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# EDITED TRANSCRIPT

## GPI - Q3 2012 Group 1 Automotive Earnings Conference Call

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**OVERVIEW:**

GPI reported 3Q12 consolidated revenues of $2b, net income of $31.3m and earnings per diluted common share of $1.32.





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## CORPORATE PARTICIPANTS

**Pete DeLongchamps** *Group 1 Automotive Inc - VP, Financial Services and Manufacturer Relations*

**Earl Hesterberg** *Group 1 Automotive Inc - President and CEO*

**John Rickel** *Group 1 Automotive Inc - SVP and CFO*

## CONFERENCE CALL PARTICIPANTS

**John Murphy** *BofA Merrill Lynch - Analyst*

**Rick Nelson** *Stephens Inc. - Analyst*

**Ravi Shanker** *Morgan Stanley - Analyst*

**Patrick Archambault** *Goldman Sachs - Analyst*

**Simeon Gutman** *Credit Suisse - Analyst*

**James Albertine** *Stifel Nicolaus - Analyst*

**Matt Nemer** *Wells Fargo Securities, LLC - Analyst*

**Brett Hoselton** *KeyBanc Capital Markets - Analyst*

## PRESENTATION

**Operator**

Good morning ladies and gentlemen, and welcome to the Group 1 Automotive' s third quarter earnings conference call.

(Operator Instructions)

Please also note that today's event is being recorded. At this time, I would like to turn your conference call over to Mr. Pete DeLongchamps, Vice President of Financial Services and Manufacturer Relations.

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**Pete DeLongchamps** - *Group 1 Automotive Inc - VP, Financial Services and Manufacturer Relations*

Thank you Jamie, and good morning everyone, and welcome to today's call. Before we begin I would like to make some brief remarks about forward-looking statements and the use of non-GAAP financial measures.

Except for historical information mentioned during the conference call, statements made by Management of Group 1 are forward-looking statements that are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve both known and unknown risks and uncertainties, which may cause the Company's actual results in future periods to differ materially from forecasted results. Those risks include, but are not limited to, risks associated with pricing, volume, and the conditions of markets. Those and other risks are described in the Company's filings with the Securities and Exchange Commission over the last 12 months. Also, copies of these filings are available from both the SEC and the Company.

In addition, certain non-GAAP financial measures, as defined under SEC rules, may be discussed on this call. As required by applicable SEC rules, the Company provides reconciliations of any such non-GAAP financial measures to the most directly comparable GAAP measures on its website.

Participating with me today on today's call, Earl Hesterberg, our President and Chief Executive Officer; John Rickel, our Senior Vice President and Chief Financial Officer; and Lance Parker, our Vice President and Corporate Controller. Also, please note that all comparisons and prepared remarks are to the same prior year period unless otherwise stated. I'd now like to hand the call over to Earl.

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

This morning Group 1 reported another all-time record-breaking quarter in revenues, gross profit, net income and diluted earnings per common share. Diluted earnings per common share were $1.32 on record net income of $31.3 million. These record profits were driven to a large degree by a 25.9% increase in our revenues, which totaled $2 billion for the third quarter. I'm proud to report that Group 1's new and used retail vehicle unit sales have significantly outpaced US industry retail sales this year, consistent with our strategy of capitalizing on the recovery of the US auto market, and on key Japanese brands. Our new vehicle unit sales increased 34% for the quarter, versus the 17% retail growth reported by LMC Automotive forecasting in the third quarter.

Our strong weighting of Japanese brands was a positive factor. Our unit sales increased nearly ever brand we offer. New vehicle grows profit grew 18.5% on the 34% increase in unit sales, while gross profit decreased $252 to $1,927 per unit. As we previously discussed, new vehicle gross profit per unit was boosted last year by the inventory shortages following the natural disasters in Japan. This midline Japanese brand sales have rebounded, profits per unit have declined some. Our average sales price also decreased 1.2%, to $33,050, reflecting the mix shift from luxury brands to midline imports, and a 390 basis point shift from trucks to cars.

Used vehicle unit retail sales continue to be strong, increasing 19.5% to 22,433 vehicles. Used retail gross profit grew 17.7%, on 22.6% higher revenues, as gross profit per unit fell slightly to $1,682. The average selling price increased 2.6%, to $20,612, partially due to our certified pre-owned business growing 150 basis points, account for 33.5% of our used retail unit sales. Finance and insurance per retail unit reached another all-time high of $1,220. Finance and insurance revenues grew 34.9% on the 27.9% retail unit increase. Parts and service gross profit grew 8.1% on the 7.1% revenue increase.

I'm delighted to report that we have continued to leverage our costs. Selling, general and administrative expenses, as percent of revenues improved 110 basis points to 10.9%. As a percent of grows profit, we saw improvement from both the prior year and second quarter periods to 74.2%. Operating margin held at 3.4%.

Turning to our third quarter new vehicle unit sales mix, as percent of Group 1's new vehicle unit sales, import brands contributed 55%, luxury 27%, and domestic rounded it out with 18% of the units sold. Toyota Lexus sales were strong, expanding to account for 31% of our new vehicle unit sales. Honda Acura sales also grew to contribute 11%. Reflecting the acquisitions we made during the past year, Volkswagen, AUDI and Porsche increased the share of our mix to account for 8% of our new vehicle unit sales. New vehicle inventory remained flat with the second quarter at a 63-day supply, or 24,469 units. We had a 30-day supply of used vehicles at September 30.

Our acquisition pace slowed in the third quarter. In August we added a Hyundai franchise in Houston that is expected to generate $30 million in annual revenues. Subsequently, on October 23, we acquired another Hyundai dealership in Oklahoma City that is expected to generate $45 million in annual revenues. Year-to-date we have acquired a total of 14 franchises that should generate $580 million in estimated annual revenues. We have also disposed of Lincoln, Nissan and Mazda franchises this year. The three franchises generated $84.8 million of total annual revenues.

I will now turn the call over to our CFO, John Rickel, to go over our third quarter financial results in more detail.

**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

The following comments will be on the year-over-year basis unless otherwise noted. Our net income for the third quarter of 2012 rose $7.5 million, or 31.6% on a comparable basis, to $31.3 million, which is the best quarter in our Company's history. While there are no adjustments made to third quarter 2012 results, the prior year's third quarter results excluded $2.3 million of after-tax non-cash asset impairment charges.

As previously announced, in early September we incurred moderate inventory and property damage at several of our gulf coast dealerships as a result of hurricane Isaac. The pretax insurance deductible expense recognized in the quarter totaled $600,000. These charges were offset by a gain recognized on the disposition of a Lincoln franchise, so no net adjustments were required this quarter. Earnings per diluted common share improved 30.7% on a comparable basis, to $1.32, which is also the best quarter in our company's history. This result continues to highlight the improvements we've made to our processes and cost structure, and demonstrates the leverage those improvements are delivering as new and used vehicle sales volumes continue to increase.

On a consolidated basis, we delivered record revenues in the third quarter of $2 billion, which were up $406.2 million, or 25.9%. This record reflects increases in each of our business segments. New vehicle revenues increased 32.3%, $1.14 billion. Our used vehicle retail revenues improved 22.6%, to $462.4 million. Used vehicle wholesale revenues grew 13.6%, $78.4 million, while our F&I revenues rose 34.9%, to $69.5 million, or $1,220 per retail unit sold, which is yet again the Company's best ever quarterly F&I performance. Revenues from the parts and service business improved $14.9 million, or 7.1%, to $225 million. Our total gross profit increased $42.5 million, or 17.1%, to $291.2 million, which also represents the best quarter in the Company's history. Gross profit results included increases of 18.5% in new vehicles, 16.4% in total used vehicles, and 8.1% in parts and service, as well as the F&I improvement that I just mentioned.

We continue to leverage our cost base, and as a result, SG&A expenses, as a percent of gross profit, improved 150 basis points, 74.2%. Floorplan interest expense increased $1 million, or 14%, to $7.9 million. This increase is primarily explained by a $342.9 million increase in weighted average borrowings as Japanese brand inventory has normalized, and overall inventory increases were required to support rising sales, as well as recent dealership acquisitions. Partially offsetting this increase in borrowing were lower weighted average interest rates, which were mainly attributable to the expiration of several higher-rate swaps during the quarter. At September 30, 2012 our new vehicle inventory stood at 24,469 units, with a value of $826 million, compared to 13,896 units, with a value of $479.6 million, as of September 30, 2011.

Manufacturers interest assistance, which we report as a reduction of new vehicle cost of sales at the time vehicles are sold, covered 115.9% of total floorplan interest expense in the third quarter, which is up from 96.8% in the third quarter a year ago. Other interest expense increased $1 million, or 11.3%, to $9.6 million, explained by increased mortgage borrowings associated with recent dealership acquisitions. Our consolidated interest expense includes non-cash discount amortization of $2.5 million related to our convertible notes.

Now, turning to the third quarter same store results, again statements are on a year-over-year basis, unless otherwise noted. In the third quarter, we reported revenues of $1.81 billion, which was an increase of $235.5 million, or 15%. Within this total, new vehicle revenue was up 20.2%, $1 billion, reflecting higher new vehicle retail unit sales. As a partial offset, our average new vehicle sales price decreased $519 per unit, to $32,948, which is primarily explained by the mix shift from luxury and trucks towards midline import brand sales, that last year's constrained import inventories have recovered.

In total, our used vehicle revenues rose 10.6%, to $493.4 million. Within that, our used retail revenues improved 12.8%, $425.3 million. Our average retail used vehicle sales price increased $347, to $20,439. Our used vehicle retail revenues decreased 1.3% to $68.2 million. F&I income for retail unit rose 7.5%, $1,243, driven primarily by increases in our penetration rates for both finance and vehicle service contracts, as well as improvement in our income per contract for most of our F&I product offerings. In total, F&I revenues were up $13.5 million or 26.2%.

We posted another positive quarter in the parts and service business. Parts and service revenues grew 0.4%. The overall increase is more than explained by an increase of 3.6% in collision revenues, while the customer pay, warranty and wholesale segments of the business all remained relatively flat.

As mentioned earlier, hurricane Isaac negatively impacted 12 of our gulf coast area dealerships during the third quarter of this year. In particular, our parts and service businesses in most of the affected areas lost opportunities for the better part of a week during late August and early September. As a reminder, our parts and service revenues are not inflated by increases in internal business. The revenue associated with internal work is eliminated in consolidation. This varies across the sector as some of our competitors account for internal work differently.

Overall our same store gross profit improved $20.3 million, or 8.1%. Our new vehicle gross profit dollars improved 5.4%, which is the result of the higher unit volume. As we previously mentioned, new vehicle gross profit per unit was inflated last year as a result of the severe industry-wide inventory constraints that resulted from the natural disasters in Japan. Given that, we would suggest a sequential comparison is more appropriate. Compared with the second quarter 2012, our consolidated new vehicle gross profit per retail unit decreased only $12, $1,927. Our used vehicle retail gross profit dollars increased 9.6%, reflecting the increase in units sold partially offset by $19 decrease in gross profit per retail unit sold, $1,689.

We continue to be proud of the leverage we are delivering on our SG&A cost. Our SG&A is percent of gross profit improved 180 basis points to 73.9%. As new and used vehicle sales increase, and gross profit continues to grow, we'd anticipate further leveraging SG&A. For example, in the third quarter of 2012 we grew gross profit by $20.3 million, and held SG&A expense growth to $10.6 million. This equates to a 48% flow through of gross profit EBITDA. A rough rule of thumb is we expect each incremental gross profit dollar will only add about $0.50 of variable SG&A expenses on a same store basis, which we believe is the appropriate way to analyze this metric, as acquired stores will clearly bring their own fixed-cost load into store key analysis the year immediately following acquisition. With this cost leverage, our same store operating margin improved 10 basis points to 3.5% on comparable basis.

Now, turning to liquidity and capital structure. During the third quarter of 2012, we generated adjusted cash flow from operations of $62.6 million. As of September 30, 2012, we had $38.8 million of cash-on-hand, and another $128.3 million that was invested in our floorplan offset account, bringing our immediately available funds to a total of $167.1 million. In addition, we had $225.7 million available on our acquisition line, that can also be used for general corporate purposes. As such, our total liquidity at September 30, 2012 was $392.8 million.

During the third quarter we used $3.4 million to pay dividends of $0.15 per share, which is an increase of $0.02 per share over third quarter 2011. We also used $13.5 million for capital expenditures during the quarter to construct new facilities, purchase equipment, and improve existing facilities. We will continue to critically evaluate all planned capital spending, and work with our manufacturer partners to maximize the return on our investments. We anticipate that our full year capital spending will be less than $63 million in 2012, which includes about $15 million for specific growth initiatives in our parts and service business.

With regards to our real estate investment portfolio, we own $477.8 million of land and buildings at September 30, which represents nearly 40% of our total real estate. To finance these holdings, we utilized our mortgage facility and executed borrowings under other real estate specific debt agreements. As of September 30, we had $57.4 million outstanding under our mortgage facility, and $236.1 million of other real estate debt, excluding capital leases. For additional detail regarding our financial condition, please refer to the schedules of additional information attached in the news release, as well as the investor presentation posted on our web site. With that I will now turn back over to Earl.

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

To wrap up our prepared remarks, this is Group 1's fourth consecutive record-breaking quarter. Once again, we delivered all-time high top-line results while leveraging our costs to drive record net profit and earnings for our shareholders. I am proud that our operating team has outpaced the industry in both new and used retail unit sales so far this year. Going forward our plans include-- gaining market share in both new and used retail vehicle sales where we're averaging more than $3,000 combined front and backend gross profit per unit; expanding our profitable parts and service business; leveraging our scale and costs; and acquiring strategic operations that will augment our diversified brand and geographic mix while keeping our balance sheets strong.

That concludes our prepared remarks. I will now turn the call over to the Operator to begin the question and answer session

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions)

John Murphy, Bank of America

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**John Murphy** - *BofA Merrill Lynch - Analyst*

First question -- on the average transaction price. It sounds like you were down 1.2%. It's a little bit different than what we are hearing from auto makers and other data feeds -- it sounds like pricing is actually positive. I just want to make sure that this decline that you are seeing is purely a function of mix. Or is there anything else going on at the dealer level where you are seeing pricing pressure that the auto makers are not seeing?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

It's just a function of mix, with Toyota and Honda being so strong. Those are more car-driven brands than truck-driven brands.

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**John Murphy** - *BofA Merrill Lynch - Analyst*

So absent the shift in mix, you think pricing is reasonably strong at this point?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Pricing for the OEMs. I think, based on our margins, you can tell that we've (laughter) -- based on our margins I think you can see it's fairly competitive at the retail end, but I don't think there has been any real change in the pricing levels -- no, certainly from the OEM viewpoint.

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**John Murphy** - *BofA Merrill Lynch - Analyst*

Okay. Second, on the parts and service gross margin, 52.5% -- it's pretty high at this point. Is that a function of mix, as well, and as we see more warranty work come back into the next couple years that might come down? Or is this level in the low 50s sustainable?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

We are comfortable in this range, around 52%. Clearly, the way we account for the growing internal work with the reconditioning in particular on used vehicles, certainly supports that. The warranty work we think is on kind of a longer-term secular decline. You get recalls from time to time that help pump it up, but the margins on recalls are not far off what we get on customer pay. So I think the bigger part of the story is the ongoing support from the internal work.

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**John Murphy** - *BofA Merrill Lynch - Analyst*

And these higher numbers you think are just better utilization and throughput in your service base, and it's really going to continue going forward?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

Yes, we are comfortable with this margin level.

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**John Murphy** - *BofA Merrill Lynch - Analyst*

Got you.

Then F&I PVR above $1,200 -- once again, that's pretty impressive, and at the higher end of the range where it's been historically. Is this because you are getting better penetration on financing in your dealerships? Or is there something else going on here that is allowing you to really break through that glass ceiling of a thousand bucks we used to think of?

**Pete DeLongchamps** - *Group 1 Automotive Inc - VP, Financial Services and Manufacturer Relations*

Our penetration rates are actually relatively stable. I think we are doing a much better job with overall penetrations with our products. I think we have also continued to further our lender relationships, which is certainly very helpful. Then we've got laser-like focus on process and compliance, and that's also made a big difference in the way that we approach some of our under-performing stores. So, it's a combination of a lot of different things, but we are pleased at the $1,200 level.

**John Murphy** - *BofA Merrill Lynch - Analyst*

Then lastly on acquisitions -- some other dealer groups have backed off acquisitions, citing that they are somewhat prohibitively expensive, yet you guys are going hot and heavy here on acquisitions, which appears to be a good thing for both short-term and long-term growth. I'm curious what you are seeing as far as pricing in the market, and if we should expect to continue to see a rapid pace going into 2013, these acquisitions, similar to what you've done in 2012?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

John, I don't think the environment has changed that much. I don't think we have bought any of the overpriced dealerships, because we can't afford to do that and deliver for our shareholders. It's still our intention and desire to grow the company, and that's still our preferred use of our cash. We still have good liquidity, as John mentioned, so we will continue to work that direction. It is difficult, and has been difficult, but over the period of a year or so, we've been able to find ways to grow our company, and we're going to continue to try to do that. I believe over time we will be able to.

**John Murphy** - *BofA Merrill Lynch - Analyst*

And Earl, do you think there is an ultimate target for the size of your company that you are gearing towards? I'm just trying to understand what the upper limits are, eventually, and obviously this is a number of years out before I would assume you'd hit that. But where you ultimately think you might go, as far as the store count or the revenue base? And what we should think about you kind of hitting the brakes on that and really just running the business for cash and just pure straight return to shareholders of that cash flow?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Well, we've never really tried to identify a target size for the company. What we target is consistent annual shareholder growth of 15% a year or more, which we have obviously been able to do particularly with the market recovering. And we think part of that consistent return to shareholders -- more than 15% a year, even when the market is flattened out a bit -- the best formula to get there is to continue to grow our company and deploy our cash flow that way.

That's in our DNA, but I can't tell you that we want to be a $10 billion company, or 250-store company. Our job is to find good opportunities for our shareholders as fast as we can find them and to the degree that we can afford them.

**John Murphy** - *BofA Merrill Lynch - Analyst*

Great; thank you very much.

**Operator**

Rick Nelson, Stephens Incorporated

**Rick Nelson** - *Stephens Inc. - Analyst*

I would like to ask you about market share with your major brands on a same-store basis. If I'm understanding the retail market was up 21% year-over-year. Your same-store new car sales were up 22%. I guess I expected a little more given your brand mix, heavily skewed toward Toyota.

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

We gained significant share on most of our key brands. Our Toyota sales were up about 44%; our Honda sales almost 52%. Another one of our key partners, Ford -- we were up 15%. So we gained share in most of our key brands, and not just in new but used. So that is a big part of our success, I think, not just this past quarter but this year. The only business that was softer than I would like to see, our BMW business was about flat. I think that will change in the fourth quarter as we now have some all-wheel drive 3-Series vehicles to sell in the northern half of the country. That has been -- customers in the northern half of the country have been waiting for the all-wheel drive, and that is a big part of our BMW volume.

**Rick Nelson** - *Stephens Inc. - Analyst*

Got it. And those growth rates you cited were same store?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Yes.

**Rick Nelson** - *Stephens Inc. - Analyst*

Okay, terrific.

I would like to cover the margin side, too, on a new car. I understand the mix shift is pressuring the margin, but if you could discuss where you are seeing pressure on a like-brand basis, and where you are seeing more stability?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Well, I think the obvious place, obviously, is Toyota and Honda, with their supply this year and those brands are trying to recover market share. But that dynamic basically sucks everyone in to that highly competitive game. Nissan, obviously, is trying to defend their market share. Ford, General Motors, and Chrysler have to compete also. So all the volume brands, I think, are a bit more competitive this year. The dynamic is driven by Toyota and Honda, I believe.

**Rick Nelson** - *Stephens Inc. - Analyst*

Yes. How about the luxury cars -- are you able to retain more margin there?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Yes, absolutely, we have been. Although I think that it's going to be a very competitive fourth quarter in the luxury brand business. There is better supply, I think, for the luxury brands in the fourth quarter than even in the second and third quarter, but certainly versus fourth quarter last year. I think there is a pretty big competitive dynamic between BMW and Mercedes at the moment. But thus far I think our luxury margins have held up reasonably well.

**Rick Nelson** - *Stephens Inc. - Analyst*

Any commentary on October sales and your thoughts about the full year? Do you have a SAAR estimate at this point?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Well, our SAAR estimate, Rick, would be $14.4 million, which hopefully will get more accurate as we have more months behind us. But I'm afraid I don't have anything brilliant to contribute to October. My first point of reference is analyst reports by you and your colleagues, those who choose to predict the SAAR, which seems to be mid-14s to high-14s, if I'm reading all of your reports. I would say that a lot of this business occurs in the last week of the month. So, mid-month data isn't all that helpful for me usually. I don't see any dynamic that has -- positive or negative, that has changed the pace of the markets. So, it still seems to be fairly stable and pretty good business right now for all of us.

**Rick Nelson** - *Stephens Inc. - Analyst*

Got you.

Finally if I could ask you about the finance market, particularly subprime. What you are seeing there? What the opportunity might be?

**Pete DeLongchamps** - *Group 1 Automotive Inc - VP, Financial Services and Manufacturer Relations*

There is plenty of opportunity. We've talked about it before. The lenders have become more full-spectrum. As you know, we have consolidated some of our lending base. But today, getting consumers financed through reputable banks is not an issue.

**Rick Nelson** - *Stephens Inc. - Analyst*

Great. Thanks a lot and good luck.

**Operator**

Ravi Shanker, Morgan Stanley

**Ravi Shanker** - *Morgan Stanley - Analyst*

Earl, if I can just follow-up on something you said earlier in this conversation about the pricing. You said that you are not seeing too much difference from the OEM in pricing, but what are you seeing from the dealers? Because so far in this earning season, we have seen a couple of dealers beat our expectations on top-line but miss on pricing. You guys were kind of the opposite. Some of the other dealers were outspoken about trying to gain share potentially of the cost of pricing. Are you seeing a lot of that in the market, or is that more isolated?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

No, I think that the auto retailers, dealers, whether they are public or private, are all fairly aggressive right now, including ourselves. So, I think everyone is trying to take advantage of a better market. There's more fish in the pond, so we are all fishing harder.

**Ravi Shanker** - *Morgan Stanley - Analyst*

Understood.

Also if I can follow-up on the acquisitions. Can you give us a little more color there on how you see those evolving? Because you had some pretty good examples, and you have a pretty good track record of leveraging a lot more out of some of these acquisitions than they had going in. So, the revenue targets you have given us -- do you think that these acquisitions stay at this level for a while? Or do you think you can get a lot more out of them?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I can't really give you any assurance one way or the other. It's such a dynamic market, and you have to be so opportunistic. I can only tell you that we're going to approach it in the same manner we have, and that is, we're going to look hard to find them. But I will admit that it's challenging, because the selling prices in the market, at least the asking prices, are high and the real estate challenges still exists.

Commercial real estate just doesn't have the same value, at the moment, that it had pre-recession. So, there is still a lot of challenges to doing deals. We have been fortunate that we've been able to and we're going try to continue that. That's about all I can tell you.

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**Ravi Shanker** - *Morgan Stanley - Analyst*

Okay. Finally, John, housekeeping question for you -- you alluded to this in your comments, but can you give us the full impact of Hurricane Isaac from both a cost and an opportunity perspective?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

From a cost perspective -- I mean the direct cost that we can measure was the insurance deductible -- turned out to be a little bit higher than what we indicated in the press release. We ended up with about $600,000 of insurance cost, primarily around some roof damage where we have a little bit higher deductibles on roofs.

On the revenue piece, it's always hard. The new and the used vehicle sales, probably defer and end up coming back. What we lost was the best part of a week at 12 dealerships on the parts and service. Once again, hard to calculate, but certainly that's capacity that you can't get back. So I'd say that was probably the main impact on the revenue side, was that loss in the parts and service area.

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**Ravi Shanker** - *Morgan Stanley - Analyst*

And have you seen that kind of rebound in Q4 so far?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

Yes, I think we are back to a stable level. We lost some business, I just couldn't tell you how much.

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**Ravi Shanker** - *Morgan Stanley - Analyst*

Understood. Thanks very much.

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**Operator**

Patrick Archambault, Goldman Sachs

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**Patrick Archambault** - *Goldman Sachs - Analyst*

I have one just on used -- you have seen the Manheim start to soften. Can you just give us a sense of how that's playing out for you? I mean, margins seem to come in line with expectations for this quarter. But how does that affect you going forward? Can you potentially capture some of that acquisition cost in savings?

Then I just have a follow-up on parts and service.

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

The value stood softened down in the quarter, particularly early in the quarter. Some of that was they were obviously high, but there is a seasonal turn also that occurs this time every year. We actually lost a little money at wholesale for the quarter, which is first time in a long time. I wasn't particularly happy about that. We actually lost a little money in wholesale in the first two months of the quarter, and by the third month we got that straightened out and we're back in the black.

So the idea -- one of the reasons we run our used car business so tightly, with 30-day supply, which I think you can see over the years, plus or minus a day, that is usually what we have. So we can reload with cheaper cars very quickly. As you go into the winter, obviously the prices of used cars do decrease. You want to be able to buy as many as you can at that lower price level. So, we very much watch that.

Very much been a change in the market, most of it's seasonal, but probably a little more than that. So we have to stay nimble and use the data available to us so we can continue to buy on the market, not have to flush out too much inventory that we bought above market prices some period of time ago.

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**Patrick Archambault** - *Goldman Sachs - Analyst*

Okay, so, right. Hopefully like the non-recurrence of some of the inventory coming down is positive, but I guess my question is -- are you finding that prices are coming down as much as -- customer prices are coming down as much as acquisition cost is? Or is there kind of an opportunity there, perhaps in future quarters?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

There is always an opportunity as you go through the winter if you manage your business carefully. You want to stock up with cars at the low price in the winter so you are ready for the spring selling season in March. You don't want to have too heavy of an inventory as you're going into the lowest part of the pricing curve in the winter. So yes, there is an opportunity for all retailers if you run your business well.

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**Patrick Archambault** - *Goldman Sachs - Analyst*

Okay. Thanks.

Just on P&S, the business did slow and I think you explained why. I mean, there was -- it was affected by some of the dealerships that were impacted by the hurricane. What do you see a sustainable growth rate as for that business? I mean, recently it's kind of had its puts and takes, but what sort of a sustainable run rate that we should be thinking about?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

In the near term, probably low single digits, but our goal would be to try to make it more mid-single digits. We didn't do well in customer pay. Our customer pay business was flat where it had been growing, and we believe the majority of that was what John mentioned -- losing some business along the Gulf Coast.

The encouraging part was that warranty came up a bit for us. Warranty was almost flat. So that was a little bit better dynamic for us. Our body shop Business was up 3.6%, which is okay, but I think we can grow faster there, also. Our goal would be to put you toward 5%; realistically, if we can grow about 3%, would probably be what the market will generate at this time.

**Patrick Archambault** - *Goldman Sachs - Analyst*

Okay. Great. Thanks a lot for the color.

**Operator**

Simeon Gutman, Credit Suisse

**Simeon Gutman** - *Credit Suisse - Analyst*

A quick question -- a follow-up, Pete, regarding credit. I think you mentioned that credit is going well. I guess about a year ago it felt like there was an inflection where credit was expanding a little more rapidly. Is there another layer -- does it feel from the lending environment, feel like there's even more lending to come, and the subprime availability's even going to get better from here?

**Pete DeLongchamps** - *Group 1 Automotive Inc - VP, Financial Services and Manufacturer Relations*

For us I don't think so. There may be availability, but as we have talked about, what we are really focusing on is making sure our business is going towards the OEM financial service partners that we have, and then really leveraging our relationship with the larger banks. We have a couple of regional banks that we use, and credit unions. We think that, with where the lending situation is today, that we can really expand our opportunities by focusing on our best partners. So, for us, I don't think there is an additional layer to come. We are very happy with the relationships we have. Our business is growing, as is theirs.

**Simeon Gutman** - *Credit Suisse - Analyst*

Okay. And then Earl mentioned that wholesale lost money in the first couple of months, and there was some issues that got fixed. Was that a market issue or is that operational issues? If you can clarify; if not, no problem.

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I believe the majority of that was market issue with the change in the Manheim price index. I like to believe that we can always do better, we should always do better than the market. I think we could have done better also, but maybe that's just me. (Laughter)

**Simeon Gutman** - *Credit Suisse - Analyst*

Okay.

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I believe the majority of it was market, but we work harder to do better, let's put it that way.

**Simeon Gutman** - *Credit Suisse - Analyst*

Okay. Then on throughput, it looks like the number was decent. I realize that the numbers we look at are imperfect because it has some noise from new business and acquisitions that come on. I don't know if there is some adjustment that you can show, or talk about just how, from an efficiency standpoint, the business performed?

**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

Yes, on a same store basis, which we think is the right way to look at that SG&A flow-through, our calculation is, we got 48%, which is pretty close to our metric of $0.50 on the incremental gross profit dollar. We felt reasonably good about that. We did have one kind of lumpy item, it's in the operating results; it is an operating item, but we did have to true up our accruals for workers' comp and liability insurance. That added about $2.4 million of added expense within the quarter. But it clearly pulled that down a little bit.

**Simeon Gutman** - *Credit Suisse - Analyst*

Okay. Thanks for that.

**Operator**

James Albertine, Stifel Nicolaus

**James Albertine** - *Stifel Nicolaus - Analyst*

Quickly -- on the used side, I just wanted to understand -- you mentioned the CPO sales up, I think you said 33% year-over-year. Could you just parse that out by the segments, by however you break it down -- CPO and then maybe three- to eight-year-old vehicles, and then beyond that?

**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

I think maybe a little misunderstanding there. What we said was that the percentage of CPOs was at 33.5%, it was up 150 basis points from same period a year ago. We had a little bit stronger mix of certified pre-owned, but I don't think the growth was -- I think that confuses with the growth.

**James Albertine** - *Stifel Nicolaus - Analyst*

Okay. Could you provide the growth levels then by segment? Or is that just something you don't want to get into?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

No, we don't have that by segment, I'm sorry.

**James Albertine** - *Stifel Nicolaus - Analyst*

Okay. Then just wanted to understand a little bit on the M&A side, how you prioritize -- given your existing mix, how you prioritize brands, and then separately, geographies? And then as a follow-up to that, maybe a little bit more detail as to the thought process behind some of the dispositions that you wrote about here recently?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Certainly. We obviously prioritize geographies where we already operate. I think that footprint is pretty clear -- and including the UK, we would intend to grow our UK business when possible. But we are not as limited by brands as we probably have been most of my 7.5 years at Group 1. We have been very successful in the last year to year and a half, with some acquisitions of Ford dealerships. Ford's become a great partner with our company. Last year we bought a Cadillac, Buick, GMC dealership, which a few years ago I wouldn't have thought we would have done that. And it has performed incredibly well. So we are much more open on brand than we've ever been before. Clearly, we have a great partnership with Volkswagen Group that has emerged over the last 1.5 years or so.

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**James Albertine** - *Stifel Nicolaus - Analyst*

Okay, and any incremental color on the dispositions?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Those were just simply dealerships that were not providing a good return on investment for our shareholders. At that point it becomes frozen capital, and we would rather free it up and deploy it to the types of dealerships I just discussed, such as the two Hyundai dealerships we bought in the most recent quarter, which is another good partnership for our company.

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

The other thing I would add is that a couple of those were also to free up real estate for more productive uses. The one set in the middle of a campus which will allow us to expand some of the other stores. And the one here in Houston was really about making room for our Lexus expansion. So, part of it is also real estate-related.

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**James Albertine** - *Stifel Nicolaus - Analyst*

Great, thanks for the color. Good luck next quarter.

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**Operator**

Matt Nemer, Wells Fargo Securities

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**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

A couple of questions. First, starting with new grosses. As you look out over the next few quarters, do you expect those to be down year-over-year until we go up against the second quarter of 2013 or 2012? And then in Q4, do you expect grosses to be down sequentially, or do you think they'll be up with the mix shift back to luxury and the improved luxury availability?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I would hope that the luxury mix should get in December and at the end of the year would be a positive mix factor. But I mentioned a little bit earlier on in the call, I do foresee a little more luxury competition in the fourth quarter this year. But I think as we look in the year ahead, grosses should be, plus or minus, pretty stable.

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

A couple additional thoughts on that. I think, sequentially, as I indicated in my comments, is the way to think about it. I think if you take a look at what we have run in the second and third quarter is probably not a bad way to think about modeling fourth quarter. I don't think you can have a big change up or down from that. Clearly we'll get some help in the US market from a little bit better luxury. December is usually a big luxury, but don't forget we've now got more UK exposure and we're not going to have the same contribution from the UK in that same period.

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Yes, due to the September plate change. There's no plate change in the fourth quarter in the UK.

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**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

That is a good point.

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

So that's why I think you are probably best served to just think about it as the same levels we had in third quarter for new vehicle margins.

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**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

And a quick follow-up to that -- how much does the plate change in September drive the overall Q3 gross up, in terms of the mix to those luxury units, and I assume higher gross transactions in the UK?

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

I haven't actually ran the math to give you a specific number. I mean it was obviously a positive contribution, because that's one of the two strongest months in the UK, and those are all luxury stores. I don't have a specific dollar amount I could share with you.

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**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

My second question is -- I'm wondering if you can provide any qualitative, or maybe quantitative, commentary about what you are seeing in truck sales? And if you think that trucks in your markets are getting any benefit from the stabilized, and maybe slowly improving, housing environment?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I can't say I have seen any lift in the truck market. But I would say that it's certainly stable and we would expect it to continue to be stable to up. General Motors has a product launch, and Chrysler has a product launch with the Ram. So, I think some of the underlying either stability or strength of the truck market is getting buried by Honda and Toyota and Volkswagen driving the car mix-up quite a bit. But there is nothing wrong with the truck business at the moment. And fuel prices are not the drag that they may have been in certain times over the past two or three years.

**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

We have seen good growth in a number of the pickup brands. Ford had a very good quarter in pickup growth. We saw strength in Dodge, with the Ram trucks; and Toyota also had a very strong quarter. We are seeing some strength in the pickup segment. Interesting enough, with the fuel prices up as much as they were, we saw good growth in both pickup and SUVs in the quarter.

**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

Okay. Great.

Then, just lastly -- I'm wondering if you can comment about any centralization initiatives you have for 2013. I know that you are pretty close to being finished with centralized accounting. Maybe you could talk to inbound call centers, or any other initiatives that you are thinking about for next year, around centralization.

**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

The main focus for 2013 will be finishing up our accounting consolidation; as you indicated, we're in the middle of that right now. By the summer of next year we will be completed with that and all of our transactional accounting will be based here in Houston. That's really the key focus right now, is to get that completed.

**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

Longer term, are there other major opportunities to centralize, or bring some kind of group efficiencies to the network?

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Yes, there are, Matt, definitely. I don't really want to talk about them right now.

**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

Fair enough. Thanks so much.

**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

For competitive reasons.

**Matt Nemer** - *Wells Fargo Securities, LLC - Analyst*

Understood.

**Operator**

Brett Hoselton, KeyBanc

**Brett Hoselton** - *KeyBanc Capital Markets - Analyst*

I was hoping you could characterize BMW inventory levels during the third quarter, and maybe contrast that with inventory levels that you anticipate, or have, going into the fourth quarter here?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Our BMW inventory levels have probably been -- they have been actually just about right. They have been thin on key models for a couple years, whether it was X5, X3, 5-Series. The only new dynamic this year was, as I mentioned earlier, the all-wheel drive 3-Series has not enabled us to capture the momentum with the new 3-Series in the northern half of the country. Those vehicles are now arriving at BMW dealerships. In addition, it appears that overall BMW inventory is going to be better in this quarter, the fourth quarter, than it has been in a long time. That would be across most all of their model lines. So, I would think that the fourth quarter will be a much better BMW quarter, certainly, for Group 1.

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**Brett Hoselton** - *KeyBanc Capital Markets - Analyst*

And then, used vehicle gross profit per unit -- as I look at slide 9, we kind of have seen a general degradation, or decline, in gross profit per unit in the used vehicle side since about 2007. My question was, can you talk about the outlook? Do you anticipate that it's going to continue to decline, or do you think you're going to see it start to bottom out here at around $1,700, where it's kind of where it's been for the past few quarters?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

My feeling is that it should be bottoming out. Some part of that has just been the difficulty in finding good quality used cars, and the fact that we are still only getting about 60% of our inventory from trade-ins and still supplementing it a bit. But the other thing is, we've been pushing hard -- we've been pushing our used car business hard. We were up 11% in the quarter. The industry was up 6%. That follows 18.5% and 15.5% the first two quarters, which is way above the market. So we've been pushing to gain share in the used business also.

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**John Rickel** - *Group 1 Automotive Inc - SVP and CFO*

I agree with everything that Earl said. The other thing I would add is that one of the things that should start to help us as we go into next year is that the return of off-lease vehicles will begin to pick up pace. Those are fabulous units for us to turn into certified pre-owns, and really good used car pieces. That's been one of the things we've really been short on, is good late-model used cars.

With leasing finally starting to gain traction again, we should start to get a better supply of those starting next year, which will be one of the things that will help with that split of how many extra cars we're having to supplement at auction. If we can continue to pick up cars there, that should help us. I agree with Earl, I think that you're kind of at hopefully a low point here.

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**Brett Hoselton** - *KeyBanc Capital Markets - Analyst*

Some other question on slide 11 -- F&I trending up since 2009. You're around $1,200 right now. Is there still an opportunity to see another $50, $100 out of F&I? Or do you think that you are more likely to see a plateau in around this $1,200 range?

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

I think I will give Pete an objective of that $100 you mentioned. (Laughter) I think there is still a little bit upside. We just know that we can perform a little bit better, but $100 is probably overstating it. Nothing wrong with going for another $20 or $30.

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**Brett Hoselton** - *KeyBanc Capital Markets - Analyst*

Excellent. Thank you very much, gentlemen.

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**Operator**

And, ladies and gentlemen, at this time, our question-and-answer session has concluded. I would like to turn the conference call back over to Mr. Earl Hesterberg for any closing remarks.

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**Earl Hesterberg** - *Group 1 Automotive Inc - President and CEO*

Thanks to all of you for joining us today. We look forward to updating you on our fourth quarter and full-year earnings results next February. Have a good day. Thank you.

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**Operator**

The conference has now concluded. We do thank you for attending today's presentation. You may now disconnect your telephone lines.

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