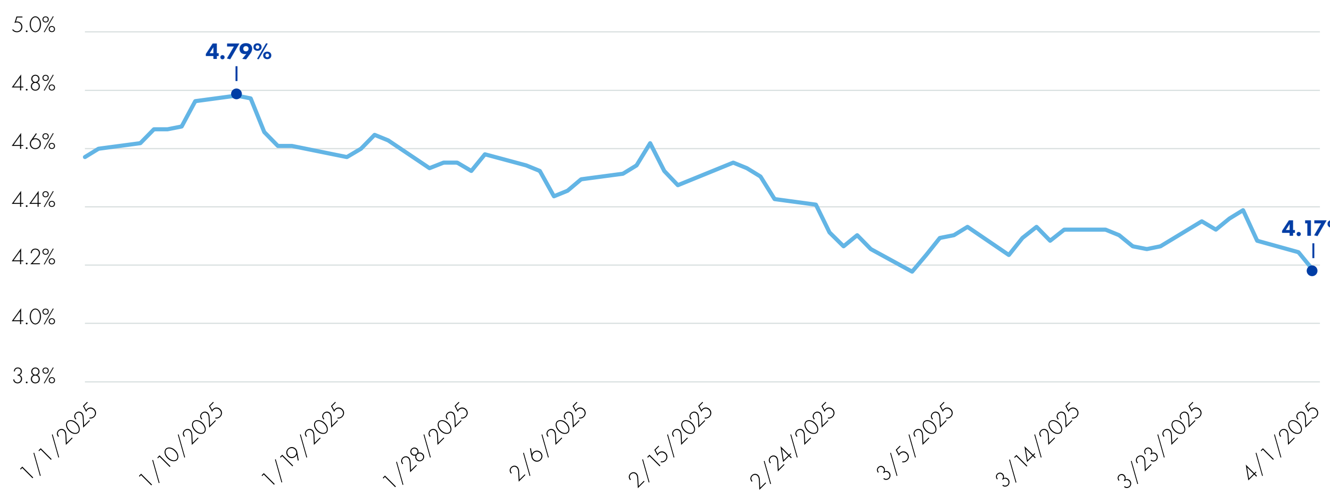
Some Wall Street rate strategists, including those at Barclays and Royal Bank of Canada, have recently lowered their year-end 10-year yield forecasts on the back of this messaging. Subadra Rajappa, head of U.S. rates strategy at Societe General, recently cut her year-end 10-year yield forecast to 3.75%.

If interest rates push lower, it will undoubtedly fuel demand for both M&A deals and net lease assets. We saw a dramatic uptick in demand for net lease car washes when the 10-year rate sunk below 4.00% between August and October of 2024. If we experience a sustained period of rates below 4.00% again, we expect a similar level of demand to emerge – demand that could be further bolstered by the return of 100% bonus depreciation.

While it is not guaranteed that rates will continue their decline in the months ahead, if we do experience lower rates, we anticipate increased deal liquidity and an eventual decrease in cap rates, though the speed of the move in cap rates will be somewhat determined by overall inventory.

U.S. 10-Year Treasury

January 1, 2025 to April 1, 2025



Source: Board of Governors of the Federal Reserve System

Inventory Outlook

On February 19, Mister Car Wash reported fourth quarter earnings and provided guidance for 2025. Our most important takeaway from the earnings call relates to the sale-leaseback market. MCW announced that they intend to raise roughly $50 million in proceeds from sale-leaseback transactions in 2025. That translates to approximately 10 deals given the average sale price for MCW sale-leasebacks last year was about $4.6 million. This number is down significantly from the nearly $130 million that MCW generated via approximately 30 sale-leaseback transactions in 2024.

Mister Car Wash being less active in the sale-leaseback market in 2025 should bode well for all other net lease car wash deals in the year ahead. Mister Car Wash has been extremely successful in leveraging their status as the perceived benchmark credit in the car wash space and has attracted significant demand from tax-motivated investors looking for car wash sale-leasebacks over the past two years – often at the expense of other net lease deals in the marketplace. Mister Car Wash has completed roughly 30 sale-leaseback transactions in each of the last two years, so investors have had plenty of inventory to choose from. With fewer Mister Car Washes available in 2025, that should push investors to other deals.

Includes net lease fee simple listings only

We have recently seen a decrease in net lease car wash inventory overall. As of mid-March, we counted 112 available net lease car washes, down from a high of 181 in December 2024.

While inventory is lower for now, we do expect new deals to enter the market as the year goes on. However, we are optimistic that improved market conditions and increased liquidity supported by 100% bonus depreciation and lower rates will help the market absorb both legacy and new inventory significantly better than it has in the past two years.

M&A Outlook

On February 25, Driven Brands announced a definitive agreement for the sale of their U.S. car wash platform, Take 5 Car Wash with 385 units, to Whistle Express Car Wash for $385 million. The sale price represents a roughly 8x multiple on more than $50 million of in-place EBITDA. The transaction is set to close in second quarter 2025 and includes a $130-million seller-financing note. Whistle Express is rumored to be executing a large sale-leaseback of Take 5 real estate in conjunction with the M&A deal – proceeds from which would contribute to the acquisition capital stack.

Whistle Express, backed by Oaktree Capital which acquired a majority stake in Whistle last July, has suggested that it will rebrand and integrate all Take 5 sites to the Whistle Express platform. However, there is speculation that Whistle Express will look to strategically divest from certain markets over time. It remains to be seen if Whistle Express will entertain divestitures, but various market participants certainly welcome the opportunity to make strategic acquisitions if Whistle does in fact look to shed assets in the future.

Most operators that we have spoken with this year expressed their desire to grow via M&A even before the Whistle/Take 5 announcement. The potential opportunity to acquire former Take 5 locations, as well as ZIPS locations as they work through their bankruptcy restructure, has only heightened operators' interest in M&A and in sourcing the capital necessary to execute opportunistic deals.

Overall, we have seen multiples in the range of 7x to 11x for M&A deals that we are directly involved in. It will be interesting to see how the potential increase in available M&A inventory impacts multiples if a number of Take 5 and ZIPS sites do become available.

Several operators of various sizes have been exploring sales in recent months. For example, it was announced on January 22 that Spotless Brand, a 200+ unit operator, is working with financial services firm William Blair to source buyers at a valuation of almost $3 billion. If we see improvements on both the bonus depreciation and interest rates fronts, we could see a significant uptick in M&A activity going forward as transactions become more financeable.

ZIPS Bankruptcy Update

On February 5, ZIPS Car Wash filed for voluntary Chapter 11 bankruptcy protection. This marks the first major bankruptcy in the car wash space, and the event has materially impacted many, including ZIPS' landlords. ZIPS' stated reasons for the bankruptcy filing include:

- Substantial debt obligations of more than $650 million
- Macro headwinds, including higher interest rates and labor costs
- Competitive pressures, as more than 900 new car wash locations have opened annually in each of the past five years
- Burdensome lease obligations

As a part of ZIPS' restructuring effort, the company has hired Hilco Real Estate as a real estate advisor charged with renegotiating in-place leases with landlords. At the time of publication, landlord negotiations were still ongoing. In the initial filing, ZIPS had proposed rejecting 39 leases by March 31 – however, it appears not all 39 leases were rejected. We have heard from landlords that some lease rejection dates have been postponed to April 30. ZIPS' final rejection list may be vastly different from the initial proposal. If ZIPS rejects a lease, it is assumed that they will vacate the subject property soon after the rejection notification.

April 10 may be an important date for landlords and other stakeholders. That date was announced at ZIPS' March 18 bankruptcy hearing as the creditor voting deadline for approval of the provisional restructuring plan. We presume that most landlord negotiations will be completed by this deadline, although that is not certain. ZIPS' next formal bankruptcy hearing will be held on April 18, and we expect that there will be at least some further guidance regarding landlords, lease rejections and ZIPS' overall restructuring plan at that time.

In its initial filing, ZIPS anticipated emerging from Chapter 11 protection in two to three months' time, and while it seems that ZIPS is generally on pace to meet that deadline, the situation remains nebulous for many stakeholders. Regardless of how the company ultimately restructures, there will be several landlords left holding materially devalued assets either in the form of vacant properties, renegotiated leases with lower monthly rent payments or shorter lease terms.

While the ZIPS situation is extremely unfortunate, we do not see this event as a symptom of broader weakness in the car wash sector. ZIPS simply overextended themselves in the pursuit of scale in an environment where growth for growth's sake was seen by some as the paramount goal. To some degree, Take 5 Car Wash was guilty of this overextension as well, and thereby finds itself in new hands following the Whistle Express acquisition.

Most car wash operators have taken a more disciplined approach to growth. In our view, recent events reflect a necessary and typical correction for an industry that has grown at lightning speed over the past five years. We expect that both ZIPS and the broader industry will emerge stronger for it as the car wash space continues to mature into a highly investable asset class.

Final Thoughts

While the market is still absorbing the full impact of the ZIPS Car Wash bankruptcy filing and the Whistle Express Car Wash acquisition of Take 5 Car Wash, we feel the potential return of 100% bonus depreciation and the overall trajectory of interest rates will be the most important drivers of demand and transaction flow going forward in 2025, particularly in the net lease and sale-leaseback arenas.

A lot has happened, and a lot more is still to come as it relates to the broader car wash universe. But generally, we feel the overall market outlook is perhaps as positive as it has been since 2021. There is a reasonable chance that 2025 could be the busiest year for car wash transactions ever. We look forward with optimism for what appears to be an active year ahead in this dynamic and rapidly evolving industry.

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