AMERICAS CARMART INC
Form 10-Q
December 08, 2017

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 October 31, 2017

Or

[ ] 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: 0-14939

AMERICA'S CAR-MART, INC.

(Exact name of registrant as specified in its charter)

Texas	63-0851141
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

802 Southeast Plaza Ave., Suite 200, Bentonville, Arkansas 72712

(Address of principal executive offices) (zip code)

(479) 464-9944

(Registrant's telephone number, including area code)

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 No

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company Emerging growth company

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.

Title of Each Class	Outstanding at December 5, 2017
Common stock, par value $.01 per share	7,150,061

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements America's Car-Mart, Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

(Dollars in thousands except share and per share amounts)

	October 31, 2017	April 30, 2017
Assets:		
Cash and cash equivalents	$ 358	$ 434
Accrued interest on finance receivables	2,334	2,098
Finance receivables, net	376,577	357,161
Inventory	31,315	30,129
Prepaid expenses and other assets	4,285	3,942
Goodwill	355	355
Property and equipment, net	28,783	30,139
Total Assets	$ 444,007	$ 424,258
Liabilities, mezzanine equity and equity:		
Liabilities:		
Accounts payable	$ 12,637	$ 11,224
Deferred payment protection plan revenue	18,956	18,472
Deferred service contract revenue	9,868	9,611
Accrued liabilities	17,102	13,796
Income taxes payable, net	296	885
Deferred income tax liabilities, net	19,888	18,918
Revolving credit facilities and notes payable	137,950	117,944
Total liabilities	216,697	190,850
Commitments and contingencies (Note J)		
Mezzanine equity:		
Mandatorily redeemable preferred stock	400	400
Equity:		
Preferred stock, par value $.01 per share, 1,000,000 shares authorized; none issued or outstanding	-	-
	130	129

Common stock, par value $.01 per share, 50,000,000 shares authorized; 13,005,928 and 12,927,413 issued at October 31, 2017 and April 30, 2017, respectively, of which 7,177,213 and 7,608,471 were outstanding at October 31, 2017 and April 30, 2017, respectively		
Additional paid-in capital	70,332	69,284
Retained earnings	338,460	325,519
Less: Treasury stock, at cost, 5,828,715 and 5,318,942 shares at October 31, 2017 and April 30, 2017, respectively	(182,112)	(162,024)
Total stockholders' equity	226,810	232,908
Non-controlling interest	100	100
Total equity	226,910	233,008
Total Liabilities, Mezzanine Equity and Equity	$ 444,007	$ 424,258

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Condensed Consolidated Statements of Operations America's Car-Mart, Inc.
(Unaudited)

(Dollars in thousands except share and per share amounts)

	Three Months Ended October 31,		Six Months Ended October 31,	
	2017	2016	2017	2016
Revenues:				
Sales	$130,427	$133,170	$258,701	$262,854
Interest and other income	18,691	17,040	36,835	33,196
Total revenue	149,118	150,210	295,536	296,050
Costs and expenses:				
Cost of sales	75,623	77,997	150,829	153,510
Selling, general and administrative	23,727	22,654	47,592	45,822
Provision for credit losses	38,746	39,441	72,906	72,822
Interest expense	1,324	1,036	2,496	1,980
Depreciation and amortization	1,108	1,080	2,187	2,176
(Gain) loss on disposal of property and equipment	57	(1)	104	399
Total costs and expenses	140,585	142,207	276,114	276,709
Income before taxes	8,533	8,003	19,422	19,341
Provision for income taxes	2,564	2,985	6,461	7,214
Net income	$5,969	$5,018	$12,961	$12,127
Less: Dividends on mandatorily redeemable preferred stock	(10)	(10)	(20)	(20)
Net income attributable to common stockholders	$5,959	$5,008	$12,941	$12,107
Earnings per share:				
Basic	$0.82	$0.64	$1.74	$1.53
Diluted	$0.79	$0.62	$1.69	$1.48
Weighted average number of shares used in calculation:				
Basic	7,354,499	7,833,061	7,451,673	7,890,993
Diluted	7,555,026	8,136,961	7,661,668	8,161,019

The accompanying notes are an integral part of these condensed consolidated financial statements.

Condensed Consolidated Statements of Cash Flows America's Car-Mart, Inc.
(Unaudited)

(In thousands)

	Six Months Ended October 31,	
Operating Activities:	2017	2016
Net income	$12,961	$12,127
Adjustments to reconcile net income to net cash used in operating activities:		
Provision for credit losses	72,906	72,822
Losses on claims for payment protection plan	7,980	6,919
Depreciation and amortization	2,187	2,176
Amortization of debt issuance costs	125	140
Loss on disposal of property and equipment	104	399
Stock based compensation	988	783
Deferred income taxes	970	1,579
Excess tax benefit from share based compensation	784	(283)
Change in operating assets and liabilities:		
Finance receivable originations	(239,007)	(244,680)
Finance receivable collections	118,609	117,126
Accrued interest on finance receivables	(236)	(552)
Inventory	18,910	17,084
Prepaid expenses and other assets	(343)	(292)
Accounts payable and accrued liabilities	2,540	1,262
Deferred payment protection plan revenue	484	1,171
Deferred service contract revenue	257	436
Income taxes, net	(1,373)	1,841
Net cash used in operating activities	(1,154)	(9,942)
Investing Activities:		
Purchase of property and equipment	(958)	(875)
Proceeds from sale of property and equipment	23	4
Net cash used in investing activities	(935)	(871)
Financing Activities:		
Exercise of stock options	3	860
Excess tax benefit from share based compensation	-	283
Issuance of common stock	58	74
Purchase of common stock	(20,088)	(8,059)
Dividend payments	(20)	(20)
Change in cash overdrafts	2,179	589
Debt issuance costs	(153)	-
Payments on note payable	(54)	(51)
Proceeds from revolving credit facilities	203,664	192,542
Payments on revolving credit facilities	(183,576)	(175,837)
Net cash provided by financing activities	2,013	10,381

Decrease in cash and cash equivalents	(76)	(432)
Cash and cash equivalents, beginning of period	434	602
Cash and cash equivalents, end of period	$358	$170

The accompanying notes are an integral part of these condensed consolidated financial statements.

Notes to Consolidated Financial Statements (Unaudited) America's Car-Mart, Inc.

A – Organization and Business

America's Car-Mart, Inc., a Texas corporation (the "Company"), is one of the largest publicly held automotive retailers in the United States focused exclusively on the "Integrated Auto Sales and Finance" segment of the used car market. References to the Company typically include the Company's consolidated subsidiaries. The Company's operations are principally conducted through its two operating subsidiaries, America's Car Mart, Inc., an Arkansas corporation ("Car-Mart of Arkansas"), and Colonial Auto Finance, Inc., an Arkansas corporation ("Colonial"). The Company primarily sells older model used vehicles and provides financing for substantially all of its customers. Many of the Company's customers have limited financial resources and would not qualify for conventional financing as a result of limited credit histories or past credit problems. As of October 31, 2017, the Company operated 140 dealerships located primarily in small cities throughout the South-Central United States.

B – Summary of Significant Accounting Policies

General

The accompanying condensed consolidated balance sheet as of April 30, 2017, which has been derived from audited financial statements, and the unaudited interim condensed financial statements as of October 31, 2017 and 2016, have been prepared in accordance with generally accepted accounting principles for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six months ended October 31, 2017 are not necessarily indicative of the results that may be expected for the year ending April 30, 2018. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended April 30, 2017.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of America's Car-Mart, Inc. and its subsidiaries. All intercompany accounts and transactions have been eliminated.

Segment Information

Each dealership is an operating segment with its results regularly reviewed by the Company's chief operating decision maker in an effort to make decisions about resources to be allocated to the segment and to assess its performance. Individual dealerships meet the aggregation criteria for reporting purposes under the current accounting guidance. The Company operates in the Integrated Auto Sales and Finance segment of the used car market, also referred to as the Integrated Auto Sales and Finance industry. In this industry, the nature of the sale and the financing of the transaction, financing processes, the type of customer and the methods used to distribute the Company's products and services, including the actual servicing of the contracts as well as the regulatory environment in which the Company operates, all have similar characteristics. Each of our individual dealerships are similar in nature and only engages in the selling and financing of used vehicles. All individual dealerships have similar operating characteristics. As such, individual dealerships have been aggregated into one reportable segment.

Use of 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 and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. Significant estimates include, but are not limited to, the Company's allowance for credit losses.

Concentration of Risk

The Company provides financing in connection with the sale of substantially all of its vehicles. These sales are made primarily to customers residing in Alabama, Arkansas, Georgia, Kentucky, Mississippi, Missouri, Oklahoma, Tennessee, and Texas, with approximately 30% of current period revenues resulting from sales to Arkansas customers.

Periodically, the Company maintains cash in financial institutions in excess of the amounts insured by the federal government. The Company's revolving credit facilities mature in December 2019.

Restrictions on Distributions/Dividends

The Company’s revolving credit facilities generally restrict distributions by the Company to its shareholders. The distribution limitations under the credit facilities allow the Company to repurchase shares of its common stock up to certain limits. Under the current limits, the aggregate amount of repurchases after October 25, 2017 cannot exceed the greater of: (a) $50 million, net of proceeds received from the exercise of stock options (plus any repurchases made during the first six months after October 25, 2017, in an aggregate amount up to the remaining availability under the $40 million repurchase limit in effect immediately prior to October 25, 2017, net of proceeds received from the exercise of stock options), provided that the sum of the borrowing bases combined minus the principal balances of all revolver loans after giving effect to such repurchases is equal to or greater than 20% of the sum of the borrowing bases; or (b) 75% of the consolidated net income of the Company measured on a trailing twelve month basis. In addition, immediately before and after giving effect to the Company’s stock repurchases, at least 12.5% of the aggregate funds committed under the credit facilities must remain available. Thus, the Company is limited in its ability to pay dividends or make other distributions to its shareholders without the consent of the Company’s lenders.

Cash Equivalents

The Company considers all highly liquid debt instruments purchased with original maturities of three months or less to be cash equivalents.

Finance Receivables, Repossessions and Charge-offs and Allowance for Credit Losses

The Company originates installment sale contracts from the sale of used vehicles at its dealerships. These installment sale contracts carry an average interest rate of approximately 16.1% using the simple effective interest method including any deferred fees. In May 2016, the Company increased its retail installment sales contract interest rate from 15.0% to 16.5% in response to continued high levels of credit losses. Contract origination costs are not significant. The installment sale contracts are not pre-computed contracts whereby borrowers are obligated to pay back principal plus the full amount of interest that will accrue over the entire term of the contract. Finance receivables are collateralized by vehicles sold and consist of contractually scheduled payments from installment contracts net of unearned finance charges and an allowance for credit losses. Unearned finance charges represent the balance of interest receivable to be earned over the entire term of the related installment contract, less the earned amount ($2.3 million at October 31, 2017 and $2.1 million April 30, 2017 on the Condensed Consolidated Balance Sheets), and as such, have been reflected as a reduction to the gross contract amount in arriving at the principal balance in finance receivables.

An account is considered delinquent when the customer is one day or more behind on their contractual payments. While the Company does not formally place contracts on nonaccrual status, the immaterial amount of interest that may accrue after an account becomes delinquent up until the point of resolution via repossession or write-off, is reserved for against the accrued interest on the Condensed Consolidated Balance Sheets. Delinquent contracts are addressed and either made current by the customer, which is the case in most situations, or the vehicle is repossessed or written off if the collateral cannot be recovered quickly. Customer payments are set to match their payday with approximately 74% of payments due on either a weekly or bi-weekly basis. The frequency of the payment due dates combined with the declining value of collateral lead to prompt resolutions on problem accounts. At October 31, 2017, 4.1% of the Company's finance receivable balances were 30 days or more past due compared to 4.8% at October 31, 2016.

Substantially all of the Company's automobile contracts involve contracts made to individuals with impaired or limited credit histories or higher debt-to-income ratios than permitted by traditional lenders. Contracts made with buyers who are restricted in their ability to obtain financing from traditional lenders generally entail a higher risk of delinquency, default and repossession, and higher losses than contracts made with buyers with better credit.

The Company strives to keep its delinquency percentages low, and not to repossess vehicles. Accounts three days late are contacted by telephone. Notes from each telephone contact are electronically maintained in the Company's computer system. In May 2017, the Company began implementing text messaging notifications at select locations which allows customers to elect to receive late notices via text message. The Company attempts to resolve payment delinquencies amicably prior to repossessing a vehicle. If a customer becomes severely delinquent in his or her payments, and management determines that timely collection of future payments is not probable, the Company will take steps to repossess the vehicle.

Periodically, the Company enters into contract modifications with its customers to extend or modify the payment terms. The Company only enters into a contract modification or extension if it believes such action will increase the amount of monies the Company will ultimately realize on the customer's account and will increase the likelihood of the customer being able to pay off the vehicle contract. At the time of modification, the Company expects to collect amounts due including accrued interest at the contractual interest rate for the period of delay. No other concessions are granted to customers, beyond the extension of additional time, at the time of modifications. Modifications are minor and are made for payday changes, minor vehicle repairs and other reasons. For those vehicles that are repossessed, the majority are returned or surrendered by the customer on a voluntary basis. Other repossessions are performed by Company personnel or third-party repossession agents. Depending on the condition of a repossessed vehicle, it is either resold on a retail basis through a Company dealership, or sold for cash on a wholesale basis primarily through physical or online auctions.

Accounts are charged-off after the expiration of a statutory notice period for repossessed accounts, or when management determines that the timely collection of future payments is not probable for accounts where the Company has been unable to repossess the vehicle. For accounts with respect to which the vehicle was repossessed, the fair value of the repossessed vehicle is charged as a reduction of the gross finance receivables balance charged-off. For the quarter ended October 31, 2017, on average, accounts were approximately 63 days past due at the time of charge-off. For previously charged-off accounts that are subsequently recovered, the amount of such recovery is credited to the allowance for credit losses.

The Company maintains an allowance for credit losses on an aggregate basis at a level it considers sufficient to cover estimated losses inherent in the portfolio at the balance sheet date in the collection of its finance receivables currently outstanding. At October 31, 2017, the weighted average total contract term was 32.5 months with 23.3 months remaining. The reserve amount in the allowance for credit losses at October 31, 2017, $115.9 million, was 25% of the principal balance in finance receivables of $492.5 million, less unearned payment protection plan revenue of $19.0 million and unearned service contract revenue of $9.9 million.

The estimated reserve amount is the Company's anticipated future net charge-offs for losses incurred through the balance sheet date. The allowance takes into account historical credit loss experience (both timing and severity of losses), with consideration given to recent credit loss trends and changes in contract characteristics (i.e., average amount financed, months outstanding at loss date, term and age of portfolio), delinquency levels, collateral values, economic conditions and underwriting and collection practices. The allowance for credit losses is reviewed at least quarterly by management with any changes reflected in current operations. The calculation of the allowance for credit losses uses the following primary factors:

- The number of units repossessed or charged-off as a percentage of total units financed over specific historical periods of time from one year to five years.

- The average net repossession and charge-off loss per unit during the last eighteen months segregat