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PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to the Group 1 Automotive Incorporated 4th Quarter and Full Year 2010 Earnings Conference Call. Please be advised that this call is being recorded. I would now like to turn the call over to Mr. DeLongchamps, Vice President of Manufacture Relations and Public Affairs. Please go ahead, Mr. DeLongchamps.

Peter DeLongchamps - *Group 1 Automotive - Vice President Manufacture Relations and Public Affairs*

Thank you, Kim. Good morning, everyone. Welcome to today's call. Before we begin, I would like to make some brief remarks about forward-looking statements and the use of non-GAAP financial measures. Except for historical information mentioned during the conference call, statements made by management of Group 1 Automotive are forward-looking statements that are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements involve both known and unknown risks and uncertainties which may cause the Company's actual results for future periods to differ materially from forecasted results. Those risks include but are not limited to risks associated with pricing, volume, and conditions of the market. Those and other risks are described in the Company's filings with the Securities & Exchange Commission over the past 12 months. Copies of these filings are also available from the SEC and the Company.

In addition, certain non-GAAP financial measures, as defined under SEC rules, may be discussed on this call. As required by applicable SEC rules, the company derives reconciliations of any such non-GAAP financial measures to the most directly comparable GAAP measured on this web site. Participating on today's call is our CEO and President, Mr. Earl Hesterberg, John

Rickel, Senior Vice President & Chief Financial Officer, and Lance Parker, our Vice President, Corporate Controller. I will now hand the call over to Earl.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thank you, Pete. Good morning, everyone. I'm glad all of you are able to join us on the call this morning. We're pleased to announce very positive results for the fourth quarter of 2010 as well as for the full year period. You may recall that in 2009, Group 1's corporate priorities were cash preservation and cost reduction. We executed a plan to trim nearly $120 million from our expense structure which significantly strengthened our balance sheet.

In 2010, our goal was to leverage that lean cost structure by gaining market share and growing the top line with a concentrated sales effort. The 22% revenue increase that we achieved is evidence that we were very successful in meeting this goal. We delivered stellar revenue growth in all segments highlighted by the 31% and 21% increases in used and new vehicles respectively. Group 1's full year new vehicle unit sales increased 17.2%, far surpassing the total industry retail sales increase of 6%. Our sales growth in Nissan, Ford, Chevrolet and Toyota brands significantly out paced the manufacturer's results.

For example, we sold nearly 12% more Toyotas in 2010, whereas Toyota reported relatively flat sales for the year. We reported 27% growth in our Ford sales versus Ford's 17% increase in 2010. We've been able to exceed the industry sales rates in most of the brands we sell primarily because of the strength of our operating team and the focus we put on improving our processes. Our growth has also been supported by our portfolio weighting to our growing brands as well as focusing our geographic footprint on growing regions both in the US and the UK.

In addition to the growth we had in new vehicle sales, used vehicle retail sales were up 22% during the year. This growth was partially driven by the 100 basis point increase in our certified pre-owned business but now accounts for more than 34% of our used retail sales. The certified pre-owned business is good for us as service retention tends to be better for these units. The increase in new and used units sold was the primary driver of the 22% revenue growth in 2010. Retail sales fuel our finance and insurance sales, as well as provide additional business opportunity for our service centers, where we had revenue increases of 24% and 6% respectively.

Although the industry had steady growth in 2010, the absolute sales rate of 11.6 million vehicles was still significantly off when compared to the more normalized 15 million to 16 million unit selling environment. 2010 sales pace only looks favorable when compared to very depressed 2009 industry results of 10.4 million units. It should be no surprise the business remains very competitive at these low absolute selling rates. Our new and used vehicle margins declined in 2010 versus 2009. A thirty basis point decline on the new side and a 100 base point decline on the used vehicle side. Given our focus on growing the company and the benefits, we made the decision to compete and are willing to trade some margin for share.

In addition to our volume focus, our brand concentration area of Toyota, Honda, and Nissan impacted our new vehicle margins negatively. Retail used vehicle margins were also pressured, as our most profitable source of vehicles is from new vehicle trade-ins. With used retail sales growth outpacing our new vehicle sales, we need to continue to source more used inventory from auction which tends to be a higher cost source of supply. In addition, we continue to increase our mix of certified pre-owned sales. These units cost more to recondition which can bring down the margin percentage but because they carry higher average selling prices, the dollar impact is less. Plus they support more on-going service business.

We anticipate both new and used vehicle margins will improve over time, as sales begin to return to more normalized levels. Parts and service gross margin expanded 50 basis points to 53.8% reflecting the focus we have on improving processes and efficiencies in this segment of the business. The last thing I will touch on relating to our full-year results is our on-going expense control. During the year, we remain focused on keeping expenses down. I'm pleased to report that adjusted SG&A expense as a percent of gross profit improved 140 basis points to 78.6%. As we continue to leverage the sales growth and scale the business, we anticipate further improvement.

Turning now to fourth quarter results, new vehicles sales increased 25% as compared to the prior year period, far surpassing the 16% industry retail growth rate in the fourth quarter. We had solid growth in all of our brands during the quarter. Group 1's Toyota, Lexus. Scion sales which account for 36% of our unit sales were up 13%. BMW/ Mini became our second best selling brand at 13% of our mix with an 18% sales increase. Nissan and Honda sales were up more than 25% each. And we retailed 38% more Ford vehicles in the quarter. These growing brands account for more than 80% our new vehicle unit sales.

On a geographic basis, we saw continued improvement in California. The central region had a 26% increase in new vehicle sales with Texas up nearly 30%. The southeast markets, also, had similar strong results. Our new vehicle inventory fell slightly to a 59 day supply at quarter end. Generally, we are comfortable with our new vehicle inventory levels given the current and projected selling environment. The 25% unit sales growth resulted in a 26% revenue increase in new vehicles. In addition, used vehicle retail revenues were up 29%, on 22% higher vehicle sales. The robust used vehicle sales reflects the continued strength in this business, including our growing certified pre-owned business. In total, we had 31 day supply of used vehicle inventory at the end of the quarter.

Finance and insurance revenues increased 29% reflecting the impact of the higher retail vehicle sales. Parts and service revenues grew 9% showing the traction we're getting from the multi-year focus we placed on this area of our business. All in, total revenues grew 25% in the quarter. Driving a 14% increase in gross profit. Profits were up in all four segments of the business.

We saw the same margin pressures we experienced throughout the year in our retail vehicle business. Finance and insurance profit expanded $42 per retail vehicle to $1,075 per unit, as we aren't seeing an improving credit environment and our penetration rates expanded during the quarter. Our attention to cost control was evident in the fourth quarter. Gross profit growth out paced expenses resulting in an improvement in adjusted SG&A as a percent of gross profit of 190 base points to 78.7%. We expect to see further leverage as the selling environment improves and we remain focused on keeping expenses down.

Before I turn the call over to John, I wanted to mention a couple of recent events that had a direct impact on our shareholders. In November, the board of directors reinstated a quarterly cash dividend of $0.10. Then in January, the Company was honored to receive the Global Automotive Shareholder Value Award for being the auto retailer the highest total shareholder return over a three-year period. Group 1 returned 80.3% to its shareholders versus a sector average of 35.9%. The award was presented at the Automotive News World Congress by PricewaterhouseCoopers and Automotive News. I mention these items to emphasize that we remain focused on generating value for our shareholders.

With that, I'll turn the call over to our CFO, John Rickel, to go over our financial results in more detail. John?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Thank you, Earl. Good morning, everyone. For the fourth quarter of 2010, our adjusted net income rose 43.4% or $4.5 million over prior year of $14.7 million. This result excludes $4.9 million of after tax, non-cash, asset impairment charges and an $810,000 income tax benefit related to the tax deductibility of goodwill written off in conjunction with the termination of the dealership franchise. For diluted share, adjusted net income rose $0.21 or 48.8% to $0.64 in the first quarter of 2010.

During the fourth quarter, on a consolidated basis, as Earl stated earlier, revenues increased $287.3 million or 25% to $1.4 billion compared to the same period a year ago reflecting increases in each of our business segments. Our gross profit increased $27 million from the fourth quarter a year ago to $217 million. Which included increases of 12.3% and new vehicle gross profit, 19.3% in used vehicle retail gross profit, 29.3% in F & I gross profit, and 7.5% in parts and service gross profit; primarily reflecting the volume increases that Earl covered with you.

Overall, our gross margin declined 140 basis points to 15.1% in the fourth quarter of 2010, primarily reflecting the mix effect of dramatically higher new and used vehicle sales. Which out paced our parts and service sales increases. In addition, both new and used vehicle retail gross margins declined 60 basis points to 5.6% and 8.2% respectively, pressured by the competitive market in used vehicle sourcing issues previously mentioned. Parts and service gross margin decreased slightly from the year ago period.

As Earl stated, adjusted SG&A expense as a percent of gross profit improved 190 basis points, from the comparable results in the fourth quarter of 2009, to 78.7% as we continue to leverage our cost basis. Floorplan interest expense increased $887,000 or 11.1% in the fourth quarter of 2010 to $8.9 million, as compare with the same period a year ago. This increased primarily reflects a $270.8 million increase in weighted average floorplan borrowings during the quarter. Buyer floor plan borrowing were partially offset by decline in our weighted average borrowing rate, as $250 million of our interest rate swaps and weighted average rate of 4.8% expired in December of 2010.

At year end, our new vehicle inventory stood at 18,700 units with a value of $572 million, compared to 14,300 units with a value of $428 million a year ago. Manufacturers interest assistance, which we record as a reduction of new vehicle cost of sales at the time the vehicles are sold, covered 69.3% of total floor plan interest expense, a 670 point basis improvement from the fourth quarter last year.Other interest expense decreased 266,000 or 3.7% to $7 million in the fourth quarter of 2010. Primarily explained by more interest earned on larger cash investments. Our consolidated interest expense includes non-cash discount amortization of $2.3 million related to our convertible notes.

Now, turning to fourth quarter same store results, in the fourth quarter, we reported revenues of $1.4 billion, which was a 21.1% increase from the 2009 period. Our new vehicle retail sales improved 22.1%, to $791.5 million on 20.9% more units which outpace the overall retail industry results by a large margin. On a per unit basis, our average new vehicle selling prices increased more than $330 to $32,869 reflecting a mix shift toward trucks, as well as a higher mix of luxury brand sales. Our used business was very strong this quarter with retail used vehicle revenues increasing 23.7% to $294.3 million on 18.3% more units. On a per unit basis, retail used vehicle revenues were up $843 or 4.5%, from 2009 levels, to $19,585.

Wholesale revenue grew 38.4% as the number of older, non-retail units that we received as trade-ins increased during the quarter, reflecting the aging car park. In addition, the comparison to the prior year period is distorted because the Cash For Clunkers Program in July and August of 2009 eliminated many of the pure wholesale units from our inventory, as vehicles taken in trade under the program were required to be scrapped and crushed. Our F & I revenues were up $9.4 million, or 27.8% compared to the same period a year ago, on the higher retail sales.

In addition to the positive impact from the increase in the retail unit sales, our F & I revenues were bolstered by a 200 basis point increase in our finance penetration rates, 71%, a 600 basis point increase in our vehicle service contract penetration rates to 36% of our retail sales. We also recognized a 14.8% increase in finance income for contract. Reflecting the focus we've had on our business processes in this area, as well as the improving economic and customer lending conditions that have allowed for lower customer down payments and higher amounts financed. Overall, our F & I income for retail unit increased $69 to $1,104 for the same period a year ago.

Turning to the core of our business, we delivered another quarter of very strong growth in our parts and service business, with revenue up 8.6% over the comparable period a year ago. This growth included a 3.8% increase in our customer pay parts and service revenues, a 21.3% improvement in our warranty business, a 9.3% increase in our collision business and 8.2% growth in our wholesale parts business. It is important to note that our parts and service revenues are not bolstered by increases in internal business. The revenues associated with internal work is eliminated in consolidation. This varies across the sector as some of our competitors account for internal work differently.

We realized improvements in customer pay revenues in most of the major brands that we represent, as the initiative's focus on customers, products and processes continue to build momentum and generate results. In addition, our domestic brand stores continue to benefit from the recent dealership closures in their respective markets with domestic customer pay revenues up more than 10% from the fourth quarter of last year. Our warranty parts and service business benefited primarily from recent recalls. The volume levels for Toyota's specific pedal adjustments and floor mat campaigns from early in 2010 have continued to decline.

Generally, we have begun to see an uptick in warranty-related activity. Decreases in our wholesale parts and collision businesses are primarily attributable to our recent focus on enhancing our business processes in these segments. Our wholesale parts sales also have benefited from the closure of competing dealerships as well as the impact of the stabilizing economy that has helped to strengthen our wholesale parts customers' credit worthiness. As a result of our strong same store revenue growth, our fourth quarter gross profit improved 12.1% compared to 2009.

However, on a per unit base, we realized 11.1% less gross profit on new vehicle sales resulting in an 80 basis point decline in our new vehicle margins. Likewise, our retail used vehicle gross margin declined 60 basis points to 8.3%. While down in percentage terms, it is interesting to note that coupled with the significant increase in average used retail selling prices, the actual used retail gross profit per unit only declined $41. And, when you factor in the better wholesaling results for the quarter, our total used vehicle profit was only off $17 to $1,035 per unit. And we sold over 20% more units in the quarter.

Our same store parts and service margin decreased 100 basis points to 53%, primarily reflecting a revenue mix shift and a slight decline in our customer pay parts and service margins. While several of our recent initiatives designed to grow market share and revenues, grew at a faster rate than other higher margin products and services. Same store SG&A expense as percent of gross profit improved 190 basis point from fourth quarter a year ago to 78.2% reflecting the leverage on our cost structure that the higher revenues provide. We would expect to continue to improve this ratio as sales grow.

So, for the full year. We realize same store revenue growth of 19.3% consisting of an 18.7% increase in new vehicle retail sales on 14.6% more units. A 27.4% increase in used vehicle retail sales on 19.9% more units. A 23.8% improvement in F & I revenues and solid growth of 6.1% in our parts and service business. Same for gross margin for 2010, came in at 16.1% which was down 100 basis points from 2009. Primarily explained by an increased mix of new and used vehicle revenues. Same store gross profit was up 12% in 2010 and a percentage of gross profit, SG&A expenses declined 140 basis points to 78.1%. On a consolidated basis, these significant improvements resulted in adjusted net income increase of 49% to $62.2 million and strong growth of 49.2% in adjusted EPS to $ 267 million.

Now, turning to liquidity and capital structure. We generated cash flow from operations of $17.1 million and $129.7 million on an adjusted basis in the fourth quarter in the full year of 2010 respectively. As of December 31, 2010, we had $19.8 million of cash on hand and another $129.2 million invested in our floorplan offset account, for an immediately available funds to a total of $149 million. In addition, we had $233.7 million available on our acquisition line that can also be used for general corporate purposes. As such, our total liquidity at December 31 was $382.7 million.

We used $15.7 million for capital expenditures during the quarter, construct new facilities, purchase equipment and improve existing facilities. And for the year, we use $28.9 million for capital expenditures. We continue to remain focused on strengthening our balance sheet by reducing debt levels and lengthening maturities. Since the end of 2007, we've reduced our non-floor plan debt by $148.4 million and, as a result, we've reduced our debt to total capitalization ratio by approximately 700 basis points to 37.3% which is one of the best in our sector.

With regards to our real estate investment portfolio, we own $385.3 million of land and buildings at year end, which represents approximately one-third of our total real estate. To finance these holdings, we've utilized our mortgage facility and executed borrowings under other real estate specific debt agreements. During the fourth quarter, we amended and restated our prior mortgage facility, reducing outstanding borrowings to $42.6 million on eight existing dealership facilities. We also executed various agreements with three of our manufacture partners capital finance companies for a total amount of $146 million with maturities of five to seven years to finance the majority of our remaining owned properties.

As we had announced previously, the net effect of re-negotiating our mortgage facility, coupled with the expiration of $250 million of swaps in December of 2010, is estimated $3.8 million reduction of pre-tax interest expense in 2011. Consistent with recent practice, we've chosen not to provide specific earnings guidance for 2011 due to the significant disparities that exist in the industry's SAR forecast for the coming year.

For additional detail regarding our financial condition, please refer to the schedules of additional information attached to the news release as well as the investor presentation posted on our web site. With that, I'll now turn it back over to Earl.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thanks, John. Looking ahead, we see continued growth in 2011. In 2010, we added ten franchises with $256 million in estimated annual revenues and we doubled our footprint in the UK. In 2011, our intention is to continue to grow our business and be a strategic acquisitions in both the US and the UK. Our balance sheet is well positioned to support external growth if we can find acquisitions that meet our return on investment requirements.

Relative to CapEx, we can tell you we anticipate spending less than $50 million on capital expenditures. These expenditures include about $10 million that will be used on specific parts and service initiatives to grow that segment of our business. With the slowly improving consumer sentiment, come the various gauges of pent up vehicle demand near record levels. Whether that is age of car park, scrapage rates or percent of GDP spent on vehicle purchases, we're comfortable with planning the business for $12.5 million to $13 million SAR in 2011, in line with JD Power's industry volume estimate.

As I mentioned earlier, we remain focused on our parts and service business. We will continue to implement initiatives that are geared toward improving our customer satisfaction and, therefore, increase our retention rates. Warranty work should also continue to be steady, as manufacturers are more sensitive to recalling vehicles as soon as an issue is recognized. We saw the impact of this in 2010 when total industry recalls, as measured on the unit basis, increased 24%.

We believe this heightened sensitivity will continue for the foreseeable future, and thereby continue to support our parts and service business, and mitigate the impact of reduced units and operation resulting from depressed new vehicle sales in 2009 and 2010. Used vehicle sales should remain strong, as it is still a relatively low volume new vehicle market. With consumers still uncertain about the future, many will continue to offer a late model used vehicle as a way to save money.

To sum it up, Group 1 Automotive is well positioned to gain market share and to grow the business. Our outstanding operating team will continue to focus on leveraging the business by improving our efficiencies, enhancing customer satisfaction, controlling costs, and adding growing brands to the markets we serve. That concludes our prepared remarks. I'll now turn the call over to the operator to begin the question-and-answer session. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions)Our first question today is from Rick Nelson from Stephens.

Nate Mendez - *Stephens Inc. - Analyst*

Hi, good morning, guys. This is actually Nate Mendez in for Rick. He's out traveling.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Good morning, Nate.

Nate Mendez - *Stephens Inc. - Analyst*

I just wanted to ask some questions on the margin front here and get a little bit more color. This is now the third quarter of new margins below 6%. Is there -- is it something that you would now consider a structural change in the industry where you would expect margins to stay around that 5.5% to 6% range? And I guess how should we think about that going forward?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

To me, the overall driving force, certainly the greatest factor is the Japanese import new vehicle margin. Toyota, Nissan and Honda. All three of them are working hard to maintain or in the case of Nissan, improve share. At least two of them have structural programs that push volume and reduce margins. So, incentive programs. So, I think when you see those brands settle down a little bit, then that will help us. We just have an awful lot of our total mix tied up in those Japanese import brands and it is a tougher selling proposition than it was back in the good old days.

Nate Mendez - *Stephens Inc. - Analyst*

When you say that -- I mean when they settle down and stop pushing volume, is that more of a function of when they see the demand, the overall demand return and the consumer I guess become a little bit more excited about the new car versus the used?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

I think so. It is overall market demand. I think in the case of Toyota and Honda, for example, their core high volume models like Corolla and Camry, they're closer to the end of life cycles, there are some new models coming. In that regard, Civic and Accord for Honda.

Toyota gets a little bit more of the recall issues behind them. I think some of this will settle out. And as fuel prices increase, if you believe they will continue to do so, that will push the market toward these brands a little bit. I think also. Because of their historic reputation in that area.

Nate Mendez - *Stephens Inc. - Analyst*

Ok. And then switching gears on to the used margin side, I think when I look back at this, on the retail side, this is the lowest margin we've seen as far back as at least I can see. I guess -- do you think we've reached a bottom on the used margins at this point? Or how do you see that playing out?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

It is hard for me to tell -- to say that on the used margins. It does seem that used vehicle prices are starting to peak because they're just pushing up against new vehicle prices. And I think that we should be pretty stable. I don't like the low margins at all on either new or used.

But until we get a little more of our vehicles sourced on trade-ins, and have to go to the auction for a little bit less, we're still going to fight that a bit. And again, in the case of our company, there is a factor that we're pushing volume. And because we got to the point where we didn't think we could cut any more costs. So, we had four quarters of pushing new and used volume and we probably gave up a little bit of margin.

Nate Mendez - *Stephens Inc. - Analyst*

Ok. Thanks for that. Then if I can just squeeze one more in. I was wondering if you could comment on the financing environment. It looks like the prime and near prime markets have been improving for some time now. We're hearing that the sub prime market is starting to show signs of life and even the deep sub prime market. Wondering if you can comment on what you're seeing there.

Peter DeLongchamps - *Group 1 Automotive - Vice President Manufacture Relations and Public Affairs*

Nate, it is Pete DeLongchamps. Everything that you said is absolutely correct. I think that -- through this downturn recession, one of the things that was learned by the banks is that automotive portfolios performed pretty darn well. And so we've actually seen many banks getting back into the market and I think that as we continue to move forward, you're going to see additional aggressive growth plans by these banks. So, it is all very positive on the credit front.

Nate Mendez - *Stephens Inc. - Analyst*

Ok, great. Thanks for that. Thank you, guys, very much and good luck with the current quarter.

Peter DeLongchamps - *Group 1 Automotive - Vice President Manufacture Relations and Public Affairs*

Thank you.

Operator

our next question is from Simeon Gutman from Credit Suisse.

Simeon Gutman - *Credit Suisse - Analyst*

Hey, guys, quick question, a follow-up on the gross margin. Just on the new vehicle side, how much control does the senior management exert over it? Is it something you completely give the autonomy to the local market level, in terms of the sales/margin trade-off or is it something that can be controlled from your level?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Well, I don't think it can ever be completely controlled by our level. We delegate a lot of responsibility for the day to day operations out to our field. We can influence it, however. And we influence it more of a macro way by priorities and pay plans. At this point, our corporate priorities are lined up with what's selling volume. More so than margin.

At this point, we haven't made any change to that. As we get into the spring selling season, then we'll revisit that. But that's the way we have the ship pointed and it is being run that way out at the field, which is where most of those decisions are made and we're not adjusting anything at the moment. But I mentioned earlier we're not thrilled with these margin levels but we are thrilled with what's dropping to the bottom line at the moment.

Simeon Gutman - *Credit Suisse - Analyst*

Right. And then I realize there's no true '11 guidance but the range of operating leverage per one million increase in SAR, I don't know if you can speak to that, what the implied run rate for new vehicle gross margin is within that number. Is it flat? Modestly up over time? How does that play into it?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Simeon, this is John Rickel. We've modeled that's consistent with that sensitivity that we provided for everybody on the call, reminder is even though I realize it is a model, we're still comfortable with a view that for every million units of top line SAR growth, the leverage for us should be about $0.50 to $0.55 of EPS growth. Within that, we've assumed basically flat margins from where we're at today. One of the upsides would be as volumes begin to rebuild, if we could get some margin growth, would be a potential plus to the model.

Simeon Gutman - *Credit Suisse - Analyst*

Ok. And that's helpful. Thanks. One more on parts and service, the momentum there is accelerating. I think you've done a great job with a lot of the initiatives and I guess driving traffic to the stores. I mean, this quarter, you saw the gross margin drop off a little. I guess, you characterize it that maybe there was a trade-off there with -- I don't know if it was a trade-off but it sounded like you said you drove some business there with margins. Are you pleased with that trade-off? How should we think about that going forward?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

This is Earl. We're fine with the trade-off at the moment. We've been pushing the customer pay business for two years or more. Some of that was because parts and services countercyclical in a recession. The other part of that is we're concerned about the reduced units and operation from a couple of years of poor sales. We had been pushing customer pay hard. We have been promoting and pricing more competitively some of the common customer pay service operations. But I'm not concerned about that half point of margin dropping.

We also had a rebound in wholesale part sales primarily because of some our wholesale customers are more credit worthy this year than they were one or two years ago. That's lower margin business. It pulls things down a bit also. So, I kind of see the margin fluctuation as just normal noise and vacillation. And we're going to continue to be aggressive and we won't be pulling back on any of those types of marketing efforts in customer pay.

Simeon Gutman - *Credit Suisse - Analyst*

On the pricing side, I realize there could always be some tweaks on an on-going basis, but there aren't big pricing changes or adjustments that need to be done. Most of it now is on more of the marketing initiatives like driving the traffic and getting them into stores?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Absolutely correct. There's no major pricing changes that we believe we need to make at this point.

Simeon Gutman - *Credit Suisse - Analyst*

Ok, great, thank you.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thank you.

Operator

Moving on, we'll take a question from Himanshu Patel. With JP Morgan. Excuse me.

Unidentified Participant - *Goldman Sachs - Analyst*

Hi, this is [Avaic Allo] for Himanshu Patel. I had one question on your parts and service business. I wanted to understand what is driving the parts and services revenues right now. I saw that warranty business was significantly stronger for you this quarter. And I noticed for the other dealer, have reported thus far, it is higher recall volumes in the quarter. Is it all recall related, do you have some different and what is the outlook on the warranty business going forward now?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

It is, for right now, the warranty part of the business is by far the strongest. That is driven by a lot of recall activity by, now a variety of manufacturers. Clearly it began with Toyota and Lexus. But we're seeing increasing recall volume from a variety of manufacturers. I think that will continue to drive a significant year-over-year warranty growth rate in 2011. The customer pay business will have to fight harder as we've done the last year or two to continue to keep that significantly positive year-over-year. But I think warranty will be the driving force this year in the overall parts and service business.

Unidentified Participant - *Goldman Sachs - Analyst*

Ok. So just to continue on that, the warranty business I guess will be impacted in the first quarter, due to the (inaudible)?So, what do you think your warranty initiative should look like in the first quarter?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

This is John Rickel. We clearly did have some benefit in the first quarter of 2010 from the Toyota business. But we continue to think that with the other recalls that have been announced, we should be able to at least hold our own against that spike in first -- you also had a little bit of that in the second quarter of 2010 as well.

Unidentified Participant - *Goldman Sachs - Analyst*

Ok. And lastly, if I can ask one more, as SG&A -- I saw that your SG&A a percentage of gross profit was 79% in the quarter. Which was slightly up compared to the last quarter. Is it all seasonal, or do you have anything special to add to this and what is the outlook on SG&A as a percentage of gross profit as we move forward?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

This is John Rickel. This is seasonality with it. First and fourth quarter tend to be a little weaker on the revenue front. So, you almost see some sequential move from third to fourth quarter. Going forward, as we stated in the -- our prepared comments, we would anticipate as revenues continue to rebound that we should continue to be able to leverage SG&A down and continue to bring that percentage down as we go forward.

Unidentified Participant - *Goldman Sachs - Analyst*

Ok. That's very helpful. Thank you.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thank you.

Operator

our next question comes from Patrick Archambault from Goldman Sachs.

Unidentified Participant - *Goldman Sachs - Analyst*

Hi, guys. This is [Addio Broyd] filling in for Pat. How are you?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Good morning.

Unidentified Participant - *Goldman Sachs - Analyst*

I wanted to ask you on your performance -- strong performance in the Texas and some of the other regions, do you think the out performance will continue in this year as well or do you think that it will probably -- the performance in those regions would start falling in line with the overall growth that you will see in the new and the used segments?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

I think overall, looking at our sales performance and growth, we tripled the market this year and that was a pleasant surprise. We certainly intended to outperform the market this year. But we were very, very pleased that we could triple the retail market growth rate. I really wouldn't expect to be able to do that this year. But I do believe that the market is forecast by most people to be up another 10% or 11% this year in total. I would think retail SAR should be close to that. So, we would expect to grow at about that rate.

So, we're still going to expect our team to at least grow with the market even though we tripled that growth rate last year. I don't see anything in the regions that would concern me. The weak region that we had during the fourth quarter would have been the northeast. But Texas and Oklahoma, they still seem to be quite strong. I think California appears to be showing some signs of life and the southeast US was very good for us. I don't see why that would change. The only regional wild card might be the economy in the northeast at least as it relates to auto sales.

Unidentified Participant - *Goldman Sachs - Analyst*

And -- thanks a lot. That's helpful. And following up on one of the questions that was asked previously, are you guys implying that your warranty business will be up year on year in the first quarter, even with the tough Toyota comp?

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John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

This is John Rickel. I'm not sure I would say it would be up significantly. I think that we stand a chance with the other recalls that are out there. To at least be even with the pretty tough comp from last year.

Unidentified Participant - *Goldman Sachs - Analyst*

That's helpful. Thanks a lot, guys.

Operator

Our next question today comes from John Murphy from Bank of America Merrill Lynch.

Elizabeth Blaine - *Bank of America Merrill Lynch - Analyst*

Good morning, this is Elizabeth Blaine on for John. I'm wondering how January and February sales looked compared to your expectations and compared to December, since there was some adverse weather conditions, particularly in your northeast markets in December, and then even more adverse conditions almost everywhere so far this year. So, I mean sales are still looking pretty strong so I'm wondering if they might have been stronger in more normal conditions.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

I think your last statement is absolutely correct. I was personally surprised by the January industry selling rate given that there were some days lost, at least in our markets to weather, and then February has been far worse. So, there have been a lot of lost days of business. Throughout the US and for us, it is not just the northeast. We've been hit all the way down to Atlanta, Georgia, where we missed several days and in the state of Oklahoma. I think we missed the best part of a week. I don't want to over react to that.

We need to kind of see when the cold goes away and what we can catch up to later in the quarter. I would have to say the weather has been beyond normal winter assumptions and expectations. But even with that, in the markets where the weather is not a factor or in the time periods when we've had normal seasonal weather, the market looks strong. The retail selling rate in January and December increased more than 20% over prior years.

So, I think if we can get these weather effects behind us, we've got some pretty optimistic feelings about the overall market. The weather has to be hurting sales in the short term. Whether it was some part of January and so far in February. So, it takes some time to catch that up. We'll have to see when it finally warms up a bit, how many days we missed.

Operator

Anything further, Mr. Murphy?

Elizabeth Blaine - *Bank of America Merrill Lynch - Analyst*

Yes, hi. Are your inventory levels a little too lean at this point at 59 days supply or is that a comfortable level? Are there any particular brands where you think you're a little light or a little heavy?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

No, we're good. We're probably about as good as we've been in a long time. That's not a bad level. Some of the products that were a bit short at the end of last year or third quarter last year like Chevrolet Equinox, some of those things have filled in nicely. And inventory is not one of our main concerns right now.

Elizabeth Blaine - *Bank of America Merrill Lynch - Analyst*

Ok. Great. I just have one more which is does Group 1 have any dealer incentive programs from luxury brands similar to what Auto Nation talked about in their fourth quarter release because they just mentioned a benefit from stair step programs and certain luxury OEMs, I wonder if Group 1 might see a benefit as volumes improve in Lexus and BMW.

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Elizabeth, this is John Rickel. Let me try to answer that. Our assumption is the program that our competitor was talking about wasn't really a stair step program. It was more tied to facility standards. Around one of the premium luxury brands. We have representation with that brand as well. Basically, we've completed most our facilities. We've got one that should finish in the first quarter of this year but we did not have any significant catch-up payments in the fourth quarter related to that.

Elizabeth Blaine - *Bank of America Merrill Lynch - Analyst*

Ok. Great. All right. Thanks very much.

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Thank you.

Operator

our next question today is from Scott Stember from Sidoti & Co.

Scott Stember - *Sidoti & Company - Analyst*

Good morning, guys.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Good morning, Scott.

Scott Stember - *Sidoti & Company - Analyst*

Can you talk about the Toyota brand now that we've seen some signs of a rebound in January and now with reports of that with this accelerator issue, that there really was no issue there whatsoever. What are you seeing on the ground level with Toyota sales in the last few weeks and what are your thoughts of a rebound in the brand throughout the year?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

John, it is Earl. I haven't seen any change yet. Toyota new vehicle sales have been sticky for quite awhile in terms of moving Camrys and Corollas which is a big volume units. But I was really pleased to see is Toyota's attacking the market and they're fighting for their share and as dealers, we love to see that. They're also very intelligent about the way they go about it with their finance -- I'm sorry, I said John and it is Scott. Sorry, Scott.

So, we like to see that. And you know, these leasing and finance supported incentives really are residual value friendly. And I think we'll get traction with them. But it is too early for us to really have experienced that yet. So, I'm optimistic that Toyota is fighting back. And that they also have quite a few new models coming throughout the course of this year. Which I think will further help Toyota. And the fuel prices continue to increase, things like the Prius and their other hybrids are likely to get more traction also. So, I would say I'm a bit bullish on Toyota at the moment.

Peter DeLongchamps - *Group 1 Automotive - Vice President Manufacture Relations and Public Affairs*

Scott, it is Pete DeLongchamps. I would like to add one more thought. If you think about the turmoil Toyota went through last year and for them to essentially have had an 11-month selling year and for them to come out flat for the year on the sales rate and with us, actually increasing our sales, I think it speaks volumes to the power of the brand. And you know, we all echo Earl's sentiments out in the field as to exactly what's going on with Toyota because we think at the end of the year, it was a real win for Toyota, with their results based on the turmoil they went through in the first half of the year.

Scott Stember - *Sidoti & Company - Analyst*

Ok. Just circling back to the parts and service area. John, I missed what the customer pay same store increase was?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

It was up in the fourth quarter, 3.8%.

Scott Stember - *Sidoti & Company - Analyst*

Ok. And could you just remind us again some of the things that you've done over the last year, year and a half to increase customer pay business, what's really working and sticking in and what could you do to advance that going forward?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Well, for competitive reasons, I don't like to go into too much of that because sometimes it shows up in some of our competitors. But we put a lot more management focus on it and a lot more oversight into some of the direct marketing efforts and pricing to make sure we're more competitive. I don't think I want to say much more than that.

Scott Stember - *Sidoti & Company - Analyst*

Fair enough. Just last question on the used side. Can you talk about what percentage of vehicles you're being sourced by trade in versus a year ago?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

I think it is about 55/45 right now. 55% trade-ins, 45% at auction in the good market of $15 million, $16 million, it would be more like 65/35.

Scott Stember - *Sidoti & Company - Analyst*

Got you. That's all I have. Thank you.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thanks, Scott.

Operator

We'll go next to Josh Dolin from Wells Fargo.

Josh Dolin - *Wells Fargo Securities - Analyst*

Morning, guys. Josh sitting in for Matt Nemer. How is everyone?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Good, Josh.

Josh Dolin - *Wells Fargo Securities - Analyst*

Good, good. Getting back to the geographic mix in the sales brand mix, do you think there was added competition in the northeast area that kind of contributed to that being down or is it just a more economic recovery issue like you mentioned? And then, we're seeing Toyota Lexus share down a bit and BMW up. Are people just not buying Lexuses and moving over to BMWs or is there something else there?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Well, my observations, which, again, are only based on our geographic footprint so they may not be representative for everyone, but in the northeast, it is a heavily competitive. Highly competitive. Dealers in the northeast and New York and Boston and places, tend to be placed very close together and in a low industry they slug it out. We're also very heavily weighted toward Toyota, in the northeast. Particularly in the Boston area. And so that -- I think it is more of a competitive factor.

I'm not really sure about any economic difference in the northeast. But that was our observation there. Lexus had a very strong close to last year, particularly in December. And I think you know there was a bit of competition among the three luxury brands or the major three luxury brands for bragging rights or the sales title last year. I think Lexus finished strong in December, but I think they were a little bit weak early in the quarter and maybe in January compared to December but there's nothing wrong with the Lexus business.

They may be not at the strongest point in their product life cycle. In terms of new model introductions. But the Lexus business is still one of the best in the global automotive industry. So, we're very happy with Lexus business.

THOMSON REUTERS

Josh Dolin - *Wells Fargo Securities - Analyst*

All right. All of my other questions were answered. Thank you very much.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thank you.

Operator

It looks like we have time for one last question. That will come from Jordan Hymowitz with Philadelphia Financial.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Hey, guys, thanks for taking my question.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Hello, Jordan.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Two quick things. One would be Mercedes incentive program for facilities improvement. Regarding the benefit generated from that if that is the right word. Did you earn that through your income statement or is that just an incentive payment that's kind of a reimbursement of CapEx?

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Jordan, this is John Rickel. It actually comes through the income statement. It is paid as additional gross on the new vehicle sale.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

So, it is added to the gross margin line.

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Correct.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Ok. And then the second question is can you break out your gross margins on Toyota versus everybody else and if you don't want to do just Toyota, can you say like you know, approximately Toyota, Nissan and Honda. Those three compared to everybody else. They substantially lowered -- in other words, are they dragging down your margins?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Yes. We won't disclose individual brands but those three are at the bottom end of the spectrum.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

How wide is the spectrum?

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Probably 200 basis points.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

All right, thank you.

John Rickel - *Group 1 Automotive - Senior Vice President & Chief Financial Officer*

Thank you.

Operator

That's all of the time we have for questions. Mr. Hesterberg, I'll turn it back over to you.

Earl Hesterberg - *Group 1 Automotive - CEO and President*

Thanks to everyone for joining us today. We look forward to updating you on our first quarter earnings results in April.

Operator

That does conclude our conference call for today. Thank you for your participation.
