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KAR Auction Services, Inc. (KAR)

Q4 2015 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the KAR Auction Services, Inc. Q4 and Full-Year 2015 Earnings Conference Call. Today's conference is being recorded. Later, we will conduct a question-and-answer session. [Operator Instructions] At this time, I would like to turn the conference over to Jonathan Peisner, Treasurer and VP, Investor Relations. Please go ahead.

Jonathan L. Peisner
Treasurer, Vice President-Investor Relations

Thanks, Cassandra. Good morning, and thank you for joining us today for the KAR Auction Services fourth quarter 2015 earnings conference call. Today, we will discuss the financial performance of KAR Auction Services for the quarter ended December 31, 2015. After concluding our commentary, we will take questions from participants.

Before Jim kicks off our discussion, I would like to remind you that this conference call contains forward-looking statements within the meaning of the Safe Harbor provision of the Private Securities Litigation Reform Act of 1995.

Investors are cautioned that such forward-looking statements involve risks and uncertainties that may affect KAR's business prospects and results of operations, and such risks are fully detailed in our SEC filings. In providing forward-looking statements, the company expressly disclaims any obligation to update these statements.

Lastly, let me mention that throughout this conference call, we will be referencing both GAAP and non-GAAP financial measures. Reconciliations of the non-GAAP financial measures to the applicable GAAP financial measures can be found in the press release that we issued yesterday, which is also available in the Investor Relations section of our website.

Now, I'd like to turn this call over to KAR Auction Services' CEO, Jim Hallett. Jim?

James P. Hallett

Chairman & Chief Executive Officer

Great. Thank you, Jon, and good morning, ladies and gentlemen and welcome to our call. Just want to outline a few things I'm going to talk about today, and then we'll get down to business. I want to talk about our 2015 results. I want to provide you with 2016 guidance. I want to speak about capital allocation, including an acquisition that we announced last night that I'm absolutely ecstatic about, and then talk about some longer term trends that we see going on within our businesses. And then finally at the end, I want to take a few minutes and clear up what I think is probably one of the most misunderstood aspects of our business.

So starting off, I believe we had a very good fourth quarter and I believe that this capped off an excellent 2015 for KAR. We saw revenue up 12%. Adjusted EBITDA was $650 million, an increase of 8.5%, and this adjusted EBITDA was led by ADESA which come in with adjusted EBITDA of plus 15%.

In terms of our guidance for 2016, we're providing adjusted EBITDA of $725 million to $750 million. And this will include approximately $25 million from the Brasher's acquisition which we expect to close in the first quarter. And this should result in free cash flow of approximately $340 million to $365 million. We do expect strong volumes in all of our business units. ADESA volumes will continue to benefit from additional off-lease vehicles, as well as the increased activity we're seeing in repossession areas.

AFC service offering continues to attract new customers and increased in loan transactions. And Insurance Auto Auctions is expected to continue to see improved volumes that will be driven primarily by low fuel prices, miles driven and the increased complexity of the vehicles that continue to drive the total loss activity.

Used car values are expected to decline somewhere in the order of 3% to 5% for 2016. But more importantly, I would ask you to focus on the number of transactions. We are a transaction business. And the transaction is far more important than the value of the vehicles. And I believe many of you are familiar with our pricing schedules. And basically, our pricing schedules go in increments of a minimum of $500 to $1,000. So, for a pricing to really affect our revenue, a vehicle would have to follow a minimum of $500 in value which we don't see happening.

So, we really don't see price changes in the wholesale market expected to hit any of the revenue per unit at ADESA. We expect that salvage values will continue to be much of what you see right now. And I believe we term that as being soft. We do begin lapping the significant decline in scrap values and foreign currency starting here in the second quarter. And so, starting in the second quarter going forward in 2016, we will have much more direct comparables as we go forward.

So, volume increases, I believe, are expected to more than offset any pressure that we're going to see on revenue per vehicle. We're going to continue focusing on controlling our SG&A, not only at Insurance Auto Auctions but within all of our business units.

And in the UK, we have implemented a number of changes at HBC that we expect will improve their performance in 2016 despite the depressed scrap prices we're seeing around the globe. AFC will continue to benefit from the ADESA volumes. The off-lease vehicles that we'll be making it to online-only open sales are an opportunity for AFC to floor higher value vehicles. And we do see an increased opportunity in the new markets following the Brasher's acquisition for AFC.

I want to take just a minute and talk a little bit about the AFC business model for a second. A number of years ago, we made a conscious decision that we were going to maintain 110 field offices or as we say loan production offices in the field. We wanted to have boots on the ground and we wanted to provide a level of service that we thought would differentiate us from our competition. And I can tell you we believe at the end of the day that these field offices will win out in terms of customer service.

When you think about being in the local market, a dealer wants a place to go where he can talk to a live human being, he can discuss his account, he can pay off a car loan, he can extend the car loan, he can pick up a title, all the things that dealers wants to do in a timely and efficient manner. And we believe that over the course of time, this will continue to differentiate us as we go forward.

I can tell you that we have had a few customers leave AFC for some very attractive pricing. But I can also tell you we've also had a number of AFC dealers that have left us recently returned. And as recently as this week, we had one of our largest AFC customers who left for an attractive pricing deal returned and that return was because of the service levels that I spoke to. So, I'm absolutely confident that we can offset any competitive pressure on pricing with our service levels at AFC and the volume of loan transactions.

Over the past several years, Eric and I have spent a great deal of time talking to you about our different businesses. And we've pointed out that we're not dependent on any one business for growth and that we have natural hedges between our business segments. And if I take you back to 2009 to 2012, I believe that we absolutely demonstrated the value of the combination of our businesses, and I think the combination of these diverse business segments is one of the greatest strengths within the KAR business model.

So, turning to capital allocation, we announced the agreement to acquire Brasher's Auctions last night, and I said at the outset, I'm absolutely ecstatic about this acquisition. Let me tell you a little bit more about this acquisition. First of all, the Brasher's family has been in business for 67 years in this industry. They're one of the most highly respected, highly regarded families within the industry. They have eight locations that we spoke about, in California, Utah, Idaho and Oregon, and other than California, these are three states where ADESA did not have any representation.

Brasher's have absolutely been the leader among the independent auctions. We reported that they're currently selling 190,000 vehicles per year. And the mix of commercial and dealer consignment vehicles are very similar to that at ADESA. We've been telling you for some time now that we're focused on expanding our buyer base, and this makes great inroads to doing that for ADESA with this acquisition. We're also very, very focused on protecting and growing our online offerings, especially our private label sites which you know is an area that we dominate that space, and we expect to continue to have those private labels going forward.

We talked about the opportunity for AFC to go in and have a presence in these new markets, and then there's the opportunity for us to introduce our ancillary services. We talk to our customers about being able to provide an end-to-end remarketing solutions, make one phone call and we can provide any service that you're going to require in terms of remarketing an automobile. And just a few of examples, we can speak to, CarsArrive and High

Tech Locksmiths and our inspection business and our dent removal business. You think about all these services that we're now able to integrate into these new acquisitions.

And as I speak about this, I haven't even spoken to you about possible synergies that will take place once we're fully integrated. You can do the math. You've seen what the purchase price was. You've seen what the EBITDA on an annual basis was and you've calculated the multiple. We believe that not only is this deal accretive, we believe it's going to be a very attractive deal, now and post-synergy and a great addition for the ADESA business.

We did report that we increased our quarterly dividend $0.02 per share. Our dividend now makes up 45% to 50% of our free cash flow. And we would tell you as well that we expect to complete additional acquisitions in 2016. There are a number of opportunities that are in the pipeline. Discussions are well underway. And I can also share with you that these acquisitions are primarily focused on the whole KAR business as we continue to take advantage of the cyclical recovery that we believe will continue in the U.S. for several more years.

I believe that all of our businesses are well positioned for 2016 and beyond. We believe that strong volumes will more than offset any softening of prices that we've seen in any of the businesses. And as I've mentioned previously, the number of transactions is far more important than the value of the vehicles in all of our business segments.

And we're working diligently on integrating our businesses that we've acquired. And quite frankly, I would tell you that I am not satisfied with how fast we've moved on getting these businesses integrated. In fact, I'm focused on eliminating the redundant SG&A with all these acquisitions. And my mandate to the organization is to have this Brasher's acquisition integrated as quickly as we possibly can, and I can tell you I will be inspecting the timelines.

So, with that, you think about the headwinds that we could possibly be facing in the business and you can say used car values may fall 3% to 5%. Foreign currency pretty much going to continue to be what it is. Scrap metal prices aren't likely to change anytime soon. And we're always going to have competition. But the good news is that we've continued to tell you that we have multiple levers that we feel that we can pull to overcome any potential headwinds that we face.

And I haven't spoken about Canada yet. The fact of the matter is we're seeing early signs of a cyclical recovery in Canada, and Canada represents about 15% of our business. We've had very nice growth in dealer consignments in Canada over the last couple of years. And now, we expect to see the commercial volumes start to rebound as we approach 2017 in Canada.

And if you think about it, we're talking about a 30% lease penetration in the U.S. Pre-recession, Canada was a 50% leasing market. And we know that that will serve us very well from 2017 going forward for several years. So, do I feel very good about our businesses for the next several years at KAR? Absolutely. We have great visibility on volumes. We have a stable automotive industry with a healthy SAAR. And even if the SAAR were to decline, we don't believe it will have a meaningful impact on our results. And in terms of our financial performance, we're expecting a 12% to 15% growth in adjusted EBITDA in 2016 which will allow us to increase our free cash flow.

So before I turn it over to Eric for his commentary, let me try and clarify what I believe is one of the most misunderstood factors in our business, and that's the SAAR. And SAAR is a topic that many of us are focused on right now. And we expect the U.S. SAAR to stay flat or even decline modestly here in 2016. But more importantly, the thing that I want to point out is SAAR is not the primary driver of wholesale used car auction volumes. The fact of the matter is we are not in the new car business. We are in the used car business.

And the thing that I would ask you to keep in mind is I would ask you to think about that car park, that chart that we've probably shown you numerous times and look at that very center dot on that car park where it shows that there are 40 million to 45 million used car transactions that take place on an annual basis. And this is what we refer to as the churn. And let me assure you that the churn of these 40 million to 45 million used cars is much more important than anything that's going to take place in the new car business.

So, I would tell you that I expect strong retail used car market in 2016 to continue. I would say it can possibly even get stronger if prices were to start to decline. And the other thing I would point out is oftentimes people think there's only a trade-in on new car transactions for one reason or another. Well, let me assure you there's as many trade-ins on used car transaction as on a new car and those used car transactions more often end up at a physical auction, perhaps in some of the new car trades because the dealers are keeping a lot of those new car trades. And this creates what I would consider additional activity with trade-ins at the auction.

So, I want to assure you that absolutely nothing has changed in my opinion on how the cycle plays out. And more importantly, I see what I would call even greater opportunities for us to deploy capital and continue to capture market share.

So, with that said, I love how we're positioned in all of our businesses, and I absolutely feel that we can handle whatever comes our way. When you think about this, this is a great business. It has a great outlook as we look forward with the visibility that we have. We know we have strong volumes. We know our earnings continue to grow. We know our free cash flow continues to improve, and I would finish by telling you that I'm absolutely convinced that we have an experienced management team that is ready to deliver results.

So, with that, I'm going to turn it to Eric, and then we'll come back for Q&A. Thank you. Eric?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

Thank you, Jim. Let me start with the summary of our 2015 performance. For the full year, revenue of $2.640 billion was up 12% over the prior year. Consolidated adjusted EBITDA of $650 million was up almost 9% over the prior year and landed right in the middle of our expectations. Adjusted net income per share of $1.70 was 5% over 2014, and our effective tax rate for the year of 37% was 1% higher than the effective tax rate in 2014.

As we have discussed throughout 2015, our primary earnings measurement will become operating adjusted net income per share. We have been reporting operating adjusted net income per share each quarter. Our operating adjusted net income per share in 2015 was $1.90, an 11% increase from $1.71 in 2014.

Beginning in the first quarter of 2016, we will not be reporting adjusted net income or adjusted net income per share any longer. We will also be working with our analysts to begin reporting operating adjusted net income per share as our primary earnings measurement. We feel operating adjusted net income per share is a representation of cash net income per share and better reflects the cash earnings power of KAR.

Now, let me provide some commentary on the business segments. ADESA had strong revenue growth, up 13% in the fourth quarter. Excluding acquisitions, ADESA's revenue was up 9% for the quarter. This strong revenue growth was driven by 12% volume growth, 10% on a same-store basis. Physical auction volumes were up 6% in the fourth quarter, with revenue per unit at physical auction of $740. In this strong ARPU performance at physical auction was net of a $20 reduction due to the weak Canadian dollar. The increase in ARPU reflects the increased ancillary and other service revenue, which is lower margin revenue than our auction services.

For 2015, ADESA's 13% revenue growth, excluding acquisitions, driven by 10% physical auction volume growth and 20% online-only volume growth. For the full year, physical auction revenue per unit was $701 compared to $685 in the prior year. This $16 increase in ARPU was net of an $18 reduction due to the weaker Canadian dollar. Online-only ARPU was $107, up $3 from the prior year and net of a $3 reduction due to the weaker Canadian dollar.

Dealer consignment volumes continued exceeding our expectations in the fourth quarter, increasing 9% over the prior year. For the full year, we had 7% growth in dealer consignment volumes at ADESA. We saw commercial volumes increased 3% in the fourth quarter and 13% for the year at physical auction. The lower commercial volume increase in the fourth quarter is not due to a lack of supply. We had a significant increase in the number of commercial cars on the ground at year-end. The consignors spent the ancillary services dollars on these vehicles and they are ready to sell early in 2016.

Acquisitions accounted for $2.2 million of adjusted EBITDA and $14.8 million of revenue in the fourth quarter for ADESA. This should assist you in computing the incremental margin for the quarter. The incremental margin at ADESA, excluding acquisitions, was 24% for the quarter. This compares to an incremental margin of 29% for the fourth quarter last year. The lower incremental margin reflects the seasonal impact of lower volumes sold at auction combined with high utilization of the lower margin ancillary and other services.

For the full year, ADESA acquisitions contributed $6.8 million of adjusted EBITDA. Incremental margins, excluding acquisitions, for the full year at ADESA were 31%. We are focusing on eliminating redundant SG&A and increasing our incremental margins in 2016.

Insurance Auto Auctions continues to perform well in a difficult pricing environment. Volumes increased 14% in the fourth quarter and 11% for the full year. This was offset by a 5% decline in revenue per unit for the fourth quarter and 4% decline for the year. The weaker Canadian dollar reduced our revenue per unit by $6 for the quarter and for the full year. Inventory continues to be strong at Insurance Auto Auctions. At December 31, 2015, inventory was up 14% over the prior year-end. Despite the pressure on revenue per unit, Insurance Auto Auctions generated 27% incremental margins in the fourth quarter and 24% for the full year.

Jim has already commented on the competitive pressure at AFC. However, another item to discuss is the increase in the provision for loan losses in the fourth quarter. We had a couple of large write-offs in the fourth quarter that were anticipated and relatively low recoveries combined with an increase in the allowance for doubtful accounts on our balance sheet.

The increased provision for loan losses accounts for a $6 decrease in revenue per loan transaction in the quarter. This is not due to an overall deterioration in the portfolio, but recognition of the 20% growth in the portfolio during the year. As you can see in our financial statements, the net provision for loan losses for the year was only $16 million with $5.5 million of those losses recorded in the fourth quarter.

In terms of free cash flow generated in 2015, KAR generated $650 million of adjusted EBITDA with $61 million in cash interest expense on corporate debt, $135 million in capital expenditures, and $116 million in cash taxes. This results in $338 million in free cash flow or $2.38 per fully diluted share. The capital expenditures include $16 million related to the ADESA Chicago greenfield project.

In addition to the adjusted EBITDA guidance for 2016 provided by Jim, we expect $85 million in cash interest expense, $145 million in capital expenditures, and $150 million to $160 million in cash taxes. This will result in free cash flow of $340 million to $365 million or $2.45 to $2.63 per fully diluted share. We are assuming an effective tax rate of 37.5% for 2016. We expect operating adjusted net income per share of $2.05 to $2.20 in 2016. This assumes weighted average shares outstanding for the year of $139 million.

Let me close with an update on our capital structure. We have increased our revolving credit facility from $250 million to $550 million. There were no other changes in terms and conditions. The increased revolver will be used to fund the purchase of Brasher's Auctions and general corporate purposes. Our 2016 guidance assumes the revolver is used to fund the acquisition as of March 31, 2016. Term loan B-1 with a balance of $637.2 million at December 31, 2015 matures in March 2017. It is our intent to refinance term loan B-1 and our revolving credit facility which expires in March of 2019 during the year 2016.

That concludes my remarks. So let's turn it back to Cassandra for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And we'll go first to Ryan Brinkman of JPMorgan.

Ryan J. Brinkman
JPMorgan Securities LLC
Q

Great. Thanks for taking my question. Firstly, congrats on Brasher's. My understanding is that they were seen as unlikely sellers, that they have an established presence and high share in the markets that they serve and therefore, could be a great geographical tuck-in. Firstly, is that understanding correct? And then secondly, if it is, does that mean that there likely wouldn't be as many cost synergies because maybe you don't have so many yards in the areas where they operate? And if so, were the synergies that Jim was talking about maybe more on the revenue side? Can you provide any color there? And then does it mean anything for AFC? Any opportunity for AFC?

James P. Hallett
Chairman & Chief Executive Officer
A

Yeah. Ryan, I think your assessment of the opportunity is spot on. It is a great acquisition. It is in a geography that we're currently not in. Again, very strong organization and as I've said, very highly respected family by our customers, regarded for their customer service levels.

I would tell you that some of those synergies that I talk about are going to be revenue synergies, but not to say that there won't be some efficiency opportunities. And in terms of AFC, as I mentioned in my commentary, absolutely an opportunity for AFC. Not to say that AFC doesn't have dealers in these markets or possibly have transacted at some of these auctions, but now this gives us a presence. As you know, we locate our AFC offices within an auction whenever possible. So, as we're able to put these as we say boots on the ground, integrate those offices, we think this is an exceptional opportunity for AFC.

Ryan J. Brinkman
JPMorgan Securities LLC
Q

Okay. Great. Thanks. And then just on IAA, too, EBITDA's been very strong there, maybe better than we would ordinarily expect, just given the stronger dollar and softer scrap metal prices. So, can you say if you're passing on higher fees that's offsetting the impact or is it more just the really strong volume giving you good expense leverage?

And just lastly on IAA, too, the volume is up 16%, that's pretty huge. Copart said on their last call that they've gained a big customer win. Should we start to see the volume gains moderate? Does that impact you? And if so, how should we think about the cadence of any tapering?

James P. Hallett
Chairman & Chief Executive Officer
A

So, Ryan. First point is I would say that the performance at IAA is primarily driven by the volume increases. And then in regards to customers, bottom line is there is wins and losses. And there is always RFPs that are going to come and go, and we're going to win some, we're going to lose some. But things I would point to and ask you to focus on is I would ask you to focus on our performance. And when you take a look at our performance year-over-year and the volume increase that we've demonstrated, I would think that would point to we're winning more than we're losing.

Ryan J. Brinkman
JPMorgan Securities LLC
Q

Yep. Okay. Thanks a lot.

James P. Hallett
Chairman & Chief Executive Officer
A

You're welcome.

Operator: And we'll go next to Elizabeth Suzuki of Bank of America.

Elizabeth Lane Suzuki
Bank of America Merrill Lynch
Q

Good morning.

James P. Hallett
Chairman & Chief Executive Officer
A

Good morning.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Good morning.

Elizabeth Lane Suzuki
Bank of America Merrill Lynch
Q

How did commercial consignment trend throughout the year and was the fourth quarter weakness just a short-term issue, supply constraint? And what should we think about as the outlook for commercial consignment in 2016 once we get past like a first quarter correction that you mentioned?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Thanks, Liz. I'll start and then Jim will probably add something. It was a fall off in the fourth quarter with a 3% increase in commercial consignment after double digit increase in the third quarter, little weaker in the first quarter, strength second, but third quarter was the strongest. And really, as I mentioned, it wasn't a lack of supply.

It's really the consignors and it's predominantly going to be the OEMs and the captive finance companies, you had the cars coming back.

They were selling aggressively on the upstream or the private label site which was up 32% for the quarter. But as it got to the physical auction, the cars are on the ground. They did the work to improve the quality of the vehicle which is the ancillary services. And while we don't discuss a specific inventory number at ADESA, those cars are building up and we're seeing, as if you visit one of our sites, you'll see a lot of cars on the ground even right now.

James P. Hallett
Chairman & Chief Executive Officer
A

Yeah. And the only thing that I would add to that is there's the impact of the holidays that could be slowing down, pushing these cars to the channel. And then I would just finish off by saying, I don't believe that this points to a trend. I believe there's an anomaly that took place in the quarter. And I think what we need to do is we need to look at what takes place here in the first quarter of the year, and into 2016, I think you'll see that volumes will get physical auction.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

And in previous calls, we've talked about the trends in lease originations from three years ago. The originations that are due to mature or expire in 2016 are at least half a million greater than the volume we had maturing or expiring in 2015. And I've seen some articles that get that number even higher than that, maybe as much as 800,000 more. So, there's no indication that there's going to be any tapering of the commercial volumes in our opinion. We expect a very good year in that part of our business.

Elizabeth Lane Suzuki
Bank of America Merrill Lynch
Q

Okay. Thanks. That's really helpful. And since it seems like the market is very concerned about another downturn in the U.S. cycle, can you just talk about what happened at ADESA in the last downturn because it seems like your worst year for growth which is 2011 only had about a 5% year-over-year decline in revenue. So, I'm curious if you can break out how much of that decline was organic versus acquisitions and what the worst case scenario would be.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Well. And again, Liz, as you focus on ADESA or do you want to focus on consolidated?

Elizabeth Lane Suzuki
Bank of America Merrill Lynch
Q

I was just looking at ADESA specifically.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Okay. So, at ADESA 2011, we had done our last acquisition of a physical auction property in August of 2008. And we put a moratorium as we were conserving capital back in that period of time. So really, what you saw is the fact that we have, as Jim has mentioned, great visibility. And the visibility is created because when there's that softening in the new car space or the retail sector, it takes two years to three years before it hits the wholesale used car market because you've got all that activity that is really derived from events that occurred two years, three years earlier. And so, we prepare for that.

And as you do that, we invested in the dealer consignment sales force. We really went after other segments of the market. And I'll turn it to Jim and he can maybe talk about the multiple levers in the businesses. There's multiple segments for us to attract volume.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. I think Eric has mentioned the good part of it here. I think we recognize that commercial volumes were going to fall. But we also recognize that was going to take a few years to run off these commercial volumes before they hit the low in 2011 and 2012. And we focused on building a dealer consignment team. And our dealer consignment team ramped up to over 300 people in the field, totally focused on working on getting more dealer consignment. And we took our dealer consignment from 25% of our business as a low, up to currently above 50% of our business. So that was the major offset, was trying to offset the commercial vehicles with the dealer consignment vehicles.

And then, as we were running off these portfolios, we got very engaged with what we refer to as Pride and enterprise optimization. And we had focused on cost and we had focused on efficiency. We were able to take price during that period of time on the vehicles that were coming to the auction. And I think overall, it was just pulling a number of levers in every direction that we possibly could to get through that period of time.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

And the last thing that I would add to it is the wholesale auctions are an opportunity for dealers to move the cars into the part of the market that can retail the vehicle. So, the focus on dealer consignment, think about the independent used car dealers, 35,000 to 40,000 independent used car dealers. Sometimes, what you're seeing when you talk about the national retailers or the franchise dealers having inventory that's too aged for their customer base, they're going to wholesale that vehicle to get it back to the independent used car dealer.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. And I – finally, I wouldn't lose sight of what took place at Insurance Auto Auctions. While ADESA was absolutely seeing this runoff of inventory and they were losing transactions on an overall basis, we saw a strong performance at IAA where – and that goes back to the comment I made about the natural hedges and their business in my commentary. IAA performed very well throughout that period. And quite frankly, I was very appreciative of the diversity of our business during that time.

Elizabeth Lane Suzuki
Bank of America Merrill Lynch

Q

Great. That's encouraging. Thank you.

James P. Hallett
Chairman & Chief Executive Officer

A

You're welcome.

Operator: And we'll go next to John Healy of Northcoast Research.

John Healy
Northcoast Research Partners LLC

Q

Thank you. Jim and Eric, I just kind of wanted to ask you kind of a bigger picture question. When you look at kind of the off-lease supply that's coming into the market and you look at kind of the areas of the retail side of the business that is absorbing this side of the business, one of the things that we've noticed is just how that's fueling the growth in the certified pre-owned market. And if you look at some of the trends there, it seems like growth there is kind of leveling off a little bit. Do you guys see that leveling off? And if that does level off, I mean is that kind of a canary in the coal mines to you, guys, that, hey, these vehicles are now going to end up at the physical lanes because the franchise dealer base just simply isn't large enough to absorb all of these units? Curious to get your kind of thoughts on kind of how that hinges together in the industry.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. John, I do see it stabilizing or leveling off and I do see more of these vehicles going through the channels and getting to the independent dealer. And I think if that happens, Eric, what were you going to say?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Yes. I mean John, I think you summed it up very well, but the car is going to sell. The car is going to go somewhere in the wholesale marketplace to some dealer who can retail the vehicle at the right price. And I think what we're focused on is the economic variables. You've got supply, you've got demand, but you have not price. And I do think we're seeing in the marketplace the used car values of those late model CPO vehicles is coming down, right, and the dealers are less focused on saying, hey, I can't get the premium. So, I'll turn it back to Jim.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

But I think that's really where the independent dealer comes in because that's the best car on their lot, not the used car on the new car dealer lot. Right, Jim?

James P. Hallett
Chairman & Chief Executive Officer

A

No question and I was going to add that. We know that they've whittled down the population of franchise dealers. It's franchise dealers that are primarily buying these cars for CPO purposes. They're not adding any more franchise dealers. So, that population is not growing. So, at some point in time, when they have enough supply that these vehicles have to get released to the open market and give the independents an opportunity to buy those vehicles.

John Healy
Northcoast Research Partners LLC

Q

Got you. And Eric, I want to ask a little bit about the loan loss movement on AFC. I know you've talked about it going up a bit. I was hoping you could give us a little bit more color on kind of your expectations on this, if there was a couple of customers where you had some write-offs. But if memory serves me right, I thought you guys lowered your reserve in the third quarter. So, is this simply kind of things catching up as you'd originally expected a quarter or so ago? I'm just trying to understand that.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

No, John. We've actually been increasing the reserve every quarter this year. What was down was the provision for loan losses and that's just the timing. What happens is the write-offs run through our provision for loan losses. And that's going to be due to the timing of when the dealers are going in and out of the business, right? And so, there was – and also, the recording of recoveries. I mentioned we had low recoveries in the fourth quarter, higher recoveries in the third quarter that nets the number down.

So, we're not seeing a trend that would tell us over the course of a year, you'll see major change. That's why I highlighted the $16 million number. But again, the timing can be – and it's not unusual to have a little bit more bad debt at the end of the year. And it's also – I'm not predicting anything, but it's also not unusual to have a little less at the beginning of the year because that's the strong used car retail season and the dealers just don't run into their struggles until later in the year.

John Healy
Northcoast Research Partners LLC

Q

Got you. And then, just one final question. There's been some headlines in the space about General Motors and their kind of entrance into this kind of preferred collection where they're trying to move units maybe directly to the consumer that come out of the lease or the rental channel. Can you guys talk about if that's something maybe you're helping them with or that's a competitor or just kind of your initial thoughts on that product?

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. A couple of thoughts there is – number one is that's very much in its infancy, so, it's just getting announced and just getting started. Secondly, I would say to you our job is not to try and direct the car or direct the customer to any one particular channel, and we're going to sell cars whatever way the customer wants to get them sold, and yes, we are very much involved in the process with General Motors of facilitating these transactions, and we will be getting fees when those transactions take place.

John Healy
Northcoast Research Partners LLC

Q

Great. Thank you, guys.

James P. Hallett
Chairman & Chief Executive Officer

A

You're welcome.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Thank you.

Operator: And we'll go next to Tony Cristello of BB&T Capital Markets.

Anthony F. Cristello
BB&T Capital Markets
Q

Thank you. Good morning.

James P. Hallett
Chairman & Chief Executive Officer
A

Good morning, Tony.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Good morning.

Anthony F. Cristello
BB&T Capital Markets
Q

First question, I think your earlier remarks, Jim, you talked about some of the industry trends and low gas prices, miles driven, and what's going on with the average age of the vehicle as it pertains to the IAA side of the business, and I'm just wondering [audio gap] (40:06) where we continue to see outsized volume growth because the age of the fleet is going to lead to potentially even a greater number of total losses. And if that's true, when you look at your business and the ability to potentially leverage or take advantage of that volume, where are sort of a key point that you'd say, hey, we think this is going to be really good for the business because of yard side or levers on fleet of movement of vehicles and those type of things?

James P. Hallett
Chairman & Chief Executive Officer
A

Yeah. Tony, I think the one thing that I would point to immediately is what we've always referred to as the differentiator in our business model and that's our hybrid methodology, the fact that we offer every car in an online venue, as well as the physical venue, and as a result of that we feel that not only do we attract more eyeballs, but we also feel that we drive higher resale or we drive higher return on these cars as well. Eric, do you want to add that?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Yeah. Tony, you kind of broke up on part of your questions. But again, the market is just in a very good place, with the complexity of vehicles, lots of miles driven, low gas prices, lots of cars on the road, they're going to run into each other. And I think we're well-positioned. As we've grown our footprint, we're adding space all over the businesses, including in the West now, adding some more properties that are investment-focused, but that gives us land to use for all of our businesses. So, I really think we're in a great position to service all of the markets of our segments.

Anthony F. Cristello
BB&T Capital Markets
Q

Okay. And then I guess shifting gears a little bit. How does demand for – whether it's – right now, [audio gap] (42:07)

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Your phone is cutting out, Tony.

Anthony F. Cristello
BB&T Capital Markets
Q

I'm sorry. Is this better?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

I can hear you now.

Anthony F. Cristello
BB&T Capital Markets
Q

Okay. I apologize. So, I guess I'm wondering, is the demand at the dealer groups right now appears to be more SUV and truck-oriented and what does seem to be coming off of these, I guess, are more vehicle cars and those type of things. Is there a dynamic there that would lead to more of that volume that hitting the auction lanes, rather than being absorbed at the dealer itself on the lease return.

James P. Hallett
Chairman & Chief Executive Officer
A

Again, Tony, I don't really see that so much as whether it's an SUV or whether it's a car or something in between. It's just transaction for us. And I don't really see – I don't see that difference taking place. Maybe I'm just not...

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

But Tony, one thing to highlight, if there's imbalance, if the market is looking for more trucks and SUVs and there's sedans coming off lease, the sedans aren't probably going to get picked off at the top of the funnel in the private label side. They're going to make it to auction, so that there's a broader market to sell to. Right, Jim?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Yeah. Theoretically, I mean, that's what you would anticipate happening. But the market kind of determines what gets sold at the top of the funnel and what gets to physical auction. And again, at the end of the day for us, I just go back saying this is just transaction.

Anthony F. Cristello
BB&T Capital Markets
Q

Okay. And maybe just on HBC, you talked about initiatives to improve the business from where it is today. Can you maybe just expand a little bit on those? And then again, thank you for taking my questions today.

James P. Hallett
Chairman & Chief Executive Officer
A

Well, you're very welcome and I would say, at a high level, what we've done is we've met with the folks in HBC and we've restructured the pricing models somewhat, and we think it will lead to an improved performance.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

But in no way are we changing the business model. We're still in the model of taking principal risk over there more so than in the United States. It's the pricing that – what price we would pay for the vehicle so there's an adequate return as we move forward.

Operator: And we'll go next to Matthew Fassler of Goldman Sachs.

Matthew J. Fassler
Goldman Sachs & Co.

Q

Thanks a lot, and good morning.

James P. Hallett
Chairman & Chief Executive Officer

A

Good morning, Matt.

Matthew J. Fassler
Goldman Sachs & Co.

Q

My first question relates to the acquisition. As we model that, I know it's primarily an auction business, but it also is a floor planning business. How much of that EBITDA number that you disclosed relates to the finance business versus the auction business, so that we can model it out appropriately?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Again, we've not disclosed the component, but I can tell you relative to the 2016 number in our guidance, there is a very modest amount for the floor plan business. Because within the details of that, we did not acquire the book as of the closing date. We are not planning to acquire that. So, there'll be a runoff and we'll fill it back up. So, it's not a significant component of the $25 million. It is a component but not significant, Tony (sic) [Matt].

Matthew J. Fassler
Goldman Sachs & Co.

Q

With the profit mix, if we were to say, for example, take IAA out of your business, would the profit mix be similar to what it is for KAR or would it be a different kind of number?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Matt, ask again. I...

Matthew J. Fassler
Goldman Sachs & Co.

Q

I guess, if you were to think about the mix of the contribution of credit, would it be similar to what you all have if you were to take your salvage business out of your P&L thinking about the contribution of credit and floor planning relative to the auction business?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Yes. It will look very much like ours. And again, when I tell you about it, you can even look at their $34 million of EBITDA compared to their $140 million of revenues, about a 24% margin. We probably have a lower cost of funds on the floor plan than they're incurring with their capital structure. So, yeah, I think there's opportunity there and it'll look very similar to our businesses.

Matthew J. Fassler
Goldman Sachs & Co.
Q

That's helpful. A second question, if we think high level and you've given us these great numbers, this great disclosure over the past couple of quarters about the incremental margins excluding acquisitions, is there a dollar number that you would attribute in 2016 EBITDA to either synergies or dollar contribution from acquisitions? I don't think you put that in the guidance, or I might have missed it there.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Well, we have included – if I have your question, Matt, we have included the $25 million from Brasher's...

Matthew J. Fassler
Goldman Sachs & Co.
Q

Exactly. And so in addition to that number sort of within that core $700 million to $725 million.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

No, what you have is just one quarter of Pittsburg because we acquired that at the end of the first quarter last year.

Matthew J. Fassler
Goldman Sachs & Co.
Q

Yeah. But it sounds...

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

And the rest of it is as you can see using the capital available to us and most of it's being committed to the Brasher's deal as of now, and that's what's in our guidance.

Matthew J. Fassler
Goldman Sachs & Co.
Q

Got it. But there should be, I think, to Jim's point some cost cuts and other profit enhancements in the acquired businesses that contribute to that number?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Yes. We do intend reducing redundant SG&A, and that is included in our outlook.

Matthew J. Fassler
Goldman Sachs & Co.
Q

Got it. And then one final question. I hate to ask kind of a technical one, but as we go through the disclosed P&L for AFC, there was, I guess, an add-back or, I guess, the opposite of an add-back, a takeout within AFC in Q4. Can you just talk about what that number relates to? You typically have add-backs, this one moved I believe in the other direction, just what that line item represents?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

That represents the interest expense on the securitization...

Matthew J. Fassler
Goldman Sachs & Co.
Q

Perfect. Okay.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

...which is included in interest and corporate now, and we do not take credit for that, because that's related to the revenue generated from that portfolio and it's an offset.

Matthew J. Fassler
Goldman Sachs & Co.
Q

Got it. Thanks so much, guys.

James P. Hallett
Chairman & Chief Executive Officer
A

Thank you.

Operator: And we'll go next to Bret Jordan of Jefferies LLC.

Bret Jordan
Jefferies LLC
Q

Hi. Good morning.

James P. Hallett
Chairman & Chief Executive Officer
A

Good morning, Bret.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Good morning.

Bret Jordan
Jefferies LLC
Q

Question on Brasher's, I guess if you look at the mix of their business and its online versus physical and maybe revenue per unit, how does it stack up to your ADESA? And is there an ability to leverage maybe some of your online efforts against their volumes?

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah, Bret. We believe there is – independents tend to sell a little bit less online than what the change do, not a huge gap, but a little bit less. So, we do see an opportunity to increase our online buyer activity there. And what was...

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

And on revenue per unit, if you just take what we gave you, there is finance income. They're a little bit below us, but they had a pretty strong revenue per unit. I think we can add some additional services that Jim mentioned. Some of the logistics we do in CarsArrive and High Tech Locksmiths would be new services in their market. So there's opportunity on the upside, but it's not a huge difference relative to what we see at our physical auction.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. Overall, I think I – well, I did state earlier that number one is the mix is very comparable. And there isn't really a major gap in either revenue per car or the number of online vehicles sold, somewhat, but nothing that we don't think we can't bring up to our levels in a very short time period.

Bret Jordan
Jefferies LLC

Q

Okay. And then on ADESA's incremental margins, you've got that negative impacts from the higher ancillary mix. Is there a tipping point where the volumes can offset what's going to be a year-over-year drag from higher ancillary? I mean, can we pick up, if we've got another 0.5 million units coming off lease this year. Are we going to see that margin gap close year-over-year despite the physical ancillary services?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Yeah. Bret, what I was focused on is the fourth quarter always has higher revenue per unit and lower margin. And I gave you the incremental margin, last year was 29%, the lowest of the year. Yes, we're not pleased that it was more like 24% this year, but it would have been lower than what we'd experienced all year. And so I just – I think the business will take care of itself. You go to the first quarter and second quarter, there's just a lot more volume. There's a lot more auction revenue. The revenue mix as well as the margin mix is much more consistent as you get into the season of the wholesale used car marketplace.

Bret Jordan
Jefferies LLC

Q

Okay.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Does that answer your question?

Bret Jordan
Jefferies LLC

Q

Yes, it does. Then one last question. You said you've signs of return in Canada, and I guess maybe you could give us a feeling for what's giving you that impression that the Canadian market is turning. That will be great.

James P. Hallett
Chairman & Chief Executive Officer

A

Yeah. There's no question that we've talked in the past that Canada as we went into the recession certainly lagged the U.S. coming out of the recession. We've seen an improvement in new car sales in Canada. We've seen absolutely an improvement in the number of vehicles that are being leased. I think if my memory serves me correctly, Canada reported record sales of new car sales last year of $1.9 million, and again, a very high percentage of those cars are being leased cars would start to fill the pipe for the out-years.

Bret Jordan
Jefferies LLC

Q

Okay. Great. Thank you.

James P. Hallett
Chairman & Chief Executive Officer

A

You're welcome.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Thank you, Bret. And Cassandra, I know we only have five minutes scheduled, so we'll try to move quickly through the last questions. I know there's a number waiting in the queue.

Operator: And we'll go to Bob Labick of CJS Securities.

Robert Labick
CJS Securities, Inc.

Q

Good morning.

James P. Hallett
Chairman & Chief Executive Officer

A

Good morning, Bob.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Good morning, Bob.

Robert Labick
CJS Securities, Inc.

Q

Hi. Just maybe a little bit background. How long have you been speaking with Brasher's and what prompted them to ultimately sell now? And are there other similar-size independent auctions out there, or are they one of the biggest ones that was left?

James P. Hallett
Chairman & Chief Executive Officer
A

Well, I can tell you, Bob, I've been speaking with Brasher's for 20 years. As a matter of fact, I told the folks the other day that when I attended my first National Auto Auction Conference, I rode a shuttle bus from the airport to the hotel with Larry Brasher. So, that goes back 20 years. But the long story of this story is we continue to talk with these independents on a regular basis. We see them at conferences, and we see them at events, and we have some initiatives that we work on in the industry together.

And so it's been a longstanding relationship, not only with myself but maybe more so with some other folks in our organization. And then secondly, I would say that we've always maintained that there's probably five to 10 really what I would call plum opportunities, although we may have captured the biggest plum here. But there's really five to 10 opportunities out there that if they became available and we could get these done at the multiples that we've maintained discipline around, then we'd be very much interested in acquiring those in the market that I 'm talking about.

Robert Labick
CJS Securities, Inc.
Q

Okay. Great. And then I know – just to be quick, on IAA, you've talked about the favorable outlook for [ph] sellers and buyers in 2023, many years ahead of growth (54:01). Could you just clarify, do you have enough capacity in your existing footprint or do you need to make acquisitions at IAA as well or can you grow your existing footprint without acquisitions? How are you planning on getting ready for all the volumes over the next five years?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Bob, good question. We're always looking for property and the ability to add property. And we have done some small acquisitions where there's an independent out there that has land and it's the best way to get to the land or we may just enter into a lease. But those acquisitions are more focused on the property.

But again, we continue – we have a real estate group that's never finished with their job. They're always looking for opportunities to get more places to park wrecked cars in the markets where the wrecked cars are increasing in number. So, we don't see any limitation. At the same time, we don't have excess land, so you're constantly looking at it.

Robert Labick
CJS Securities, Inc.
Q

Great. Thank you very much.

James P. Hallett
Chairman & Chief Executive Officer
A

You're welcome.

Operator: And we'll go next to Shreyas Patil of Credit Suisse.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)
Q

Hey. Thanks, guys.

James P. Hallett
Chairman & Chief Executive Officer
A

Good morning, Shreyas.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)
Q

I just have a couple of quick questions. I just wanted to confirm, so the guidance that you've given, that doesn't include the Chicago Greenfield, right, like that's coming on I think later in 2016?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

No, that would be the Chicago Greenfield. We've anticipated the start date and that's in – the impact of that is included in our guidance. And we've mentioned before, it can take anywhere from 12 months to 24 months to reach positive cash flow at a new site. And that's been contemplated in our guidance.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)
Q

Okay. So, there is an EBITDA contribution from that?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

There is an EBITDA impact. And again, early on, there is more cost than there is revenue as you build it. So, without getting into details, the impact is in your guidance.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)
Q

Okay. And then I may have missed this. But what was your free cash flow in 2015?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

$338 million.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)
Q

And then just lastly, I just wanted to come back to the GM comments that you were talking about earlier. So, it does sound like these vehicles are going through your site, which is I think is a good thing. But I'm wondering if GM starts reselling units that may have been designated to physical auction by trying to sell them through this online platform. Is that a potential risk or do you not see that occurring?

James P. Hallett
Chairman & Chief Executive Officer
A

Yeah. If I understand your question. Again, it goes back to what I said. We're going to accommodate the customer however they want to sell cars. I think this is an initiative by GM to get in front of the re-marketing cycle and basically, post these cars on a website where the customer can go in, can view the inventory. If a customer is able to identify a car that he or she wishes to purchase, then they connect them with the dealer and the dealer transacts the deal and then as I mentioned we're involved in the processing of the deal. So, it's not taking – I don't see it's necessarily taking anything away from the physical site at ADESA. In fact, overall, I would say that we would view it as an opportunity.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

And let me clarify, Shreyas, when we say processing, we're involved in the processing of a wholesale transaction, not the retail transaction.

Shreyas Patil
Credit Suisse Securities (USA) LLC (Broker)

Q

Correct. Okay. Thanks a lot.

James P. Hallett
Chairman & Chief Executive Officer

A

You're welcome.

Operator: And we'll go next to Ben Bienvenu of Stephens, Inc.

Benjamin Bienvenu
Stephens, Inc.

Q

Yeah. Thanks. Good morning. Thanks for taking my questions.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

Good morning.

James P. Hallett
Chairman & Chief Executive Officer

A

Good morning.

Benjamin Bienvenu
Stephens, Inc.

Q

So, looking at the IAA segment, the strong unit growth there of 16%, how much of that would be what you would characterize as same-store unit sales or would we think all of it as same-store or same site?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

No. For IAA, the same-store growth for the quarter was 9% and for the year was 8%.

Benjamin Bienvenu
Stephens, Inc.

Q

Okay. Great. And then one last one on Brasher's. You said that you expect to achieve some revenue synergies. Are there any one-time costs that you have to put to work to enhance capabilities there? Are there any dissynergies initially that you expect to incur?

James P. Hallett
Chairman & Chief Executive Officer
A

Quite frankly, I'd say to you, you know what, I just think the ink just got dry in the contract from getting signed last night prior to the market closing. And I believe that as we work through a lot of diligence as we work through more of a diligence, complete our diligence and we get more involved with the management teams there, I think we'll identify what some of the real opportunities are going forward. But I think it's a little bit early to really state what we think could be done on a one-time basis.

Benjamin Bienvenu
Stephens, Inc.
Q

Okay. Fair enough. Thanks. Good luck.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Thank you.

Operator: And we'll go next to Bill Armstrong of C.L. King & Associates.

James P. Hallett
Chairman & Chief Executive Officer
A

Hi, Bill.

William R. Armstrong
C.L. King & Associates, Inc.
Q

Good morning, Jim. Good morning, Eric.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President
A

Good morning, Bill. Before you start, Ben asked a question and I actually have a sheet in front of me. The volume growth same-store was actually 14% for the quarter and 13% year-to-date. I gave the revenue growth number. I apologize. I wanted to clarify that.

James P. Hallett
Chairman & Chief Executive Officer
A

Okay. Now, it's your turn.

William R. Armstrong
C.L. King & Associates, Inc.
Q

Okay. Great. On Insurance Auto Auctions, you might – I think I heard you say in your opening comments that you expect the revenue per vehicle or average selling prices to start to stabilize in 2016 versus the declines that we've been seeing. Did I get that right? And if so, what will drive that?

James P. Hallett
Chairman & Chief Executive Officer
A

Well, yeah, I think I said that we expect pretty much what you see. We think that when you consider the drivers of that business and what's going on with foreign currency and what's going on with commodity prices, we think it's kind of hit a level where it's going to be stable. We're going to be able to maintain that level. Don't think it's going to get a lot worse. And I think my comment was what you see is probably what you get going forward.

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

And Bill, let me add, it was the second half of the first quarter last year when scrap prices fell through the bottom. They continued to fall, but relative to proceeds, that was the big drop, and the same on the strengthening of U.S. dollar. We saw the biggest impact on foreign currencies towards the end of the first quarter. So, what we're saying is the movements after that weren't as drastic relative to what we're experiencing now year-over-year.

William R. Armstrong
C.L. King & Associates, Inc.

Q

Got it. Okay. And then, two real quick ones on Brasher's. Are there any overlaps between their auction sites and some of your existing ones such that you may have to consolidate or close any?

James P. Hallett
Chairman & Chief Executive Officer

A

As you know, this is subject to HSR approval. And we do have one market in California where there is an overlap. Now that's not to say that we know what the outcome of that will be. But we'll wait and get approvals in due course.

William R. Armstrong
C.L. King & Associates, Inc.

Q

Okay. And then just finally on Brasher's, you're including about $25 million of EBITDA and in your guidance they do $34 million annualized. I assume that's because you'll have them for three quarters of the year. Are there any other adjustments there as well?

Eric M. Loughmiller
Chief Financial Officer & Executive Vice President

A

No. We are not providing a pro forma presentation. So it does not reflect to the beginning of the year. So it's three-fourths of their performance.

William R. Armstrong
C.L. King & Associates, Inc.

Q

Okay. Great. Thank you.

Operator: And there are no further questions from the phone lines. At this time, I will turn the call back to KAR CEO, Jim Hallett for any additional or closing remarks.

James P. Hallett
Chairman & Chief Executive Officer

Okay. Thank you, Cassandra. And I just want to say thank you to the folks that have been on the phone. Again, we believe it's a good story and a good performance and we believe going forward we're going to be able to deliver on the projections that we pointed out here. And I would say thank you for your continued interest and investment in our company. And have a great day. Thank you.

Operator: And that concludes our conference for today. We thank you for your participation and you may now disconnect.