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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

|  |                               |
|--|-------------------------------|
| Class A common stock without par value | 24,022,953                    |
| Class B common stock without par value | 1,000,000                     |
| (Class)                                | Outstanding at August 2, 2017 |

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LITHIA MOTORS, INC.  
FORM 10-Q  
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## LITHIA MOTORS, INC. AND SUBSIDIARIES

## Consolidated Balance Sheets

(In thousands)

(Unaudited)

|  | June 30,<br>2017 | December 31,<br>2016 |
|--|------------------|----------------------|
| Assets   |                  |                      |
| Current Assets:  |                  |                      |
| Cash and cash equivalents  | \$31,177         | \$ 50,282            |
| Accounts receivable, net of allowance for doubtful accounts of \$6,457 and \$5,281                       | 359,010          | 417,714              |
| Inventories, net   | 1,878,780        | 1,772,587            |
| Other current assets   | 54,801           | 46,611               |
| Total Current Assets   | 2,323,768        | 2,287,194            |
| Property and equipment, net of accumulated depreciation of \$184,283 and \$167,300                       | 1,067,104        | 1,006,130            |
| Goodwill   | 259,399          | 259,399              |
| Franchise value  | 184,763          | 184,268              |
| Other non-current assets   | 141,461          | 107,159              |
| Total Assets   | \$3,976,495      | \$ 3,844,150         |
| Liabilities and Stockholders' Equity   |                  |                      |
| Current Liabilities:   |                  |                      |
| Floor plan notes payable   | \$99,932         | \$ 94,602            |
| Floor plan notes payable: non-trade  | 1,534,715        | 1,506,895            |
| Current maturities of long-term debt   | 20,901           | 20,965               |
| Trade payables   | 89,795           | 88,423               |
| Accrued liabilities  | 212,309          | 211,109              |
| Total Current Liabilities  | 1,957,652        | 1,921,994            |
| Long-term debt, less current maturities  | 777,814          | 769,916              |
| Deferred revenue   | 92,335           | 81,929               |
| Deferred income taxes  | 57,919           | 59,075               |
| Other long-term liabilities  | 102,948          | 100,460              |
| Total Liabilities  | 2,988,668        | 2,933,374            |
| Stockholders' Equity:  |                  |                      |
| Preferred stock - no par value; authorized 15,000 shares; none outstanding                               | —                | —                    |
| Class A common stock - no par value; authorized 100,000 shares; issued and outstanding 23,757 and 23,382 | 158,527          | 165,512              |
| Class B common stock - no par value; authorized 25,000 shares; issued and outstanding 1,262 and 1,762    | 157              | 219                  |
| Additional paid-in capital   | 34,280           | 41,225               |
| Retained earnings  | 794,863          | 703,820              |
| Total Stockholders' Equity   | 987,827          | 910,776              |
| Total Liabilities and Stockholders' Equity   | \$3,976,495      | \$ 3,844,150         |

See accompanying condensed notes to consolidated financial statements.



## LITHIA MOTORS, INC. AND SUBSIDIARIES

Consolidated Statements of Operations  
(In thousands, except per share amounts)  
(Unaudited)

|   | Three Months Ended June 30, |             | Six Months Ended June 30, |             |
|---|-----------------------------|-------------|---------------------------|-------------|
|   | 2017                        | 2016        | 2017                      | 2016        |
| Revenues:   |                             |             |                           |             |
| New vehicle   | \$1,384,055                 | \$1,209,037 | \$2,594,359               | \$2,305,092 |
| Used vehicle retail                                   | 633,635                     | 553,647     | 1,235,858                 | 1,086,373   |
| Used vehicle wholesale                                | 69,512                      | 66,714      | 141,015                   | 131,860     |
| Finance and insurance                                 | 94,851                      | 81,043      | 181,628                   | 158,681     |
| Service, body and parts                               | 246,005                     | 202,265     | 478,579                   | 398,940     |
| Fleet and other                                       | 38,978                      | 20,633      | 71,698                    | 35,254      |
| Total revenues  | 2,467,036                   | 2,133,339   | 4,703,137                 | 4,116,200   |
| Cost of sales:  |                             |             |                           |             |
| New vehicle   | 1,303,516                   | 1,136,175   | 2,443,702                 | 2,165,464   |
| Used vehicle retail                                   | 559,129                     | 486,422     | 1,092,569                 | 954,871     |
| Used vehicle wholesale                                | 67,800                      | 65,228      | 137,786                   | 128,544     |
| Service, body and parts                               | 123,525                     | 103,666     | 242,905                   | 204,222     |
| Fleet and other                                       | 37,795                      | 19,812      | 69,252                    | 33,881      |
| Total cost of sales                                   | 2,091,765                   | 1,811,303   | 3,986,214                 | 3,486,982   |
| Gross profit  | 375,271                     | 322,036     | 716,923                   | 629,218     |
| Asset impairments                                     | —                           | 3,498       | —                         | 6,996       |
| Selling, general and administrative                   | 257,290                     | 215,526     | 500,062                   | 434,632     |
| Depreciation and amortization                         | 14,031                      | 12,503      | 26,770                    | 24,166      |
| Operating income                                      | 103,950                     | 90,509      | 190,091                   | 163,424     |
| Floor plan interest expense                           | (9,332)                     | (6,209)     | (17,384)                  | (12,118)    |
| Other interest expense, net                           | (7,169)                     | (5,502)     | (13,840)                  | (10,961)    |
| Other income (expense), net                           | 387                         | (1,495)     | 10,232                    | (3,021)     |
| Income before income taxes                            | 87,836                      | 77,303      | 169,099                   | 137,324     |
| Income tax provision                                  | (34,636)                    | (25,875)    | (65,172)                  | (45,626)    |
| Net income  | \$53,200                    | \$51,428    | \$103,927                 | \$91,698    |
| Basic net income per share                            | \$2.12                      | \$2.02      | \$4.14                    | \$3.58      |
| Shares used in basic per share calculations           | 25,053                      | 25,462      | 25,116                    | 25,639      |
| Diluted net income per share                          | \$2.12                      | \$2.01      | \$4.13                    | \$3.56      |
| Shares used in diluted per share calculations         | 25,106                      | 25,534      | 25,177                    | 25,754      |
| Cash dividends declared per Class A and Class B share | \$0.27                      | \$0.25      | \$0.52                    | \$0.45      |

See accompanying condensed notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES  
 Consolidated Statements of Comprehensive Income  
 (In thousands)  
 (Unaudited)

|  | Three Months<br>Ended June 30, |          | Six Months Ended<br>June 30, |          |
|--|--------------------------------|----------|------------------------------|----------|
|  | 2017                           | 2016     | 2017                         | 2016     |
| Net income   | \$53,200                       | \$51,428 | \$103,927                    | \$91,698 |
| Other comprehensive income, net of tax:  |                                |          |                              |          |
| Gain on cash flow hedges, net of tax expense of \$0, \$72, \$0, and \$175,<br>respectively | —                              | 114      | —                            | 277      |
| Comprehensive income   | \$53,200                       | \$51,542 | \$103,927                    | \$91,975 |

See accompanying condensed notes to consolidated financial statements.

## LITHIA MOTORS, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

|   | Six Months Ended June 30,<br>2017 | 2016      |
|---|-----------------------------------|-----------|
| Cash flows from operating activities:   |                                   |           |
| Net income  | \$ 103,927                        | \$ 91,698 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                   |           |
| Asset impairments   | —                                 | 6,996     |
| Depreciation and amortization   | 26,770                            | 24,166    |
| Stock-based compensation  | 5,432                             | 6,018     |
| (Gain) loss on disposal of other assets   | 256                               | (4,512)   |
| Gain on disposal of franchise   | —                                 | (1,102)   |
| Deferred income taxes   | (1,156)                           | 5,704     |
| (Increase) decrease (net of acquisitions and dispositions):                       |                                   |           |
| Trade receivables, net  | 70,908                            | 6,564     |
| Inventories   | (36,078)                          | (114,052) |
| Other assets  | 479                               | 5,652     |
| Increase (decrease) (net of acquisitions and dispositions):                       |                                   |           |
| Floor plan notes payable  | 1,330                             | 8,685     |
| Trade payables  | 414                               | 6,678     |
| Accrued liabilities   | (3,684)                           | 17,595    |
| Other long-term liabilities and deferred revenue                                  | 9,957                             | 10,668    |
| Net cash provided by operating activities   | 178,555                           | 70,758    |
| Cash flows from investing activities:   |                                   |           |
| Capital expenditures  | (32,266)                          | (43,247)  |
|   | 2,870                             | 197       |



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|  |           |   |           |   |
|--|-----------|---|-----------|---|
| Proceeds from sales of assets                                      |           |   |           |   |
| Cash paid for other investments                                    | (7,748    | ) | (16,690   | ) |
| Cash paid for acquisitions, net of cash acquired                   | (88,075   | ) | (18,807   | ) |
| Proceeds from sales of stores                                      | —         |   | 11,837    |   |
| Net cash used in investing activities                              | (125,219  | ) | (66,710   | ) |
| Cash flows from financing activities:                              |           |   |           |   |
| (Repayments)   |           |   |           |   |
| borrowings on floor plan notes payable, net: non-trade             | (32,124   | ) | 58,622    |   |
| Borrowings on lines of credit                                      | 773,500   |   | 487,623   |   |
| Repayments on lines of credit                                      | (808,846  | ) | (468,955  | ) |
| Principal payments on long-term debt and capital leases, scheduled | (8,825    | ) | (8,026    | ) |
| Principal payments on long-term debt and capital leases, other     | (35,765   | ) | (2,303    | ) |
| Proceeds from issuance of long-term debt                           | 74,065    |   | 12,080    |   |
| Proceeds from issuance of common stock                             | 3,519     |   | 3,329     |   |
| Repurchase of common stock   | (24,913   | ) | (104,858  | ) |
| Dividends paid   | (13,052   | ) | (11,524   | ) |
| Net cash used in financing activities                              | (72,441   | ) | (34,012   | ) |
| Decrease in cash and cash equivalents                              | (19,105   | ) | (29,964   | ) |
| Cash and cash equivalents at beginning of period                   | 50,282    |   | 45,008    |   |
| Cash and cash equivalents at end of period                         | \$ 31,177 |   | \$ 15,044 |   |

Supplemental disclosure of cash

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flow information:

|   |           |           |
|---|-----------|-----------|
| Cash paid during the period for interest                | \$ 33,476 | \$ 24,960 |
| Cash paid during the period for income taxes, net       | 62,274    | 9,684     |
| Floor plan debt paid in connection with store disposals | —         | 5,284     |

Supplemental schedule of non-cash activities:

|  |          |       |
|--|----------|-------|
| Debt issued in connection with acquisitions                      | \$ 1,748 | \$ —  |
| Non-cash assets transferred in connection with acquisitions      | —        | 2,637 |
| Debt assumed in connection with acquisitions                     | 11,837   | —     |
| Issuance of class A common stock in connection with acquisitions | 2,137    | —     |

See accompanying condensed notes to consolidated financial statements.

LITHIA MOTORS, INC. AND SUBSIDIARIES  
 CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

Note 1. Interim Financial Statements

Basis of Presentation

These condensed Consolidated Financial Statements contain unaudited information as of June 30, 2017 and for the three and six months ended June 30, 2017 and 2016. The unaudited interim financial statements have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain disclosures required by accounting principles generally accepted in the United States of America for annual financial statements are not included herein. In management's opinion, these unaudited financial statements reflect all adjustments (which include only normal recurring adjustments) necessary for a fair presentation of the information when read in conjunction with our 2016 audited Consolidated Financial Statements and the related notes thereto. The financial information as of December 31, 2016 is derived from our Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 28, 2017. The interim condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and the notes thereto included in our 2016 Annual Report on Form 10-K. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

Reclassifications

Certain reclassifications of amounts previously reported have been made to the accompanying condensed Consolidated Financial Statements to maintain consistency and comparability between periods presented. These reclassifications were related to our adoption of ASU 2016-09, "Compensation - Stock Compensation - Improvements to Employee Share-Based Payment Accounting." Specifically, we reclassified the presentation of excess tax benefits on our Consolidated Statements of Cash Flows between financing and operating cash flows and recorded reclassifications between additional paid-in capital and retained earnings. See also Note 12.

Note 2. Accounts Receivable

Accounts receivable consisted of the following (in thousands):

|   | June 30,<br>2017 | December 31,<br>2016 |
|---|------------------|----------------------|
| Contracts in transit                                | \$ 179,556       | \$ 233,506           |
| Trade receivables                                   | 51,009           | 47,450               |
| Vehicle receivables                                 | 40,120           | 43,937               |
| Manufacturer receivables                            | 73,067           | 76,948               |
| Auto loan receivables                               | 74,123           | 69,859               |
| Other receivables                                   | 1,057            | 1,600                |
|   | 418,932          | 473,300              |
| Less: Allowance                                     | (6,457 )         | (5,281 )             |
| Less: Long-term portion of accounts receivable, net | (53,465 )        | (50,305 )            |
| Total accounts receivable, net                      | \$ 359,010       | \$ 417,714           |

Accounts receivable classifications include the following:

• Contracts in transit are receivables from various lenders for the financing of vehicles that we have arranged on behalf of the customer and are typically received approximately ten days after selling a vehicle.

Trade receivables are comprised of amounts due from customers for open charge accounts, lenders for the commissions earned on financing and others for commissions earned on service contracts and insurance products.

• Vehicle receivables represent receivables for the portion of the vehicle sales price paid directly by the customer.

• Manufacturer receivables represent amounts due from manufacturers, including holdbacks, rebates, incentives and warranty claims.

• Auto loan receivables include amounts due from customers related to retail sales of vehicles and certain finance and insurance products.

Interest income on auto loan receivables is recognized based on the contractual terms of each loan and is accrued until repayment, charge-off, or repossession. Direct costs associated with loan originations are capitalized and expensed as an offset to interest

income when recognized on the loans. All other receivables are recorded at invoice and do not bear interest until they are 60 days past due.

The allowance for doubtful accounts is estimated based on our historical write-off experience and is reviewed monthly. Consideration is given to recent delinquency trends and recovery rates. Account balances are charged against the allowance after all appropriate means of collection have been exhausted and the potential for recovery is considered remote. The annual activity for charges and subsequent recoveries is immaterial.

The long-term portion of accounts receivable was included as a component of other non-current assets in the Consolidated Balance Sheets.

### Note 3. Inventories

The components of inventories, net, consisted of the following (in thousands):

|                       | June 30,<br>2017 | December 31,<br>2016 |
|-----------------------|------------------|----------------------|
| New vehicles          | \$1,376,995      | \$ 1,338,110         |
| Used vehicles         | 428,361          | 368,067              |
| Parts and accessories | 73,424           | 66,410               |
| Total inventories     | \$1,878,780      | \$ 1,772,587         |

Inventories are valued at the lower of net realizable value or cost, using a pooled approach for vehicles and the specific identification method for parts. Certain inventories are valued using the last-in first-out (LIFO) method.

### Note 4. Goodwill and Franchise Value

The changes in the carrying amounts of goodwill are as follows (in thousands):

|  | Domestic  | Import    | Luxury   | Consolidated |
|--|-----------|-----------|----------|--------------|
| Balance as of December 31, 2015 <sup>1</sup> | \$97,903  | \$84,384  | \$30,933 | \$ 213,220   |
| Additions through acquisitions <sup>2</sup>  | 18,154    | 21,795    | 7,448    | 47,397       |
| Reductions through divestitures              | (1,218 )  | —         | —        | (1,218 )     |
| Balance as of December 31, 2016 <sup>1</sup> | 114,839   | 106,179   | 38,381   | 259,399      |
| Additions through acquisitions <sup>3</sup>  | —         | —         | —        | —            |
| Balance as of June 30, 2017 <sup>1</sup>     | \$114,839 | \$106,179 | \$38,381 | \$ 259,399   |

<sup>1</sup> Net of accumulated impairment losses of \$299.3 million recorded during the year ended December 31, 2008.

<sup>2</sup> Our purchase price allocation is preliminary for our acquisition of the Carbone Auto Group. The initial purchase price allocation is subject to change upon final valuation analysis. The primary balances still subject to analysis are the segment allocation of goodwill and other intangible assets.

<sup>3</sup> Our purchase price allocation is preliminary for the acquisition of the Baierl Auto Group. Unallocated items, including goodwill and other intangible values, are recorded as a component of other non-current assets in the Consolidated Balance Sheets. See also Note 11.

The changes in the carrying amounts of franchise value are as follows (in thousands):

|   | Franchise<br>Value |
|---|--------------------|
| Balance as of December 31, 2015             | \$157,699          |
| Additions through acquisitions <sup>1</sup> | 27,087             |
| Reductions through divestitures             | (518 )             |
| Balance as of December 31, 2016             | 184,268            |

|   |           |
|---|-----------|
| Additions through acquisitions <sup>2</sup> | 495       |
| Balance as of June 30, 2017                 | \$184,763 |

<sup>1</sup> Our purchase price allocation is preliminary for the acquisitions related to the Carbone Auto Group. The initial purchase price allocation is subject to change upon final valuation analysis. The primary balances still subject to analysis are certain intangible assets.

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<sup>2</sup> Our purchase price allocation is preliminary for the acquisition of the Baierl Auto Group. Unallocated items, including franchise value and other intangible values, are recorded as a component of other non-current assets in the Consolidated Balance Sheets. See also Note 11.

#### Note 5. Stockholders' Equity

##### Repurchases of Class A Common Stock

Repurchases of our Class A Common Stock occurred under a repurchase authorization granted by our Board of Directors and related to shares withheld as part of the vesting of restricted stock units ("RSUs"). In February 2016, our Board of Directors authorized the repurchase of up to \$250 million of our Class A common stock. Share repurchases under this authorization were as follows:

|                                     | Repurchases<br>Occurring in the<br>Six Months<br>Ended June 30,<br>2017 |                  | Cumulative<br>Repurchases as<br>of June 30, 2017 |                  |
|-------------------------------------|---|------------------|--|------------------|
|                                     | Shares  | Average<br>Price | Shares   | Average<br>Price |
| 2016 Share Repurchase Authorization | 247,000   | \$ 87.94         | 960,725  | \$ 81.85         |

As of June 30, 2017, we had \$171.4 million available for repurchases pursuant to our 2016 share repurchase authorization.

In addition, during the first six months of 2017, we repurchased 32,143 shares at an average price of \$99.32 per share, for a total of \$3.2 million, related to tax withholdings associated with the vesting of RSUs. The repurchase of shares related to tax withholdings associated with stock awards does not reduce the number of shares available for repurchase as approved by our Board of Directors.

#### Note 6. Fair Value Measurements

##### Fair Value Disclosures for Financial Assets and Liabilities

We determined the carrying value of cash equivalents, accounts receivable, trade payables, accrued liabilities and short-term borrowings approximate their fair values because of the nature of their terms and current market rates of these instruments. We believe the carrying value of our variable rate debt approximates fair value.

We have fixed rate debt and calculate the estimated fair value of our fixed rate debt using a discounted cash flow methodology. Using estimated current interest rates based on a similar risk profile and duration (Level 2), the fixed cash flows are discounted and summed to compute the fair value of the debt. As of June 30, 2017, this debt had maturity dates between December 31, 2017 and December 31, 2050. There were no changes to our valuation techniques during the six-month period ended June 30, 2017.

A summary of the aggregate carrying values and fair values of our long-term fixed interest rate debt is as follows (in thousands):

|                | June 30,<br>2017 | December 31,<br>2016 |
|----------------|------------------|----------------------|
| Carrying value | \$370,768        | \$ 286,660           |
| Fair value     | 368,142          | 293,522              |

#### Note 7. Net Income Per Share of Class A and Class B Common Stock

We compute net income per share of Class A and Class B common stock using the two-class method. Under this method, basic net income per share is computed using the weighted average number of common shares outstanding during the period excluding common shares underlying equity awards that are unvested or subject to forfeiture. Diluted net income per share is computed using the weighted average number of common shares and, if dilutive, potential common shares outstanding during the period. Potential common shares consist of the common shares issuable upon the net exercise of stock options and unvested RSUs and is reflected in diluted earnings per share by application of the treasury stock method. The computation of the diluted net income per share of Class A common stock assumes the conversion of Class B common stock, while the diluted net income per share of Class B common stock does not assume the conversion of those shares.

Except with respect to voting and transfer rights, the rights of the holders of our Class A and Class B common stock are identical. Under our Articles of Incorporation, the Class A and Class B common stock share equally in any dividends, liquidation proceeds or other distribution with respect to our common stock and the Articles of Incorporation can only be amended by a vote of the shareholders. Additionally, Oregon law provides that amendments to our Articles of Incorporation that would adversely alter the



rights, powers or preferences of a given class of stock, must be approved by the class of stock adversely affected by the proposed amendment. As a result, the undistributed earnings for each year are allocated based on the contractual participation rights of the Class A and Class B common shares as if the earnings for the year had been distributed. Because the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis.

Following is a reconciliation of net income and weighted average shares used for our basic earnings per share (“EPS”) and diluted EPS (in thousands, except per share amounts):

| Three Months Ended June 30,<br>(in thousands, except per share data)                         | 2017     |         | 2016     |         |
|--|----------|---------|----------|---------|
|  | Class A  | Class B | Class A  | Class B |
| Net income applicable to common stockholders - basic   | \$50,520 | \$2,680 | \$47,869 | \$3,559 |
| Reallocation of net income as a result of conversion of dilutive stock options               | 1        | (1)     | 1        | (1)     |
| Reallocation of net income due to conversion of Class B to Class A common shares outstanding | 340      | —       | 440      | —       |
| Conversion of Class B common shares into Class A common shares                               | 2,334    | —       | 3,109    | —       |
| Effect of dilutive stock options on net income   | 5        | (5)     | 9        | (9)     |
| Net income applicable to common stockholders - diluted                                       | \$53,200 | \$2,674 | \$51,428 | \$3,549 |
| Weighted average common shares outstanding – basic   | 23,791   | 1,262   | 23,700   | 1,762   |
| Conversion of Class B common shares into Class A common shares                               | 1,262    | —       | 1,762    | —       |
| Effect of dilutive stock options on weighted average common shares                           | 53       | —       | 72       | —       |
| Weighted average common shares outstanding – diluted   | 25,106   | 1,262   | 25,534   | 1,762   |
| Net income per common share - basic  | \$2.12   | \$2.12  | \$2.02   | \$2.02  |
| Net income per common share - diluted  | \$2.12   | \$2.12  | \$2.01   | \$2.01  |

| Three Months Ended June 30,<br>Diluted EPS  | 2017    |         | 2016    |         |
|---|---------|---------|---------|---------|
|   | Class A | Class B | Class A | Class B |
| Antidilutive Securities   |         |         |         |         |
| Shares issuable pursuant to stock options not included since they were antidilutive | 22      | —       | —       | —       |

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| Six Months Ended June 30,<br>(in thousands, except per share data)                                       | 2017      |         | 2016     |         |
|--|-----------|---------|----------|---------|
|  | Class A   | Class B | Class A  | Class B |
| Net income applicable to common stockholders - basic   | \$98,337  | \$5,590 | \$84,445 | \$7,253 |
| Reallocation of distributed net income as a result of conversion of dilutive stock options               | 2         | (2 )    | 5        | (5 )    |
| Reallocation of distributed net income due to conversion of Class B to Class A common shares outstanding | 700       | —       | 907      | —       |
| Conversion of Class B common shares into Class A common shares   | 4,876     | —       | 6,313    | —       |
| Effect of dilutive stock options on net income   | 12        | (12 )   | 28       | (28 )   |
| Net income applicable to common stockholders - diluted   | \$103,927 | \$5,576 | \$91,698 | \$7,220 |
| Weighted average common shares outstanding – basic   | 23,765    | 1,351   | 23,611   | 2,028   |
| Conversion of Class B common shares into Class A common shares   | 1,351     | —       | 2,028    | —       |
| Effect of dilutive stock options on weighted average common shares                                       | 61        | —       | 115      | —       |
| Weighted average common shares outstanding – diluted   | 25,177    | 1,351   | 25,754   | 2,028   |
| Net income per common share - basic  | \$4.14    | \$4.14  | \$3.58   | \$3.58  |
| Net income per common share - diluted  | \$4.13    | \$4.13  | \$3.56   | \$3.56  |
| Six Months Ended June 30,  | 2017      |         | 2016     |         |
| Diluted EPS  | Class A   | Class B | Class A  | Class B |
| Antidilutive Securities  |           |         |          |         |
| Shares issuable pursuant to stock options not included since they were antidilutive                      | 11        | —       | 10       | —       |

Note 8. Equity-Method Investment

In October 2014, we acquired a 99.9% membership interest in a limited liability company managed by U.S. Bancorp Community Development Corporation with a total equity contribution of \$49.8 million. This investment generated new markets tax credits under the New Markets Tax Credit Program (“NMTC Program”). The NMTC Program was established by Congress in 2000 to spur new or increased investments into operating businesses and real estate projects located in low-income communities.

While U.S. Bancorp Community Development Corporation exercised management control over the limited liability company, due to the economic interest we held in the entity, we determined our ownership portion of the entity was appropriately accounted for using the equity method. We exited this equity-method investment in December 2016.

We estimated the value of our equity-method investment, which was recorded at fair value on a non-recurring basis, based on a market valuation approach. We used prices and other relevant information generated primarily by recent market transactions involving similar or comparable assets. Because these valuations contained unobservable inputs, we classified the measurement of fair value of our equity-method investment as Level 3.

The following amounts related to this equity-method investment were recorded in our Consolidated Statements of Operations (in thousands):

|  | Three Months Ended June 30, 2016 | Six Months Ended June 30, 2016 |
|--|----------------------------------|--------------------------------|
| Asset impairments to write investment down to fair value | \$-\$3,498                       | \$-\$6,996                     |
| Our portion of the partnership’s operating losses        | —2,065                           | —4,131                         |

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|   |        |         |
|---|--------|---------|
| Non-cash interest expense related to the amortization of the discounted fair value of future equity contributions | —62    | —154    |
| Tax benefits and credits generated  | —6,837 | —12,782 |

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## Note 9. Segments

While we have determined that each individual store is a reporting unit, we have aggregated our reporting units into three reportable segments based on their economic similarities: Domestic, Import and Luxury.

Our Domestic segment is comprised of retail automotive franchises that sell new vehicles manufactured by Chrysler, General Motors and Ford. Our Import segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by Honda, Toyota, Subaru, Nissan and Volkswagen. Our Luxury segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by BMW, Mercedes-Benz and Lexus. The franchises in each segment also sell used vehicles, parts and automotive services, and automotive finance and insurance products.

Corporate and other revenue and income includes the results of operations of our stand-alone body shop offset by unallocated corporate overhead expenses, such as corporate personnel costs, and certain unallocated reserve and elimination adjustments. Additionally, certain internal corporate expense allocations increase segment income for Corporate and other while decreasing segment income for the other reportable segments. These internal corporate expense allocations are used to increase comparability of our dealerships and reflect the capital burden a stand-alone dealership would experience. Examples of these internal allocations include internal rent expense, internal floor plan financing charges, and internal fees charged to offset employees within our corporate headquarters that perform certain dealership functions.

We define our chief operating decision maker (“CODM”) to be certain members of our executive management group. Historical and forecasted operational performance is evaluated on a store-by-store basis and on a consolidated basis by the CODM. We derive the operating results of the segments directly from our internal management reporting system. The accounting policies used to derive segment results are substantially the same as those used to determine our consolidated results, except for the internal allocation within Corporate and other discussed above. Our CODM measures the performance of each operating segment based on several metrics, including earnings from operations, and uses these results, in part, to evaluate the performance of, and to allocate resources to, each of the operating segments.

Certain financial information on a segment basis is as follows (in thousands):

|                               | Three Months Ended |             | Six Months Ended |             |
|-------------------------------|--------------------|-------------|------------------|-------------|
|                               | June 30,           |             | June 30,         |             |
|                               | 2017               | 2016        | 2017             | 2016        |
| Revenues:                     |                    |             |                  |             |
| Domestic                      | \$954,949          | \$830,410   | \$1,854,707      | \$1,602,312 |
| Import                        | 1,101,314          | 930,317     | 2,072,787        | 1,793,060   |
| Luxury                        | 413,088            | 371,866     | 776,891          | 718,679     |
|                               | 2,469,351          | 2,132,593   | 4,704,385        | 4,114,051   |
| Corporate and other           | (2,315 )           | 746         | (1,248 )         | 2,149       |
|                               | \$2,467,036        | \$2,133,339 | \$4,703,137      | \$4,116,200 |
| Segment income*:              |                    |             |                  |             |
| Domestic                      | \$27,857           | \$28,999    | \$53,299         | \$52,129    |
| Import                        | 32,465             | 29,680      | 54,637           | 53,943      |
| Luxury                        | 10,088             | 9,730       | 14,801           | 14,312      |
|                               | 70,410             | 68,409      | 122,737          | 120,384     |
| Corporate and other           | 38,239             | 28,394      | 76,740           | 55,088      |
| Depreciation and amortization | (14,031 )          | (12,503 )   | (26,770 )        | (24,166 )   |
| Other interest expense        | (7,169 )           | (5,502 )    | (13,840 )        | (10,961 )   |
| Other income (expense), net   | 387                | (1,495 )    | 10,232           | (3,021 )    |

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Income before income taxes    \$87,836      \$77,303      \$169,099      \$137,324

\*Segment income for each of the segments is defined as income before income taxes, depreciation and amortization, other interest expense and other income (expense), net.

|                              | Three Months Ended June 30, |          | Six Months Ended June 30, |           |
|------------------------------|-----------------------------|----------|---------------------------|-----------|
|                              | 2017                        | 2016     | 2017                      | 2016      |
| Floor plan interest expense: |                             |          |                           |           |
| Domestic                     | \$8,716                     | \$6,233  | \$16,670                  | \$12,729  |
| Import                       | 6,793                       | 4,393    | 12,666                    | 8,627     |
| Luxury                       | 3,383                       | 2,650    | 6,459                     | 5,308     |
|                              | 18,892                      | 13,276   | 35,795                    | 26,664    |
| Corporate and other          | (9,560 )                    | (7,067 ) | (18,411 )                 | (14,546 ) |
|                              | \$9,332                     | \$6,209  | \$17,384                  | \$12,118  |

|                     | June 30, 2017 | December 31, 2016 |
|---------------------|---------------|-------------------|
| Total assets:       |               |                   |
| Domestic            | \$1,253,814   | \$1,225,387       |
| Import              | 1,037,626     | 959,355           |
| Luxury              | 491,627       | 511,779           |
| Corporate and other | 1,193,428     | 1,147,629         |
|                     | \$3,976,495   | \$3,844,150       |

#### Note 10. Contingencies

##### Litigation

We are party to numerous legal proceedings arising in the normal course of our business. Although we do not anticipate that the resolution of legal proceedings arising in the normal course of business or the proceedings described below will have a material adverse effect on our business, results of operations, financial condition, or cash flows, we cannot predict this with certainty.

##### California Wage and Hour Litigations

In June 2012, Mr. Robles and Mr. Laredo brought claims against DCH Tustin Acura (Robles v. Tustin Motors, Inc., Case No. 30-2012-579414, filed in the Superior Court of California, Orange County) alleging that the employer underpaid technicians citing California Wage Order provisions that require an employer to pay at least two times the minimum wage for each hour worked if the employee is required to bring his or her own tools. The plaintiffs amended the complaint in late 2013 to include allegations that the employer failed to pay technicians for non-productive time and time spent performing tasks not compensated by the flat-rate compensation system; off-the-clock time worked; and wages due at termination. The amended complaint also alleged that the employer failed to provide technicians accurate and complete wage statements; and statutory meal and rest periods. The plaintiffs are seeking relief on behalf of all employees at all DCH Auto Group dealerships in California in addition to attorney fees and costs. These plaintiffs (and several other former technicians in separate but partially overlapping actions) also seek relief under California's Private Attorney General Action (PAGA) provisions, which allow private plaintiffs to recover civil penalties on behalf of the State of California. DCH successfully compelled arbitration based on arbitration agreements between these claimants and the employer, although certain representative claims were excluded and stayed pending arbitration.

During the pendency of Robles, related cases were filed that made substantially similar technician claims including Holzer (see below). DCH and the Robles claimants settled their individual claims in mediation in 2015. In April 2016, DCH and all technician plaintiffs in Robles and the related cases agreed in principle to settle the representative claims, and this settlement has been approved by the California courts. DCH Auto Group (USA) Limited must indemnify Lithia Motors, Inc. for losses related to this claim pursuant to the stock purchase agreement between Lithia Motors,

Inc. and DCH Auto Group (USA) Limited dated June 14, 2014. We believe the exposure related to this lawsuit, when considered in relation to the terms of the stock purchase agreement, is immaterial to our financial statements.

In August 2014, Ms. Holzer filed a complaint in the Central District of California (Holzer v. DCH Auto Group (USA) Inc., Case No. BC558869) alleging that her employer, an affiliate of DCH Auto Group (USA) Inc., failed to provide vehicle finance and sales persons, service advisors, and other clerical and hourly workers accurate and complete wage statements; and statutory meal and rest periods. The complaint also alleges that the employer failed to pay these employees for off-the-clock time worked; and wages due at termination. The plaintiffs also seek attorney fees and costs. DCH has sought to compel arbitration based on plaintiffs' arbitration agreements. The plaintiffs (and several other employees in separate actions) are seeking relief under California's PAGA provisions.

During the pendency of Holzer, related cases were filed that made substantially similar non-technician claims. DCH and all non-technician claimants settled their individual claims in mediation in 2017. In January 2017, DCH and all non-technician plaintiffs agreed in principle to settle the representative claims, although this settlement has not yet been approved by the California courts as expressly contemplated by the parties and required by applicable law as a condition of the agreed release of claims. DCH Auto Group (USA) Limited must indemnify Lithia Motors, Inc. for losses related to this claim pursuant to the stock purchase agreement between Lithia Motors, Inc. and DCH Auto Group (USA) Limited dated June 14, 2014. We believe the exposure related to this lawsuit, when considered in relation to the terms of the stock purchase agreement, is immaterial to our financial statements.

#### Note 11. Acquisitions

In the first six months of 2017, we completed the following acquisition:

On May 1, 2017, Baierl Auto Group, an eight store platform based in Pennsylvania.

Revenue and operating income contributed by the 2017 acquisition subsequent to the date of acquisition were as follows (in thousands):

|                  |          |
|------------------|----------|
| Revenue          | \$69,445 |
| Operating income | \$2,168  |

In 2016, we completed the following acquisitions:

- On January 26, 2016, Singh Subaru in Riverside, California.
- On February 1, 2016, Ira Toyota in Milford, Massachusetts.
- On June 23, 2016, Helena Auto Center, LLC in Helena, Montana.
- On August 1, 2016, Kemp Ford in Thousand Oaks, California.
- On September 12, 2016, Carbone Auto Group, a nine store platform based in New York and Vermont.
- On September 28, 2016, Greiner Ford Lincoln in Casper, Wyoming.
- On October 5, 2016, Woodland Hills Audi in Woodland Hills, California.
- On November 16, 2016, Honolulu Ford in Honolulu, Hawaii.

All acquisitions were accounted for as business combinations under the acquisition method of accounting. The results of operations of the acquired stores are included in our Consolidated Financial Statements from the date of acquisition.

The following tables summarize the consideration paid for the 2017 acquisition and the amount of identified assets acquired and liabilities assumed as of the acquisition date (in thousands):

|                                       | Consideration |
|---------------------------------------|---------------|
| Cash paid, net of cash acquired       | \$ 88,075     |
| Equity securities issued <sup>1</sup> | 2,137         |
|                                       | \$ 90,212     |

<sup>1</sup> In partial consideration for the purchase of Baierl Auto Group, we issued 4,489 shares of our class A common stock on May 1, 2017 and will issue an additional 17,957 shares over the next 4 years for a total of 22,446 shares. As of May 1, 2017, these shares were deemed outstanding for purposes of calculating basic and diluted EPS and had a market value of \$2.1 million, based on the closing price of our class A common stock on May 1, 2017 of \$95.22 per share. See also Note 7.

The purchase price allocations for the Baierl Auto Group acquisition are preliminary and we have not obtained and evaluated all of the detailed information necessary to finalize the opening balance sheet amounts in all respects. We recorded the purchase price allocations based upon information that is currently available. Unallocated items are recorded as a component of other non-current assets in the Consolidated Balance Sheets.





|                                    |             |
|------------------------------------|-------------|
|                                    | Assets      |
|                                    | Acquired    |
|                                    | and         |
|                                    | Liabilities |
|                                    | Assumed     |
| Trade receivables, net             | \$ 12,203   |
| Inventories                        | 78,820      |
| Property and equipment             | 54,433      |
| Other assets                       | 39,345      |
| Floor plan notes payable           | (70,960 )   |
| Debt and capital lease obligations | (13,585 )   |
| Other liabilities                  | (10,044 )   |
|                                    | \$ 90,212   |

In the six months ended June 30, 2017, we recorded \$2.1 million in acquisition expense as a component of selling, general and administrative expense. We did not have any material acquisition expenses for the same period in 2016.

The following unaudited pro forma summary presents consolidated information as if all acquisitions in the three and six-month periods ended June 30, 2017 and 2016 had occurred on January 1, 2016 (in thousands, except per share amounts):

| Three Months Ended June 30,  | 2017        | 2016        |
|------------------------------|-------------|-------------|
| Revenue                      | \$2,502,299 | \$2,452,886 |
| Net income                   | 53,380      | 54,019      |
| Basic net income per share   | 2.13        | 2.12        |
| Diluted net income per share | 2.13        | 2.12        |

| Six Months Ended June 30, 2017 | 2017        | 2016        |
|--------------------------------|-------------|-------------|
| Revenue                        | \$4,838,047 | \$4,735,415 |
| Net income                     | 104,546     | 96,687      |
| Basic net income per share     | 4.16        | 3.77        |
| Diluted net income per share   | 4.15        | 3.75        |

These amounts have been calculated by applying our accounting policies and estimates. The results of the acquired stores have been adjusted to reflect the following: depreciation on a straight-line basis over the expected lives for property and equipment; accounting for inventory on a specific identification method; and recognition of interest expense for real estate financing related to stores where we purchased the facility. No nonrecurring pro forma adjustments directly attributable to the acquisitions are included in the reported pro forma revenues and earnings.

#### Note 12. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued accounting standards update ("ASU") 2014-09, "Revenue from Contracts with Customers," which amends the accounting guidance related to revenues. This amendment will replace most of the existing revenue recognition guidance when it becomes effective. The new standard, as amended in July 2015, is effective for fiscal years beginning after December 15, 2017 and entities are allowed to adopt the standard as early as annual periods beginning after December 15, 2016, and interim periods therein. The standard permits the use of either the retrospective or cumulative effect transition method. We have evaluated the effect this amendment will have on our most significant types of transactions and expect the timing of our revenue recognition to generally remain the same.

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In February 2016, the FASB issued ASU 2016-02, "Leases." ASU 2016-02 increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and requires disclosing key information about leasing arrangements. ASU 2016-02 is effective for annual periods beginning after December 15, 2018, and interim periods within those annual periods. We are evaluating the effect this pronouncement will have on our consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, "Compensation - Stock Compensation - Improvements to Employee Share-Based Payment Accounting." ASU 2016-09 simplifies the accounting for several aspects of share-based payment transactions, including

the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. In January 2017, we adopted this new guidance. As a result, we recorded the following:

Reclassified \$0.2 million as a decrease to additional paid-in capital and an increase to retained earnings related to our policy election to record forfeitures as they occur.

All prior periods presented in our Consolidated Statements of Cash Flows have been adjusted for the presentation of excess tax benefits on the cash flow statement. This resulted in a \$4.4 million reclassification between financing and operating cash flows.

We had \$0.3 million of tax-affected state net operating loss carryforwards related to excess tax benefits for which a deferred tax asset had not been recognized. At adoption, this amount was recorded with the offset to retained earnings. Additionally, we do not believe that it is more-likely-than-not that the asset will be utilized and, as a result, a valuation allowance in the same amount was recorded that offset the impact to retained earnings.

In August 2016, the FASB issued ASU 2016-15, "Classification of Certain Cash Receipts and Cash Payments." ASU 2016-15 provides guidance for eight cash flow classification issues to reduce diversity in practice. The clarification includes guidance on items such as debt prepayment or debt extinguishment cost, contingent consideration payment made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies and distributions received from equity method investees. ASU 2016-15 is effective for annual periods beginning after December 15, 2017, and interim periods within those annual periods. Early adoption is permitted. We are evaluating the effect this pronouncement will have on our consolidated financial statements and related disclosures.

In January 2017, the FASB issued ASU 2017-04, "Intangibles - Goodwill and Other (Topic 350) - Simplifying the Test for Goodwill Impairment." ASU 2017-04 simplifies the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. Under the updated standard, an entity should perform its goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value, if applicable. The loss recognized should not exceed the total amount of goodwill allocated to the reporting unit. The same impairment test also applies to any reporting unit with a zero or negative carrying amount. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. ASU 2017-04 is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2019, on a prospective basis. Early adoption is permitted for interim or annual goodwill impairment tests performed after January 1, 2017. We do not expect the adoption of ASU 2017-04 to have a material effect on our financial position, results of operations or cash flows.

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718) - Scope of Modification Accounting." ASU 2017-09 reduces both diversity in practice and cost and complexity when changing the terms or conditions of a share-based payment award. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. ASU 2017-09 is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2017. Early adoption is permitted, including adoption in any interim period for which financial statements have not yet been issued. The amendments in this update should be applied prospectively to an award modified on or after the adoption date. We do not expect the adoption of ASU 2017-09 to have a material effect on our financial position, results of operations or cash flows.

#### Note 13. Subsequent Events

##### Common Stock Dividend

On July 24, 2017, our Board of Directors approved a dividend of \$0.27 per share on our Class A and Class B common stock related to our second quarter 2017 financial results. The dividend will total approximately \$6.8 million and will

be paid on August 25, 2017 to shareholders of record on August 11, 2017.

#### 5.25% Senior Notes Due 2025

On July 24, 2017, we issued \$300 million in aggregate principal amount of 5.25% Senior Notes due 2025 ("the Notes") to eligible purchasers in a private placement under Rule 144A and Regulation S of the Securities Act of 1933. Interest accrues on the Notes from July 24, 2017 and is payable semiannually on February 1 and August 1. The first interest payment is on February 1, 2018. We may redeem the Notes in whole or in part at any time prior to August 1, 2020 at a price equal to 100% of the principal amount plus a make-whole premium set forth in the Indenture and accrued and unpaid interest. After August 1, 2020, we may redeem some or all of the Notes subject to the redemption prices set forth in the Indenture. If we experience specific kinds of changes of control, as described in the Indenture, we must offer to repurchase the Notes at 101% of their principal amount plus accrued and unpaid interest to the date of purchase.

We paid approximately \$5 million in underwriting and other fees in connection with this issuance, which will be amortized as interest expense over the term of the Notes. The Notes are fully and unconditionally guaranteed, jointly and severally, on a senior unsecured basis by each of the Company's existing and future restricted subsidiaries that is a borrower under or that guarantees obligations under the Company's credit facility or other indebtedness of the Company or any subsidiary guarantor. The terms of the Notes, in certain circumstances, may restrict our ability to, among other things, incur additional indebtedness, pay dividends, repurchase our common stock, or merge, consolidate or sell all or substantially all our assets.

#### Credit Facility

On August 1, 2017, we amended our existing credit facility to increase the total financing commitment to \$2.4 billion. This syndicated credit facility is comprised of 18 financial institutions, including seven manufacturer-affiliated finance companies. Our credit facility provides for up to \$1.9 billion in new vehicle inventory floor plan financing, up to \$250 million in used vehicle inventory floor plan financing and a maximum of \$250 million in revolving financing for general corporate purposes, including acquisitions and working capital. This credit facility may be expanded to \$2.75 billion total availability, subject to lender approval.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### Forward-Looking Statements and Risk Factors

Certain statements under the sections entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Risk Factors" and elsewhere in this Form 10-Q constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Generally, you can identify forward-looking statements by terms such as "project," "outlook," "target," "may," "will," "would," "should," "seek," "expect," "plan," "intend," "anticipate," "believe," "estimate," "predict," "potential," "likely," "goal," "strategy," "future," "maintain," and "continue" or other similar terms or other comparable terms. Examples of forward-looking statements in this Form 10-Q include, among others, statements we make regarding:

- Future market conditions, including anticipated national new car sales levels;
- Expected operating results, such as improved store performance; continued improvement of SG&A as a percentage of gross profit and all projections;
- Anticipated continued success of acquisitions;
- Anticipated ability to capture additional market share;
- Anticipated ability to find accretive acquisitions;
- Anticipated additions of dealership locations to our portfolio in the future;
- Anticipated availability of liquidity from our unfinanced operating real estate; and
- Anticipated levels of capital expenditures in the future.

The forward-looking statements contained in this Form 10-Q involve known and unknown risks, uncertainties and situations that may cause our actual results to materially differ from the results expressed or implied by these statements. Certain important factors that could cause actual results to differ from our expectations are discussed in Part II - Other Information, Item 1A in this Form 10-Q and in the Risk Factors section of our 2016 Annual Report on Form 10-K, as supplemented and amended from time to time in Quarterly Reports on Form 10-Q and our other filings with the Securities and Exchange Commission.

By their nature, forward-looking statements involve risks and uncertainties because they relate to events that depend on circumstances that may or may not occur in the future. You should not place undue reliance on these forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made. We assume no obligation to update or revise any forward-looking statement.

#### Overview

We are one of the largest automotive retailers in the highly fragmented American auto retail industry. As of August 2, 2017, we offered 30 brands of new vehicles and all brands of used vehicles in 160 stores in the United States and online at over 200 websites. We sell new and used vehicles and replacement parts, provide vehicle maintenance, warranty, paint and repair services, arrange related financing, and sell service contracts, vehicle protection products and credit insurance.

In 2016, we were the fifth largest public automotive retailer in the U.S., as measured by revenue. Our stores are located in 18 states with concentrations west of the Mississippi and in the Northeast and offer 30 brands of new vehicles and all major brands of used vehicles. Our operations consist of domestic, import and luxury stores in markets ranging from mid-sized regional cities to metropolitan urban areas.

Results of Operations

For the three months ended June 30, 2017 and 2016, we reported net income of \$53.2 million, or \$2.12 per diluted share, and \$51.4 million, or \$2.01 per diluted share, respectively. For the six months ended June 30, 2017 and 2016, we reported net income of \$103.9 million, or \$4.13 per diluted share, and \$91.7 million, or \$3.56 per diluted share, respectively.

Key Revenue and Gross Profit Metrics

Key performance metrics for revenue and gross profit were as follows (dollars in thousands):

| Three Months Ended<br>June 30, 2017 | Revenues    | Percent of<br>Total Revenues | Gross Profit | Gross<br>Profit<br>Margin | Percent<br>of Total<br>Gross<br>Profit |
|-------------------------------------|-------------|------------------------------|--------------|---------------------------|--|
| New vehicle                         | \$1,384,055 | 56.1 %                       | \$ 80,539    | 5.8 %                     | 21.5 %                                 |
| Used vehicle retail                 | 633,635     | 25.7                         | 74,506       | 11.8                      | 19.9                                   |
| Used vehicle wholesale              | 69,512      | 2.8                          | 1,712        | 2.5                       | 0.5                                    |
| Finance and insurance <sup>1</sup>  | 94,851      | 3.8                          | 94,851       | 100.0                     | 25.3                                   |
| Service, body and parts             | 246,005     | 10.0                         | 122,480      | 49.8                      | 32.6                                   |
| Fleet and other                     | 38,978      | 1.6                          | 1,183        | 3.0                       | 0.2                                    |
|                                     | \$2,467,036 | 100.0 %                      | \$ 375,271   | 15.2 %                    | 100.0%                                 |

| Three Months Ended<br>June 30, 2016 | Revenues    | Percent of<br>Total Revenues | Gross Profit | Gross<br>Profit<br>Margin | Percent<br>of Total<br>Gross<br>Profit |
|-------------------------------------|-------------|------------------------------|--------------|---------------------------|--|
| New vehicle                         | \$1,209,037 | 56.7 %                       | \$ 72,862    | 6.0 %                     | 22.6 %                                 |
| Used vehicle retail                 | 553,647     | 26.0                         | 67,225       | 12.1                      | 20.9                                   |
| Used vehicle wholesale              | 66,714      | 3.1                          | 1,486        | 2.2                       | 0.5                                    |
| Finance and insurance <sup>1</sup>  | 81,043      | 3.8                          | 81,043       | 100.0                     | 25.2                                   |
| Service, body and parts             | 202,265     | 9.5                          | 98,599       | 48.7                      | 30.6                                   |
| Fleet and other                     | 20,633      | 0.9                          | 821          | 4.0                       | 0.2                                    |
|                                     | \$2,133,339 | 100.0 %                      | \$ 322,036   | 15.1 %                    | 100.0%                                 |

<sup>1</sup> Commissions reported net of anticipated cancellations.

| Six Months Ended<br>June 30, 2017  | Revenues    | Percent of<br>Total Revenues | Gross Profit | Gross<br>Profit<br>Margin | Percent<br>of Total<br>Gross<br>Profit |
|------------------------------------|-------------|------------------------------|--------------|---------------------------|--|
| New vehicle                        | \$2,594,359 | 55.2 %                       | \$ 150,657   | 5.8 %                     | 21.0 %                                 |
| Used vehicle retail                | 1,235,858   | 26.3                         | 143,289      | 11.6                      | 20.0                                   |
| Used vehicle wholesale             | 141,015     | 3.0                          | 3,229        | 2.3                       | 0.5                                    |
| Finance and insurance <sup>1</sup> | 181,628     | 3.9                          | 181,628      | 100.0                     | 25.3                                   |
| Service, body and parts            | 478,579     | 10.2                         | 235,674      | 49.2                      | 32.9                                   |
| Fleet and other                    | 71,698      | 1.4                          | 2,446        | 3.4                       | 0.3                                    |
|                                    | \$4,703,137 | 100.0 %                      | \$ 716,923   | 15.2 %                    | 100.0%                                 |

| Six Months Ended<br>June 30, 2016 | Revenues    | Percent of<br>Total Revenues | Gross Profit | Gross<br>Profit<br>Margin | Percent<br>of Total<br>Gross<br>Profit |
|-----------------------------------|-------------|------------------------------|--------------|---------------------------|--|
| New vehicle                       | \$2,305,092 | 56.0 %                       | \$ 139,628   | 6.1 %                     | 22.2 %                                 |



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|                                    |             |       |   |            |       |          |
|------------------------------------|-------------|-------|---|------------|-------|----------|
| Used vehicle retail                | 1,086,373   | 26.4  |   | 131,502    | 12.1  | 20.9     |
| Used vehicle wholesale             | 131,860     | 3.2   |   | 3,316      | 2.5   | 0.5      |
| Finance and insurance <sup>1</sup> | 158,681     | 3.9   |   | 158,681    | 100.0 | 25.2     |
| Service, body and parts            | 398,940     | 9.7   |   | 194,718    | 48.8  | 30.9     |
| Fleet and other                    | 35,254      | 0.8   |   | 1,373      | 3.9   | 0.3      |
|                                    | \$4,116,200 | 100.0 | % | \$ 629,218 | 15.3  | % 100.0% |

<sup>1</sup> Commissions reported net of anticipated cancellations.

## Same Store Operating Data

We believe that same store comparisons are an important indicator of our financial performance. Same store measures demonstrate our ability to grow revenues in our existing locations. As a result, same store measures have been integrated into the discussion below.

Same store measures reflect results for stores that were operating in each comparison period and only include the months when operations occurred in both periods. For example, a store acquired in May 2016 would be included in same store operating data beginning in June 2017, after its first full complete comparable month of operation. The second quarter operating results for the same store comparisons would include results for that store in only the period of June for both comparable periods.

## New Vehicle Revenue and Gross Profit

| (Dollars in thousands, except per unit amounts) | Three Months Ended June |             | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|---|-------------------------|-------------|------------------------|--------------------------|
|   | 30,<br>2017             | 2016        |                        |                          |
| Reported  |                         |             |                        |                          |
| Revenue   | \$1,384,055             | \$1,209,037 | \$175,018              | 14.5 %                   |
| Gross profit                                    | \$80,539                | \$72,862    | \$7,677                | 10.5                     |
| Gross margin                                    | 5.8                     | % 6.0       | % (20 )                | bp <sup>1</sup>          |
| Retail units sold                               | 40,876                  | 36,059      | 4,817                  | 13.4                     |
| Average selling price per retail unit           | \$33,860                | \$33,529    | \$331                  | 1.0                      |
| Average gross profit per retail unit            | \$1,970                 | \$2,021     | \$(51 )                | (2.5 )                   |
| Same store                                      |                         |             |                        |                          |
| Revenue   | \$1,217,563             | \$1,208,561 | \$9,002                | 0.7                      |
| Gross profit                                    | \$71,492                | \$72,759    | \$(1,267 )             | (1.7 )                   |
| Gross margin                                    | 5.9                     | % 6.0       | % (10 )                | bp                       |
| Retail units sold                               | 35,893                  | 36,042      | (149 )                 | (0.4 )                   |
| Average selling price per retail unit           | \$33,922                | \$33,532    | \$390                  | 1.2                      |
| Average gross profit per retail unit            | \$1,992                 | \$2,019     | \$(27 )                | (1.3 )                   |

<sup>1</sup> A basis point is equal to 1/100<sup>th</sup> of one percent

| (Dollars in thousands, except per unit amounts) | Six Months Ended |             | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|---|------------------|-------------|------------------------|--------------------------|
|   | June 30,<br>2017 | 2016        |                        |                          |
| Reported  |                  |             |                        |                          |
| Revenue   | \$2,594,359      | \$2,305,092 | \$289,267              | 12.5 %                   |
| Gross profit                                    | \$150,657        | \$139,628   | \$11,029               | 7.9                      |
| Gross margin                                    | 5.8              | % 6.1       | % (30 )                | bp                       |
| Retail units sold                               | 76,492           | 68,808      | 7,684                  | 11.2                     |
| Average selling price per retail unit           | \$33,917         | \$33,500    | \$417                  | 1.2                      |
| Average gross profit per retail unit            | \$1,970          | \$2,029     | \$(59 )                | (2.9 )                   |
| Same store                                      |                  |             |                        |                          |
| Revenue   | \$2,314,266      | \$2,302,695 | \$11,571               | 0.5                      |
| Gross profit                                    | \$135,303        | \$139,512   | \$(4,209 )             | (3.0 )                   |

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|                                       |          |          |       |          |
|---------------------------------------|----------|----------|-------|----------|
| Gross margin                          | 5.8      | % 6.1    | % (30 | )bp      |
| Retail units sold                     | 68,108   | 68,729   | (621  | ) (0.9 ) |
| Average selling price per retail unit | \$33,979 | \$33,504 | \$475 | 1.4      |
| Average gross profit per retail unit  | \$1,987  | \$2,030  | \$(43 | ) (2.1 ) |

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New vehicle sales increased 14.5% and 12.5% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, primarily driven by an increase in volume related to acquisitions.

Same store new vehicle unit sales decreased 0.4% and 0.9%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. These volume decreases were offset by a 1.2% and 1.4% increase, respectively, in average price per unit for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. On a same store basis, our stores performed better than national new vehicle sales levels, which decreased 2.9% and 2.2%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016.

Same store unit sales increased (decreased) as follows:

|   | Three months ended June 30, 2017 compared to the same period of 2016 | National growth in the three months ended June 30, 2017 compared to the same period of 2016 <sup>1</sup> | Six months ended June 30, 2017 compared to the same period of 2016 | National growth in the six months ended June 30, 2017 compared to the same period of 2016 <sup>1</sup> |
|---|--|--|--|--|
| Domestic brand same store unit sales change | (3.0 )%  | (4.2 )%  | (1.5 )%  | (4.0 )%  |
| Import brand same store unit sales change   | 2.0  | (1.7 )   | 1.6  | (1.2 )   |
| Luxury brand same store unit sales change   | (4.6 )   | (2.5 )   | (10.8 )  | 1.7  |
| Overall                                     | (0.4 )   | (2.9 )   | (0.9 )   | (2.2 )   |

<sup>1</sup> National auto unit sales and seasonally adjusted annual rate ("SAAR") data obtained from Stephens Auto Unit Sales and SAAR report as of June 2017.

National new vehicle sales market growth continues to moderate for all brands. Our domestic brand unit volume change outperformed the national average for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Our performance, compared to the national trend for domestic brands, was mainly driven by Ford, which had a same store sales increase of 2.2% and decrease of 1.5%, respectively, and Chrysler, which had same store sales decreases of 2.2% and 0.3%, respectively, for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. This performance compares to national market decreases of 3.6% and 3.9%, respectively, for Ford and 5.2% and 6.9%, respectively, for Chrysler for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016.

Our import brand unit volume outperformed the national average for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Our Toyota stores, which comprise 19.1% of our total new vehicle unit sales in the second quarter of 2017 grew 3.7% for the three months ended June 30, 2017 and were essentially flat for the six months ended June 30, 2017, compared to the same periods in 2016. This compares to national market decreases of 1.0% and 3.6%, respectively, for the three and six-months ended June 30, 2017 compared to the same periods of 2016. Our Honda stores, which comprised 23.3% of our total new vehicle unit sales in the second quarter of 2017, had a same store unit decrease of 1.9% and an increase of 0.6%, respectively, for the three and six-month period ended June 30, 2017 compared to the same period of 2016. The national average unit volume decrease was 1.9% and 0.1%, respectively, for Honda in the three and six-month period ended June 30, 2017 compared to the same period of

2016.

The period-over-period volume decrease for our luxury brand unit volume exceeded the national average in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. The decreases were primarily associated with our BMW and Mercedes stores, which comprised 4.1% and 1.1%, respectively, of our total new vehicle unit sales in the second quarter of 2017. Our BMW stores had same store unit sales decreases of 12.6% and 15.5%, respectively, for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. This compares to national average decreases for BMW of 8.0% and 4.1% for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Our Mercedes stores had same store unit sales decrease of 9.9% and 14.8%, respectively, for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. This compares to national average decreases for Mercedes of 4.9% and 0.8% for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Our luxury brands were down more than the national average due to decreases in our local markets. We are concentrated in areas such as Portland, Seattle and New Jersey where new vehicle registrations were down. Additionally, both our BMW and Mercedes stores lost market share.

We seek to grow our new vehicle sales organically by gaining share in the markets we serve. To increase awareness and customer traffic, we use a combination of traditional, digital and social media advertisements to reach customers. We have established a

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company-wide target of achieving 25% higher sales than the national OEM average. As of June 30, 2017, our sales were 9% higher than the national OEM average.

New vehicle gross profit increased 10.5% and 7.9%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. On a same store basis, new vehicle gross profit decreased 1.7% and 3.0% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. The same store average gross profit per unit for new vehicles decreased \$27 and \$43 in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016.

Under our business strategy, we believe that our new vehicle sales create incremental profit opportunities through certain manufacturer incentive programs, arranging of third party financing, vehicle service and insurance contracts, future resale of used vehicles acquired through trade-in and parts and service work.

#### Used Vehicle Retail Revenue and Gross Profit

| (Dollars in thousands, except per unit amounts) | Three Months Ended |           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|---|--------------------|-----------|------------------------|--------------------------|
|   | June 30,<br>2017   | 2016      |                        |                          |
| <b>Reported</b>                                 |                    |           |                        |                          |
| Retail revenue                                  | \$633,635          | \$553,647 | \$79,988               | 14.4 %                   |
| Retail gross profit                             | \$74,506           | \$67,225  | \$7,281                | 10.8                     |
| Retail gross margin                             | 11.8 %             | 12.1 %    | (30 )bp                |                          |
| Retail units sold                               | 32,171             | 27,716    | 4,455                  | 16.1                     |
| Average selling price per retail unit           | \$19,696           | \$19,976  | \$(280 )               | (1.4 )                   |
| Average gross profit per retail unit            | \$2,316            | \$2,425   | \$(109 )               | (4.5 )                   |
| <b>Same store</b>                               |                    |           |                        |                          |
| Retail revenue                                  | \$575,410          | \$552,634 | \$22,776               | 4.1                      |
| Retail gross profit                             | \$69,273           | \$67,121  | \$2,152                | 3.2                      |
| Retail gross margin                             | 12.0 %             | 12.1 %    | (10 )bp                |                          |
| Retail units sold                               | 28,937             | 27,657    | 1,280                  | 4.6                      |
| Average selling price per retail unit           | \$19,885           | \$19,982  | \$(97 )                | (0.5 )                   |
| Average gross profit per retail unit            | \$2,394            | \$2,427   | \$(33 )                | (1.4 )                   |

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| (Dollars in thousands, except per unit amounts) | Six Months Ended |             | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|---|------------------|-------------|------------------------|--------------------------|
|   | June 30,<br>2017 | 2016        |                        |                          |
| <b>Reported</b>                                 |                  |             |                        |                          |
| Retail revenue                                  | \$1,235,858      | \$1,086,373 | \$149,485              | 13.8 %                   |
| Retail gross profit                             | \$143,289        | \$131,502   | \$11,787               | 9.0                      |
| Retail gross margin                             | 11.6             | % 12.1      | % (50                  | )bp                      |
| Retail units sold                               | 62,954           | 55,147      | 7,807                  | 14.2                     |
| Average selling price per retail unit           | \$19,631         | \$19,700    | \$(69                  | ) (0.4 )                 |
| Average gross profit per retail unit            | \$2,276          | \$2,385     | \$(109                 | ) (4.6 )                 |
| <b>Same store</b>                               |                  |             |                        |                          |
| Retail revenue                                  | \$1,137,210      | \$1,083,257 | \$53,953               | 5.0                      |
| Retail gross profit                             | \$134,190        | \$131,217   | \$2,973                | 2.3                      |
| Retail gross margin                             | 11.8             | % 12.1      | % (30                  | )bp                      |
| Retail units sold                               | 57,438           | 54,977      | 2,461                  | 4.5                      |
| Average selling price per retail unit           | \$19,799         | \$19,704    | \$95                   | 0.5                      |
| Average gross profit per retail unit            | \$2,336          | \$2,387     | \$(51                  | ) (2.1 )                 |

Used vehicle retail sales are a strategic focus for organic growth. We offer three categories of used vehicles: manufacturer certified pre-owned ("CPO") vehicles; core vehicles, or late-model vehicles with lower mileage; and value autos, or vehicles with over 80,000 miles. We have established a company-wide target of achieving a per store average of 85 used retail units per month. Strategies to achieve this target include reducing wholesale sales and selling the full spectrum of used units, from late model certified pre-owned models to vehicles over ten years old.

Same store sales increased in all three categories of used vehicles as follows:

|                              | Three<br>months<br>ended<br>June 30,<br>2017<br>compared<br>to the<br>same<br>period of<br>2016 | Six<br>months<br>ended<br>June 30,<br>2017<br>compared<br>to the<br>same<br>period of<br>2016 |
|------------------------------|---|---|
| Certified pre-owned vehicles | 0.9 %   | 1.0 %   |
| Core vehicles                | 4.4   | 5.7   |
| Value autos                  | 10.6  | 11.6  |
| Overall                      | 4.1   | 5.0   |

The increase in same store used vehicle sales was primarily driven by increased unit sales in all three categories. For value autos, average selling prices increased 5.2% and 6.1%, respectively for the three and six-months ended June 30, 2017 compared to the same periods of 2016. On an annualized average, as of June 30, 2017 and 2016, each of our stores sold 67 and 64 retail used vehicle units, respectively, per month.

Used retail vehicle gross profit increased 10.8% and 9.0% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. On a same store basis, gross profit increased 3.2% and 2.3% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, driven by volume growth, partially offset by a decrease in the average gross profit per unit sold. The same store gross profit per unit decreased \$33 and \$51, respectively, for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016.

Our used vehicle operations provide an opportunity to generate sales to customers unable or unwilling to purchase a new vehicle, sell brands other than the store's new vehicle franchise(s) and increase sales from finance and insurance and parts and service.



## Used Vehicle Wholesale Revenue and Gross Profit

| (Dollars in thousands, except per unit amounts)<br>Reported | Three Months Ended<br>June 30, |           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|---|--------------------------------|-----------|------------------------|--------------------------|
|   | 2017                           | 2016      |                        |                          |
| Wholesale revenue   | \$69,512                       | \$66,714  | \$2,798                | 4.2 %                    |
| Wholesale gross profit                                      | \$1,712                        | \$1,486   | \$226                  | 15.2                     |
| Wholesale gross margin                                      | 2.5 %                          | 2.2 %     | 30 bp                  |                          |
| Wholesale units sold  | 10,906                         | 9,774     | 1,132                  | 11.6                     |
| Average selling price per wholesale unit                    | \$6,374                        | \$6,826   | \$(452)                | (6.6)                    |
| Average gross profit per retail unit                        | \$157                          | \$152     | \$5                    | 3.3                      |
| Same store  |                                |           |                        |                          |
| Wholesale revenue   | \$57,789                       | \$66,583  | \$(8,794)              | (13.2)                   |
| Wholesale gross profit                                      | \$1,377                        | \$1,528   | \$(151)                | (9.9)                    |
| Wholesale gross margin                                      | 2.4 %                          | 2.3 %     | 10 bp                  |                          |
| Wholesale units sold  | 8,912                          | 9,754     | (842)                  | (8.6)                    |
| Average selling price per wholesale unit                    | \$6,484                        | \$6,826   | \$(342)                | (5.0)                    |
| Average gross profit per wholesale unit                     | \$155                          | \$157     | \$(2)                  | (1.3)                    |
| (Dollars in thousands, except per unit amounts)<br>Reported | Six Months Ended<br>June 30,   |           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|   | 2017                           | 2016      |                        |                          |
| Wholesale revenue   | \$141,015                      | \$131,860 | \$9,155                | 6.9 %                    |
| Wholesale gross profit                                      | \$3,229                        | \$3,316   | \$(87)                 | (2.6)                    |
| Wholesale gross margin                                      | 2.3 %                          | 2.5 %     | (20) bp                |                          |
| Wholesale units sold  | 21,746                         | 19,287    | 2,459                  | 12.7                     |
| Average selling price per wholesale unit                    | \$6,485                        | \$6,837   | \$(352)                | (5.1)                    |
| Average gross profit per retail unit                        | \$148                          | \$172     | \$(24)                 | (14.0)                   |
| Same store  |                                |           |                        |                          |
| Wholesale revenue   | \$120,921                      | \$131,596 | \$(10,675)             | (8.1)                    |
| Wholesale gross profit                                      | \$2,803                        | \$3,380   | \$(577)                | (17.1)                   |
| Wholesale gross margin                                      | 2.3 %                          | 2.6 %     | (30) bp                |                          |
| Wholesale units sold  | 18,506                         | 19,242    | (736)                  | (3.8)                    |
| Average selling price per wholesale unit                    | \$6,534                        | \$6,839   | \$(305)                | (4.5)                    |
| Average gross profit per wholesale unit                     | \$151                          | \$176     | \$(25)                 | (14.2)                   |

Wholesale transactions are vehicles we have purchased from customers or vehicles we have attempted to sell via retail that we elect to dispose of due to age or other factors. Wholesale vehicles are typically sold at or near cost and do not comprise a meaningful component of our gross profit.



## Finance and Insurance

|  | Three Months Ended |               | Increase | % Increase |   |
|--|--------------------|---------------|----------|------------|---|
| (Dollars in thousands, except per unit amounts) Reported | June 30, 2017      | June 30, 2016 |          |            |   |
| Revenue  | \$94,851           | \$81,043      | \$13,808 | 17.0       | % |
| Average finance and insurance per retail unit            | \$1,298            | \$1,271       | \$27     | 2.1        | % |
| Same store   |                    |               |          |            |   |
| Revenue  | \$87,653           | \$80,988      | \$6,665  | 8.2        | % |
| Average finance and insurance per retail unit            | \$1,352            | \$1,271       | \$81     | 6.4        | % |
|  | Six Months Ended   |               | Increase | % Increase |   |
| (Dollars in thousands, except per unit amounts) Reported | June 30, 2017      | June 30, 2016 |          |            |   |
| Revenue  | \$181,628          | \$158,681     | \$22,947 | 14.5       | % |
| Average finance and insurance per retail unit            | \$1,302            | \$1,280       | \$22     | 1.7        | % |
| Same store   |                    |               |          |            |   |
| Revenue  | \$169,784          | \$158,446     | \$11,338 | 7.2        | % |
| Average finance and insurance per retail unit            | \$1,352            | \$1,281       | \$71     | 5.5        | % |

We believe that arranging timely vehicle financing is an important part of our ability to sell vehicles and we attempt to arrange financing for every vehicle we sell. We also offer related products such as extended warranties, insurance contracts and vehicle and theft protection.

The increases in same store finance and insurance revenue in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016 were primarily due to higher unit volume and increases in the average finance and insurance amount per retail unit. On a same store basis, our finance and insurance revenues per retail unit increased \$81 and \$71, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, mainly driven by improved penetration rates for service contracts.

Trends in penetration rates for total new and used retail vehicles sold are detailed below:

|   | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 30, 2017      | June 30, 2016 | June 30, 2017    | June 30, 2016 |
| Finance and insurance                   | 75%                | 78%           | 76%              | 78%           |
| Service contracts                       | 49                 | 44            | 48               | 43            |
| Lifetime lube, oil and filter contracts | 27                 | 27            | 27               | 27            |

We seek to increase our penetration of vehicle financing on the number of vehicles that we sell and to offer a comprehensive suite of products. We target an average F&I per unit retailed of \$1,450. We believe improved performance from sales training and revised pay plans will be critical factors in achieving this target.





largest contributor to our overall profitability. Earnings from service, body and parts have historically been more resilient during economic downturns, when owners have tended to repair their existing vehicles rather than buy new vehicles.

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Our service, body and parts sales grew in all areas in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. There are more late-model units in operation as new vehicle sales volumes have been increasing since 2010. We believe this increase in units in operation will continue to benefit our service, body and parts sales in the coming years as more late-model vehicles age and require repairs and maintenance.

We focus on retaining customers by offering competitively-priced routine maintenance and through our marketing efforts. We increased our same store customer pay business 7.0% and 7.1%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016.

Same store warranty sales increased 7.3% and 8.2%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. We continue to experience the impact of the significant recalls across multiple manufacturers. Combined with a growing number of units in operation, our warranty sales have steadily increased.

The increases in same-store warranty work by segment were as follows:

|          | Three<br>months<br>ended<br>June 30,<br>2017<br>compared<br>to the<br>same<br>period of<br>2016 | % | Six<br>months<br>ended<br>June 30,<br>2017<br>compared<br>to the<br>same<br>period of<br>2016 | % |
|----------|---|---|---|---|
| Domestic | 6.5   | % | 4.7   | % |
| Import   | 2.0   |   | 6.5   |   |
| Luxury   | 18.1  |   | 16.0  |   |

Same store wholesale parts increased 5.4% and 5.5% in the three and six-month periods ending June 30, 2017 compared to the same periods of 2016. We target independent repair shops, competing new vehicle dealers and wholesale accounts to expand parts sales to other repair shops.

Same store body shop increased 10.1% and 10.7%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Our stores have increased production through calculated adjustments to optimize personnel and equipment.

Same store service, body and parts gross profit increased 9.3% and 8.5%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, which is in line with our revenue growth. Our gross margins increased as our mix shifted toward customer pay, which has a higher margin than other service.

#### Segments

Certain financial information by segment is as follows:

| (Dollars in thousands) | Three Months Ended<br>June 30,<br>2017 | 2016      | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|------------------------|--|-----------|------------------------|--------------------------|
| Revenues:              |  |           |                        |                          |
| Domestic               | \$954,949                              | \$830,410 | \$124,539              | 15.0 %                   |

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|                     |             |             |           |          |
|---------------------|-------------|-------------|-----------|----------|
| Import              | 1,101,314   | 930,317     | 170,997   | 18.4     |
| Luxury              | 413,088     | 371,866     | 41,222    | 11.1     |
|                     | 2,469,351   | 2,132,593   | 336,758   | 15.8     |
| Corporate and other | (2,315 )    | 746         | (3,061 )  | (410.3 ) |
|                     | \$2,467,036 | \$2,133,339 | \$333,697 | 15.6 %   |

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| (Dollars in thousands)        | Six Months Ended |                | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|-------------------------------|------------------|----------------|------------------------|--------------------------|
|                               | June 30,<br>2017 | 2016           |                        |                          |
| Revenues:                     |                  |                |                        |                          |
| Domestic                      | \$ 1,854,707     | \$ 1,602,312   | \$ 252,395             | 15.8 %                   |
| Import                        | 2,072,787        | 1,793,060      | 279,727                | 15.6                     |
| Luxury                        | 776,891          | 718,679        | 58,212                 | 8.1                      |
|                               | 4,704,385        | 4,114,051      | 590,334                | 14.3                     |
| Corporate and other           | (1,248 )         | 2,149          | (3,397 )               | (158.1 )                 |
|                               | \$ 4,703,137     | \$ 4,116,200   | \$ 586,937             | 14.3 %                   |
|                               |                  | Three Months   |                        |                          |
|                               |                  | Ended June 30, |                        |                          |
| (Dollars in thousands)        | 2017             | 2016           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
| Segment income*:              |                  |                |                        |                          |
| Domestic                      | \$ 27,857        | \$ 28,999      | \$ (1,142 )            | (3.9 )%                  |
| Import                        | 32,465           | 29,680         | 2,785                  | 9.4                      |
| Luxury                        | 10,088           | 9,730          | 358                    | 3.7                      |
|                               | 70,410           | 68,409         | 2,001                  | 2.9                      |
| Corporate and other           | 38,239           | 28,394         | 9,845                  | 34.7                     |
| Depreciation and amortization | (14,031 )        | (12,503 )      | 1,528                  | 12.2                     |
| Other interest expense        | (7,169 )         | (5,502 )       | 1,667                  | 30.3                     |
| Other income (expense), net   | 387              | (1,495 )       | NM                     | NM                       |
| Income before income taxes    | \$ 87,836        | \$ 77,303      | \$ 10,533              | 13.6 %                   |

NM – not meaningful

\*Segment income for each reportable segment is defined as income before income taxes, depreciation and amortization, other interest expense and other expense, net.

| (Dollars in thousands)        | Six Months Ended |            | Increase<br>(Decrease) | % Increase |
|-------------------------------|------------------|------------|------------------------|------------|
|                               | June 30,<br>2017 | 2016       |                        |            |
| Segment income*:              |                  |            |                        |            |
| Domestic                      | \$ 53,299        | \$ 52,129  | \$ 1,170               | 2.2 %      |
| Import                        | 54,637           | 53,943     | 694                    | 1.3        |
| Luxury                        | 14,801           | 14,312     | 489                    | 3.4        |
|                               | 122,737          | 120,384    | 2,353                  | 2.0        |
| Corporate and other           | 76,740           | 55,088     | 21,652                 | 39.3       |
| Depreciation and amortization | (26,770 )        | (24,166 )  | 2,604                  | 10.8       |
| Other interest expense        | (13,840 )        | (10,961 )  | 2,879                  | 26.3       |
| Other income (expense), net   | 10,232           | (3,021 )   | (13,253 )              | NM         |
| Income before income taxes    | \$ 169,099       | \$ 137,324 | \$ 31,775              | 23.1 %     |

NM – Not meaningful

|                                | Three Months        |        | Increase | % Increase |
|--------------------------------|---------------------|--------|----------|------------|
|                                | Ended June 30, 2017 | 2016   |          |            |
| Retail new vehicle unit sales: |                     |        |          |            |
| Domestic                       | 13,256              | 11,712 | 1,544    | 13.2 %     |
| Import                         | 23,287              | 20,080 | 3,207    | 16.0       |
| Luxury                         | 4,423               | 4,317  | 106      | 2.5        |
|                                | 40,966              | 36,109 | 4,857    | 13.5       |
| Allocated to management        | (90 )               | (50 )  | 40       | NM         |
|                                | 40,876              | 36,059 | 4,817    | 13.4 %     |

NM – Not meaningful

|                                | Six Months          |        | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|--------------------------------|---------------------|--------|------------------------|--------------------------|
|                                | Ended June 30, 2017 | 2016   |                        |                          |
| Retail new vehicle unit sales: |                     |        |                        |                          |
| Domestic                       | 25,496              | 22,441 | 3,055                  | 13.6 %                   |
| Import                         | 43,122              | 38,114 | 5,008                  | 13.1                     |
| Luxury                         | 8,039               | 8,380  | (341 )                 | (4.1 )                   |
|                                | 76,657              | 68,935 | 7,722                  | 11.2                     |
| Allocated to management        | (165 )              | (127 ) | 38                     | NM                       |
|                                | 76,492              | 68,808 | 7,684                  | 11.2 %                   |

#### Domestic

A summary of financial information for our Domestic segment follows:

|                               | Three Months        |           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|-------------------------------|---------------------|-----------|------------------------|--------------------------|
|                               | Ended June 30, 2017 | 2016      |                        |                          |
| (Dollars in thousands)        |                     |           |                        |                          |
| Revenue                       | \$954,949           | \$830,410 | \$124,539              | 15.0 %                   |
| Segment income                | \$27,857            | \$28,999  | \$(1,142 )             | (3.9 )                   |
| Retail new vehicle unit sales | 13,256              | 11,712    | 1,544                  | 13.2                     |

|                               | Six Months Ended |             | Increase  | % Increase |
|-------------------------------|------------------|-------------|-----------|------------|
|                               | June 30, 2017    | 2016        |           |            |
| (Dollars in thousands)        |                  |             |           |            |
| Revenue                       | \$1,854,707      | \$1,602,312 | \$252,395 | 15.8 %     |
| Segment income                | \$53,299         | \$52,129    | \$1,170   | 2.2        |
| Retail new vehicle unit sales | 25,496           | 22,441      | 3,055     | 13.6       |

Our Domestic segment revenue increased 15.0% and 15.8%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. Since June 30, 2016, we acquired eleven additional domestic brand stores, which contributed to increases in new vehicle, used vehicle retail, finance and insurance and service body and parts sales.

Our Domestic segment income decreased 3.9% and increased 2.2%, respectively, in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. In the three-months ended June 30, 2017, the decrease in segment income was due to gross profits growth of 15.3%, in line with revenues, offset by SG&A expense growth of

19.9% and a floor plan interest increase of 39.8% primarily related to rising interest rates. For the six months ended June 30, 2017, segment income grew 2.2% but lagged our revenue growth. Growth in SG&A expenses of 19.0% and floor plan interest of 31.0% were the main drivers of the slower segment income growth compared to revenue growth.

### Import

A summary of financial information for our Import segment follows:

| (Dollars in thousands)        | Three Months Ended |           | Increase  | % Increase |
|-------------------------------|--------------------|-----------|-----------|------------|
|                               | June 30, 2017      | 2016      |           |            |
| Revenue                       | \$1,101,314        | \$930,317 | \$170,997 | 18.4 %     |
| Segment income                | \$32,465           | \$29,680  | \$2,785   | 9.4        |
| Retail new vehicle unit sales | 23,287             | 20,080    | 3,207     | 16.0       |

  

| (Dollars in thousands)        | Six Months Ended |             | Increase<br>(Decrease) | % Increase |
|-------------------------------|------------------|-------------|------------------------|------------|
|                               | June 30, 2017    | 2016        |                        |            |
| Revenue                       | \$2,072,787      | \$1,793,060 | \$279,727              | 15.6 %     |
| Segment income                | \$54,637         | \$53,943    | \$694                  | 1.3        |
| Retail new vehicle unit sales | 43,122           | 38,114      | 5,008                  | 13.1       |

Our Import segment revenue increased 18.4% and 15.6% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016 due to increases in all major business lines. Since June 30, 2016, we added ten import brand stores.

Segment income for our Import segment increased 9.4% and 1.3% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. In the three months ended June 30, 2017, the 9.4% growth in segment income was due to gross profits growth of 17.3%, in line with revenues, offset by SG&A expense growth of 18.3% and a floor plan interest increase of 53.2% related to rising interest rates. These factors resulted in slower Import segment income growth compared to revenue growth. For the six months ended June 30, 2017, segment income grew 1.3% and lagged our revenue growth. Gross profit growth was 13.0% and lagged behind revenue growth for the period. Additionally, growth in SG&A expenses was 14.8% slightly higher than the growth in gross profit and floor plan interest increased 46.1% due to increased inventory levels and rising interest rates. The net effect of these factors was slower segment income growth compared to revenue growth.

### Luxury

A summary of financial information for our Luxury segment follows:

| (Dollars in thousands)        | Three Months Ended |           | Increase | % Increase |
|-------------------------------|--------------------|-----------|----------|------------|
|                               | June 30, 2017      | 2016      |          |            |
| Revenue                       | \$413,088          | \$371,866 | \$41,222 | 11.1 %     |
| Segment income                | \$10,088           | \$9,730   | \$358    | 3.7        |
| Retail new vehicle unit sales | 4,423              | 4,317     | 106      | 2.5        |

  

| (Dollars in thousands)        | Six Months Ended |           | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|-------------------------------|------------------|-----------|------------------------|--------------------------|
|                               | June 30, 2017    | 2016      |                        |                          |
| Revenue                       | \$776,891        | \$718,679 | \$58,212               | 8.1 %                    |
| Segment income                | \$14,801         | \$14,312  | \$489                  | 3.4                      |
| Retail new vehicle unit sales | 8,039            | 8,380     | (341)                  | (4.1)                    |

Our Luxury segment revenue increased 11.1% and 8.1% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016 due to increases in used vehicle retail, finance and insurance and service body

and parts sales. In the past twelve months, we added two luxury brand stores.

Our Luxury segment income increased 3.7% and 3.4% for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. In the three months ended June 30, 2017, the 3.7% growth in segment income was due to gross profits growth of 10.1%, lagging behind revenue growth. SG&A expense grew 9.8%, slower than growth in gross profit growth, and was offset by a floor plan interest increase of 30.1% related to rising interest rates. These factors result in slower Luxury segment income growth compared to revenue growth. For the six months ended June 30, 2017, segment income grew 3.4% and lagged our

revenue growth for that period. Gross profit growth was 9.2%, slightly better than revenue growth for the period. This was offset by growth in SG&A expense of 9.1% and floor plan interest growth of 22.9% due to rising interest rates. These factors resulted in slower segment income growth than revenue growth.

#### Corporate and Other

Revenues attributable to Corporate and other include the results of operations of our stand-alone body shop, offset by certain unallocated reserve and elimination adjustments related to vehicle sales.

|                        | Three Months              |          | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|------------------------|---------------------------|----------|------------------------|--------------------------|
|                        | Ended<br>June 30,<br>2017 | 2016     |                        |                          |
| (Dollars in thousands) |                           |          |                        |                          |
| Revenue, net           | \$(2,315 )                | \$746    | \$ (3,061 )            | (410.3 )%                |
| Segment income         | \$38,239                  | \$28,394 | \$ 9,845               | 34.7                     |

|                        | Six Months Ended |          | Increase<br>(Decrease) | % Increase<br>(Decrease) |
|------------------------|------------------|----------|------------------------|--------------------------|
|                        | June 30,<br>2017 | 2016     |                        |                          |
| (Dollars in thousands) |                  |          |                        |                          |
| Revenue, net           | \$(1,248 )       | \$2,149  | \$ (3,397 )            | (158.1 )%                |
| Segment income         | \$76,740         | \$55,088 | \$ 21,652              | 39.3                     |

The decreases in Corporate and other revenue in the three and six month periods ended June 30, 2017 compared to the same periods of 2016 were primarily related to changes to certain reserves that are not specifically identified with our domestic, import or luxury segment revenue, such as our reserve for revenue reversals associated with unwound vehicle sales and elimination of revenues associated with internal corporate vehicle purchases and leases with our stores.

Segment income attributable to Corporate and other includes amounts associated with the operating income from our stand-alone body shop and certain internal corporate expense allocations that reduce reportable segment income but increase Corporate and other income. These internal corporate expense allocations are used to increase comparability of our dealerships and reflect the capital burden a stand-alone dealership would experience. Examples of these internal allocations include internal rent expense, internal floor plan financing charges, and internal fees charged to offset employees within our corporate headquarters who perform certain dealership functions.

Corporate and other segment income increased \$9.8 million and \$21.7 million for the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. These increases in segment income were due to the addition of 23 stores in the past twelve months. The three and six month periods ended June 30, 2017 include acquisition expenses of \$2.1 million and an insurance reserve charge of \$3.9 million. The 2016 results included impairment charges of \$3.5 million and \$7.0 million, respectively, for the three and six month periods ended June 30, 2016.

#### Asset Impairments

Asset impairments consist of the following:

|                          | Three      | Six        |
|--------------------------|------------|------------|
|                          | Months     | Months     |
|                          | Ended      | Ended      |
|                          | June 30,   | June 30,   |
| (Dollars in thousands)   | 2017       | 2016       |
| Equity-method investment | \$-\$3,498 | \$-\$6,996 |

The asset impairments recorded in 2016 were associated with our equity-method investment in a limited liability company. We evaluated this equity-method investment at the end of each reporting period and identified indications of loss resulting from other than temporary declines in value. We exited this equity-method investment in December 2016. See Note 8 of the Condensed Notes to the Consolidated Financial Statements for additional information.

## Selling, General and Administrative Expense (“SG&amp;A”)

SG&A includes salaries and related personnel expenses, advertising (net of manufacturer cooperative advertising credits), rent, facility costs, and other general corporate expenses.

| (Dollars in thousands) | Three Months |            | Increase  | % Increase |
|------------------------|--------------|------------|-----------|------------|
|                        | 2017         | 2016       |           |            |
| Personnel              | \$ 167,324   | \$ 144,530 | \$ 22,794 | 15.8 %     |
| Advertising            | 22,988       | 19,784     | 3,204     | 16.2       |
| Rent                   | 7,227        | 6,944      | 283       | 4.1        |
| Facility costs         | 14,252       | 10,373     | 3,879     | 37.4       |
| Other                  | 45,499       | 33,895     | 11,604    | 34.2       |
| Total SG&A             | \$ 257,290   | \$ 215,526 | \$ 41,764 | 19.4 %     |

| As a % of gross profit | Three Months |        | Increase<br>(Decrease) |
|------------------------|--------------|--------|------------------------|
|                        | 2017         | 2016   |                        |
| Personnel              | 44.6 %       | 44.9 % | (30 )bp                |
| Advertising            | 6.1          | 6.1    | —                      |
| Rent                   | 1.9          | 2.2    | (30 )                  |
| Facility costs         | 3.8          | 3.2    | 60                     |
| Other                  | 12.2         | 10.5   | 170                    |
| Total SG&A             | 68.6 %       | 66.9 % | 170 bp                 |

| (Dollars in thousands) | Six Months Ended |            | Increase  | % Increase |
|------------------------|------------------|------------|-----------|------------|
|                        | 2017             | 2016       |           |            |
| Personnel              | \$ 330,996       | \$ 293,254 | \$ 37,742 | 12.9 %     |
| Advertising            | 42,944           | 39,119     | 3,825     | 9.8        |
| Rent                   | 14,448           | 13,346     | 1,102     | 8.3        |
| Facility costs         | 29,379           | 18,432     | 10,947    | 59.4       |
| Other                  | 82,295           | 70,481     | 11,814    | 16.8       |
| Total SG&A             | \$ 500,062       | \$ 434,632 | \$ 65,430 | 15.1 %     |

| As a % of gross profit | Six Months |        | Increase<br>(Decrease) |
|------------------------|------------|--------|------------------------|
|                        | 2017       | 2016   |                        |
| Personnel              | 46.2 %     | 46.6 % | (40 )bp                |
| Advertising            | 6.0 %      | 6.2 %  | (20 )                  |
| Rent                   | 2.0 %      | 2.1 %  | (10 )                  |
| Facility costs         | 4.1 %      | 2.9 %  | 120                    |
| Other                  | 11.5 %     | 11.3 % | 20                     |
| Total SG&A             | 69.8 %     | 69.1 % | 70 bp                  |

SG&A expense increased 19.4% and 15.1% in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016. A majority of these increases were in facility costs and other expenses. The increase in facility costs were mainly due to lower costs as a result of a \$3.4 million gain for property-related insurance proceeds and a \$1.1 million gain on the sale of stores in the first quarter 2016. Other expenses in the three and six-month periods ended June 30, 2017 include acquisition expense of \$2.1 million and a hail storm insurance reserve related charge of



\$3.9 million .

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SG&A expense adjusted for non-core charges was as follows (in thousands):

|                         | Three Months   |           | Increase | % Increase |
|-------------------------|----------------|-----------|----------|------------|
|                         | Ended June 30, |           |          |            |
| (Dollars in thousands)  | 2017           | 2016      |          |            |
| Personnel               | \$167,324      | \$144,530 | \$22,794 | 15.8 %     |
| Advertising             | 22,988         | 19,783    | 3,205    | 16.2       |
| Rent                    | 7,227          | 6,944     | 283      | 4.1        |
| Adjusted facility costs | 14,252         | 10,373    | 3,879    | 37.4       |
| Adjusted other          | 39,484         | 33,896    | 5,588    | 16.5       |
| Adjusted total SG&A     | \$251,275      | \$215,526 | \$35,749 | 16.6 %     |

|                         | Three Months   |        | Increase<br>(Decrease) |
|-------------------------|----------------|--------|------------------------|
|                         | Ended June 30, |        |                        |
| As a % of gross profit  | 2017           | 2016   |                        |
| Personnel               | 44.6 %         | 44.9 % | (30 )bp                |
| Advertising             | 6.1 %          | 6.1 %  | —                      |
| Rent                    | 1.9 %          | 2.2 %  | (30 )                  |
| Adjusted facility costs | 3.8 %          | 3.2 %  | 60                     |
| Adjusted other          | 10.6 %         | 10.5 % | 10                     |
| Adjusted total SG&A     | 67.0 %         | 66.9 % | 10 bp                  |

|                         | Six Months Ended |           | Increase | % Increase |
|-------------------------|------------------|-----------|----------|------------|
|                         | June 30,         |           |          |            |
| (Dollars in thousands)  | 2017             | 2016      |          |            |
| Personnel               | \$330,996        | \$293,254 | \$37,742 | 12.9 %     |
| Advertising             | 42,944           | 39,119    | 3,825    | 9.8 %      |
| Rent                    | 14,448           | 13,346    | 1,102    | 8.3 %      |
| Adjusted facility costs | 29,379           | 19,519    | 9,860    | 50.5 %     |
| Adjusted other          | 76,280           | 68,575    | 7,705    | 11.2 %     |
| Adjusted total SG&A     | \$494,047        | \$433,813 | \$60,234 | 13.9 %     |

|                         | Six Months     |        | Increase<br>(Decrease) |
|-------------------------|----------------|--------|------------------------|
|                         | Ended June 30, |        |                        |
| As a % of gross profit  | 2017           | 2016   |                        |
| Personnel               | 46.2 %         | 46.6 % | (40 )bp                |
| Advertising             | 6.0 %          | 6.2 %  | (20 )                  |
| Rent                    | 2.0 %          | 2.1 %  | (10 )                  |
| Adjusted facility costs | 4.1 %          | 3.1 %  | 100                    |
| Adjusted other          | 10.6 %         | 10.9 % | (30 )                  |
| Adjusted total SG&A     | 68.9 %         | 68.9 % | —                      |

Adjusted SG&A excludes acquisition expense of \$2.1 million and an insurance reserve related charge of \$3.9 million for the three and six month periods ended June 30, 2017. We did not have any adjustments in the three months ended June 30, 2016 and had adjustments related to a \$1.1 million gain for the disposal of stores offset by a \$1.9 million legal reserve adjustment for the six month period ended June 30, 2016. See “Non-GAAP Reconciliations” for more details.



### Depreciation and Amortization

Depreciation and amortization is comprised of depreciation expense related to buildings, significant remodels or improvements, furniture, tools, equipment and signage and amortization of certain intangible assets, including customer lists and non-compete agreements.

|                               | Three Months   |           |          |            |
|-------------------------------|----------------|-----------|----------|------------|
| (Dollars in thousands)        | Ended June 30, | 2016      | Increase | % Increase |
|                               | 2017           |           |          |            |
| Depreciation and amortization | \$ 14,031      | \$ 12,503 | \$ 1,528 | 12.2 %     |
|                               | Six Months     |           |          |            |
| (Dollars in thousands)        | Ended June 30, | 2016      | Increase | % Increase |
|                               | 2017           |           |          |            |
| Depreciation and amortization | \$ 26,770      | \$ 24,166 | \$ 2,604 | 10.8 %     |

The increases in depreciation and amortization in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016 were primarily due to capital expenditures and acquisitions that occurred since June 30, 2016. Our largest capital investments were related to expanding and improving facilities subsequent to the acquisition of stores, as well as investments in improvements at our existing facilities. These investments increase the amount of depreciable assets and amortizable expenses. In the full year of 2016 and the first six months of 2017, we had capital expenditures of \$100.8 million and \$32.3 million, respectively.

### Operating Margin

Operating income as a percentage of revenue, or operating margin, was as follows:

|   | Three Months   |      | Six Months     |      |
|---|----------------|------|----------------|------|
|   | Ended June 30, | 2016 | Ended June 30, | 2016 |
|   | 2017           |      | 2017           |      |
| Operating margin  | 4.2%           | 4.2% | 4.0%           | 4.0% |
| Operating margin adjusted for non-core charges <sup>1</sup> | 4.5%           | 4.4% | 4.2%           | 4.2% |

<sup>1</sup> See "Non-GAAP Reconciliations" for more details.

In the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, our operating margin remained steady. Adjusting for non-core charges, as detailed below in Non-GAAP Reconciliations, adjusted operating margin improved slightly in the three months ended June 30, 2017 compared to the same period in 2016 and was consistent with the prior year for the six months ended June 30, 2017. We continue to focus on cost control, which allows us to leverage our cost structure in an environment of improving sales.

### Floor Plan Interest Expense and Floor Plan Assistance

Floor plan interest expense increased \$3.1 million and \$5.3 million in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016, primarily as a result of increasing LIBOR interest rates and increased average outstanding balances on our floor plan facilities.

Floor plan assistance is provided by manufacturers to support store financing of new vehicle inventory. Under accounting standards, floor plan assistance is recorded as a component of new vehicle gross profit when the specific vehicle is sold. However, because manufacturers provide this assistance to offset inventory carrying costs, we believe a comparison of floor plan interest expense to floor plan assistance is a useful measure of the efficiency of our new vehicle sales relative to stocking levels.

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The following tables detail the carrying costs for new vehicles and include new vehicle floor plan interest net of floor plan assistance earned.

| (Dollars in thousands)   | Three Months |           | %       |         |
|--|--------------|-----------|---------|---------|
|  | 2017         | 2016      | Change  | Change  |
| Floor plan interest expense (new vehicles)                     | \$9,332      | \$6,209   | \$3,123 | 50.3 %  |
| Floor plan assistance (included as an offset to cost of sales) | (13,268)     | (11,270)  | (1,998) | 17.7    |
| Net new vehicle carrying costs                                 | \$(3,936)    | \$(5,061) | \$1,125 | (22.2)% |

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| (Dollars in thousands)   | Six Months Ended |            |          | % Change |
|--|------------------|------------|----------|----------|
|  | June 30,         |            | Change   |          |
|  | 2017             | 2016       |          |          |
| Floor plan interest expense (new vehicles)                     | \$17,384         | \$12,118   | \$5,266  | 43.5 %   |
| Floor plan assistance (included as an offset to cost of sales) | (25,056 )        | (21,570 )  | (3,486 ) | 16.2     |
| Net new vehicle carrying costs                                 | \$(7,672 )       | \$(9,452 ) | 1,780    | (18.8)%  |

#### Other Interest Expense

Other interest expense includes interest on debt incurred related to acquisitions, real estate mortgages, our used vehicle inventory financing facility and our revolving line of credit.

| (Dollars in thousands)       | Three Months Ended June 30, |         | Increase (Decrease) | % Increase (Decrease) |
|------------------------------|-----------------------------|---------|---------------------|-----------------------|
|                              | 2017                        | 2016    |                     |                       |
| Mortgage interest            | \$4,694                     | \$3,699 | \$ 995              | 26.9                  |
| Other interest               | 2,585                       | 1,931   | 654                 | 33.9                  |
| Capitalized interest         | (110 )                      | (128 )  | (18 )               | (14.1 )               |
| Total other interest expense | \$7,169                     | \$5,502 | 1,667               | 30.3 %                |

  

| (Dollars in thousands)       | Six Months Ended June 30, |          | Increase (Decrease) | % Increase (Decrease) |
|------------------------------|---------------------------|----------|---------------------|-----------------------|
|                              | 2017                      | 2016     |                     |                       |
| Mortgage interest            | \$9,085                   | \$7,247  | \$ 1,838            | 25.4 %                |
| Other interest               | 4,948                     | 3,950    | 998                 | 25.3                  |
| Capitalized interest         | (193 )                    | (236 )   | (43 )               | (18.2 )               |
| Total other interest expense | \$13,840                  | \$10,961 | 2,879               | 26.3 %                |

The increases of \$1.7 million and \$2.9 million in other interest expense in the three and six-month periods ended June 30, 2017 compared to the same periods of 2016 were primarily due to higher volumes of borrowing on our credit facility and higher mortgage interest due to additional mortgage financings and increased interest rates.

#### Other Income (Expense), Net

| (Dollars in thousands)      | Three Months Ended June 30, |           | Increase | % Increase |
|-----------------------------|-----------------------------|-----------|----------|------------|
|                             | 2017                        | 2016      |          |            |
| Other Income (Expense), net | \$387                       | \$(1,495) | \$ 1,882 | NM         |

  

| (Dollars in thousands)      | Six Months Ended June 30, |           | Increase  | % Increase |
|-----------------------------|---------------------------|-----------|-----------|------------|
|                             | 2017                      | 2016      |           |            |
| Other Income (Expense), net | \$10,232                  | \$(3,021) | \$ 13,253 | NM         |

Other income (expense), net includes a gain related to legal settlements with OEMs recorded in the first quarter of 2017. Other income (expense), net in 2016 included the gains and losses related to equity-method investments, which we exited in December of 2016.

## Income Tax Provision

Our effective income tax rate was as follows:

|  | Three Months Ended<br>June 30, |       | Six Months Ended<br>June 30, |       |
|--|--------------------------------|-------|------------------------------|-------|
|  | 2017                           | 2016  | 2017                         | 2016  |
| Effective income tax rate  | 39.4%                          | 33.5% | 38.5%                        | 33.2% |
| Effective income tax rate excluding tax credits generated through our equity-method investment and other non-core items <sup>1</sup> | 39.1%                          | 39.5% | 38.4%                        | 39.3% |

<sup>1</sup> See “Non-GAAP Reconciliations” for more details.

Our 2016 tax rate was positively affected by new markets tax credits that were generated through our equity-method investment with U.S. Bancorp Community Development Corporation. Our effective tax rates for the three and six-month periods ended June 30, 2017 were favorably impacted by excess tax benefits related to our stock-based compensation. The adoption of this new guidance was applied prospectively beginning in 2017. See Note 12 of the Condensed Notes to the Consolidated Financial Statements for additional information.

Excluding the tax credits generated by our equity-method investment and adjusting for other non-core items, our effective tax rate was slightly impacted by the recognition of excess tax benefits related to our stock-based compensation for the three and six month periods ended June 30, 2017 compared to the same period of 2016.

## Non-GAAP Reconciliations

We believe each of the non-GAAP financial measures below improves the transparency of our disclosures, provides a meaningful presentation of our results from the core business operations because they exclude adjustments for items not related to our ongoing core business operations and other non-cash adjustments, and improves the period-to-period comparability of our results from the core business operations. We use these measures in conjunction with GAAP financial measures to assess our business, including our compliance with covenants in our credit facility and in communications with our Board of Directors concerning financial performance. These measures should not be considered an alternative to GAAP measures.

The following tables reconcile certain reported non-GAAP measures to the most comparable GAAP measure from our Consolidated Statements of Operations:

| (Dollars in Thousands, Except per Share Amounts) | Three Months Ended June 30, 2017 |                     |                      |           |
|--|----------------------------------|---------------------|----------------------|-----------|
|  | As reported                      | Reserve Adjustments | Acquisition expenses | Adjusted  |
| Selling, general and administrative              | \$257,290                        | \$ (3,878 )         | \$ (2,137 )          | \$251,275 |
| Operating income                                 | 103,950                          | 3,878               | 2,137                | 109,965   |
| Income before income taxes                       | \$87,836                         | \$ 3,878            | \$ 2,137             | \$93,851  |
| Income tax provision                             | (34,636 )                        | (1,231 )            | (821 )               | (36,688 ) |
| Net income                                       | \$53,200                         | \$ 2,647            | \$ 1,316             | \$57,163  |
| Diluted net income per share                     | \$2.12                           | \$ 0.11             | \$ 0.05              | \$2.28    |
| Diluted share count                              | 25,106                           |                     |                      |           |

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| (Dollars in thousands, except per share amounts) | Three Months Ended June 30, 2016 |                          |           |
|--|----------------------------------|--------------------------|-----------|
|  | As reported                      | Equity-method investment | Adjusted  |
| Asset impairment                                 | \$3,498                          | \$ (3,498 )              | \$—       |
| Operating income                                 | 90,509                           | 3,498                    | 94,007    |
| Other income (expense)                           | (1,495 )                         | 2,065                    | 570       |
| Income before income taxes                       | \$77,303                         | \$ 5,563                 | \$82,866  |
| Income tax provision                             | (25,875 )                        | (6,837 )                 | (32,712 ) |
| Net income (loss)                                | \$51,428                         | \$ (1,274 )              | \$50,154  |
| Diluted net income (loss) per share              | \$2.01                           | \$ (0.05 )               | \$1.96    |
| Diluted share count                              | 25,534                           |                          |           |

| (Dollars in thousands, except per share amounts) | Six Months Ended June 30, 2017 |                     |                      |                |           |
|--|--------------------------------|---------------------|----------------------|----------------|-----------|
|  | As reported                    | Reserve adjustments | Acquisition expenses | OEM settlement | Adjusted  |
| Selling, general and administrative              | \$500,062                      | \$ (3,878 )         | \$ (2,137 )          | \$—            | \$494,047 |
| Operating income                                 | 190,091                        | 3,878               | 2,137                | —              | 196,106   |
| Other (expense) income, net                      | 10,232                         | —                   | —                    | (9,111 )       | 1,121     |
| Income (loss) before income taxes                | \$169,099                      | \$ 3,878            | \$ 2,137             | \$ (9,111 )    | \$166,003 |
| Income tax (provision) benefit                   | (65,172 )                      | (1,231 )            | (821 )               | 3,423          | (63,801 ) |
| Net income (loss)                                | \$103,927                      | \$ 2,647            | \$ 1,316             | \$ (5,688 )    | \$102,202 |
| Diluted net income (loss) per share              | \$4.13                         | \$ 0.11             | \$ 0.05              | \$ (0.23 )     | \$4.06    |
| Diluted share count                              | 25,177                         |                     |                      |                |           |

| (Dollars in thousands, except per share amounts) | Six Months Ended June 30, 2016 |                                 |                          |                          |           |
|--|--------------------------------|---------------------------------|--------------------------|--------------------------|-----------|
|  | As reported                    | Disposal gain on sale of stores | Equity-method investment | Legal reserve adjustment | Adjusted  |
| Asset impairment                                 | \$6,996                        | \$—                             | \$ (6,996 )              | \$—                      | \$—       |
| Selling, general and administrative              | 434,632                        | 1,087                           | —                        | (1,906 )                 | 433,813   |
| Operating Income (expense)                       | 163,424                        | (1,087 )                        | 6,996                    | 1,906                    | 171,239   |
| Other (expense) income, net                      | (3,021 )                       | —                               | 4,131                    | —                        | 1,110     |
| Income (loss) before income taxes                | \$137,324                      | \$(1,087)                       | \$ 11,127                | \$ 1,906                 | \$149,270 |
| Income tax (provision) benefit                   | (45,626 )                      | 426                             | (12,782 )                | (747 )                   | (58,729 ) |
| Net income (loss)                                | \$91,698                       | \$(661 )                        | \$ (1,655 )              | \$ 1,159                 | \$90,541  |
| Diluted net income (loss) per share              | \$3.56                         | \$(0.03 )                       | \$ (0.06 )               | \$ 0.05                  | \$3.52    |
| Diluted share count                              | 25,754                         |                                 |                          |                          |           |

#### Liquidity and Capital Resources

We manage our liquidity and capital resources to fund our operating, investing and financing activities. We rely primarily on cash flows from operations and borrowings under our credit facilities or in capital markets as the main



sources for liquidity. We use

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those funds to invest in capital expenditures, increase working capital and fulfill contractual obligations. Remaining funds are used for acquisitions, debt retirement, cash dividends, share repurchases and general business purposes.

#### Available Sources

Below is a summary of our immediately available funds:

| (Dollars in thousands)                      | As of June 30, |           | Increase | % Increase |
|---|----------------|-----------|----------|------------|
|   | 2017           | 2016      |          |            |
| Cash and cash equivalents                   | \$31,177       | \$15,044  | \$16,133 | 107.2 %    |
| Available credit on the credit facilities   | 185,173        | 134,608   | 50,565   | 37.6       |
| Total current available funds               | 216,350        | 149,652   | 66,698   | 44.6       |
| Estimated funds from unfinanced real estate | 192,067        | 163,505   | 28,562   | 17.5       |
| Total estimated available funds             | \$408,417      | \$313,157 | \$95,260 | 30.4 %     |

Cash flows generated by operating activities and borrowings under our credit facility and other types of debt are our most significant sources of liquidity. We also have the ability to raise funds through mortgaging real estate. As of June 30, 2017, our unencumbered owned operating real estate had a book value of \$256 million. Assuming we can obtain financing on 75% of this value, we estimate we could have obtained additional funds of approximately \$192 million at June 30, 2017; however, no assurances can be provided that the appraised value of these properties will match or exceed their book values or that this capital source will be available on terms acceptable to us.

In July 2017, we issued \$300 million in aggregate principal amount of 5.25% senior notes due 2025 in a private placement under Rule 144A and Regulation S of the Securities Act of 1933. We intend to use the net proceeds for general corporate purposes, which may include funding acquisitions, capital expenditures and debt repayment. Pending final application, all or a portion of the approximately \$295 million in net proceeds will be applied to reduce indebtedness, including under our used vehicle floor plan and revolving credit facilities.

In addition to the above sources of liquidity, potential sources include the placement of subordinated debt or loans, the sale of equity securities and the sale of stores or other assets. We evaluate all of these options and may select one or more of them depending on overall capital needs and the availability and cost of capital, although no assurances can be provided that these capital sources will be available in sufficient amounts or with terms acceptable to us.

Information about our cash flows, by category, is presented in our Consolidated Statements of Cash Flows. The following table summarizes our cash flows:

| (Dollars in thousands)                    | Six Months Ended |           | Increase<br>(Decrease)<br>in Cash<br>Flow |
|---|------------------|-----------|---|
|   | June 30,<br>2017 | 2016      |   |
| Net cash provided by operating activities | \$178,555        | \$70,758  | \$107,797                                 |
| Net cash used in investing activities     | (125,219 )       | (66,710 ) | (58,509 )                                 |
| Net cash used in financing activities     | (72,441 )        | (34,012 ) | (38,429 )                                 |

#### Operating Activities

Cash provided by operating activities for the six months ended June 30, 2017 increased \$107.8 million compared to the same period of 2016, primarily related to changes in trade receivables, net, inventory and accrued liabilities.

Borrowings from and repayments to our syndicated lending group related to our new vehicle inventory floor plan financing are presented as financing activities. To better understand the impact of changes in inventory and the associated financing, we also consider our adjusted net cash provided by operating activities to include borrowings or repayments associated with our new vehicle floor plan credit facility.



Adjusted net cash provided by operating activities is presented below (in thousands):

| (Dollars in thousands)   | Six Months Ended<br>June 30, |           | Increase<br>(Decrease)<br>in Cash<br>Flow |
|--|------------------------------|-----------|---|
|  | 2017                         | 2016      |   |
| Net cash provided by operating activities – as reported  | \$178,555                    | \$70,758  | \$107,797                                 |
| Add: Net borrowings on floor plan notes payable, non-trade   | (32,124 )                    | 58,622    | (90,746 )                                 |
| Less: Borrowings on floor plan notes payable, non-trade associated with acquired new vehicle inventory | —                            | (7,120 )  | 7,120                                     |
| Net cash provided by operating activities – adjusted   | \$146,431                    | \$122,260 | \$24,171                                  |

Inventories are the most significant component of our cash flow from operations. As of June 30, 2017, our new vehicle days supply was 75, or seven days higher than our days supply as of December 31, 2016. Our days supply of used vehicles was 60 days as of June 30, 2017, or four days higher than our days supply as of December 31, 2016. We calculate days supply of inventory based on current inventory levels, excluding in-transit vehicles, and a 30-day historical cost of sales level. We have continued to focus on managing our unit mix and maintaining an appropriate level of new and used vehicle inventory.

#### Investing Activities

Net cash used in investing activities totaled \$125.2 million and \$66.7 million, respectively, for the six-month periods ended June 30, 2017 and 2016. Cash flows from investing activities relate primarily to capital expenditures, acquisition and divestiture activity and sales of property and equipment.

Below are highlights of significant activity related to our cash flows from investing activities:

| (Dollars in thousands)                           | Six Months Ended<br>June 30, |            | Increase<br>(Decrease)<br>in Cash<br>Flow |
|--|------------------------------|------------|---|
|  | 2017                         | 2016       |   |
| Capital expenditures                             | \$(32,266)                   | \$(43,247) | \$10,981                                  |
| Cash paid for acquisitions, net of cash acquired | (88,075 )                    | (18,807 )  | (69,268 )                                 |
| Cash paid for other investments                  | (7,748 )                     | (16,690 )  | 8,942                                     |
| Proceeds from sales of stores                    | —                            | 11,837     | (11,837 )                                 |

#### Capital Expenditures

Below is a summary of our capital expenditure activities:

| (Dollars in thousands)                    | Six Months<br>Ended June 30, |          |
|---|------------------------------|----------|
|   | 2017                         | 2016     |
| Post-acquisition capital improvements     | \$7,304                      | \$18,277 |
| Purchases of previously leased facilities | —                            | 5,081    |
| Existing facility improvements            | 7,734                        | 8,035    |
| Maintenance                               | 17,228                       | 11,854   |
| Total capital expenditures                | \$32,266                     | \$43,247 |

Many manufacturers provide assistance in the form of additional incentives or assistance if facilities meet specified standards and requirements. We expect that certain facility upgrades and remodels will generate additional manufacturer incentive payments. Also, tax laws allowing accelerated deductions for capital expenditures reduce the overall investment needed and encourage accelerated project timelines.

We expect to use a portion of our future capital expenditures to upgrade facilities that we recently acquired. This additional capital investment is contemplated in our initial evaluation of the investment return metrics applied to each acquisition and is usually associated with manufacturer standards and requirements.

If we undertake a significant capital commitment in the future, we expect to pay for the commitment out of existing cash balances, construction financing and borrowings on our credit facility. Upon completion of the projects, we believe we would have the ability to secure long-term financing and general borrowings from third party lenders for 70% to 90% of the amounts expended, although no assurances can be provided that these financings will be available to us in sufficient amounts or on terms acceptable to us.

We expect to make expenditures of approximately \$113 million in 2017 for capital improvements at recently acquired stores, purchases of land for expansion of existing stores, facility image improvements, purchases of store facilities, purchases of previously leased facilities and replacement of equipment.

#### Acquisitions

We focus on acquiring stores at attractive purchase prices that meet our return thresholds and strategic objectives. We look for acquisitions that diversify our brand and geographic mix as we continue to evaluate our portfolio to minimize exposure to any one manufacturer and achieve financial returns.

We are able to subsequently floor new vehicle inventory acquired as part of an acquisition; however, the cash generated by this transaction is recorded as borrowings on floor plan notes payable, non-trade.

Adjusted net cash paid for acquisitions, as well as certain other acquisition-related information is presented below:

|  | Six Months Ended<br>June 30, |          |
|--|------------------------------|----------|
|  | 2017                         | 2016     |
| Number of stores acquired  | 8                            | 2        |
| Number of stores opened  | 1                            | —        |
| Number of franchises added   | —                            | 1        |
| (Dollars in thousands)   |                              |          |
| Cash paid for acquisitions, net of cash acquired   | \$88,075                     | \$18,807 |
| Less: Borrowings on floor plan notes payable: non-trade associated with acquired new vehicle inventory | —                            | (7,120 ) |
| Cash paid for acquisitions, net of cash acquired – adjusted  | \$88,075                     | \$11,687 |

We evaluate potential capital investments primarily based on targeted rates of return on assets and return on our net equity investment.

#### Financing Activities

Net cash used in financing activities, adjusted for borrowing on floor plan facilities: non-trade was as follows:

|  | Six Months Ended<br>June 30, |            | Increase<br>(Decrease)<br>in Cash<br>Flow |
|--|------------------------------|------------|---|
| (Dollars in thousands)   | 2017                         | 2016       |   |
| Cash used in financing activities, as reported                         | \$(72,441)                   | \$(34,012) | \$(38,429 )                               |
| Adjust: Repayments (borrowings) on floor plan notes payable: non-trade | 32,124                       | (58,622 )  | 90,746                                    |
| Cash used in financing activities – adjusted                           | \$(40,317)                   | \$(92,634) | \$52,317                                  |

Below are highlights of significant activity related to our cash flows from financing activities, excluding net borrowings on floor plan notes payable: non-trade, which are discussed above:

|  | Six Months Ended<br>June 30, |          | Increase<br>(Decrease)<br>in Cash<br>Flow |
|--|------------------------------|----------|---|
| (Dollars in thousands)   | 2017                         | 2016     |   |
| Net (repayments) borrowings on lines of credit                       | \$(35,346)                   | \$18,668 | \$(54,014 )                               |
| Principal payments on long-term debt and capital leases, unscheduled | (35,765 )                    | (2,303 ) | (33,462 )                                 |
| Proceeds from issuance of long-term debt                             | 74,065                       | 12,080   | 61,985                                    |

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|                             |           |           |          |
|-----------------------------|-----------|-----------|----------|
| Repurchases of common stock | (24,913 ) | (104,858) | 79,945   |
| Dividends paid              | (13,052 ) | (11,524 ) | (1,528 ) |

**Borrowing and Repayment Activity**

During the first six months of 2017, we raised net mortgage proceeds of \$38.3 million, which was mainly used to pay down our outstanding balances on our long-term debt and our lines of credit and fund repurchases of common stock. Our debt to total capital ratio, excluding floor plan notes payable, was 44.7% at June 30, 2017 compared to 44.4% at June 30, 2016.

### Equity Transactions

On February 25, 2016, our Board of Directors authorized the repurchase of up to \$250 million of our Class A common stock. We repurchased a total of 279,143 shares of our Class A common stock at an average price of \$89.25 per share in the first six months of 2017. This included 247,000 shares as part of the repurchase plan at an average price per share of \$87.94 and 32,143 shares related to tax withholding on vesting RSUs at an average price of \$99.32. As of June 30, 2017, we had \$171.4 million remaining available for repurchases and the authorization does not have an expiration date.

In the first six months of 2017, we declared and paid dividends on our Class A and Class B common stock as follows:

|                | Dividend amount of              | Total dividend        |
|----------------|---------------------------------|-----------------------|
| Dividend paid: | amount per share (in thousands) | amount (in thousands) |
| March 2017     | \$ 0.25                         | \$ 6,292              |
| May 2017       | \$ 0.27                         | \$ 6,760              |

We evaluate performance and make a recommendation to the Board of Directors on dividend payments on a quarterly basis.

### Summary of Outstanding Balances on Credit Facilities and Long-Term Debt

Below is a summary of our outstanding balances on credit facilities and long-term debt:

|   | As of June 30, 2017 |                     |                 |
|---|---------------------|---------------------|-----------------|
| (Dollars in thousands)                    | Outstanding         | Remaining Available |                 |
| Floor plan note payable: non-trade        | \$1,534,715         | \$ —                | <sup>1</sup>    |
| Floor plan notes payable                  | 99,932              | —                   |                 |
| Used vehicle inventory financing facility | 213,093             | 10,032              | <sup>2</sup>    |
| Revolving lines of credit                 | 105,068             | 175,141             | <sup>2, 3</sup> |
| Real estate mortgages                     | 470,073             | —                   |                 |
| Other debt                                | 10,481              | —                   |                 |
| Total debt                                | \$2,433,362         | \$ 185,173          |                 |

<sup>1</sup> As of June 30, 2017, we had a \$1.55 billion new vehicle floor plan commitment as part of our credit facility.

<sup>2</sup> The amount available on the credit facility is limited based on a borrowing base calculation and fluctuates monthly.

<sup>3</sup> Available credit is based on the borrowing base amount effective as of May 31, 2017. This amount is reduced by \$8.3 million for outstanding letters of credit.

### Credit Facility

On August 1, 2017, we amended our existing credit facility to increase the total financing commitment by \$350 million to \$2.4 billion and extend the maturity to August 2022. This syndicated credit facility is comprised of 18 financial institutions, including seven manufacturer-affiliated finance companies. Under our credit facility we are permitted to allocate the total financing commitment among floor plan financing for new vehicle inventory, floor plan financing for used vehicles (up to a maximum of 16.5% of the total aggregate commitment) and revolving financing for general corporate purposes, including acquisitions and working capital (up to a maximum of 18.75% of the total commitment). Our credit facility may be expanded to \$2.75 billion total availability, subject to lender approval. All borrowings from, and repayments to, our lending group are presented in the Consolidated Statements of Cash Flows as financing activities.



Our obligations under our revolving syndicated credit facility are secured by a substantial amount of our assets, including our inventory (including new and used vehicles, parts and accessories), equipment, accounts (and other rights to payment) and our equity interests in certain of our subsidiaries. Under our revolving syndicated credit facility, our obligations relating to new vehicle floorplan loans are secured only by collateral owned by borrowers of new vehicle floorplan loans under the credit facility.

We have the ability to deposit up to \$50 million in cash in Principal Reduction (PR) accounts associated with our new vehicle inventory floor plan commitment. The PR accounts are recognized as offsetting credits against outstanding amounts on our new vehicle floor plan commitment and would reduce interest expense associated with the outstanding principal balance. As of June 30, 2017, we had no balances in our PR accounts.

If the outstanding principal balance on our new vehicle inventory floor plan commitment, plus requests on any day, exceeds 95% of the loan commitment, a portion of the revolving line of credit must be reserved. The reserve amount is equal to the lesser of \$15.0 million or the maximum revolving line of credit commitment less the outstanding balance on the line less outstanding letters

of credit. The reserve amount will decrease the revolving line of credit availability and may be used to repay the new vehicle floor plan commitment balance.

The interest rate on the credit facility varies based on the type of debt, with the rate of one-month LIBOR plus 1.25% for new vehicle floor plan financing, one-month LIBOR plus 1.50% for used vehicle floor plan financing; and a variable interest rate on the revolving financing ranging from the one-month LIBOR plus 1.25% to 2.50%, depending on our leverage ratio. The annual interest rate associated with our new vehicle floor plan commitment was 2.47% at June 30, 2017. The annual interest rate associated with our used vehicle inventory financing facility and our revolving line of credit was 2.72% and 2.97%, respectively, at June 30, 2017.

Under the terms of our credit facility we are subject to financial covenants and restrictive covenants that limit or restrict our incurring additional indebtedness, making investments, selling or acquiring assets and granting security interests in our assets.

Under our credit facility, we are required to maintain the ratios detailed in the following table:

| Debt Covenant Ratio         | Requirement                 | As of<br>June 30,<br>2017 |
|-----------------------------|-----------------------------|---------------------------|
| Current ratio               | Not less than 1.10 to 1     | 1.28 to 1                 |
| Fixed charge coverage ratio | Not less than 1.20 to 1     | 2.96 to 1                 |
| Leverage ratio              | Not more than 5.00 to 1     | 2.02 to 1                 |
| Funded debt restriction     | Not to exceed \$900 million | \$518.8<br>million        |

As of June 30, 2017, we were in compliance with all covenants. We expect to remain in compliance with the financial and restrictive covenants in our credit facility and other debt agreements. However, no assurances can be provided that we will continue to remain in compliance with the financial and restrictive covenants.

If we do not meet the financial and restrictive covenants and are unable to remediate or cure the condition or obtain a waiver from our lenders, a breach would give rise to remedies under the agreement, the most severe of which are the termination of the agreement, acceleration of the amounts owed and the seizure and sale of our assets comprising the collateral for the loans. A breach would also trigger cross-defaults under other debt agreements.

#### Floor Plan Notes Payable

We have floor plan agreements with manufacturer-affiliated finance companies for new vehicles at certain stores and vehicles designated for use as service loaners. The variable interest rates on these floor plan notes payable commitments vary by manufacturer. At June 30, 2017, \$99.9 million was outstanding on these arrangements. Borrowings from, and repayments to, manufacturer-affiliated finance companies are classified as operating activities in the Consolidated Statements of Cash Flows.

#### 5.25% Senior Notes Due 2025

On July 24, 2017, we issued \$300 million in aggregate principal amount of 5.25% Senior Notes due 2025 ("the Notes") to eligible purchasers in a private placement under Rule 144A and Regulation S of the Securities Act of 1933. Interest accrues on the Notes from July 24, 2017 and is payable semiannually on February 1 and August 1. The first interest payment is on February 1, 2018. We may redeem the Notes, in whole or in part, at any time prior to August 1, 2020 at a price equal to 100% of the principal amount plus a make-whole premium set forth in the Indenture and accrued and unpaid interest. After August 1, 2020, we may redeem some or all of the Notes subject to the redemption prices set forth in the Indenture. If we experience specific kinds of changes of control, as described in the Indenture, we must offer to repurchase the Notes at 101% of their principal amount plus accrued and unpaid interest to the date

of purchase.

We paid approximately \$5 million of underwriting and other fees in connection with this issuance, which is being amortized as interest expense over the term of the Notes. The Notes will be fully and unconditionally guaranteed, jointly and severally, on a senior unsecured basis by each of the Company's existing and future restricted subsidiaries that is a borrower under or that guarantees obligations under the Company's credit facility or other indebtedness of the Company or any subsidiary guarantor. The terms of the Notes, in certain circumstances, may restrict our ability to, among other things, incur additional indebtedness, pay dividends, repurchase our common stock, or merge, consolidate or sell all or substantially all our assets.

We intend to use the net proceeds for general corporate purposes, which may include funding acquisitions, capital expenditures and debt repayment. Pending final application, all or a portion of the approximately \$295 million in net proceeds will be applied to reduce indebtedness, including under Lithia's used vehicle floor plan and revolving credit facilities.

#### Real Estate Mortgages and Other Debt

We have mortgages associated with our owned real estate. Interest rates related to this debt ranged from 2.5% to 5.0% at June 30, 2017. The mortgages are payable in various installments through October 2034. As of June 30, 2017, we had fixed interest rates on 76% of our outstanding mortgage debt.

Our other debt includes capital leases and sellers' notes. The interest rates associated with our other debt ranged from 3.1% to 8.0% at June 30, 2017. This debt, which totaled \$10.5 million at June 30, 2017, is due in various installments through December 2050.

#### Recent Accounting Pronouncements

See Note 12 of the Condensed Notes to Consolidated Financial Statements in this Quarterly Report on Form 10-Q.

#### Critical Accounting Policies and Use of Estimates

There have been no material changes in the critical accounting policies and use of estimates described in our 2016 Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 28, 2017.

#### Seasonality and Quarterly Fluctuations

Historically, our sales have been lower in the first quarter of each year due to consumer purchasing patterns and inclement weather in certain of our markets. As a result, financial performance is expected to be lower during the first quarter than during the second, third and fourth quarters of each fiscal year. We believe that interest rates, levels of consumer debt, consumer confidence and manufacturer sales incentives, as well as general economic conditions, also contribute to fluctuations in sales and operating results.

#### Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our reported market risks or risk management policies since the filing of our 2016 Annual Report on Form 10-K, which was filed with the Securities and Exchange Commission on February 28, 2017.

### Item 4. Controls and Procedures

#### Evaluation of Disclosure Controls and Procedures

We evaluated, with the participation and under the supervision of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure and that such information is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

#### Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during our last fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

See Note 10 of the Condensed Notes to the Consolidated Financial Statements for additional information.

Item 1A. Risk Factors

The risk factors below are modified from those that are included in our 2016 Annual Report on Form 10-K which was filed with the Securities and Exchange Commission on February 28, 2017 to account for our recent note placement and the expansion of

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our credit facility. The information in this Form 10-Q should be read in conjunction with the risk factors and information disclosed in that report.

Our indebtedness and lease obligations could materially adversely affect our financial health, limit our ability to finance future acquisitions and capital expenditures and prevent us from fulfilling our financial obligations. Much of our debt is secured by a substantial portion of our assets. Much of our debt has a variable interest rate component that may significantly increase our interest costs in a rising rate environment.

Our indebtedness and lease obligations could have important consequences to us, including the following:

- limitations on our ability to complete acquisitions;
- impaired ability to obtain additional financing for acquisitions, capital expenditures, working capital or general corporate purposes;
- reduced funds available for our operations and other purposes, as a larger portion of our cash flow from operations would be dedicated to the payment of principal and interest on our indebtedness; and
- exposure to the risk of increasing interest rates as certain borrowings are, and will continue to be, at variable rates of interest.

In addition, our loan agreements and the indenture governing our 5.25% notes due in 2025 contain covenants that limit our discretion with respect to business matters, including incurring additional debt, granting additional security interests in our assets, acquisition activity, disposing of assets and other business matters. Other covenants are financial in nature, including current ratio, fixed charge coverage and leverage ratio calculations. A breach of any of these covenants could result in a default under the applicable agreement. In addition, a default under one agreement could result in a default and acceleration of our repayment obligations under the other agreements under the cross-default provisions in such other agreements. For example, a default under our \$2.4 billion syndicated credit facility could trigger a default and acceleration of our repayment obligations under the indenture governing our \$300 million aggregate principal amount 5.25% Notes due in 2025, and vice versa.

We have granted in favor of certain of our lenders and other secured parties, including those under our \$2.4 billion revolving syndicated credit facility, a security interest in a substantial portion of our assets. If we default on our obligations under those agreements, the secured parties may be able to foreclose upon their security interests and otherwise be entitled to obtain or control those assets.

Certain debt agreements contain subjective acceleration clauses based on a lender deeming itself insecure or if a “material adverse change” in our business has occurred. If these clauses are implicated, and the lender declares that an event of default has occurred, the outstanding indebtedness could become immediately due and owing.

If these events were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Even if new financing were available, it may not be on terms acceptable to us. As a result of this risk, we could be forced to take actions that we otherwise would not take, or not take actions that we otherwise might take, in order to comply with these agreements.

In addition, the lenders’ obligations to make loans or other credit accommodations under certain credit agreements is subject to the satisfaction of certain conditions precedent including, for example, that our representations and warranties in the agreement are true and correct in all material respects as of the date of the proposed credit extension. If any of our representations and warranties in those agreements are not true and correct in all material respects as of the date of a proposed credit extension, or if other conditions precedent are not satisfied, we may not be able to request new loans or other credit accommodations under those credit facilities, which could have a material adverse impact on our business, results of operations, financial condition and cash flows.

Additionally, our real estate debt generally has a five to ten-year term, after which the debt needs to be renewed or replaced. A decline in the appraised value of real estate or a reduction in the loan-to-value lending ratios for new or renewed real estate loans could result in our inability to renew maturing real estate loans at the debt level existing at maturity, or on terms acceptable to us, requiring us to find replacement lenders or to refinance at lower loan amounts.

As of June 30, 2017, approximately 80% of our total debt was variable rate. The majority of our variable rate debt is indexed to the one-month LIBOR rate. The current interest rate environment is at historically low levels, and interest rates will likely increase in the future. In the event interest rates increase, our borrowing costs may increase substantially. Additionally, fixed rate debt that matures may be renewed at interest rates significantly higher than current levels. As a result, this could have a material adverse impact on our business, results of operations, financial condition and cash flows.

We may not be able to satisfy our debt obligations upon the occurrence of a change in control or another event of default under our credit agreement or indenture.

Upon the occurrence of a change in control or another event of default as defined in our credit agreement, the agent under the credit agreement will have the right to declare all outstanding obligations immediately due and payable and to terminate the availability of future advances to us. There can be no assurance that we would have sufficient resources available to satisfy all of our obligations under the credit agreement in the event of a change in control or fundamental change. A "change in control" as defined in our credit agreement includes, among other events, the acquisition by any person, or two or more persons acting in concert, in either case other than Lithia Holdings Company, L.L.C., Sid DeBoer or Bryan DeBoer, of beneficial ownership (within the meaning of Rule 13d-3 of the SEC under the Securities Exchange Act of 1934) of 20% or more of the outstanding shares of our voting stock on a fully diluted basis.

Upon a change of control as defined in the indenture governing our 5.25% Senior Notes due in 2025, the holders of the notes may require the Company to repurchase all or a portion of the notes at a purchase price of 101% of their principal amount plus accrued and unpaid interest, if any, to the date of purchase. Generally, if an event of default occurs under the indenture, the trustee or the holders of at least 25% in principal amount of the then outstanding notes may declare all of the notes to be due and payable.

In the event we were unable to satisfy the above obligations, it could have a material adverse impact on our business and our common stock holders.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

We repurchased the following shares of our Class A common stock during the second quarter of 2017:

|       | Total<br>number of<br>shares<br>purchased <sup>2</sup> | Average<br>price<br>paid per<br>share | Total<br>number of<br>shares<br>purchased<br>as part of<br>publicly<br>announced<br>plans <sup>1</sup> | Maximum<br>dollar value<br>of shares<br>that may yet<br>be purchased<br>under<br>publicly<br>announced<br>plan (in<br>thousands) <sup>1</sup> |
|-------|--|---------------------------------------|--|---|
| April | 141,000  | \$ 82.78                              | 141,000  | \$ 175,403  |
| May   | 22,157   | 91.15                                 | 22,000   | 173,398   |
| June  | 22,000   | 92.41                                 | 22,000   | 171,365   |
|       | 185,157  | \$ 84.93                              | 185,000  | \$ 171,365  |

<sup>1</sup> Effective February 29, 2016, our Board of Directors authorized the repurchase of up to \$250 million of our Class A common stock. This authorization does not have an expiration date and it replaced the previous authorizations, which limited the number of shares we were authorized to repurchase.

<sup>2</sup> Of the shares repurchased in the second quarter of 2017, 157 shares were related to the tax withholdings on vesting RSUs.



Item 6. Exhibits

The following exhibits are filed herewith and this list is intended to constitute the exhibit index.

- 3.1 Restated Articles of Incorporation of Lithia Motors, Inc., as amended May 13, 1999 (incorporated by reference to exhibit 3.1 to our Form 10-K for the year ended December 31, 1999).
- 3.2 2013 Amended and Restated Bylaws of Lithia Motors, Inc. (incorporated by reference to exhibit 3.1 to Form 8-K dated August 20, 2013 and filed with the Securities and Exchange Commission on August 26, 2013).
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 32.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.
- 32.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.
- 101.INS XBRL Instance Document.
- 101.SCH XBRL Taxonomy Extension Schema Document.
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: August 2, 2017 LITHIA MOTORS, INC.

By: /s/ John F. North III  
John F. North III  
Senior Vice President and Chief Financial Officer  
(Duly Authorized Officer and Principal Financial and  
Accounting Officer)