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GPI - Q1 2014 Group 1 Automotive Earnings Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Group 1 Automotive 2014 first quarter conference call. Please be advised this call is being recorded. I would like to turn the call over to Mr. Pete DeLongchamps, Group 1's Vice President of Financial Services and Manufacturer Relations. Please go ahead, Mr. DeLongchamps.

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

Thank you, Amy, and good morning, everyone. Welcome to today's call. The earnings release that we issued this morning and the related slide presentation that include reconciliations related to the adjusted results we refer to on this call for comparison purposes have been posted to the Group 1 website.

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 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. 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 on the call today, 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. Please note that all comparisons in the prepared remarks are the same prior period unless otherwise stated. I would now like to turn the call over to Earl.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Thank you, Pete, and good morning, everyone. I'm pleased to announce that due to an extremely strong performance in March, Group 1 earned $31.3 million in the first quarter. This equates to $1.19 per diluted share, a 2.6% increase versus our adjusted results last year.

It is appropriate to compare our results to our adjusted results in 2013 as our Q1 results last year included $7.1 million in one time costs primarily associated with the acquisition of our Brazilian business. So on a GAAP basis, our $31.3 million net income represents a 41.5% increase but on an adjusted basis equates to a 7.1% increase.

As we noted in our February 18 release, our business was severely hampered by extreme weather during the first quarter causing store closures, reduced traffic and incremental costs. In total we lost about 9% of our total available selling days through the 16 of February.

Our businesses in New Hampshire, Massachusetts, New York, New Jersey and Maryland bore the brunt of the lost business, but there was also multiple closures in South Carolina, Georgia and North Texas, which is very unusual. This is evident in some of our same store growth metrics as well as the impact on our cost leverage.

With the severe winter behind us we expect to return to more normalized cost leverage for the remainder of this year. Fortunately, the quarter ended strongly with March delivering an extremely strong sales month across the US and in the UK.

On a consolidated basis for the quarter, we retailed 37,749 new vehicles and 26,877 used retail units; driving a $297 million increase in revenue to $2.3 billion. New vehicle revenue rose 14.3% as the average retail sales price increased $66 per unit. Used vehicle retail revenues grew 16.7% as the average retail sales price rose $174 per unit.

Group 1's new vehicle unit sales mix was 79.4% US, 10.7% Brazil and 9.9% UK. Toyota Lexus sales accounted for 25.8% of our new vehicle unit sales while Ford, Honda Acura and BMW Mini all represented over 10% of our new vehicle unit sales; while Nissan Infinity was just below 10% at 9.7%. New vehicle inventory came down to 67-day supply or 34,400 units at the end of the first quarter compared to a 72-day supply at the end of 2013.

Used vehicle inventory stood at 13,700 units or a 30-day supply compared to 35-day supply as of December 31, 2013.

It is not possible to recover much of the parts and service business lost to bad weather as many of our shops run at or near full capacity. Yet even with the extensive closures across our network, we delivered strong same store revenue growth of 6.3% in parts and service.

We also generated a 15.4% increase in finance and insurance revenue. Both of thesewere important contributors to our 15.1% total consolidated revenue growth as well as a 5.9% improvement in same store revenue. Our same store finance and insurance income per retail unit increased $136 to $1,391.

Relative to our cost perform performance on a consolidated basis, selling, general and administrative expenses as a percent of gross profit increased an adjusted 80 basis points to 76.2%, primarily reflecting a full quarter of Brazil's results. Total SG&A as a percent of gross profit in the US and UK improved 10 basis points and 470 basis points, respectively.

The impact of added costs and lost days from the severe winter weather negatively affected the US SG&A leverage and flow through. We continue to monitor and adjust our cost structure, as we have in recent quarters, to address the ongoing pressure on new and used vehicle margins.

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

John Rickel - *Group 1 Automotive - SVP, CFO*

Thank you, Earl, and good morning, everyone.

Our net income for the first quarter of 2014 rose $2.1 million over our adjusted 2013 results of $31.3 million, and our earnings per diluted common share increased $0.03 from the adjusted prior year results to $1.19. While no adjustments were made to the first quarter 2014 figures, the 2013 results excluded $7.1 million of net after tax costs primarily associated with the acquisition in Brazil.

As Earl mentioned, severe weather during the first two months of the quarter significantly disrupted operations. While a good portion of the lost vehicle sales business was recaptured during the strong month of March and we were aided by record results from our UK operations, the severe weather did have an overall negative impact on the quarter for our US operations.

Starting with the summary of our consolidated results, for the quarter we generated $2.26 billion in total revenues. This was an improvement of $297 million or 15.1% over the same period a year ago and reflects increases in each of our business units.

Our gross profit increased $37.6 million or 12.5% from the first quarter a year ago to $338.1 million. For the quarter, SG&A as a percent of gross profit increased an adjusted 80 basis points to 76.2% and operating margin was 3.1%.

The increase in SG&A as a percent of gross profit relates primarily to having a full three months in Brazil and the consolidating results month versus only one month in the first quarter a year ago. It should be noted that the SG&A in our foreign operations runs relatively higher mainly due to both the higher cost of real estate and the lack of similar scale advantages we benefit from here in the US.

Floorplan interest expense increased $1.5 million or 16.5% from prior year to $10.9 million. This increase is primarily explained by a full three months of Brazil operations now included in our consolidated results.

Other interest expense increased $1.3 million or 13.8% to $10.5 million. This increase is attributable to an increase in weighted average debt outstanding of $122.9 million primarily explained by additional real estate related financing including mortgage borrowings associated with recent dealership acquisitions and an increase in borrowings on our acquisition line. As a reminder, our consolidated interest expense for the first quarter of 2014 includes incremental noncash discount amortization of $2.8 million related to our convertible notes.

Our consolidated effective tax rate for the quarter of 36.4% was positively affected by country mix with the UK contributing record results, as previously mentioned. We would expect our tax rate to increase to approximately 38% over the remainder of 2014.

Turning to the first quarter same store results which now include one month of Brazil results from each period. In the first quarter we reported revenues of $2 billion which was $111.7 million or a 5.9% increase from the comparable 2013 period.

Within this total, new vehicle revenue was up 4.2% and used vehicle retail revenues improved 7.4%. Both finance and insurance and parts and service delivered another strong quarter, growing revenues 15.4% and 6.3% respectively. Although difficult to quantify, the selling days lost to winter weather did negatively impact these metrics with the biggest impact being in parts and service.

New vehicle revenue increased to $1.11 billion on 3.5% higher unit sales and an increase in our average new vehicle sales price of $239 to $34,087 per unit.

Our used retail revenues improved $490.9 million on 5% more unit, an increase in our average used vehicle retail sales price of $465 to $20,810.

F&I revenue per retail unit rose 10.8% to $1,391 driven by increases in both penetration rate and income per contract for most of our major product offerings.

The 6.3% revenue growth in parts and service is explained by increases of 2% in customer pay, 5.2% in warranty, 11.6% in collision and 14.1% in wholesale parts. As a reminder, our parts and service revenues are not impacted by increases in internal business. Revenue associated with internal work is eliminated upon consolidation. This varies across the sector as some of our competitors account for internal work differently.

In aggregate, our same store gross profit grew $15.1 million or 5.2% to $304.9 million.

Our same store new vehicle gross profit dollars declined 4.5%. These slightly higher volumes were more than offset by $150 decline in gross profit per unit to $1,785.

Our used vehicle retail gross profit dollars declined slightly as increased volume was offset by a $126 decline in gross profit per unit to $1,611.

Our F&I gross profit grew $10.4 million or 15.4%, reflecting unit volume growth in the improved [PRU] previously mentioned.

Finally, parts and service gross profit grew $8 million or 6.7%, primarily reflecting the strong revenue growth and a 20 basis point improvement in margins to 52.8%.

For the first quarter we grew our total gross profit by $15.1 million while adjusted SG&A expenses rose $11.5 million. As a result, our adjusted SG&A as a percent of gross profit increased 10 basis points to 74.9%, primarily due to the impact of the winter weather which drove added snow removal costs and wage costs for lost days. Our same store adjusted operating margin remains steady at 3.4%.

Turning now to our geographic segment starting with the US market on an actual basis. As a reminder, we've rebalanced our US dealership portfolio over the last 12 months, and, as a result, acquired a net of eight franchises representing additional annualized revenues of approximately $340 million.

As a result, our consolidated results are not fully reflective of underlying same store performance in the US. In addition, the weather impacts were all related to our US operations.

Total US revenues grew 6.6% to $1.83 billion, primarily driven by increases of 7.7% in used retail revenue, 6.5% in parts and service revenue, and 5.2% in new vehicle revenue.

The increase in used vehicle retail revenues is fully explained by the 7.7% growth in retail units sold as the average retail sales price per unit remained unchanged. Increase in our parts and service revenues reflects growth in all areas of the business. Our F&I revenue growth of 15% reflects the increase in retail vehicle sales volume coupled with the improved profitability per retail unit which grew $119 or 8.9% to $1,458.

Total gross profit improved 6.2% driven by a 6.5% increase in parts and service as well as the F&I increase that I just mentioned.

For the first quarter we grew gross profit by $16.8 million while adjusted SG&A expense rose $12.3 million. As a result, our adjusted SG&A as a percent of gross profit improved 10 basis points to 74.7%.

Adjusted operating margins in US business segment decreased 10 basis points to 3.5% with both the SG&A and operating margin negatively impacted by the severe weather experienced during the first two months of the quarter.

Related to our UK segment, we are pleased to announce that we delivered a record March with profit up nearly 50% from the previous record set in the prior year. As a reminder the months of March and September are by far the most profitable months of the year in the UK because that is when license plates change over to a new numbering sequence.

Total revenues for the UK segment were up 44.8% for the quarter. It should be noted that while a portion of this increase is due to the two additional months of operating our four Ford dealerships acquired in the first quarter of 2013, same store revenue growth of 29.7% is the main driver of this increase.

New vehicle revenues grew 37.7% on 32.5% more retail unit sales and an increase of $1,331 in the average sales price per unit to $34,873.

Used vehicle retail revenues improved 59% on 58.5% more retail units.

Parts and service revenues improved 44.6% of which 24.4% related to same store growth.

Our F&I income growth of 67.7% reflects the 42.3% increase in total retail unit sales and a 17.9% increase in gross profit per retail unit to $712.

During the first quarter, total gross profit grew 49.9% reflecting healthy increases across each business segment. We also leveraged our costs, and adjusted SG&A as a percent of gross profit improved 470 basis points to 78.2%.

Operating margin for the UK business segment improved [60] basis points to 2.2%.

Related to our Brazil segment, there is only one month of activity as reflected in prior year results. All metrics will be discussed on a same store basis. On a macro basis, the economy has slowed from the beginning of last year and Carnival was 23 days later this year which also served to push business out of the first quarter.

For the month of March we retailed 1,243 new units compared to 1,491 in March 2014. We also retailed 334 used units versus 394 units in the prior year. We generated $54.4 million in total revenues and $6.1 million in gross profit compared to $71 million and $8.4 million respectively in the previous year period.

Our adjusted SG&A as a percent of gross profit was 93.9% in the one month compared to 80% a year ago, while our operating margin decreased 160 basis points to 0.4%. Seasonally the first quarter is the weakest in Brazil. In total we lost money this quarter, but still expect to be profitable for the full year.

Turning to our consolidated liquidity and capital structure. As of March 31, 2014, we had $17.7 million of cash on hand and another $33.6 million that was invested in our floorplan offset account, bringing immediately available funds to a total of $51.3 million.

In addition, we had a $198.8 million available on our acquisition line that can also be used for general corporate purposes. As such our total liquidity at March 31, 2014 is $250.1 million.

Year-to-date for 2014 we have generated $69.7 million of operating cash flow on an adjusted basis.

With regards to our real estate investment portfolio, we own $642 million of land and buildings at March 31 which represents approximately 40% of our dealership locations.

The financing holdings, we've utilized our mortgage facility and executed borrowings under other real estate specific debt agreements. As of March 31, we have $67.2 million outstanding under our mortgage facility and $278.4 million of other real estate debt, excluding capital leases.

During the first quarter we use used $4.1 million to pay dividend of $0.17 per share, an increase of $0.02 per share over the first quarter of last year. We also repurchased approximately 270,000 shares of our outstanding stock at an average price of $62.74 for a total of $16.9 million. As of March 31, we had $54.5 million of share repurchase authorization remaining.

For additional detail regarding our financial condition please refer to the schedules of additional information attached to the news release, as well as the investor presentation posted on our website. With that I will now turn it back over to Earl.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Thanks. Thanks, John. Related to our 2014 corporate development efforts, we previously announced the acquisition of a Ford dealership and Hyundai dealership in southern California in January. Since then we opened a new Peugeot franchise in Brazil. We estimate total annualized revenues from these 2014 acquisitions to be $155 million.

We have also been granted two additional franchises, both of which we expect to open late next year. A Nissan franchise in Austin, Texas and a Land Rover franchise in Brazil. We will provide annualized revenue estimates when we announce the opening of these dealerships.

We also disposed of a franchise in April. A Hyundai franchise in New Orleans, Louisiana with annualized revenues of $20 million.

I will now turn the call over to the operator for your questions. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). Our first question comes from John Murphy, Bank of America Merrill Lynch.

Liz Suzuki - *BofA Merrill Lynch - Analyst*

Hi, this is Liz Suzuki on for John. In February, you had estimated a $0.15 to $0.20 negative EPS impact due to lost selling days for weather. How much of that, if any, do you think of that was recaptured in March, or do you think that your earnings would have been closer to $1.34 to $1.39 if January and February hadn't been so severe?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes, Liz, this is John Rickel. We certainly did do better in March, I think, than what we anticipated when we put that release out in February.

Some of that definitely was recapture of the business that got pushed out. If I had to give you a rough estimate, I would tell you that I think the weather ended up net probably impacting us by about $0.10 on the quarter.

Liz Suzuki - *BofA Merrill Lynch - Analyst*

Great, thank you. Regarding recalls, in the Toyota recall back in 2010 your parts and service operations got a pretty nice boost in same store sales volume and gross margin. Now, we have another Toyota recall that is about three times the size of that 2010 recall and Group 1 has the largest exposure to Toyota of the public dealers. Should we expect to see another short-term boost in parts and service for recalls on top of the underlying improvement in [UIOs]?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

This is Earl. I think it will certainly contribute to what is already a strong business. But I believe in this case the cars are a bit older, and that there may not be the same financial benefit per unit. But, it certainly is a positive factor.

I think the overall quality, however, of Toyota vehicles on the warranty side has improved somewhat also. So there is a couple of moving pieces within the Toyota business, and they both show up in warranty.

Liz Suzuki - *BofA Merrill Lynch - Analyst*

Okay. Thanks. I am going to squeeze in one more quick one.

On your cost structure in Brazil, the SG&A as a percent of gross profit was obviously much higher than the overall business. And seasonally, a lighter quarter there in a structurally higher cost region. What are the biggest opportunities in Brazil to cut costs and is there any low hanging fruit that can improve the cost structure over the next year or so?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes, Liz, this is John. We are very focused on working with our the Brazil team. And clearly as you indicate, basically the numbers I quoted were for one month which was a very light volume month because of where Carnival fell, so it distorts it.

The cost areas are similar to what we would have here in the US. It is in personnel. There is probably a little bit in advertising, though advertising isn't as big a part of the equation down there. And then it is in outside services are the primary areas that we are focused on.

And beyond that, even though it is not an SG&A item, we also think there is some healthy opportunities in floorplan interest expense.

Liz Suzuki - *BofA Merrill Lynch - Analyst*

Okay. Thanks very much.

Operator

The next question comes from Rick Nelson at Stephens.

Rick Nelson - *Stephens Inc. - Analyst*

Thanks. Good morning.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Good morning, Rick.

Rick Nelson - *Stephens Inc. - Analyst*

Could you have performed well particularly of late as has the UK, Brazil obviously more challenging. Can you discuss the outlook for sales in each of the three markets?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Let me begin, Rick, this is Earl, with the US. We had a projection before the year started at 16.3 million units for the US industry and I really don't see any reason to change that.

I still think that is a good number and a reasonably significant growth over last year's 15.6 million units. I think the US market is still quite solid.

I know a lot of us got skittish with the bad weather in the first 45 days of the year. But it seems that the underlying trend is still one of growth, so that is solid.

The UK industry continues to kind of defy logic, particularly given all the economic issues that have been on the continent the last few years even though the continent is starting to bounce back a little bit. And the nice thing about the UK is that it has been driven by the retail market increase, not the fleet increase and half of that market, or thereabouts, is fleet.

So wouldn't see the same percentage year-over-year increase in the UK this year as last, but you can tell from the first quarter in the March plate change there is still some growth going on in the UK. We are still optimistic about the UK.

Brazil in the first quarter of this year, Brazil is very difficult for anyone to predict in any way. Whether it is politics or GDP or commodity prices, and so forth.

In the first quarter, the Brazilian market was down 2% or 3%. In March it was down 15% because, as John mentioned, there was a Carnival shift and that messed up March this year where as some of those sales were moved from March into February.

There is also a presidential election. There is this bit about Olympics and World Cup, so Brazil is very choppy, but I think the market is not strong. I think the economy is flat at best and auto sales are probably less than flat.

But our business is a little different from the typical auto business in Brazil because there is four big brands there that dominate the market. They also have enough muscle to create sales that maybe shouldn't be sales whether it is rental cars or other kinds of push tactics.

Our brands are smaller brands; Toyota, Nissan, BMW and Land Rover, so we can outperform the market. So we are mostly concentrated on our business, and getting it rationalized and strong. I think there is no opinion that the Brazilian auto market is going to be strong in the foreseeable future.

Rick Nelson - *Stephens Inc. - Analyst*

And Earl, is there anything structural over there that would challenge you on the SG&A side to get that more in line with the volume declines and the margin pressures in Brazil?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

The challenge, I don't know that it will prevent us, but one of the more frustrating things is a lack of a single DMS provider that is available in that market. A computer system like we use ADP in the US. There is no dominant provider.

What we are concentrating on right now is getting a standard chart of accounts which is the same thing we did in the US many years ago so we have apples to apples cost reporting across all of our brands and businesses which we are starting to make some progress on. The lack of IT support is one of the bigger challenges.

But at the end of the day we will benefit from a little bit more scale there in terms of selling more cars, and anything we can do to grow the business and in having more of a management process to control costs like we use in the US and the UK. It is more challenging, but clearly we believe it is doable.

John Rickel - *Group 1 Automotive - SVP, CFO*

Rick, this is John. The only other structural thing I'd mention is that we lease all of our property there. That givesyou a higher cost base to begin with and maybe a little less flexibility.

Rick Nelson - *Stephens Inc. - Analyst*

Okay. And if I could squeeze in one more on the SG&A. As I look at the consolidated 76.2% ratio, the same store SG&A 74.9%, is that acquisitions that are coming in that are less efficient and some opportunities there from an SG&A standpoint?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes. Basically that is the main difference, Rick.

Rick Nelson - *Stephens Inc. - Analyst*

Very good. Thanks a lot. Good luck.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Thanks.

Operator

The next question comes from Brett Hoselton at KeyBanc.

Brett Hoselton - *KeyBanc Capital Markets - Analyst*

Good morning, gentlemen.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Good morning, Brett.

Brett Hoselton - *KeyBanc Capital Markets - Analyst*

I wanted to talk about two questions here. First, can you maybe go into a little bit more detail on gross profit through put for the quarter? I calculated a fairly low number, maybe my calculation is incorrect. What kind of a number are you looking at?

Then secondly, can you talk about maybe some of the drivers for what appears to be a lower gross profit through put?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes, Brett, this is John Rickel. You are right. We were not satisfied with the through put, but it was largely driven by the impact of the weather.

We certainly paid wages on days when we had stores closed. We had higher snow removal costs. You didn't have the gross generation from parts and service.

So basically, I think a lot of it was driven by that. When I parsed out the impact of the weather, I tell you kind of $0.06 of that earnings impact that I quoted to Liz was really on the cost front. And if you adjust for that, you are more into the 40% to 45% flow through that you would normally expect from us.

Brett Hoselton - *KeyBanc Capital Markets - Analyst*

Okay. And then as we think about the outlook -- changing gears -- as we think about the outlook for acquisitions, can you talk a little bit about the current environment? Whether it be deal flow relative to where we were maybe a year ago and valuation relative to where we were maybe a year ago? Have things improved, deteriorated, favorable, unfavorable?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

This is Earl. I think overall there is still a lot of sellers in the market. In fact, maybe even more this year than last year.

I think part of that is motivated by the recognition that some of these franchise values have peaked or more than peaked due to market share trends and things like that. And also a lot of capital expenditure requirements in a lot of brands that have recovered after the recession.

So, I think there is probably as many or more opportunities as past years. I think the pricing is more challenging than ever to get something that works based on looking at the future three years instead of the past three years.

The sellers look at the past. Buyers look at the future. So I think there will be more opportunities for everyone in our sector, but I think they have become increasingly difficult to put together.

Brett Hoselton - *KeyBanc Capital Markets - Analyst*

And then can you just talk briefly about gross profit per unit trends in the US in new and used. They have gotten a little softer here again in the first quarter.

What are your thoughts there? What are the primary drivers?

And then secondly, when do these bottom out? What is your outlook there?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Well, I think there is still extreme pressure on new vehicle margins particularly in the volume brands and even within that, the import volume brands. We continue to try to fight that.

We have been working to improve our margins on the new vehicle side, but I would have to tell you we haven't done very well. And, it just highly competitive out there right now.

I think the luxury brands still do reason reasonably well, and to a lesser degree, the bigger vehicles such as full sized trucks and SUVs. It is still very difficult and I don't see any change on the new vehicle margin pressure.

Used vehicle margins, I don't think we did a particularly good job in the first quarter, but again much of that came from the eastern half of the country. After we had 45 days of dreadful sales, we started to really move out a lot of our used vehicle inventory.

We keep a 30-day supply and we had a lot of aging vehicles. I think we retailed some at margins that we wouldn't normally and we also wholesaled more than we normally would.

To give you some flavor for the pressure we felt in the East Coast in the first quarter; we had a decent same store new vehicle sales increase in the first quarter, but the eastern half of the US even after a great March was still down double digits in the same store new vehicle sales. In New York and New Jersey we were down for the quarter 25%, and that was after a good March. When your activity backs up like that, it really damages your business which is what we were concerned about when we made our announcement in mid February.

Brett Hoselton - *KeyBanc Capital Markets - Analyst*

Thank you very much, gentlemen.

Operator

Next question comes from David Lim at Wells Fargo.

David Lim - *Wells Fargo Securities, LLC - Analyst*

Good morning. Can you hear me?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Good morning, David. Yes.

David Lim - *Wells Fargo Securities, LLC - Analyst*

How are you?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Good, how are you doing?

David Lim - *Wells Fargo Securities, LLC - Analyst*

Good, good. So the question that I have is momentum from March through April. Our channels are basically saying that it hasn't really petered out going into April. I mean can you comment on how April is trending for you guys?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Well, I don't want to make any specific comments about our business, but my general observations and what I read in the press and hear from everyone, and I don't have anything that would make me feel differently, is that April is very consistent with what we experienced in March and that is also what we experienced before the problems in January and February. So, I think that your observation is similar to mine, and that is that the underlying demand for new and used vehicles in the US is still pretty strong and on a growth trend.

David Lim - *Wells Fargo Securities, LLC - Analyst*

When we talk about the new vehicle gross margin pressure, how much of that is or if you could bucket that, how much of that is due to consumers being better informed about invoice prices versus let's say incentive actions from the OEM's and whether it be a stair step or volume bonus?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

That is a brilliant question. And I don't know, but those are the two factors. I guess I just simplify it and say it is 50/50.

David Lim - *Wells Fargo Securities, LLC - Analyst*

50/50.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Extreme pressure from market share from all of the OEMs, and that includes the luxury brands. And, yes, you do have a much more transparent market place nowadays with the digital media.

David Lim - *Wells Fargo Securities, LLC - Analyst*

And then finally my last question, Earl and John and Pete, when it comes to UIO's are we going to see like double digit growth relative to your same store parts and service? I know that you guys said roughly 6%, 7% last quarter. And I was thinking as the UIO numbers consistently grow, I would think that it would start materially outpacing let's say your used vehicle or new vehicle retail sales on a same store basis?

Earl Hesterberg - *Group 1 Automotive - President, CEO*

David, yes. We get that question about double digit all the time.

David Lim - *Wells Fargo Securities, LLC - Analyst*

I'm sure you do.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

I can't quite bring myself to mouth that with all of you on the call. But I would expect an above average performance for us in the coming quarter, and we have had pretty powerful comps for a long time.

I did look back and notice we had an 8.8% growth in the second quarter last year in parts and service, so I get a little bit nervous about piling 8% and 9% on top of 8% and 9%. But that is still clearly the strong part of our business model at the moment, and we did lose parts and service business in the first quarter. There is no doubt about it.

You only have so many loan cars and so many hours, and you can sell so many service bays and so many technicians. We definitely lost some business in Q1 in parts and service.

David Lim - *Wells Fargo Securities, LLC - Analyst*

I see. Congratulations on the quarter. Thank you.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Thank you.

Operator

The next -- I'm sorry. (Operator Instructions). Next question comes from Bill Armstrong at CL King & Associates.

Bill Armstrong - *CL King & Associates - Analyst*

Good morning. Forgive me if you addressed this already. I missed a little bit.

UK, your SG&A percentage had a huge improvement, 470 basis points. I was wondering if you could you just run through the drivers of that?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes, Bill, this is John Rickel. The biggest piece is just driven by the growth of the business. We had huge increases in revenues and gross profit generated, and the guys were able to do a good job controlling costs. They didn't have to add it in as fast as this grew the top line and we really started to lever.

One of the things we have been hampered with over there is just not enough scale and as we've added stores, and now the market is starting to rebound, we are finally starting to get enough scale that we can lever that growth. That is really what the team delivered which is a fabulous result in the first quarter for us.

Bill Armstrong - *CL King & Associates - Analyst*

To what extent was that improvement driven by having a full quarter of those four Ford dealerships under your belt?

John Rickel - *Group 1 Automotive - SVP, CFO*

That was a small piece of it. The bigger piece was just the overall same store growth with the existing stores and being able to lever that.

Bill Armstrong - *CL King & Associates - Analyst*

I see. Okay. That's great. Thanks.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

The Ford stores are very good performers, but the gross margins on the Ford business are not what they are on Audi and BMW business. So when you are looking at SG&A as a percent of gross, Ford inherently isn't going to give you a big mix benefit when you look at SG&A as a percent of gross because it is a volume brand.

Bill Armstrong - *CL King & Associates - Analyst*

Sounds like this improvement sounds pretty sustainable then?

John Rickel - *Group 1 Automotive - SVP, CFO*

Yes, we think so.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Yes.

Bill Armstrong - *CL King & Associates - Analyst*

Okay. All right, great, thank you.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

Thanks.

Operator

At this time we show no further questions.

Earl Hesterberg - *Group 1 Automotive - President, CEO*

All right. Well, thank you.

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

Okay. Thanks to everyone for joining us today. We look forward to updating you on our second quarter earnings call in July.

Operator

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.