OPENLANE, Inc.

First Quarter 2024 Earnings Conference Call

Wednesday, May 01, 2024, 4:30 PM Eastern

CORPORATE PARTICIPANTS

Peter Kelly - *Chief Executive Officer*

Brad Lakhia - *Chief Financial Officer*

Mike Eliason - *Treasurer, Vice President of Investor Relations*

PRESENTATION

Operator
Good day, and welcome to the OPENLANE First Quarter 2024 Earnings Conference Call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "*" key followed by "0." After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press "*" then "1" on a touchtone phone. To withdraw your question, please press "*" then "2." Please note this event is being recorded.

I would now like to turn the conference over to Mike Eliason, Treasurer and Vice President of Investor Relations. Please go ahead.

Mike Eliason
Thanks, Cindy. Good afternoon and thank you for joining us today for the OPENLANE first quarter 2024 earnings conference call. Today, we will discuss the financial performance of OPENLANE for the quarter ended March 31st, 2024. After concluding our commentary, we will take questions from participants.

Before Peter 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 OPENLANE's business, prospects and results of operation 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.

Let me also 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 measure can be found in the press release that we issued this afternoon, which is also available in the investor relations section of our website.

Now, I'd like to turn this call over to OPENLANE's CEO, Peter Kelly. Peter.

Peter Kelly
Thank you, Mike, and good afternoon, everybody. I'm delighted to be here today to provide you with an update on OPENLANE. Joining me is OPENLANE's Chief Financial Officer, Brad Lakhia. I will begin with a discussion of our company strategy and how we are positioning OPENLANE for growth. Then, I'll hand the call over to Brad to cover the majority of our financial and operating metrics for the quarter.

To start, I'm very pleased with the results that OPENLANE delivered in the first quarter. On a consolidated basis, we grew adjusted EBITDA to $75 million, and we also generated $100 million in free cash flow from operations.

These Q1 results were largely driven by significantly improved performance in the OPENLANE marketplace, which grew volumes 13% compared to Q1 of last year, grew adjusted EBITDA by 40% on a clean basis, and contributed 47% of our total company adjusted EBITDA during the quarter. AFC was also a strong contributor, generating approximately $40 million of adjusted EBITDA in Q1.

These results demonstrate the positive impact of our brand and platform consolidation efforts, and also the strong scalability characteristics of our company. A leaner, more agile operating model, accelerated innovation, and a differentiated experience that makes wholesale easy for our customers. And I believe that Q1 is a compelling preview of the value that OPENLANE is capable of delivering.

So, let me turn to our strategy and how we plan to build on this positive momentum. OPENLANE is highly focused on growth, growth in volume and market share, as well as growth in our financial results. We view these goals as complementary, and OPENLANE has spent several years transforming our business models to advance them simultaneously.

Our strategy for growth is anchored in our purpose, which is to make wholesale easy so our customers can be more successful, and guided by our vision, which is to build the world's greatest digital marketplace for used vehicles.

OPENLANE has several strategic advantages that I believe will help us achieve our purpose, vision, and further accelerate profitable, scalable growth. These advantages include: first, our expanding volume and share in the commercial and dealer segments. Second, the opportunities enabled by our asset-light digital model, and third, our focus on the customer experience.

Let me address each of these individually, and I'll start with volume growth and share. In the first quarter, OPENLANE grew its marketplace volumes by 13%, increased growth merchandise value by 17% to $7 billion, and also increased market share. The volume, GMV, and share growth were largely driven by our US business. These results, coupled with the financial performance that I referenced earlier, purely demonstrate the strength of our marketplace. And at the heart of that strength is a differentiated mix of commercial and dealer inventory.

In terms of commercial off-lease volumes, OPENLANE remains a clear market leader. Our commercial off-lease volumes were up substantially in both the United States and Canada during the quarter. And based on AuctionNet industry data, our volume growth meaningfully outperformed the US commercial market.

Commercial off-lease supply is still well below pre-pandemic levels, and we expect volumes to remain pressured in the second half of this year and into 2025, given the low level of leases written in 2021 and 2022. However, current lease originations of new vehicles are rising. They increased again in the first quarter, making Q1, the fourth quarter in a row where that has happened, and they're expected to increase further throughout 2024. So, OPENLANE will be a beneficiary of these future off-lease volumes when these leases mature.

Additionally, given the financial results we produced in Q1, with just a modest increase in off-lease volumes. I'm increasingly optimistic about what OPENLANE can deliver when off-lease volumes are even more robust. We also see additional growth opportunities in the commercial segment, including expanding the products and services that we offer, growing vehicle consignment from new off-lease, rental and repo customers, as well as, increasing conversion, particularly in higher revenue channels.

From a dealer volume perspective, we are also well-positioned for growth. First, we have a very strong dealer-to-dealer platform that delivers excellent results for our dealer customers in terms of time-to-sale, cost-of-sale, and financial outcomes. We are growing the number of franchise and independent dealer registrations across our geographies, and through our private label programs, we have the unique ability to transition thousands of franchise private label buyers into multi-channel buyers and sellers on OPENLANE.

The story with respect to OPENLANE's Q1 dealer volumes is nuanced. At an industry level, we saw declines in total dealer volumes sold in the US and to an even greater degree in Canada. Additionally, we also saw significant growth in commercial vehicle supply in the OPENLANE marketplace.

This resulted in some dealers who in recent periods would have purchased dealer-consigned vehicles, in effect trading up and purchasing commercially-consigned vehicles instead. This is a direct result of our diverse inventory and is actually a positive trend for our marketplace.

So, the net-net of all of this for OPENLANE was as follows. Canada represented the majority of our dealer volume headwinds during the quarter. In the US, we saw increased supply from our network of selling dealers, we increased our D2D market share versus physical auctions, and we grew the total volume of open marketplace transactions in the United States.

As I look to the future, there are several key factors that will support our dealer volume growth. First, there remains a large addressable market with the majority of industry volumes still being transacted at physical auctions. We believe we will continue to take shares here, as our digital marketplace enables faster and easier buying and selling and delivers better outcomes. Also, we now have a single platform experience with the unified sales team focused on growing our new customer base and our wallet share with existing customers.

And then finally, we're also highly-focused on expanding our relationships with the largest dealer groups in the country. Many still utilize physical auctions, but again, our digital marketplace capabilities have already opened the door to many new opportunities and relationships.

So, in summary, OPENLANE is well-positioned with both commercial and dealer customers, and there is growing evidence that having all of the buyers, all of the sellers, and all of the vehicles all in one place creates a more active and vibrant marketplace.

In addition to the volume opportunities, I believe we can accelerate growth by capitalizing on the opportunities that are enabled by our asset-light digital model. We continue to make good progress combining disparate tools and technology into a single marketplace platform. This will reduce our costs over time, but more importantly, it increases our operating leverage and also accelerates the speed at which we can bring new innovations to market. At our core, we are a technology company, developing and launching new digital products and features on a regular basis.

Let me give you a few examples from the quarter. As we previewed on our last earnings call, during the first quarter, we launched our new Visual Boost AI condition report technology, which is aimed at improving the accuracy and transparency of condition reports in our marketplace. To-date, we believe we are still the only digital marketplace that gives buyers access to an AI-powered inspection visualization on every dealer vehicle listed in our marketplace.

Our data has shown that buyers who utilize Visual Boost AI submit twice as many bids and offers on the vehicles that they view, and more bids leads to more seller confidence that we are achieving the best market outcome possible. One large volume buyer described Visual Boost AI as a game-changing technology. Others said it allows their dealerships to view the car as if I was standing right in front of it, and several have mentioned that it helps them buy with more confidence. So, Visual Boost AI is a powerful differentiator for us that is driving increased trust and transparency on the OPENLANE marketplace.

Another OPENLANE innovation that was deployed in Q1 is our absolute sale feature. This was deployed in the US marketplace. Absolute sale is available to all sellers and visible to all buyers on that marketplace. Once the bidding has reached an acceptable price point to the seller, the seller can click on the absolute sale button to signal to the marketplace that this is…they are now 100% committed to selling this vehicle. After the absolute sale process has been initiated, typically we see buyer bidding increasing rapidly, because buyers now know that if they submit the highest bid, they are guaranteed to win that vehicle.

Sellers like this because it increases buyer engagement on their vehicles, and participating sellers have seen sale prices increased by an average of almost $500 after they have activated the absolute sale feature. Based on this, it's evident that absolute sale is also driving higher marketplace engagement, increased velocity of sale, and better outcomes for sellers. These are just two examples of a very robust and progressive portfolio of innovation that we're investing in to create the greatest digital marketplace for used vehicles.

And then finally, let me turn to customer experience, which is an area where I believe there is tremendous opportunity for differentiation, and an area that I believe will help drive meaningful growth.

During the quarter, we formed a centralized customer experience team that will lead our customer experience strategy across OPENLANE, and leverage the data, the processes, and best practices from all of our business. This team is already advancing a broad portfolio of initiatives with two main goals. First, address any known customer pain points or issues, and second, identify the new products and features that will help make OPENLANEs a preferred platform for buyers and sellers.

In the first quarter, we designed a new customer NPS framework that is now being implemented across our business. This will help us monitor experience delivery more consistently than ever before and will also help us benchmark with other companies and in other industries. We also deployed new technology to enhance key aspects of the customer experience and aggregate customer feedback in a way that will help inform and prioritize our products development pipeline.

So, it's evident that we made positive progress on each of these fronts in the first quarter, growing our volumes, deploying new innovation, and improving customer experience. It's also evident that when combined, these strategic areas are capable of driving a highly scalable business. In the case of the first quarter, we saw 40% adjusted EBITDA growth…approximately 40% adjusted EBITDA growth in the marketplace on a 13% increase in volume, also with strong cash flows.

As I look to the future, OPENLANE will build on this strong foundation and lean more heavily into our go-to-market strategy, investing further into sales, marketing, technology, and innovation to continue driving growth.

And in terms of our finance business, AFC remains an industry leader and a strategic asset for OPENLANE. It increases buyer engagement and stickiness on our marketplace platforms and contributes meaningfully to our bottom line. Consistent with comments on our last call, I believe the risk environment is flattening and we remain committed to managing risk and growing responsibly in the AFC business.

So that was the quarter. But before I hand things over to Brad, I just want to reinforce OPENLANE's key strengths in terms of our value proposition for investors and our ability to deliver stockholder value. OPENLANE is an asset-light digital marketplace leader for wholesale use vehicles. There is a large addressable market in North America and Europe, and we are well-positioned to capture the opportunities to grow both dealer and commercial volumes.

Our brand and platform consolidation efforts are enabling us to accelerate innovation and product development. Our focus on operational efficiency gives us the financial headroom to invest in innovation without sacrificing financial results. We are cash flow positive with a strong balance sheet, and we believe our business has the capability to generate meaningful earnings growth over the next several years.

With that, I'll hand it over to Brad for a deeper discussion on our operational and financial metrics in the quarter. Brad.

Brad Lakhia
Thank you, Peter, and good afternoon, everyone. Before I begin, I'd like to remind everyone that all financial metrics I comment on at a consolidated level and a total marketplace segment level are on a net revenue basis, which specifically excludes the impact of purchased vehicle sales. In addition, my comments will be on a first quarter, year-over-year basis, unless I state otherwise.

As Peter mentioned, we are very pleased with our first quarter results. On a comparable basis, our consolidated net revenue was up 4% year-over-year, mainly driven by the 13%-unit volume growth in our marketplace segment. In our reported results, you will see our net revenue was down 2% as we continue to realize the impact from the transportation accounting change we made in the fourth quarter of last year. This resulted in a $22 million impact to net revenue in the quarter.

Consolidated gross profit improved $6 million, or 3%, and gross margin improved on a year-over-year basis for the fifth quarter in a row, this time by 270 basis points to 56.5%. Gross profit and margin benefited from higher auction and service fees, higher marketplace volumes, and continued improvements to our cost structure.

Consolidated SG&A in the quarter was $109 million and essentially flat to last year, even though our volumes were up 13%. We believe our digital model and our ongoing cost efforts will allow us to continue to scale efficiently, and we expect absolute SG&A to subsequently remain at these levels for the remainder of the year.

Consolidated adjusted EBITDA was $75 million, an increase of $16 million. Last year, we incurred an $11 million charge related to an early-stage investment. Accounting for this, adjusted EBITDA was up $5 million.

Turning to the marketplace segment, our total volumes were up, primarily driven by our US business. Our total marketplace dealer volumes declined, and this was primarily driven by our Canadian business. Similar to late last year, we continue to see Canadian buyers migrate towards commercial vehicles where supply has improved, and we expect this to continue as the overall wholesale mix of commercial and dealer vehicles shifts to pre-pandemic norms.

In terms of pricing and fees, for the third quarter in a row, we saw auction fees grow at double-digit rates. Total auction fee revenue increased 10%, driven by strong volume growth.

On a comparable year-over-year basis, services revenue was up 4%, driven by higher repossession, inspection, and key service revenue. We continue to focus on driving greater attachment of our ancillary services to our marketplace offerings. I want to note that our reported revenues show service revenue down 9%, again, primarily due to the transportation accounting change I discussed earlier.

The collective positive impact of our volumes, pricing, and disciplined cost management resulted in marketplace adjusted EBITDA of $35 million. Adjusting for the prior year one-time charge, this is approximately a 40% increase and represents 47% of OPENLANE's total adjusted EBITDA compared to 36% in the first quarter of last year.

Marketplace SG&A was flat, and as mentioned in my earlier comments…consolidated comments, we expect similar levels of SG&A for the balance of the year. As Peter said, we are very pleased with these improved results. But more importantly, we believe these improvements are sustainable and position us to deliver further improvements as we capture incremental value from our one marketplace solution.

Turning to our finance segment, loan transaction units in the quarter were relatively flat as we continue to balance growth and risk. Revenues for the quarter were down 2%, primarily driven by increased net credit losses and lower interest income resulting from lower vehicle values within the portfolio. These two factors were also the primary driver of our finance segment adjusted EBITDA result of $40 million, down $5 million versus last year.

The provision for credit losses was 2.3%, which was slightly better than our expectations. The higher loss rate versus historical performance is attributable to the ongoing impact of higher interest rates, declines in used vehicle values, continued consumer inflationary pressures, and tightening retail credit availability. We are encouraged by the recent improvements we are seeing and the severity of losses. This is the result of stabilizing fundamentals and proactive risk mitigation actions we have taken over the last year.

As I mentioned in our year-end call, we continue to expect the overall first half loss rate to be comparable to the second half of 2023. As a result, as usual, I will provide an updated outlook for our second half 2024 expectations during our next earnings call. And I'd like to reiterate that our long-term loss rate target of 1.5% to 2% remains unchanged. As Peter and I have said previously, we're very pleased with OPENLANE's portfolio of businesses and assets. As it relates to AFC, we value AFC's market leadership, the synergies with our marketplace, and its leading financial performance and cash flow characteristics.

Moving to the balance sheet and capital allocation, consistent with prior quarters, we continue to generate strong cash flow. Cash flow from operating activities was $100 million in the quarter, and our consolidated net leverage was approximately one times adjusted EBITDA. This level of cash generation demonstrates the value of our asset-light, digitally-focused marketplace business in combination with our leading floor plan finance business.

Overall, our capital allocation priorities remained unchanged. We continue to prioritize the funding of organic investments in our core digital businesses, while ensuring flexibility for high return, complementary strategic opportunities, and shareholder returns. At the end of the quarter, we continue to have $125 million remaining on our share repurchase authorization. And looking to the future, we have a $210 million senior note maturing in June of 2025. We intend to use cash flow generated by the business, along with our strong liquidity position, to fund this maturity.

Wrapping up, our 2024 adjusted EBITDA expectations remain unchanged. We are still guiding to adjusted EBITDA between $285 million and $305 million for the year. Other guidance metrics also remain unchanged and are available in our earnings release.

To summarize, we remain pleased with the business and financial performance. We generated $100 million of cash from operations in the quarter, and we were pleased with our overall volume growth. Our finance business credit losses were better than expected. And finally, on a comparable basis, our marketplace adjusted EBITDA grew approximately 40%, and we believe we are well-positioned to continue to deliver continued improvement.

With that, I'll turn the call over to the operator for questions.

QUESTION AND ANSWER

Operator
We will now begin the question-and-answer session. To ask a question, you may press "*" then "1" on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press "*" then "2." At this time, we will pause momentarily to assemble our roster.

Our first question comes from Rajat Gupta of JP Morgan. Go ahead, please.

Peter Kelly
Hi Rajat.

Operator
I'm sorry. One moment, please. Okay, go ahead, Rajat. You're in the question queue. Thank you.

Rajat Gupta
Can you hear me now?

Peter Kelly
Yes, Rajat. Good afternoon.

Rajat Gupta
Good afternoon. Thanks for taking the questions. Could you give us a little more color on the trajectory of the dealer-to-dealer volumes in the US? What was your growth rate there? Any color on market share that you can provide in the quarter, and relatively, any color on profitability of that business as well, would be helpful? And I have a follow-up. Thanks.

Peter Kelly
Thanks, Rajat. So, I guess, first of all, just in terms of overall volume, dealer and commercial, we grew 13%. We believe that was a greater growth rate than the industry demonstrated. So, we think it's a quarter where we gain share in the industry overall. If I look at US dealers, we saw growth in dealer consignment, volume of vehicles offered for sale. We increased our share vis-à-vis physical auctions. Physical auctions showed a decline in the quarter. And we grew the absolute number of open marketplace transactions in the US, the vast majority of which are dealer-to-dealer transactions. So, we had a strong quarter. We believe we gained share

overall, and we believe we gained share in the dealer-to-dealer segment, at least in comparison with physical auctions, which is the only data we have to compare with at this moment.

So generally pleased with that. I'd also say, Rajat, profitability, while we don't break out profitability by the business units, our D2D business is profitable in the US and in Canada and making a material contribution to our overall results. And I'd say we saw a significant improvement in the profitability of the US model, because in Q1 of last year, it was still an unprofitable business, whereas in Q1 this year, it was a positive contributor.

Rajat Gupta
Understood. Thanks for the color. And maybe like just a quick follow-up on the previous question. Any expected cadence for profitability in the US D2D business, just given 1Q is typically a seasonally strong quarter? So, I'm wondering if we can continue growing profitability there, despite some of the seasonal dynamics in the second half?

Peter Kelly
Yes, Rajat. Well, first of all, the business transition to being a positive contributor to our overall earnings in the middle of last year, I believe. So, it's been a number of quarters now. So, we expect this to continue. That is certainly the plan of the strategy. And again, the D2D business has a lot of strengths. This digital model, as I mentioned in my remarks, is very…is getting very good results for customers, high conversion rates, high…fast time to sale, low cost of sale, great price outcomes. So, we're seeing great feedback from customers, strong adoption, as I said, consignment of vehicles our selling dealers is increasing. Conversion rates are strong, the business is profitable, so I'm feeling good about that, Rajat.

I will say that in the quarter, and this was evident in both US and Canada, we saw a significant growth in commercial volumes, 30% overall approximately for the quarter. So, that's positive for our business for sure, but one of the impacts of that is for a buyer in the marketplace, they're going to see a lot more commercial vehicles than they saw, say, in prior periods. And for a lot of these buyers, the commercial vehicles are the more desirable vehicles. So, a lot of franchise buyers would rather buy from the commercial consignment than from other dealer consignments. So, we certainly saw from a buyer appetite perspective a trading up, I would describe it, from dealers that might have bought more dealer consignment last year now that there's more commercial supply buying more there. So, there's an interplay between those two things, they don't exist in isolation between each other. But on a combined basis, as I said, we grew volumes 13%. Obviously, most of that driven, as I said, by US growth, which was the strongest part of our business here in Q1, I'm very pleased about that, and again, driven a lot by commercial supply as well.

Rajat Gupta
Got it. And just on like your off-lease dynamic, given what you're seeing in terms of return versus retention rates in the consumer, how do you think…any updated thoughts on like how the dynamic should play out here in the second half once we start to lap like the drop in lease origination from 2021 onwards. I'm just curious, like, how are you seeing that interplay so far, based on the return rate? Thanks.

Peter Kelly
Great. Well, obviously, Rajat, and you know, this off-lease volume is the most significant part of the commercial segment in our business. So, a lot of the increase that we saw in Q1 was driven by increase in off-lease volume. And that was really driven, Rajat, by a lower percentage of consumer buyouts of their off-lease vehicles. Again, in normal times, consumer buyouts might

be 20%, 30%. In the last few years that increased to like 70%, 80%. We're now seeing that drop again, and that drove some increased supply. And you can see how that flows through our model, drove some of the volume and profitability increases that we talked about.

But I would also say that in the first quarter, our actual off-lease volumes, I'd still say we're about 50% of normal. So still well below what we would characterize as normal or well below pre-pandemic levels. If you look to the next period of time here, the next few quarters where you know, the second half of this year and into next year, there's definitely going to be fewer vehicles at the top of the funnel. We understand that. I've got clear data on that from our customers. But offsetting that, we expect the consumer buyout percentage to continue to drop. Okay, and that's going to mean more cars entering remarketing, a higher percentage of cars entering remarketing. And the interplay of those two factors is difficult to predict with precision, but I suspect you know, we…I don't suspect it will be as bad as what we had to endure in the sort of 2022 and 2023 year. That's my own view on it, and that's the feedback I'm also getting from customers.

And then on a very positive note, we're seeing new lease originations increase. I believe in the first quarter, new lease originations increased by approximately 25% compared to Q1 of last year. That's now the fourth quarter in a row, we've seen increasing new lease originations. I'm hearing from our customers they expect that to continue, they expect to have more incentives and more leasing on vehicles. And that obviously was very positive for us as those vehicles mature. So, in this off-lease segment, I certainly see the light at the end of the tunnel at this point. I see the increased volume showing up in Q1. That's very positive. I recognize we still have some challenging quarters to get through, but I think we're generally on more positive trajectory in that category.

Rajat Gupta
Got it. Great. Thanks for all the color and good luck.

Peter Kelly
Thank you, Rajat.

Operator
The next question comes from John Murphy of Bank of America. Go ahead, please.

John Murphy
Good afternoon, guys. Peter, just wanted to ask a question about your comment about market share gains in digital versus physical auctions especially here in the US and where you think we are on that? And then also, I just wanted to get it gauged where you guys are on your market share in closed auctions, specifically here in the US. So, the shift in the market from digital…from physical to digital, and then what your market share is in closed auctions?

Peter Kelly
Yes, John, I guess what I'd say, when we look at our volumes, first of all, our volumes are entirely digital. It's a digital marketplace business. And again, if I look at our total volume growth of 13% in Q1, that I believe is greater than the volume growth in the industry overall in Q1. So that would point to increasing market share on a sort of overall level basis based on the data we're looking at.

And then, it's possible to sort of subdivide or estimate how much of that volume is commercial versus dealer. And again, when we look at it through that lens, we believe we outperformed both in the commercial and in the dealer category in the United States during Q1 as well. So that's what we speak of in terms of market share. We think it's a positive quarter in that regard.

In terms of what is the pace of transition, I was talking about off-lease vehicles. The majority of those off-lease vehicles sell in a digital format. We enable obviously a lot of that for a lot of customers. So, the majority of our customer's vehicles are selling online in the digital format. A mix of close and open.

In the dealer-to-dealer category, the majority of vehicles are still selling in a physical format, going to physical auctions. That is still true, I believe, in the United States. But we see the digital channels gaining share. And again, we believe our Q1 volumes gain share versus physical volumes in the first quarter. It looks just at the D2D category. So, John, you know, the industry…this industry takes time to evolve and adopt new technologies. But I think over time, it does, and these trends become evident. And certainly, when I'm talking to franchise dealer customers, I think there's an increasing acceptance and understanding among that customer group that digital really is the future. But digital offers a lot of benefits to them, both in terms of time; cost, price realization and they're very receptive to a greater adoption of digital channels as they look to the future.

John Murphy
Can you also comment on your market share in these closed auctions because it sounds like we're going to head more in that direction. So, it seems like as more vehicles come off of lease, more of those vehicles are going to be ending in closed auctions than maybe ever before. I think you have a pretty big market share there. Just curious if you could talk about that position?

Peter Kelly
Yes, John, good point. Sorry, I missed that. I forgot to answer that part. The majority of the off-lease vehicles were selling today sell within these closed auction marketplaces. So that is a fact. And those are obviously very, very important to our OEMs and franchise dealer networks because a lot of OEMs, they want to keep a high percentage of these vehicles within their franchised dealer network and support the brand and the used car portfolio. But importantly, they do also flow into the open, and that's an opportunity for us as well as for our customers to liquidate some of the vehicles there. But you're right, John, the closed auctions are very, very important. And we have our closed auction technology supports the majority of OEMs and captive finance companies in North America. And I'd also say, just want to point on customer attention, while it has been a challenging few years in the off-lease segment and volumes have been way, way down…down lower than levels I would have ever imagined candidly. We have not lost customers through that period. We still have those OEM relationships, those captive finance relationships, and those are very positive relationships for us and for our customers.

John Murphy
And as these volumes are coming back in whatever form they come back, I mean, obviously, it's all going to be digital that you process these vehicles. Can you talk about just what the operating leverage is? I know we're kind of still bouncing off the bottom, so it was a good volume quarter, but op-leverage wasn't necessarily huge. But I mean, overtime, as you kind of fill up the pipe here and units return to something that might be vaguely normal over time. How should we think about operating leverage? You're selling units; I don't know if you maybe say revenue were up 5% or 10%. What kind of flow through do you get to EBITDA or maybe you talk about the EBIT level, things have changed, and the model has changed. So, I'm just curious if you could talk about what you think that is.

Peter Kelly
Yes, I might answer that in sort of qualitative terms and, Brad, if you want to answer…to add any further colors to that, please do. But, John, I guess having sort of worked in digital businesses for best part of my career at this point, I think the operating leverage is really, really strong in these models, because so much of our cost structure is essentially fixed, the cost of our platform, the cost of our overhead, the cost of our sales team, and the marginal cost for incremental vehicles sold is pretty low. And frankly, I think Q1, we had really strong evidence of operating leverage, at the end of the day we had a 13% volume increase, but a 40% EBITDA increase in the marketplace segment, and I think that's very, very strong. The other thing frankly is, I do model out each month our volume versus our adjusted EBITDA performance in the business and we continue to take steps to increase that operating leverage. We talked about some of the platform consolidation that we're doing. That reduces our costs, it increases our operating leverage, it also increases the speed at which we can deploy new innovation. So, I think this business has a ton of operating leverage. I think we got a glimpse of that in Q1. Again, I would reiterate commercial off-lease volumes in my view were still 50% below normal in Q1. So, the sort of mental experiment I do is, okay, what if we had that 50% of volume flowing through here? What would the returns look like at that point? They would look, I believe, really, really strong. Now, obviously, that's not going to happen in the next quarter. We won't have to wait and work for that, but I think that opportunity exists.

Brad, I don't know if you want to add anything.

Brad Lakhia
Yes. No, I just say, I mean I commented, John, on our SG&A performance in the quarter compared to last year's overall flat SG&A, and so the revenue, it's kind of the top line unit growth, volume growth benefit of that. SG&A is certainly much more fixed, as Peter was alluding to. So, I think you can see that in a year-over-year comparable. I would also say just to go maybe a low level deeper, if you're in the direct expense category, we do have more variable costs as it relates to inspections. So, if you think about volumes coming back, inspection costs are more purely variable, not purely variable, but more so. I think that's one. And then, I would say in the legacy off-lease private label business, what legacy used to call OPENLANE, that's largely more of a fixed cost business. So as those volumes come back, there's a lot of scalability there.

John Murphy
Okay and then maybe just one last one. Peter, you mentioned something about absolute sale, just sort of this neat feature of basically a vehicle kicking over the reserve and that being kind of disclosed to everybody to create a feeding frenzy around that vehicle. What does that ultimately mean to you as far as getting something converted that may have not been converted before or the price higher? What does that actually mean? And how many other sorts of, I would call that a neat little trick. It's actually a very smart feature to turn on. But how many other sorts of somewhat simple innovations that are very important, do you think there are to make out there to drive the business going forward other than big tear ups in the tech stack?

Peter Kelly
Yes, good point, John. First of all, absolute sale, I agree. Listen, we've all been to auctions of different types of products where you see that happening when it's like, okay, it's on the market, it's going to sell, it draws renewed interest in the sale, and that's what this does. And by the way, absolute sale has become very popular like in less than three months since deployment. It's now the preferred selling mechanism for most of our franchise dealers in the US

marketplace already. So, we've seen a massive adoption of it and the sellers really like it for that reason.

And John, not only do they like the fact that on average, once they hit the button, they're seeing another $500 on average or close to that in terms of price realization. But then they get that one car where the car runs up $2,000 or $2,500 and that leaves a real lasting kind of memory in the minds of the seller, that one car where I press the button and suddenly it just stops off. That's a real kind of aha moment in terms of their experience of the platform. So…but listen, we're watching it, we think it's driving…we think it's improving, kind of helping improve conversion, helping improve price, helping improve stickiness, so that's positive. John, without going into specifics, listen, we're looking at all the opportunities that exist across our marketplace and, obviously, we're looking for the easier to deploy ways we can create a value add or eliminate a pain point. And there are plenty of those available to us rather than sort of having to sort of reengineer the whole tech stack. So, more to come, I look forward to speaking about more of the innovations on future calls.

John Murphy
Great. Thank you very much, guys.

Peter Kelly
Thank you, John.

Operator
The next question comes from Gary Prestopino of Barrington Research. Go ahead, please.

Gary Prestopino
Hi, Peter and Brad how are you?

Peter Kelly
Hey, Gary, how are you?

Brad Lakhia
Hi, Gary.

Gary Prestopino
Good. A couple of questions here, the commercial vehicle growth was really sensational. Was the bulk of that what you're seeing in return in off-lease, or were there other buckets that are also starting to come back for you?

Peter Kelly
Good question, Gary. Off-lease is the biggest category. We saw growth in rental consignment and sales. We saw growth in commercial in all our geographies, Europe, Canada, and North America. So, it's…off-lease is the most of it. We saw growth in all categories. That would be the short answer.

Gary Prestopino
Okay. That's fine. And then, as I'm looking at my numbers here, it looks like your gross auction proceeds were up about somewhat 17%. It looks like your gross auction proceeds for vehicles were up about 3.5%. So, obviously, that's the impact of selling a lot more commercial vehicles. But yet, your auction fees for vehicles were down about 2.4%. So, could you maybe square that with me, I mean, I think if you're selling a higher priced car, your auction fees for vehicle should

be going higher. Now, is there some distortion in there from the Canadian business that you purchased, or…?

Peter Kelly
No, but good observation. You're correct. So, GMV increased 17%, volume increased 13%, the GMV for vehicle was up 4%, sort of 3.7%, whatever number you said, I think is probably accurate. It's really driven by what John spoke too, increased volume of commercial vehicles, A, higher percentage of those are selling in the closed sales where we have a lower revenue per unit…lower auction fee revenue per unit. But Gary, offsetting that, we also have a lower direct cost per unit as well. So those commercial cars tend to come with lower ARPU, but sometimes with higher gross profit [indiscernible] percentage margin. So, I think…so I kind of look at it as volumes grew 13%. I think auction fees grew 10% in the quarter. So, there was a little bit of dilution in auction fee per vehicle.

Gary Prestopino
Got it. Okay. That's helpful. Thank you.

Peter Kelly
You're welcome, Gary. Thank you.

Operator
The next question comes from Craig Kennison of Baird. Go ahead, please.

Craig Kennison
Yes, thanks for taking my question. It's Craig from Baird. Just a quick follow-up on absolute sale. I'm guessing the seller can set that feature to the…to on prior to the sale, or is that something they have to monitor in real time?

Peter Kelly
Craig, thank you. Good to hear from you again. So, the way it's deployed at least initially, the seller sort of manually activates the absolute sale button when they believe they've got enough sort of action on the vehicle that gives them the confidence to say "hey, this car is going to sell no matter what." Okay, so that was our initial deployment. Given its popularity, we're exploring exactly what you said, Craig, of…can we set up some automated rules that enable this to be activated either immediately in the auction or once a certain price level has been attained without the seller having to actively engage. So, these are all part of the roadmap, Craig. I confess I don't know the exact timeline of either of those two items. It's possible one of them may be live already, but that's the plan.

Craig Kennison
Thank you for that. And then, naturally, you're going to get some growth if we see the off-lease cycle turn positive for you. But I'm curious about your sales effort and where you're focusing those sales dollars. Are you trying to add more dealers to the network, or are you focused more on increasing the number of volume or the amount of cars you can do your existing network of dealers?

Peter Kelly
Craig, thank you. Listen, I think one of the strengths of the business is we have a very strong network of participating dealers in all our geographies, tens of thousands of dealers' active each month and each quarter on our business. I mentioned given the traction we're seeing and the one marketplace leaning in more into our go-to-market efforts, I would say principally, Craig, increasing the size of the network. I mentioned we've got a lot of private label franchise buyers,

franchise dealers who are buyers that are not yet sellers. So how do we work with those and convince them that OPENLANE is a great place to sell their vehicles as well. So, there's opportunities there, converting buyers into sellers. And then, obviously, getting a greater share of wallet with the customers we already have. So we've got initiatives really addressing all of those aspects, but obviously size and scale of the network, both on the sell side and the buy side is obviously an important one.

Craig Kennison
That's great. Hey, thank you.

Peter Kelly
Thanks, Craig.

Operator
The next question comes from Bob Labick of CJS Securities. Go ahead, please.

Bob Labick
Great. Thank you. Good afternoon.

Brad Lakhia
Hi, Bob.

Peter Kelly
Hi, Bob.

Bob Labick
Hi. I wanted to dig in further, obviously, lots been addressed so far. We're just digging a little further on the off-lease. Equity in off-lease vehicles is kind of stubbornly high in 2024. It's picked up a little bit, I think, even since the end of last year. But it's obviously down a lot since the beginning of 2023. So how does that factor into the lessee retaining the vehicle or the grounding dealer buying the vehicle, meaning, keeping them from going to auction? Is equity in leases low enough now that we're kind of normalized or is there more benefit for you to come as that equity in leases continues to revert back to prior norms of zero to negative?

Peter Kelly
Yes, Bob, great question. So, I liked your phrase, stubbornly high. It has been stubbornly high. I agree with that. From my view, very, very stubbornly high, but that's where it's been. But it has declined, and that is leading to an increased percentage of vehicles being returned. However, the percentage being returned is still way below normal. So that's why our volumes, as I've said, are still about 50% below, what I'd say, off-lease volumes still about 50% below normal, even with the increase in Q1.

Then, Bob, in terms of the timing, in Q1, typically, there's a spring market phenomenon, as you know, in our industry, and that typically supports prices in Q1. So, the equity gap didn't really decline that much in Q1. In fact, by some metrics increased a little bit again like it did in Q1 of last year. But the expectation, I think, from speaking to some of our finance customers, is this equity gap will, over time, continue to decline. And I think there are two reasons for that. One is, continue downward pressure on used vehicle prices as dealers have more cars on their lot, as manufacturers put more incentives on new cars, that flows through into being downward pressure on used vehicle prices. So, there's probably some level of that that will still take place here.

And then secondly, as we're sort of lapping new cohorts of leases that were written, they were sold at higher prices…higher average transaction prices, and leased at higher residual values. So, I think the expectation, Bob, is that ultimately this will all kind of revert to normal, but it's going to take time. But we're obviously dealing with that, and obviously trying to maximize our performance, given the constraints that exist at the moment. But I'm pleased with at least some of the breaks that we saw in Q1.

Bob Labick
Okay. Great, it was fantastic commercial volume, despite the higher equity. And then, so kind of related to that the dealer growth, I know you mentioned this potential trade-off if someone's on the state and you could get a commercial car, a dealer car, you take the commercial car, now that's…so that'll impact dealer cars as well. But it's been hard to come by for dealer-to-dealer growth for you guys for a little while now. What's going to change? What has to change and what will change to get dealer car volumes up in absolute volume?

Peter Kelly
Yes. So good question, Bob. Listen, I agree with your comment, I think dealer volume growth has been hard to come by. And I would say probably in the industry, the dealer volume growth has been more flat at an industry level as well in fact at an industry dealer volumes physical auctions were down in Q1 based on the data we have. So, listen, what I'd say Bob is we launched our one marketplace OPENLANE in late in Q4, so really Q1 was the first full quarter where we had that offering in market. I'm pleased with the performance of that marketplace we grew our open sale transactions in aggregate compared to Q1 of last year, so that's positive. Obviously, a lot of that growth was driven by commercial, but dealer consignment was also very strong. We saw increased consignments from dealers. We gained share vis-à-vis physical auctions in Q1. So, I'm encouraged by that. I'm also encouraged by the reaction we're getting from customers. So, what are we doing, I think things like I mentioned absolute sale improving condition report those are things that we're doing.

We're increasing our dialogue and focus with some of the largest dealer groups in the industry, making some positive progress there as well. And we're looking at our sales and marketing operations, we've had a brand change to OPENLANE, there's still a bit of a brand awareness who is OPENLANE and oh I didn't really know, you had this great dealer-to-dealer solution. So, we've heard that as we've done some research. And we've got some areas where maybe we could use an extra person or two on the ground in certain regions of the country. So all of these things are being addressed and, obviously, it's a top focus of mine and of this company to continue to grow this part of the business particularly in an era, where we think the industry is fundamentally shifting in a more digital direction.

Bob Labick
Okay. Super. I appreciate that. Thank you.

Peter Kelly
Thank you, Bob. I think we have time for one more question.

Operator
Okay. The last question is from Bret Jordan of Jefferies. Go ahead, please.

Bret Jordan
Thanks, guys. I'll make it quick. As you look at the off-lease volumes and next year is the trough year here in lease returns. And, I guess, you make some assumptions about equity gap

and buyout rates. Do you see your off-lease business growing in 2025, given it's a trough here in units, but with the lower buyouts that are likely coming offset that?

Peter Kelly
So, Bret, great question and thank you for that. This is a scenario where it's possible to model and it's very difficult to predict with confidence, is how I describe it. So, we, obviously, have done quite a detailed amount of modeling around this and various sorts of scenario planning. And I guess, what I'd say, Bret, is my current assessment is that the interplay of the two things that you just mentioned, the lower volumes at the top of the funnel, but also the lower percentage of consumer buyouts. I think in most scenarios that we model that will be a net positive for us. There are some scenarios where maybe it's more of a wash, maybe it's more flat, but there are plenty of scenarios where if you apply what I think is a reasonable judgment to the situation, our volumes can still move in a positive direction. Now, that remains to be seen, I'm not committing to that on this call. But, obviously, we do a lot of planning and we're looking at it through that lens.

And then the positive news, I just want to reiterate that again, is that we're now four quarters into increasing lease originations. And I believe in Q1, lease origination increased by about 25% versus Q1 of last year. So, the trough is a fact, but it also comes to an end, and leasing is rebounding, new vehicle incentives are increasing, number of new vehicles on dealer's lots are increasing, and volumes of off-lease vehicles will increase. And frankly, that is not too far away at this point. We can see the light at the end of the tunnel. And I think that will be very positive for this company. I think we're in a great position to serve our customer base as those volumes come to market.

Bret Jordan
Great. Thank you.

CONCLUSION

Peter Kelly
Thank you, Bret. So, I think that concludes our questions So, before we end the call, I just would like to acknowledge Mike Eliason, our Treasurer and Vice President of Investor Relations. Mike will be retiring from OPENLANE before our next earnings call. Mike has been with this company for 25 years and has always kept our investor community updated and informed on OPENLANE's performance, and all of the transactions and transformations that we've gone through over the past years. So, Mike, a sincere thank you for your many contributions to OPENLANE as well as to our investors, and we wish you all the very best.

To the audience, thank you for joining us today. I look forward to speaking to you again on our next call and sharing more about how OPENLANE is making wholesale easy, so our customers can be more successful. Thank you very much.

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