KAR Auction Services

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Matt Fassler: Good afternoon, everyone. I'm Matt Fassler from Goldman Sachs and, along with my colleague Matt Vigneau who is up with here at the podium, I'm delighted to introduce members of the management of KAR Auction Services, which is here at our Retail Conference for the first time.

Sitting to my far left is the Chief Executive Officer of the Company, Jim Hallett. Jim joined the Company in 1993, so 20 years ago now, as President of Adesa Canada and he became CEO of Adesa proper in 1996. Save for a two-year venture in another related business, he's been at the Company since that time.

Sitting directly to his right and kind of in the middle there is Eric Loughmiller. Eric is the Chief Financial Officer of the Company. He has been at KAR Auction Services for six years.

Those of you who follow this company know that this is a fairly unique business and, I think, a fairly unique opportunity. It's interesting, those of you who've heard the tone of questioning to a number of the retailers today or who sat on our private equity panel, there's sort of a perception right now of retailer as victim and a lot of people are playing in a fairly open competitive field. And it sounds like Amazon is the big aggressor and the real question to most retailers; how are you going to deal with this?

This is a company that operates in a relatively controlled competitive environment. It is one of the two largest players in each of its two key businesses, as you'll hear Jim and Eric, I'm sure, discuss, and as we'll address in our Q&A discussion.

Beyond that, though, and that's certainly been the case for a while, the market dynamics in this space recently turned more favorable than they've been for a while, based on supply dynamics. You have very good visibility to supply for the various vehicle patterns that drive supply and demand. And they've been moving in the right direction and the numbers have been moving in the right direction, as well.

So, with that, what we'll do is have a brief introduction from Jim and then we'll begin our fireside chat.

Jim Hallett: Okay, great. Thank you, Matt. Good afternoon, ladies and gentlemen, and welcome. We do have a handout if anybody needs one, located over here on the table. In my

introduction, I'm just going to walk through the first couple slides and then I think we're going to probably move to Q&A, is the format we've got set up.

But let me say at the outset that KAR, we operate three very distinct businesses. We're in the vehicle re-marketing business. Our first business and our largest business is Adesa Car Auctions and we refer to Adesa as the whole-car business. Whole-car being straight cars; those are the cars that you and I drive up and down the road every day.

Then we have another company called Insurance Auto Auctions. Insurance Auto Auctions is our salvage auction company and we sell vehicles that have been declared total losses by insurance companies; primarily total losses in that business. And then we have a company called Automotive Finance Corporation, which is an inventory financing business, providing inventory financing, primarily for the independent used car dealer that doesn't have access to that of the franchise dealers.

In each of our businesses, we operate in duopolies, I think is what Matt had mentioned. Our 2012 consolidated results, we sold 3.3 million vehicles with revenues right at $2 billion and our adjusted EBITDA at $500 million.

I don't know if you're following your slides or not but we'll flip to slide 5 in the handout. And this really describes our marketplace. When you think about where our marketplace is, we refer to the North American car park. And, if you take a look at this chart and I'll walk you through it, in the North American market there are approximately 270 million vehicles that are operating on the roads today.

Each year, there are approximately 16 million vehicles coming into the car park, new vehicles coming into the car park each year. And there are about 13 million vehicles being removed from the car park each year. Of the vehicles being removed from the car park each year, approximately 3 million to 4 million of those vehicles end up at a salvage auction and this is space that Insurance Auto Auction plays in. And then, if you take a look in the very center of that chart, there are 43 million used vehicles that change hands on an annual basis and that's made up of 12 million vehicles being sold consumer to consumer and the other 30 million-plus vehicles being sold by retail used car dealers and franchise dealers.

And where do they get the supply for those vehicles? Approximately 8 million to 10 million of those vehicles are supplied by what we call whole-car auctions and this is the space that Adesa plays in. And then the other 20 million or 22 million units are made up by used car trade-ins and other purchases. So, that's kind of our marketplace. That's the market that we operate in and that's the market that we supply.

And then, just finally, we are a B2B business, obviously. We provide the marketplace. And, on slide 6, we talk about really how we make our money. As I say, this is the money page. On the left-hand side of the page, you have your consigners. Those are the people that consign cars that sell with us. And on the right-hand side of the page you have your buyers that are buying cars from us.

In each case, we are a fee-based company. We take fees from our sellers and we take fees from our buyers. As well, we provide ancillary services to our sellers and buyers and that makes up our total revenue. The revenue varies according to the business unit but on our whole-car side of the business, we average $560 per transaction. Insurance Auto Auctions, we average $450 revenue per transaction. And AFC, our financing company, we average $160 per transaction with our average loan balance being about $8500.

So, I think it's important to understand this business, that we do not take principal risk in these vehicles. We do not take title to the vehicle. We simply provide the marketplace. We provide the infrastructure, the real estate. We bring the buyers and the sellers together and we act as the broker, collecting fees on all sides of the equation.

So, with that introduction, Matt, I think we'll just open it up to Q&A. And, if there's anything in particular you want Eric or I to address that's in the presentation, we'd be happy to address that as well.

Matt Fassler: Great. I'm happy to get started. Matt Vigneau and I have a few questions and we'll have plenty of time for those of you in the audience to chime in as well.

Let me start off by asking you about the volume growth at Adesa. We saw 10% volume growth of late. It was a nice breakout quarter, I guess; the second quarter, from that perspective. Can you talk about the pace and the duration of the end-market recovery that you think you'll see in the whole-car business?

Jim Hallett: I will, Matt. And maybe for those of you who are maybe not totally familiar with the story, I'll back up just a little bit to give you a little bit of history and then walk you into what we're talking about as a cyclical recovery that's taking place.

You know, when the market melted down in 2008, two very large drivers of our business are off-lease vehicles and repossessed vehicles. Well, leasing came to a standstill in 2008 and the credit markets froze. So, what was happening is there were no vehicles being leased and there were no vehicles being financed so we sold off those portfolios in 2009 and 2010.

And then leasing got rebooted in 2010. The credit markets opened up again in 2010. But we don't see those cars start to come out of the pipe, as we say, until three years later. And so what we're seeing now is we're seeing the leases that we're written in 2010 at maturity in 2013. And we're also seeing the credit markets get back to what I would call a more normal state and, obviously, more credit written, more repossessions coming our way.

So we talked about the cyclical recovery that was going to take place. We've been telling you for over the past that it would take place in the second quarter of 2013 and it's certainly happened in the second quarter. As Matt reported, we had a 10% increase year-over-year in 2013 and we said that that volume would get stronger in the second half of 2013. It would get stronger again in 2014 and then get stronger again in 2015.

That's not just our opinion but this is an opinion that's shared by our customers. We have the opportunity to have great visibility with our customers. We know the book of business that they've written, in terms of the leases. We know what they have on the books, in terms of loans. And we have good visibility into what will be returned and what to expect to come to auction.

If you think about the leasing business, in 2008 time period the industry was selling approximately 1.5 million off-lease vehicles annually. That number dropped down to as low as 800,000 vehicles in 2011. That off-lease number will return to almost 1 million vehicles in 2013 and the number will grow to over 1.5 million vehicles in 2015.

Recent articles out last week, you may have read that leasing is now at an all-time high. Leasing is representing 27.5% of all new vehicles sold and that number's expected to grow. There have been articles that say that leasing may get to as much as 50% off all

new car sales by the year 2017. And if you look at the Canadian market and many of the international markets, leasing has already exceeded 50% of the market.

So, again, being very strong drivers, Matt, I think that addresses the volume question. We know the volume was coming as predicted. We've delivered in the second quarter. We've had a little insight into the third quarter and there's nothing to change our opinion about how this volume will continue to come about for the balance of the next few years.

Matt Fassler: Just to clarify, and I promise I'm not trying to be cute with words, but when you talk about getting better, you talk about up year over year or better than 10%? Just to make sure I understand the implications.

Jim Hallett: Talking about being better year-over-year.

Matt Fassler: Got it. That's helpful. And then following through on that, we have a bunch more questions about the fundamentals of the whole-car business but, with 10% revenue growth, or good revenue growth, whatever that number is, there's the opportunity for operating leverage. And you lived through a period where the revenue picture was tough and you held in okay. How do you think about operating leverage? How much do you want to deliver to the bottom line? Are there reinvestment opportunities that you feel incumbent upon to commit to? What's the flow-through, guys, that you think you might see?

Jim Hallett: You know, we were highly-levered when we did this deal in 2007 when times were good. We we're levered up at almost 7 times. So we understand that but we were committed to de-lever the business to 3 times. We're slightly over 3 times now and we're committed to be at 3 times or less by the end of 2013.

Eric Loughmiller: Let me get into the cost structure. I think Matt wants to get into that. You know, we're sitting here through a tough time but we've been able to manage with gross profit actually improving over the past few years on a percentage-of-revenue basis and we think we can continue that.

But the mix shift that may occur on the revenue front could put a little pressure on gross profit percent but generate more gross profit dollars. So, in terms of our capital investment in the facilities, I think we have what we need for, at least, what's covering through 2015 and even into 2016. There's no step functions in it.

At the same time, we can use the scale of this increased commercial volume and maybe get another 200 basis points to 250 basis points of gross profit out of the consolidated business over that period. Keep the SG&A flat, which we think can get us to an improving EBITDA margin business.

The Adesa business has been operating below 25% EBITDA margin. And the IA business has been above 30% until this year. With Sandy, it's a little below 30%. We feel both of those businesses can operate at 30% EBITDA margin or close. In the case of Adesa, if not 30%, very close to 30%; in that 29% to 30% range.

And in terms of investments, Jim might talk to you a little bit. We are beginning to invest in activities that expand our marketplace a little bit, not to the point where it impacts our results, but creates opportunity. So, Jim, maybe you'd talk about that.

Jim Hallett: Yes. Eric, thanks for picking me up in that. I misunderstood your question. So, thank you.

Eric Loughmiller: Not at all.

Jim Hallett: Good pick-up man. I talked a little bit about de-levering the business so I'll just finish off on that. So, we're committed to be at 3 times or less at the end of this year.

But then, in terms of opportunities, there is some opportunity to do some bolt-on acquisitions in all of our businesses. We continue to look at that. But, more so, we're primarily a North American company; Canada, United States, and a couple sites in Mexico. We think there are opportunities in the international markets. As a matter of fact, we've been spending a lot of time in the international markets over the past three or four years, establishing those relationships. And we think there are a number of different opportunities, a number of different ways that we can get there.

Some can be through brick and mortar but some, more likely, is to go asset-lite with our technologies. We have a number of technologies that we think are very much in demand around the world. We've licensed some of our technologies already in different countries and we feel there's an opportunity to do more in the international markets and we may do that.

Opportunity to get into some adjacent space; we have a lot of land and a lot of facilities. And we think we can leverage that land and those facilities to get into adjacent space such as, perhaps, as we refer to heavy-duty equipment or yellow metal; the Ritchie Brothers type products. We've acquired a heavy-duty equipment sale and we're experimenting and learning and trying to understand that business. We're looking at boats and RVs and specialty equipment, heavy-duty trucks.

And then there's the opportunity, we feel today we are primarily focused on serving the B2B space. You saw on that first chart that there are 12 million vehicles that do transact consumer to consumer and there's nobody that really stands in the middle of a consumer-to-consumer transaction today. There are a number of companies that are matchmakers. You know them; eBay and Cars.com and Auto Trader and Craigslist. They will all introduce us to one another but nobody stands in the middle of that transaction.

And the number-one reason that more cars aren't transacted between consumers online is because of the trust and credibility factors. And we think that we have all the tools that we provide in the B2B world, we think we can provide those to the C2C space and take a slice of that 12 million vehicles that are being sold on an annual basis. And recently, our board has approved us to do a pilot in the C2C space and we're exploring that area as well. So, that's a little bit of color on some of the expansion.

Matt Fassler: I feel I want to throw out my whole sheet of questions and follow up on all those. So, first of all, international. Given that this is largely a real estate business, as you said, what are the synergies? Is it the same sellers that you're doing business with? How do you think about what you bring to the table other than know-how, of course? But, is there anything in particular that you leverage when you take your current business model and take it outside the U.S.?

Jim Hallett: I think the biggest thing is our technologies. That's the biggest opportunity is with our technologies. And then, second to that would be the relationships because, in many cases, the relationships extend around the world. The companies that we're dealing with are global companies. And many of the decision makers that we've dealt with here in North America we're now dealing with in the international markets.

But, then the real focus is our technology. We have an e-business platform that allows customers to sell the vehicles online. We're the largest seller of vehicles online in the industry. We have a product called OPENLANE that some of you may be familiar with. And we provide private-label selling sites where it's really our technology driving the manufacturers' brands and we represent 90% of all the manufacturers here in North America. We have 100% of the business in Canada. We have over 90% of the business here in the Unites States, of those private-label brands. And we feel there's an opportunity to take OPENLANE into the international markets and replicate what we've done here in North America.

Matt Fassler: A second follow-up question, if I could. If you could clarify the role that you would play in C2C transactions. I understand there's a trust factor. Whether it's technology or actual physical intervention or touching the car up, what have you, reconditioning it, that is; talk about where you would fit into that equation.

Jim Hallett: Right. Well, what do we do well in the B2B business? First of all we have 230 physical sites, which could act as trading posts where you could actually meet to conduct business and to conclude business. We're very good at transferring title and transferring funds, arranging logistics and transportation. We can provide reconditioning services, whether it be mechanical, paint and body work, detailing work. Eric?

Eric Loughmiller: Inspections; for a buyer of vehicle at one of our auctions, they often have a post-sale inspection to ensure the car was as-represented. We're a third-party independent and can give them a set advise that says, before you take that car, is there frame damage or something that was undisclosed.

Jim Hallett: So, with that, and I guess the number-one thing is back to the trust factor. If there is an issue, we can unwind the deal. And we can absolutely assure you that you're going to get what you thought you bought. And you're not going to buy a flooded car. You're not going to buy an accidented car. You're not going to buy a car that's been misrepresented. The same protection we give dealers in the B2B space, we provide that in the C2C space. So, really it's everything we do in the dealer world, we would bring to the consumer world.

Matt Fassler: Does anyone like eBay, which I know intermediates many, many automotive transactions C2C, have any element of services like that that they provide? Or is it basically buyer beware?

Jim Hallett: For the most part it's buyer beware. And, as I said at the outset, it's really putting people together and introducing people. I know there are some services that are made available in terms of transferring funds but, other than that, there is nobody that's really doing this in the C2C space.

Matt Fassler: And then the final follow-on relates to you talked about boats and heavy vehicles, etc. But basically, you're good at auctions, you have real estate. Let's bring these other asset classes in. What are the gating factors, be they competitive or otherwise, maybe getting flow that would prevent you from getting big in these spaces fast?

Jim Hallett: I think it's just a question of being able to build that customer list. And we've been dabbling with many of these different aspects but I think it's really to establish the relationships with the sellers and the buyers to be able to bring them and have them registered. And to be able make sure that we understand the business before we dive in, in terms of expanding it. And, as I say, with the heavy-duty equipment business, we're really learning that business and understanding that business. We really don't have the

expertise and maybe we need to bring -- we are bringing some of that expertise in to help to facilitate moving into some of these businesses?

Matt Fassler: My last question on this line of questioning, I promise. Is it a much less-concentrated customer or seller list than, say, the cars. I know you do business with the rental car companies and big fleets and such. There is probably a short list of customers who do do a lot of business. Is there a parallel, a similar set of customers in the other asset classes?

Jim Hallett: I'd say, less concentrated.

Matt Fassler: Okay, yes.

Matt Vigneau: Moving back to the core whole-car business, could you touch upon the differences between margin from your different sources of vehicles; dealer, consignment versus institutional vehicles? And then specifically what the drivers of the margin differences are? Whether it's ASP or conversion-rate driven?

Jim Hallett: Eric?

Eric Loughmiller: Sure. You know, when we look at it, the first thing is let's not look at the seller; let's look at the venue in which they sell. And in whole-car, we now are very actively involved with online selling through our Adesa.com site. And the online-only venue, where the car is off-premise -- that's going to be our new term we've learned this morning -- an off-premise vehicle, meaning sold from somebody else's property, is going to be a lower revenue per vehicle but a higher gross margin percent because I don't have the labor component. And, in fact, the OPENLANE platform, which is the foundation of this, operates at about a 70% gross profit and with a fixed SG&A because it's technology. And that would apply whether I'm selling it closed or open.

When I go to the physical auction or the on-premise where it's on our property and we're selling it. There we start moving the car around. We do reconditioning. My revenue-per-vehicle opportunity goes up significantly. My auction revenue generates about a 60%, or slightly less than that, gross profit but then I add ancillary services. When I get into the ancillary services; very low margin if I'm transporting a car. It's almost a pass-through in many cases and, if not a pass-through, probably a single-digit margin.

Everything else we do, which is substantial, is body work, mechanic work; that generates probably a 35% to 40% margin across most of what we do. Some are a little better. Some are slightly worse, depending on the volume and how labor-intense it is. But again, the margin profile; ancillary services, Matt, are generally lower margin than the auction itself but offer a tremendous upside on the revenue per vehicle.

So that kind of walks you through on whole-car. Is that what you were after?

Matt Vigneau: Yes, and just but there's no general differences between dealer consignment versus different institutional -- or even the mix within institution.

Eric Loughmiller: Okay. When you get to mix, dealer consignment has very little opportunity for ancillary services because the dealer himself has all those facilities. So the margin profile isn't different but the revenue potential is less than with a commercial vehicle. And now, within commercial, off-lease is probably the biggest segment that uses the ancillary services across the spectrum of our offerings. And so it has the greatest revenue potential.

In fact, Jim and I have been talking all day about it. An off-lease car has an average ticket of about $600 in ancillary services. Now, the numbers he gave you earlier were, a third of our revenue of that $560 was from ancillary services is on every car we sell, many of which use zero ancillary services. And I have a very high conversion rate on an off-lease car. If I don't sell, I sell it the next time I run it because they don't move them somewhere else. Where a dealer car has a lower conversion rate because they can take it back to dealership and retail it. They have alternative for selling it.

So the dealer car is all auction services, high gross profit versus at a little bit lower revenue. Add to the ancillary service. I really want a mix of both but I can actually make money by gross profit dollars, not percentages. So we really are anxious for these off-lease cars to come back to market and that will be a big part of our cyclical recovery and our improved performance over the next few years.

Matt Fassler: There are a couple questions we're asking companies across the board. I will try to tilt this to be most relevant to you. The first relates to the operating environment in the second half of 2013, relative to the second quarter. And I guess the element that I'll introduce that's specific to your company relates to your AFC Finance business, given that you're in a dynamic interest rate environment. Rates are moving up for the first time in a number of years. I would ask you to speak about the business overall but to please make sure that you address AFC within that context too.

Jim Hallett: Yes. Maybe I'll talk a little bit about AFC and let Eric weigh in a little bit as well. AFC is our inventory financing. So, we provide inventory financing to independent used car dealers. As you know, the franchise dealers have the captives that they can go to. The Toyota dealer has Toyota Motor Credit. The Nissan dealer has their captive finance, yada, yada, yada.

Well, the independent dealer doesn't have that source of financing that he can go to other than the banks. So what we do is we provide inventory financing for these dealers. We have 11,000 registered used car dealers or independent dealers that are approved to do business with us.

This is very short-term financing. The average duration is about 50 days. The average line of credit is less than $150,000. So again, small independent dealers, small lines of credit. Mind you, we do have some lines of credit that extend up to millions of dollars but the average line of credit is about $150,000. And we're really providing the financing for those dealers to be able to buy their inventory and we're financing that.

And the way we charge the dealers for this business, it's not just on interest rate. It's actually primarily based on a fee. Of the total revenue of $160 per loan transaction that I mentioned, it's two-thirds flat fee and a one-third interest rate spread. So, with that, huge margins. Margins run in excess of 60%. As much as 70%, Eric? Maybe you want to take it a little bit further.

Eric Loughmiller: Yes. You know, we have a little more than $1 billion outstanding on the portfolio, of which most of it is securitized. About $752 million, I think was the number at the last quarter. And the securitization, the one thing I will say, Matt, is we're not experiencing increasing interest rates right now because this is an asset-backed product and, while LIBOR has remained fairly constant, we have a fixed spread that's been negotiated. So, I don't have a risk for it being built into it, like I'm sure some of your other clients are experiencing. So, we're in a pretty good environment.

The other thing is we can re-price the loan itself, daily. And these turn so quickly, as Jim mentioned. Less than 60 days is the average term of a loan and it's fee-based. And I get the same fee whether that loan remains outstanding 10 days or 60 days. These loans are by individual vehicle. They're repaid within 48 hours after sale of the vehicle. So, the risk profile will probably look much different than a lot of what your other clients have been up talking about. And it's a very good business to be in.

We do have the potential for a little bit of margin compression because we put a primary floor in, in the fall of 2008, at 5% prime. And we loan on prime, we borrow on LIBOR, just because our independent dealers don't understand what LIBOR is. But prime is easy to find. I get a little compression if I can't pass it on in fees or changing the spread, which we're doing now. So I have a little potential but, again, it's not that meaningful relative to the size of this business. It would be pretty minor and probably we would adjust for it within a very short period of time on all new loans.

Matt Fassler: And if you think about that element of your business, AFC aside, that is somewhat cyclical, I guess. Salvage business would be the closest to it but it, too, has its own sort of its own clock. Is the environment better, the same, or worse in the second half as in the second quarter?

Eric Loughmiller: Sorry?

Matt Fassler: Second half of this year, relative to second quarter, or the quarter that just ended.

Jim Hallett: You know, I would talk about the quarter that's just behind us, Eric

Eric Loughmiller: We've given some good information. We had Sandy in the first half of this year, and the second quarter in particular. That's done. And so on the salvage front, and we've given the only indicator, Matt -- good fishing expedition, by the way -- the good indicators, our inventory levels were up over 15% year-over-year at the end of Q2. That's inventory that we'll sell in the subsequent quarter.

And we talked early on about the cyclical recovery at Adesa. The second half of this year is when we expected the volumes to start to return more consistently. So the second quarter was good and we expect, again, not talking percentages, to get more consistent growth. So, I would just tell you, we feel very positive about all of our businesses as we go into the second half of the year.

Matt Fassler: A second question, a kind of a high-level question, not to put too fine a numerical point on it. If you think about all the puts and takes in your business and you think about your operating margin over the next 12 months, relative to the prior 12 months -- and obviously Sandy put a big hole in your numbers. I kind of want to back that out. Would you say that your operating margin rate would be better, given the revenue expectations that you've put out there?

Eric Loughmiller: Clearly the cyclical recovery at Adesa drives us. As for volume at Adesa, we'll get a greater leverage of operating margin and improvement. And in IA, he's hit the nail on the head. It's really been a Sandy impact. It's caused us some costs and some vehicles sold with no profit that have run through. They're out of there. So I would say, generally speaking, over the next 12 months we're expecting conditions to improve to generate a higher operating margin as a percent of revenue and in absolute dollars.

Matt Fassler: There's a third standardized question we're asking, which I think is actually very relevant and hardly a formality for you guys. You really distinguished yourself, I think, with

dividend implementation last fall. You kind of came out of the gates with a 4% yield which now through share price appreciation is kind of in the mid to high 2%'s. If you think about capital allocation going forward and you prioritize CapEx; M&A, which seems like it's on the table; debt reduction; buy back; dividend. All five of these are actually really germane for KAR. How would you think about that prioritization?

Eric Loughmiller: Alright, Jim. I'll take this one. While we're not talking about what our dividend level will be, we think it's important to differentiate our company based upon its free cash flows and the best way to do that is a recurring dividend that stands out in the marketplace. And so we've gone on record as telling you that we want, over a period of time, our dividend to be at a premium to the S&P 500 average for dividend-paying stocks. I'm not committing to anything. As our stock price appreciates, though, you can see our cash flows are improving.

Our M&A activity is as much, while strategic opportunistic as to when these things come about, we do not chase things. We are very disciplined on what we pay for anything we acquire. As a result, you have to wait for the seller as much as you have to go create the opportunity. And also we don't see anything that was an OPENLANE-size transaction where we spent over $200 million on a technology business. So, we think we can absorb any M&A over the next several years within our free cash flows.

Therefore, we're really looking at the allocation of capital between return to shareholders, primarily in the form of dividend. Because of the private equity ownership, stock buy backs are not something that we've utilized to date. And I have a basket that's available for dividend or stock buyback. And so I have $106 million commitment right now for dividends and I started at $75 million with builder basket. It's unlikely that we would build it large enough to do a substantial stock buyback in the short term. It is allowed in our credit agreement but, again, it's a tradeoff between that or dividend. I don't get to do both unless I create enough capacity in that basket.

So, at this point in time, low interest rates, we've locked in LIBOR at the floor on $1.2 billion of our $1.7 billion in term loan B. So, interest rates for the next two years will remain below 4% for us on substantially all of our debt. So, I would tell you that we're likely to be allocating to some type of return to shareholders as a high priority.

CapEx, the last component, that's relatively consistent for us. While it may move a little bit, current year we're expecting, as we indicated on our last earnings call, I'm not updating that number but it was about $95 million. That's a number we can live with. It might grow a little bit as we grow the business but not in step function. It just goes up a little bit. So, we're not allocating more to CapEx.

Matt Fassler: Great. We have a couple of minutes left. Great, we have a question already. Fantastic. We have a mic coming to you. There you go.

Unidentified Audience Member: Can you talk about how the certified used car market affects your business?

Jim Hallett: A number of the manufacturers have certified programs. In some cases, we get to certify those cars for the manufacturers before they go to auction and the dealers can buy them certified. In some cases, the dealer will buy the car and then take it back to their shop and certify the car. But we do have the opportunity to get involved in performing many of mechanical services and many of the inspections that it takes to certify these cars. And obviously this is good ancillary revenue for us.

Eric Loughmiller: And with the return of off-lease cars, those are highly-likely candidates for the certified programs and so those volumes are coming back. That will be very good for everyone.

Matt Fassler: Great. Other questions? Please, from the back.

Unidentified Audience Member: (inaudible - microphone inaccessible)

Eric Loughmiller: AFC growth?

Unidentified Audience Member: (inaudible - microphone inaccessible)

Jim Hallett: Do you want to take that?

Eric Loughmiller: Yes. I mean it's an interesting phenomenon because we typically would expect it to grow as the auction volumes grow because the primary source of their floor plan activity are cars acquired at auction. On the other hand, we've seen declining volumes since 2009 and AFC's number of loan transactions has grown double-digit or greater than 20% two years ago; about 17% or 18% last year. So, we see that leveling off but here's the good news. As more cars come to auction, they're going to be acquired by independent used car dealers. So, we expect that to continue growing. We have, though, caution; probably not at the rates that we saw in 2010, 2011, and 2012 because, again, the law of big numbers.

The other thing that I think is missed a little bit; we took some fairly dramatic action in 2008 to make sure that we did not get upside down with a market that was changing with the dealers, the number of dealers going out of business. So, we downsized our portfolio very aggressively in conjunction with our customers' business plans. A lot of that growth was then returning to the healthy levels that they had achieved previously and the unhealthy dealers were gone. So, we have, as Jim mentioned in his opening remarks, we have a very strong portfolio, over 99% current for several years now, and a strong base to build off of because they're the strongest dealers that we've done business with for a long time.

Matt Fassler: Great. Thank you so much for your time and for your time. This concludes the first day of our conference. We have a great day tomorrow. Please join me in thanking Jim and Eric for their remarks.

Eric Loughmiller: Thank you.