PENSKE AUTOMOTIVE GROUP, INC.
Form 10-Q
May 01, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2015

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-12297

Penske Automotive Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**22-3086739** (I.R.S. Employer Identification No.)
2555 Telegraph Road, **Bloomfield Hills, Michigan** (Address of principal executive offices)	**48302-0954** (Zip Code)

Registrant s telephone number, including area code:
(248) 648-2500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o

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

As of April 24, 2015, there were 90,243,407 shares of voting common stock outstanding.

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED BALANCE SHEETS

	March 31, 2015	December 31, 2014
	(Unaudited) (In millions, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	$ 66.8	$ 36.3
Accounts receivable, net of allowance for doubtful accounts of $4.2 and $3.5	746.4	701.4
Inventories	2,885.7	2,819.2
Other current assets	106.7	124.7
Assets held for sale	62.2	186.1
Total current assets	3,867.8	3,867.7
Property and equipment, net	1,326.6	1,328.8
Goodwill	1,271.1	1,266.3
Other indefinite-lived intangible assets	386.6	386.2
Equity method investments	350.9	352.8
Other long-term assets	24.6	26.4
Total assets	$ 7,227.6	$ 7,228.2
LIABILITIES AND EQUITY		
Floor plan notes payable	$ 1,915.8	$ 1,812.6
Floor plan notes payable non-trade	1,021.5	920.5
Accounts payable	454.1	417.6
Accrued expenses	342.9	310.3
Current portion of long-term debt	34.5	36.6
Liabilities held for sale	43.3	132.7
Total current liabilities	3,812.1	3,630.3
Long-term debt	1,174.1	1,316.0
Deferred tax liabilities	385.0	409.9
Other long-term liabilities	185.0	190.8
Total liabilities	5,556.2	5,547.0
Commitments and contingent liabilities (Note 9)		
Equity		
Penske Automotive Group stockholders equity:		
Preferred Stock, $0.0001 par value; 100,000 shares authorized; none issued and outstanding		
Common Stock, $0.0001 par value, 240,000,000 shares authorized; 90,242,407 shares issued and outstanding at March 31, 2015; 90,244,840 shares issued and outstanding at December 31, 2014		
Non-voting Common Stock, $0.0001 par value, 7,125,000 shares authorized; none issued and outstanding		
Class C Common Stock, $0.0001 par value, 20,000,000 shares authorized; none issued and outstanding		
Additional paid-in-capital	680.3	690.7
Retained earnings	1,070.7	1,015.4
Accumulated other comprehensive income (loss)	(107.8)	(53.3)
Total Penske Automotive Group stockholders equity	1,643.2	1,652.8
Non-controlling interest	28.2	28.4
Total equity	1,671.4	1,681.2
Total liabilities and equity	$ 7,227.6	$ 7,228.2

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF INCOME

	Three Months Ended March 31,			
	2015		2014	
	(Unaudited) (In millions, except per share amounts)			
Revenue:				
Retail automotive dealership	$	4,175.0	$	3,919.2
Retail commercial truck dealership		192.7		
Commercial vehicle distribution and other		103.4		96.0
Total revenues	$	4,471.1	$	4,015.2
Cost of sales:				
Retail automotive dealership		3,546.9		3,321.5
Retail commercial truck dealership		159.9		
Commercial vehicle distribution and other		75.6		79.7
Total cost of sales		3,782.4		3,401.2
Gross profit		688.7		614.0
Selling, general and administrative expenses		534.5		477.2
Depreciation		18.6		16.1
Operating income		135.6		120.7
Floor plan interest expense		(10.1)		(11.1)
Other interest expense		(16.3)		(12.4)
Equity in earnings of affiliates		6.7		5.1
Income from continuing operations before income taxes		115.9		102.3
Income taxes		(38.8)		(34.7)
Income from continuing operations		77.1		67.6
Income (loss) from discontinued operations, net of tax		(1.2)		0.3
Net income		75.9		67.9
Less: Income attributable to non-controlling interests		0.7		0.4
Net income attributable to Penske Automotive Group common stockholders	$	75.2	$	67.5
Basic earnings per share attributable to Penske Automotive Group common stockholders:				
Continuing operations	$	0.85	$	0.74
Discontinued operations	$	(0.01)	$	0.00
Net income attributable to Penske Automotive Group common stockholders	$	0.83	$	0.75
Shares used in determining basic earnings per share (Note 6)		90.3		90.4
Diluted earnings per share attributable to Penske Automotive Group common stockholders:				
Continuing operations	$	0.85	$	0.74
Discontinued operations	$	(0.01)	$	0.00
Net income attributable to Penske Automotive Group common stockholders	$	0.83	$	0.75
Shares used in determining diluted earnings per share (Note 6)		90.3		90.5
Amounts attributable to Penske Automotive Group common stockholders:				
Income from continuing operations	$	77.1	$	67.6
Less: Income attributable to non-controlling interests		0.7		0.4
Income from continuing operations, net of tax		76.4		67.2
Income (loss) from discontinued operations, net of tax		(1.2)		0.3
Net income attributable to Penske Automotive Group common stockholders	$	75.2	$	67.5

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014
	(Unaudited) (In millions)	
Net income	$ 75.9	$ 67.9
Other comprehensive income:		
Foreign currency translation adjustment	(52.8)	9.3
Unrealized gain (loss) on interest rate swaps:		
Unrealized gain (loss) arising during the period, net of tax benefits		(0.2)
Reclassification adjustment for loss included in floor plan interest expense, net of tax provision of $0.7		1.1
Unrealized gain (loss) on interest rate swaps, net of tax		0.9
Other adjustments to comprehensive income, net	(2.3)	(4.0)
Other comprehensive income (loss), net of taxes	(55.1)	6.2
Comprehensive income	20.8	74.1
Less: Comprehensive income attributable to non-controlling interests	0.1	0.2
Comprehensive income attributable to Penske Automotive Group common stockholders	$ 20.7	$ 73.9

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31, 2015	2014
	(Unaudited) (In millions)	
Operating Activities:		
Net income	$ 75.9	$ 67.9
Adjustments to reconcile net income to net cash from continuing operating activities:		
Depreciation	18.6	16.1
Earnings of equity method investments	(6.7)	(5.1)
(Income) loss from discontinued operations, net of tax	1.2	(0.3)
Deferred income taxes	(22.6)	(0.1)
Changes in operating assets and liabilities:		
Accounts receivable	(45.1)	(75.8)
Inventories	(19.7)	(0.8)
Floor plan notes payable	103.2	36.9
Accounts payable and accrued expenses	67.9	84.6
Other	20.9	9.1
Net cash provided by continuing operating activities	193.6	132.5
Investing Activities:		
Purchase of equipment and improvements	(33.6)	(39.8)
Acquisitions net, including repayment of sellers floor plan notes payable of $41.2 and $22.4, respectively	(86.4)	(81.8)
Net cash used in continuing investing activities	(120.0)	(121.6)
Financing Activities:		
Proceeds from borrowings under U.S. credit agreement revolving credit line	398.9	323.0
Repayments under U.S. credit agreement revolving credit line	(398.9)	(313.0)
Repayment of U.S. commercial truck capital loan	(60.5)	
Net repayments of other long-term debt	(78.8)	(36.3)
Net borrowings of floor plan notes payable non-trade	101.0	6.8
Payment of deferred financing fees	(1.2)	
Repurchases of common stock	(14.0)	
Dividends	(19.9)	(16.2)
Net cash used in continuing financing activities	(73.4)	(35.7)
Discontinued operations:		
Net cash provided by (used in) discontinued operating activities	13.6	(17.8)
Net cash provided by discontinued investing activities	105.4	33.6
Net cash (used in) provided by discontinued financing activities	(85.6)	13.8
Net cash provided by discontinued operations	33.4	29.6
Effect of exchange rate changes on cash and cash equivalents	(3.1)	
Net change in cash and cash equivalents	30.5	4.8
Cash and cash equivalents, beginning of period	36.3	50.3
Cash and cash equivalents, end of period	$ 66.8	$ 55.1
Supplemental disclosures of cash flow information:		
Cash paid for:		
Interest	$ 13.6	$ 17.6
Income taxes	13.3	9.2

See Notes to Consolidated Condensed Financial Statements

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PENSKE AUTOMOTIVE GROUP, INC.

CONSOLIDATED CONDENSED STATEMENT OF EQUITY

(Unaudited)
(Dollars in millions)

	Common Stock Issued Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Penske Automotive Group Stockholders Equity	Non-controlling Interest	Total Equity
Balance, January 1, 2015	90,244,840	$	$ 690.7	$ 1,015.4	$ (53.3)	$ 1,652.8	$ 28.4	$ 1,681.2
Equity compensation	280,567		3.6			3.6		3.6
Repurchase of common stock	(283,000)		(14.0)			(14.0)		(14.0)
Dividends				(19.9)		(19.9)		(19.9)
Distributions to non-controlling interests							(0.3)	(0.3)
Foreign currency translation					(52.2)	(52.2)	(0.6)	(52.8)
Other					(2.3)	(2.3)		(2.3)
Net income				75.2		75.2	0.7	75.9
Balance, March 31, 2015	90,242,407	$	$ 680.3	$ 1,070.7	$ (107.8)	$ 1,643.2	$ 28.2	$ 1,671.4

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PENSKE AUTOMOTIVE GROUP, INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Unaudited)

(In millions, except per share amounts)

1. Interim Financial Statements

Business Overview

Unless the context otherwise requires, the use of the terms PAG, we, us, and our in these Notes to the Consolidated Condensed Financial Statements refers to Penske Automotive Group, Inc. and its consolidated subsidiaries.

We are an international transportation services company that operates automotive and commercial truck dealerships principally in the United States and Western Europe, and distributes commercial vehicles, diesel engines, gas engines, power systems and related parts and services principally in Australia and New Zealand.

Retail Automotive Dealership. We believe we are the second largest automotive retailer headquartered in the U.S. as measured by the $16.6 billion in total retail automotive dealership revenue we generated in 2014. As of March 31, 2015, we operated 328 automotive retail franchises, of which 180 franchises are located in the U.S. and 148 franchises are located outside of the U.S. The franchises outside the U.S. are located primarily in the U.K. In the three months ended March 31, 2015, we retailed and wholesaled more than 122,000 vehicles. We are diversified geographically, with 60% of our total retail automotive dealership revenues in the three months ended March 31, 2015 generated in the U.S. and Puerto Rico and 40% generated outside the U.S. We offer over 40 vehicle brands, with 72% of our retail automotive dealership revenue in the three months ended March 31, 2015 generated from premium brands, such as Audi, BMW, Mercedes-Benz and Porsche. Each of our dealerships offer a wide selection of new and used vehicles for sale. In addition to selling new and used vehicles, we generate higher-margin revenue at each of our dealerships through maintenance and repair services and the sale and placement of third-party finance and insurance products, third-party extended service and maintenance contracts and replacement and aftermarket automotive products. We operate these dealerships under franchise agreements with a number of automotive manufacturers and distributors which are subject to certain rights and restrictions typical of the industry.

During the three months ended March 31, 2015, we acquired one U.S. retail automotive franchise, Land Rover Darien, in Connecticut which complements our existing franchises in Danbury, Fairfield and Greenwich, Connecticut.

Retail Commercial Truck Dealership. In November 2014, we acquired a controlling interest (91%) in a heavy and medium duty truck dealership group located in Texas, Oklahoma and New Mexico, which we have renamed Penske Commercial Vehicles US (PCV US). Prior to this transaction, we held a 32% interest in PCV US and accounted for this investment under the equity method. PCV US operates sixteen locations, including ten full-service dealerships offering principally Freightliner, Western Star, and Sprinter-branded trucks. Two of these locations, Freightliner of Chattanooga and Freightliner of Knoxville, were acquired in February 2015. PCV US also offers a full range of used trucks available for sale as well as service and parts departments, many of which are open 24 hours a day, seven days a week.

Commercial Vehicle Distribution. Since August 2013, we have been the exclusive importer and distributor of Western Star heavy duty trucks (a Daimler brand), MAN heavy and medium duty trucks and buses (a VW Group brand), and Dennis Eagle refuse collection vehicles, together with associated parts across Australia, New Zealand and portions of the Pacific. The business, known as Penske Commercial Vehicles Australia, distributes commercial vehicles and parts to a network of more than 70 dealership locations, including three company-owned retail commercial vehicle dealerships.

In October 2014, we acquired MTU Detroit Diesel Australia Pty Ltd., a leading distributor of diesel and gas engines and power systems, representing MTU, Detroit Diesel, Mercedes-Benz Industrial, Allison Transmission and MTU Onsite Energy. We have renamed this business Penske Power Systems. Penske Power Systems offers products across the on- and off-highway markets in Australia, New Zealand and the Pacific and supports full parts and aftersales service through a network of branches, field locations and independent dealers across the region. The on-highway portion of this business complements our existing Penske Commercial Vehicles Australia distribution business.

Penske Truck Leasing. We hold a 9.0% limited partnership interest in Penske Truck Leasing Co., L.P. (PTL), a leading provider of transportation and supply chain services.

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Basis of Presentation

The following unaudited consolidated condensed financial statements of PAG have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and disclosures normally included in our annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the SEC rules and regulations. The information presented as of March 31, 2015 and for the three month periods ended March 31, 2015 and 2014 is unaudited, but includes all adjustments which our management believes to be necessary for the fair presentation of results for the periods presented. We have changed the presentation of revenue and cost of sales within the Consolidated Condensed Statements of Income to reflect the addition of the retail commercial truck dealership business for the current and comparative periods presented. We have also identified the retail commercial truck dealership business as a new reportable segment and have retroactively presented the segment data for all periods presented within the segment information footnote. Additionally, the consolidated condensed financial statements for the prior periods have been revised for entities that have been treated as discontinued operations, and results for interim periods are not necessarily indicative of results to be expected for the year. These consolidated condensed financial statements should be read in conjunction with our audited financial statements for the year ended December 31, 2014, which are included as part of our Annual Report on Form 10-K.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. ASU No. 2014-08 changes the requirements for reporting discontinued operations to only allow presentation of a disposal of an entity or component of an entity as a discontinued operation if it represents a strategic shift that has (or will have) a major effect on an entity s operations or financial results. We adopted this accounting standard update effective January 1, 2015. See Assets Held for Sale and Discontinued Operations below for additional discussion.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). This ASU supersedes the revenue recognition requirements in ASC 605, Revenue Recognition. ASU No. 2014-09 will require an entity to recognize revenue when it transfers promised goods or services to customers using a five-step model that requires entities to exercise judgment when considering the terms of the contracts. This ASU can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption. In April 2015, the FASB proposed a one-year deferral of the effective date from January 1, 2017 to January 1, 2018 but would allow for early adoption as of January 1, 2017. We are currently assessing the impact the adoption of this update will have on our consolidated financial position, results of operations, and cash flows.

In April 2015, the FASB issued ASU No. 2015-03, Interest Imputation of Interest (Subtopic 835-30) - Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This ASU is effective for us beginning after January 1, 2016. We are currently assessing the impact the adoption of this update will have on our consolidated financial position, results of operations, and cash flows.

Assets Held for Sale and Discontinued Operations

We classify an entity as held for sale in the period in which all of the following criteria are met:

- management, having the authority to approve the action, commits to a plan to sell the entity;
- the entity is available for immediate sale in its present condition;
- an active program to locate a buyer and other actions required to complete the plan to sell have been initiated;
- the sale is probable and transfer is expected to be completed within one year;
- the entity is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and
- actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

As discussed previously, in April 2014, the FASB issued ASU No. 2014-08 that changes the definition of a discontinued operation to include only those disposals of components of an entity or components of an entity that are classified as held for sale that represent a strategic shift that has (or will have) a major effect on an entity s operations and financial results. We adopted this accounting standard update effective January 1, 2015.

Prior to the adoption of ASU No. 2014-08, we accounted for dispositions as discontinued operations when it was evident that the operations and cash flows of an entity being disposed of would be eliminated from ongoing operations and we would not have any significant continuing involvement in its operations. The results of operations for those entities that were classified as discontinued operations prior to adoption of ASU No. 2014-08 are included in Income (loss) from discontinued operations in the accompanying Consolidated Condensed Statements of Income for all periods presented and will continue to be reported within discontinued operations in the future. Beginning with disposals or entities classified as held for sale subsequent to January 1, 2015, only those that represent a strategic shift that has, or will have, a major impact on our operations and financial results will be included in discontinued operations.

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We had no entities newly classified as held for sale during the three months ended March 31, 2015. As such, the combined financial information presented below represents only retail automotive dealerships and our car rental business that were classified as discontinued operations prior to adoption of ASU No. 2014-08:

	Three Months Ended March 31, 2015		2014	
Revenues	$	40.3	$	79.4
Pre-tax income (loss)	$	(4.1)	$	(10.0)
Pre-tax gain on disposal	$	2.3	$	14.8

	March 31, 2015		December 31, 2014	
Inventories	$	33.6	$	34.7
Other assets		28.6		151.4
Total assets	$	62.2	$	186.1
Floor plan notes payable (including non-trade)	$	29.0	$	27.9
Other liabilities		14.3		104.8
Total liabilities	$	43.3	$	132.7

Divestitures

In February 2015, we divested our car rental business which included Hertz car rental franchises in the Memphis, Tennessee market and certain markets throughout Indiana. We received proceeds of $17.8 million from the sale excluding sales of car rental vehicles. The results of operations of our car rental business are included in discontinued operations for the three months ended March 31, 2015 and 2014.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The accounts requiring the use of significant estimates include accounts receivable, inventories, income taxes, intangible assets and certain reserves.

Fair Value of Financial Instruments

Accounting standards define fair value as the price that would be received from selling an asset or paid to transfer a liability in the principal