
AutoCanada

# MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For the three month period ended March 31, 2016

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# About us

AutoCanada is one of Canada's largest multi-location automobile dealership groups, currently operating 53 dealerships, comprised of 60 franchises, (see "GROWTH, ACQUISITIONS, RELOCATIONS AND REAL ESTATE") in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick and Nova Scotia. In 2015, our dealerships sold approximately 62,800 vehicles and processed approximately 848,000 service and collision repair orders in our 912 service bays.

Our dealerships derive their revenue from the following four inter-related business operations: new vehicle sales; used vehicle sales; parts, service and collision repair; and finance and insurance. While new vehicle sales are the most important source of revenue, they generally result in lower gross profits that used vehicle sales, parts, service and collision repair operations and finance and insurance sales. Overall gross profit margins increase as revenues from higher margin operations increase relative to revenues from lower margin operations.

# 1. READER ADVISORIES

This Management's Discussion & Analysis ("MD&A") was prepared as of May 5, 2016 to assist readers in understanding AutoCanada Inc.'s (the "Company" or "AutoCanada") consolidated financial performance for the three month period ended March 31, 2016 and significant trends that may affect AutoCanada's future performance. The following discussion and analysis should be read in conjunction with the unaudited condensed interim consolidated financial statements and accompanying notes (the "Interim Consolidated Financial Statements") of AutoCanada as at and for the three month period ended March 31, 2016, the audited annual consolidated financial statements and accompanying notes (the "Consolidated Financial Statements") of AutoCanada as at and for the year ended December 31, 2015, and MD&A for the year ended December 31, 2015. Results are reported in Canadian dollars. Certain dollars have been rounded to the nearest thousand dollars, unless otherwise stated.

To provide more meaningful information, this MD&A typically refers to the operating results for the three month period ended March 31, 2016 of the Company, and compares these to the operating results of the Company for the three month period ended March 31, 2015. Until July 11, 2014, the Company had investments in associates comprised of six General Motors dealerships and accounted for the investments utilizing the equity method, whereby the operating results of these investments were included in one line item on the statement of comprehensive income known as income from investments in associates. As a result, the Company did not incorporate the consolidated results of its investments in associates in its discussion and analysis prior to Q3 2014. On July 11, 2014, the Company completed a business combination under common control, resulting in the accounting consolidation of the results of its investments in associates using the predecessor values method.

This MD&A contains forward-looking statements. Please see the section "FORWARD-LOOKING STATEMENTS" for a discussion of the risks, uncertainties and assumptions used to develop our forward-looking information. This MD&A also makes reference to certain non-GAAP measures to assist users in assessing AutoCanada's performance. Non-GAAP measures do not have any standard meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. These measures are identified and described under the section "NON-GAAP MEASURES."

Additional information regarding our Company, including our 2015 Annual Information Form, dated March 17, 2016, is available on SEDAR at www.sedar.com and our website www.autocan.ca. Such additional information is not incorporated by reference herein, unless otherwise specified, and should not be deemed to be made part of this MD&A.

# 2. OUR PERFORMANCE

***Performance vs. the First Quarter of Prior Year***

AutoCanada's higher sales, gross profits and net earnings in the first quarter of 2016 are a direct result of acquisitions made subsequent to the end of the first quarter of 2015. Lower same store sales and same store gross profits are a result of reduced economic activity, particularly in Alberta.

Management considers gross profit to be a key measure of overall corporate performance. Overall revenues can vary significantly year over year as a result of fluctuations in sales mix, as well as fluctuations in lower margin fleet sales and used vehicle wholesale sales. As such, Management believes that gross profit is a key indicator of overall corporate performance.

Gross profit increased in new vehicle, used vehicle, and parts, service and collision revenue streams and overall gross profit increased by 5.9% compared to the same period of 2015, as a result of acquisitions made subsequent to the first quarter of 2015. Same store gross profit decreased by 5.5% in the first quarter of 2016, as compared to the same period of 2015, which is due primarily to gross profit decreases in new vehicle retail, finance and insurance sales offset by increases in used vehicle retail and parts, service and collision.

New vehicle same store gross profit decreased by 9.3% and gross profit margin declined to 7.4% from 7.6%, as a result of tightening markets. Achievement of sales volume incentives in certain stores remains low and continues to weigh on new vehicle gross margins and gross profit margin. At this time, Management is unable to predict the level of future incentive rebates that will be provided by manufacturers.

Used vehicle retail same store gross profit has increased by 8.6%, while gross profit margin has declined 0.3% compared to the same period of 2015 due to a change in consumer patterns. Due to the difficult economy, consumers who would typically purchase new vehicles are instead buying nearly-new used vehicles which have higher gross margin than the average used vehicle.

Finance and insurance same store gross profit decreased by 20.0% while gross profit margin in this revenue stream decreased to 92.2% from 92.7% in the comparative period. The cause of the decrease in gross profit margin is due to consumers reducing their purchase of premium F&I products when buying a vehicle, as well as decreased commissions earned on financing. With lower interest rates on financing agreements, the commission earned is reduced. Lower consumer costs on financing agreements are used by manufacturers to drive new vehicle sales; this leads to higher vehicle sales, however the dealership is impacted by the corresponding lower commission revenue.

Parts, service and collision same store gross profit increased by 4.8% as a result of an increase in the number of repair orders completed during the period. Same store gross profit margin also increased by 5.9% over the comparative period due to an increase in higher margin repair orders. Management's focus on this area over the past twelve months continues to provide year-over-year growth and management continues to focus on the performance of non-same stores in this area to improve margins throughout the integration period.

The Company has been focused on integrating the dealerships acquired in the prior two years. Due to the increase of acquisition activity over the past two years, integration of individual dealerships has been a main focus in ensuring the new dealerships implement policies and procedures, as well as best practices which we believe are main drivers in delivering long term shareholder value. During 2016, 17 dealerships will become same store dealerships.

***Performance vs. the Canadian New Vehicle Market***

New light vehicle sales in Canada in the three month period ended March 31, 2016 were up 9.3% when compared to the same period in 2015. Sales of new vehicles in Alberta and British Columbia, our primary markets, were down by 7.1% and up by 9.3% during the three month period ended March 31, 2016, respectively. The Company's same store unit sales of new retail vehicles decreased by 17.8% during the three month period ended March 31, 2016 due to our same store concentration in Alberta . The Company's same store total revenue for the three month period ended March 31, 2016 in Alberta decreased by 20.5%, while British Columbia increased by 9.7%.

The first quarter of 2016 continued to be a challenging retail environment for the Alberta market as well as the Company. Our concentration of Alberta dealerships hindered the Company's new vehicle sales performance relative to the Canadian average change in light vehicle sales as reported by DesRosiers Automotive Consultants. Management continues to work closely with its dealerships to ensure that they are adjusting their processes to best capitalize on all sales opportunities and is confident that progress is being made, with continued focus on non-same stores to improve margins throughout the integration period.

The following table summarizes Canadian new light vehicle sales for the three month periods ended March 31, 2016 and March 31, 2015 by Province:

### March Year to Date Canadian New Vehicle Sales by Province[1,2]

| | March Year to Date | | Percent | Unit |
|---|---|---|---|---|
| | 2016 | 2015 | Change | Change |
| British Columbia | 48,000 | 43,916 | 9.3% | 4,084 |
| Alberta | 48,865 | 52,605 | (7.1)% | (3,740) |
| Saskatchewan | 10,738 | 11,144 | (3.6)% | (406) |
| Manitoba | 11,639 | 11,313 | 2.9% | 326 |
| Ontario | 162,287 | 141,752 | 14.5% | 20,535 |
| Quebec | 93,592 | 84,621 | 10.6% | 8,971 |
| New Brunswick | 9,128 | 7,607 | 20.0% | 1,521 |
| PEI | 1,526 | 1,212 | 25.9% | 314 |
| Nova Scotia | 10,836 | 8,724 | 24.2% | 2,112 |
| Newfoundland | 6,285 | 5,679 | 10.7% | 606 |
| **Total** | 402,896 | 368,573 | 9.3% | 34,323 |

1 *DesRosiers Automotive Consultants Inc.*

2 *Readers are cautioned that the above table includes sales channels that the Company does not fully participate in such as daily rentals.*

The following table summarizes the number of same stores for the month ended March 31, 2016 by Province:

### Number of Same Stores[1] by Province

| | British Columbia | Alberta | Manitoba | Ontario | Atlantic | Total |
|---|---|---|---|---|---|---|
| Chrysler/FIAT | 3 | 5 | 1 | – | 2 | 11 |
| Hyundai | 2 | 2 | – | 2 | – | 6 |
| Volkswagen | 3 | 1 | 1 | – | – | 5 |
| Nissan/Infiniti | 1 | 1 | – | – | – | 2 |
| Audi | – | – | 1 | – | – | 1 |
| Mitsubishi | – | 1 | – | – | – | 1 |
| Subaru | – | 1 | – | – | – | 1 |
| **Total** | 9 | 11 | 3 | 2 | 2 | 27 |

1 *Same store means the franchised automobile dealership has been owned for at least 2 full years since acquisition. The dealership is then included in the quarter thereafter, for same store analysis.*

## Same Store Revenue and Vehicles Sold

| Revenue Source (in thousands of dollars) | For the Three Months Ended March 31, 2016 | March 31, 2015 | % Change |
|---|---|---|---|
| New vehicles - Retail | 143,165 | 152,816 | (6.3)% |
| New vehicles - Fleet | 33,896 | 37,544 | (9.7)% |
| **Total New vehicles** | 177,061 | 190,360 | (7.0)% |
| Used vehicles - Retail | 72,586 | 64,299 | 12.9% |
| Used vehicles - Wholesale | 26,271 | 25,453 | 3.2% |
| **Total Used vehicles** | 98,857 | 89,752 | 10.1% |
| Finance, insurance and other | 14,705 | 18,275 | (19.5)% |
| **Subtotal** | 290,623 | 298,387 | (2.6)% |
| Parts, service and collision repair | 39,802 | 42,605 | (6.6)% |
| **Total** | 330,425 | 340,992 | (3.1)% |
| New retail vehicles sold | 3,353 | 4,080 | (17.8)% |
| New fleet vehicles sold | 825 | 1,047 | (21.2)% |
| Used retail vehicles sold | 2,468 | 2,650 | (6.9)% |
| **Total** | 6,646 | 7,777 | (14.5)% |
| Total vehicles retailed | 5,821 | 6,730 | (13.5)% |

## Same Store Gross Profit and Gross Profit Percentage

| | For the Three Months Ended | | | | | |
|---|---|---|---|---|---|---|
| | Gross Profit | | | Gross Profit % | | |
| Revenue Source (in thousands of dollars) | March 31, 2016 | March 31, 2015 | % Change | March 31, 2016 | March 31, 2015 | % Change |
| New vehicles - Retail | 12,914 | 14,364 | (10.1)% | 9.0% | 9.4% | (0.4)% |
| New vehicles - Fleet | 270 | 167 | 61.7% | 0.8% | 0.4% | 0.4% |
| **Total New vehicles** | 13,184 | 14,531 | (9.3)% | 7.4% | 7.6% | (0.2)% |
| Used vehicles - Retail | 5,347 | 4,923 | 8.6% | 7.4% | 7.7% | (0.3)% |
| Used vehicles - Wholesale | 275 | 79 | 248.1% | 1.0% | 0.3% | 0.7% |
| **Total Used vehicles** | 5,622 | 5,002 | 12.4% | 5.7% | 5.6% | 0.1% |
| Finance, insurance and other | 13,562 | 16,946 | (20.0)% | 92.2% | 92.7% | (0.5)% |
| **Subtotal** | 32,368 | 36,479 | (11.3)% | 11.1% | 12.2% | (1.1)% |
| Parts, service and collision repair | 21,498 | 20,512 | 4.8% | 54.0% | 48.1% | 5.9% |
| **Total** | 53,866 | 56,991 | (5.5)% | 16.3% | 16.7% | (0.4)% |

The following table summarizes same store total revenue for the three months ended March 31, 2016 by Province:

| (in thousands of dollars) | For the Three Months Ended March 31, 2016 | March 31, 2015 | % Change |
|---|---|---|---|
| British Columbia | 125,149 | 114,095 | 9.7% |
| Alberta | 125,376 | 157,631 | (20.5)% |
| Manitoba | 26,202 | 26,656 | (1.7)% |
| Ontario | 14,315 | 11,343 | 26.2% |
| Atlantic | 39,383 | 31,267 | 26.0% |
| **Total** | 330,425 | 340,992 | (3.1)% |

The following table summarizes same store gross profit for the three months ended March 31, 2016 by Province:

| | For the Three Months Ended | | |
|---|---|---|---|
| **(in thousands of dollars)** | **March 31, 2016** | **March 31, 2015** | **% Change** |
| British Columbia | 17,392 | 17,853 | (2.6)% |
| Alberta | 23,547 | 27,769 | (15.2)% |
| Manitoba | 5,117 | 5,049 | 1.3% |
| Ontario | 2,251 | 1,705 | 32.0% |
| Atlantic | 5,559 | 4,615 | 20.5% |
| **Total** | 53,866 | 56,991 | (5.5)% |

# 3. SELECTED QUARTERLY FINANCIAL INFORMATION

The following table shows the unaudited results of the Company for each of the eight most recently completed quarters. The results of operations for these periods are not necessarily indicative of the results of operations to be expected in any given comparable period.

| (in thousands of dollars, except Gross Profit %, Earnings per share, and Operating Data) | Q1 2016[1] | Q4 2015[1] | Q3 2015[1] | Q2 2015[1] | Q1 2015[1] | Q4 2014[1,6] | Q3 2014[1] | Q2 2014 |
|---|---|---|---|---|---|---|---|---|
| **Income Statement Data** | | | | | | | | |
| New vehicles | 363,181 | 368,242 | 471,018 | 483,435 | 345,542 | 379,094 | 456,810 | 289,918 |
| Used vehicles | 180,108 | 167,100 | 179,270 | 194,956 | 163,243 | 148,579 | 158,779 | 102,025 |
| Parts, service and collision repair | 94,721 | 102,220 | 93,139 | 99,304 | 92,951 | 91,225 | 77,680 | 46,078 |
| Finance, insurance and other | 28,862 | 34,752 | 37,778 | 39,182 | 31,671 | 36,355 | 37,267 | 27,038 |
| **Revenue** | 666,872 | 672,314 | 781,205 | 816,877 | 633,407 | 655,253 | 730,536 | 465,059 |
| New vehicles | 27,267 | 27,482 | 34,300 | 34,861 | 25,765 | 29,325 | 35,086 | 23,792 |
| Used vehicles | 10,420 | 10,326 | 10,949 | 11,000 | 8,354 | 7,808 | 9,637 | 6,505 |
| Parts, service and collision repair | 47,669 | 51,760 | 48,336 | 49,859 | 43,913 | 45,687 | 38,913 | 23,373 |
| Finance, insurance and other | 26,353 | 34,354 | 35,088 | 33,955 | 27,407 | 31,109 | 34,714 | 24,077 |
| **Gross profit** | 111,709 | 123,922 | 128,673 | 129,675 | 105,439 | 113,929 | 118,350 | 77,747 |
| Gross Profit % | 16.8% | 18.4% | 16.5% | 15.9% | 16.6% | 17.4% | 16.2% | 16.7% |
| Operating expenses | 96,047 | 101,310 | 100,824 | 100,568 | 93,175 | 90,283 | 90,695 | 59,227 |
| Operating expenses as a % of gross profit | 86.0% | 81.8% | 78.4% | 77.6% | 88.4% | 79.2% | 76.6% | 76.2% |
| Income from investments in associates | – | – | – | – | – | – | 359 | 2,238 |
| Income from loan to associate | 315 | 49 | – | – | – | – | – | – |
| Impairment (recovery) of intangible assets and goodwill | – | 18,757 | – | – | – | (1,767) | – | – |
| Net earnings (loss) attributable to AutoCanada shareholders[5] | 7,272 | (7,631) | 11,690 | 13,523 | 4,969 | 14,240 | 17,765 | 12,831 |
| EBITDA attributable to AutoCanada shareholders[2,5] | 18,312 | 23,353 | 26,379 | 27,397 | 12,687 | 24,605 | 28,674 | 21,702 |
| Basic earnings per share | 0.27 | (0.29) | 0.48 | 0.56 | 0.20 | 0.60 | 0.74 | 0.59 |
| Diluted earnings per share | 0.27 | (0.29) | 0.47 | 0.56 | 0.20 | 0.59 | 0.74 | 0.59 |
| Basic adjusted earnings per share | 0.31 | 0.34 | 0.51 | 0.56 | 0.22 | 0.52 | 0.71 | 0.61 |
| Dividends declared per share` | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.24 | 0.23 |
| **Operating Data** | | | | | | | | |
| Vehicles (new and used) sold excluding GM | 10,728 | 12,345 | 13,092 | 14,723 | 11,343 | 12,774 | 14,966 | 9,887 |
| Vehicles (new and used) sold including GM[3] | 13,301 | 14,150 | 17,086 | 17,739 | 13,824 | 15,415 | 18,079 | 12,414 |
| New vehicles sold including GM[3] | 8,502 | 9,210 | 12,018 | 12,296 | 8,933 | 10,570 | 12,821 | 8,658 |
| New retail vehicles sold | 7,078 | 8,016 | 9,985 | 9,929 | 7,393 | 8,907 | 10,686 | 5,980 |
| New fleet vehicles sold | 1,424 | 1,194 | 2,033 | 2,367 | 1,540 | 1,663 | 2,135 | 1,146 |
| Used retail vehicles sold | 4,799 | 4,940 | 5,068 | 5,443 | 4,891 | 4,845 | 5,258 | 2,761 |
| # of service and collision repair orders completed[3] | 209,194 | 230,772 | 202,692 | 215,142 | 199,096 | 216,427 | 198,612 | 97,559 |
| Absorption rate[2] | 83% | 93% | 91% | 94% | 85% | 85% | 93% | 92% |
| # of dealerships at period end | 53 | 54 | 50 | 49 | 48 | 48 | 45 | 34 |
| # of same store dealerships | 27 | 28 | 26 | 24 | 23 | 23 | 23 | 23 |
| # of service bays at period end | 898 | 912 | 862 | 842 | 822 | 822 | 734 | 516 |
| Same store revenue growth[4] | (3.1)% | (12.1)% | (6.9)% | (2.8)% | (3.5)% | 10.9% | 8.9% | 4.1% |
| Same store gross profit growth[4] | (5.5)% | (14.3)% | (14.1)% | (11.0)% | (8.5)% | 5.7% | 11.4% | 5.4% |
| **Balance Sheet Data** | | | | | | | | |
| Cash and cash equivalents | 72,878 | 62,274 | 77,071 | 77,676 | 66,351 | 72,462 | 64,559 | 91,622 |
| Trade and other receivables | 116,092 | 90,821 | 118,853 | 124,683 | 104,753 | 92,138 | 115,074 | 85,837 |
| Inventories | 628,641 | 596,542 | 581,258 | 620,837 | 625,779 | 563,277 | 471,664 | 324,077 |
| Revolving floorplan facilities | 600,578 | 548,322 | 550,857 | 607,694 | 601,432 | 527,780 | 437,935 | 313,752 |

1 *In conjunction with the business combination under common control completed on July 11, 2014, the Selected Quarterly Financial Information subsequent to July 11, 2014 includes the consolidated results of the Company's GM stores from July 11, 2014. All financial information subsequent to July 11, 2014 includes 100% of the results of the GM stores, except for Net earnings, EBITDA, and EPS amounts, which are presented net of non-controlling interests.*

2 *EBITDA and absorption rate have been calculated as described under "NON-GAAP MEASURES."*

3 *This number includes 100% of vehicles and service and collision repair orders sold by these dealerships in which we have less than 100% investment.*

4 *Same store revenue growth and same store gross profit growth is calculated using franchised automobile dealerships that we have owned for at least 2 full years, excluding the GM stores, as these stores have been treated as acquisitions as at July 11, 2014. Same store growth is in comparison with the same quarter in the prior year.*

5 *The results from operations have been lower in the first and fourth quarters of each year, largely due to consumer purchasing patterns during the holiday season, inclement weather and the reduced number of business days during the holiday season. As a result, our financial performance is generally not as strong during the first and fourth quarters than during the other quarters of each fiscal year. The timing of acquisitions may have also caused significant fluctuations in operating results from quarter to quarter.*

6 *Data presented for Q4, 2014 has been amended subsequent to initial presentation to correct an immaterial clerical error which impacted the computation of Q4, 2014. The annual 2014 results are unchanged as previously presented.*

# 4. OUTLOOK

The outlook regarding new retail vehicle sales in Canada is difficult to predict as manufacturers do not publicly disclose fleet and rental sales separately. Total Canadian new light vehicle unit sales of all types are currently forecasted to increase by 3.0% in 2016 as compared to the prior year as follows:

**New Vehicle Sales Outlook by Province ***

| | 1994 - 2005 (Average) | 2006 - 2013 (Average) | 2014 | 2015 | 2016F |
|---|---|---|---|---|---|
| **Canada** | **1,446** | **1,618** | **1,851** | **1,898** | **1,955** |
| **Atlantic** | **102** | **121** | **137** | **140** | **140** |
| **Central** | **936** | **1,002** | **1,139** | **1,205** | **1,271** |
| Quebec | 366 | 410 | 420 | 444 | 470 |
| Ontario | 570 | 592 | 719 | 761 | 801 |
| **West** | **408** | **495** | **575** | **553** | **544** |
| Manitoba | 42 | 47 | 56 | 56 | 56 |
| Saskatchewan | 36 | 48 | 56 | 54 | 53 |
| Alberta | 166 | 227 | 269 | 236 | 220 |
| British Columbia | 164 | 173 | 194 | 207 | 215 |

* *Includes cars and light trucks (units presented above are in thousands.) Source: Scotia Economics - Global Auto Report, April 8, 2016.*

AutoCanada is satisfied with our first quarter results, in isolation and as an indication of our growth from the first quarter of 2015. Highlights of Q1, 2016 include:

- Net earnings attributable to AutoCanada shareholders, in the first quarter, has increased by 46%, from $5.0 million in 2015 to $7.3 million in 2016
- Free cash flow – 12 month trailing has increased by $7.2 million to $45.9 million from the fourth quarter of 2015
- Basic earnings per share has increased by $0.07, from $0.20 in Q1, 2015 to $0.27 in Q1, 2016, exceeding consensus of $0.26. Included in the $0.27 was a gain on disposition of Newmarket Infiniti Nissan.
- Total vehicles (new and used) sold remained consistent at 13,301 during the first quarter of 2016 compared to 13,824 during the same period of 2015

During the quarter, Alberta industry new vehicle sales decreased by 7.1% over the same quarter in 2015, while national industry new vehicle sales were up 9.3%.

Given that the industry continues to be challenging in Western Canada, we are pleased with our financial metrics in Q1, 2016.

- Same store revenue was $330.4 million, down 3.1% from $341 million in Q1, 2015, and up from $326.2 million in Q4, 2015
- Same store gross profit was $53.9 million, down 5.5% from $57.0 million in Q1, 2015
- Same store gross profit percentage was 16.7%, compared to 16.3% in Q1, 2015

The retail automotive industry is proven to provide consistent profitability in all market conditions, as all of our dealerships are profitable with the exception of one recently opened dealership. AutoCanada continues to have significant earnings potential and we have the ability to generate increased cash-flow when the economy improves in Western Canada where we have a heavy concentration of same stores.

In support of AutoCanada's continued growth, we have reduced the dividend, from $0.25 to $0.10 per quarter. This action will allow the Company to retain $16.5 million annually that can be used to support growth and fund acquisitions. The current economic conditions allows AutoCanada to be opportunistic in our due diligence around potential acquisitions. Our strategy is to acquire dealerships that provide accretive strong returns, focusing on large dealerships in major metropolitan markets. In addition to funding growth, the reduced dividend allows AutoCanada to further strengthen our balance sheet while also increasing liquidity.

Throughout the first quarter, and into the balance of 2016, Management continues to employ our five point strategy to deal with the current downward pressure we face in this economic environment:

- The Company continues to seek regional diversity through larger acquisitions in metropolitan markets. Management is pleased with the acquisition opportunities outside of Alberta and continues to explore and evaluate potential targets.
- The Company has directed resources to increase integration efforts for the dealerships recently acquired to support same store metric improvement year-over-year.
- The Company continues to manage the balance sheet as evidenced by the increase in free cash flow – 12 month trailing.
- The Company is rolling-out new sales process technologies to enhance the customer experience in each of our dealerships.
- The Company is reviewing all costs within the group to reduce or eliminate costs where possible. This focused effort on cost reduction is a project that began early in the first quarter and will continue throughout the calendar year. We have been able to decrease operating expenses as a percentage of gross profit from 88.4% in Q1, 2015 to 86.0% in Q1, 2016. Variable expenses have decreased by 3.3% compared to the first quarter of 2015.

Management is pleased with the progress made thus far on these strategies and we anticipate further success throughout 2016.

# 5. MARKET

The Company's geographical profile is illustrated below by number of dealerships and revenues by province for the three month periods ended March 31, 2016 and March 31, 2015.

| | March 31, 2016 | | | | | |
|---|---|---|---|---|---|---|
| **Location of Dealerships** | **Number of Franchises[1]** | **Number of Dealerships[1]** | **Revenue** | **Revenue % of Total** | **Gross Profit** | **Gross Profit % of Total** |
| British Columbia | 13 | 11 | 147,478 | 22% | 21,741 | 20% |
| Alberta | 27 | 24 | 273,924 | 41% | 50,670 | 45% |
| Saskatchewan | 4 | 4 | 51,238 | 8% | 9,378 | 8% |
| Manitoba | 4 | 4 | 41,537 | 6% | 7,923 | 7% |
| Ontario | 6 | 6 | 47,317 | 7% | 6,849 | 6% |
| Quebec | 4 | 2 | 65,995 | 10% | 9,589 | 9% |
| Atlantic | 2 | 2 | 39,383 | 6% | 5,559 | 5% |
| **Total** | 60 | 53 | 666,872 | 100% | 111,709 | 100% |

| | March 31, 2015 | | | | | |
|---|---|---|---|---|---|---|
| **Location of Dealerships** | **Number of Franchises[1]** | **Number of Dealerships[1]** | **Revenue** | **% of Total** | **Gross Profit** | **Gross Profit % of Total** |
| British Columbia | 12 | 10 | 124,922 | 20% | 20,047 | 19% |
| Alberta | 25 | 22 | 285,337 | 45% | 49,463 | 47% |
| Saskatchewan | 4 | 4 | 54,841 | 9% | 9,202 | 9% |
| Manitoba | 4 | 4 | 40,607 | 6% | 7,641 | 7% |
| Ontario | 5 | 4 | 31,345 | 5% | 4,489 | 4% |
| Quebec | 4 | 2 | 65,087 | 10% | 9,982 | 10% |
| Other | 2 | 2 | 31,268 | 5% | 4,615 | 4% |
| **Total** | 56 | 48 | 633,407 | 100% | 105,439 | 100% |

1 *"Dealerships" refers to each physical storefront while "Franchises" refers to each separate franchise agreement.*

The following table sets forth the dealerships that we currently own and operate and the date opened or acquired by the Company or its predecessors, organized by location.

| **Location** | **Operating Name** | **Franchise** | **Year Opened or Acquired** | **Same Store[1]** |
|---|---|---|---|---|
| **Wholly-Owned Dealerships:** | | | | |
| Abbotsford, British Columbia | Abbotsford Volkswagen | Volkswagen | 2011 | Y |
| Chilliwack, British Columbia | Chilliwack Volkswagen | Volkswagen | 2011 | Y |
| Kelowna, British Columbia | Okanagan Chrysler Jeep Dodge FIAT | FIAT / Chrysler | 2003 | Y |
| Maple Ridge, British Columbia | Maple Ridge Chrysler Jeep Dodge FIAT | FIAT / Chrysler | 2005 | Y |
| Maple Ridge, British Columbia | Maple Ridge Volkswagen | Volkswagen | 2008 | Y |
| Prince George, British Columbia | Northland Chrysler Jeep Dodge | Chrysler | 2002 | Y |
| Prince George, British Columbia | Northland Hyundai | Hyundai | 2005 | Y |
| Prince George, British Columbia | Northland Nissan | Nissan | 2007 | Y |
| Victoria, British Columbia | Victoria Hyundai | Hyundai | 2006 | Y |
| Airdrie, Alberta | Airdrie Chrysler Jeep Dodge Ram | Chrysler | 2015 | Q3 2017 |
| Calgary, Alberta | Courtesy Chrysler Dodge | Chrysler | 2013 | Y |
| Calgary, Alberta | Calgary Hyundai | Hyundai | 2014 | Q3 2016 |
| Calgary, Alberta | Crowfoot Hyundai | Hyundai | 2014 | Q3 2016 |
| Calgary, Alberta | Hyatt Mitsubishi | Mitsubishi | 2014 | Q3 2016 |
| Calgary, Alberta | Northland Volkswagen | Volkswagen | 2014 | Q3 2016 |

| Location | Operating Name | Franchise | Year Opened or Acquired | Same Store[1] |
|---|---|---|---|---|
| Calgary, Alberta | Fish Creek Nissan | Nissan | 2014 | Q4 2016 |
| Calgary, Alberta | Hyatt Infiniti | Infiniti | 2014 | Q4 2016 |
| Calgary, Alberta | Tower Chrysler Jeep Dodge Ram | Chrysler | 2014 | Q4 2016 |
| Edmonton, Alberta | Crosstown Chrysler Jeep Dodge FIAT | FIAT / Chrysler | 1994 | Y |
| Edmonton, Alberta | Capital Chrysler Jeep Dodge FIAT | FIAT / Chrysler | 2003 | Y |
| Edmonton, Alberta | North Edmonton Kia | Kia | 2014 | Q4 2016 |
| Grande Prairie, Alberta | Grande Prairie Chrysler Jeep Dodge FIAT | FIAT / Chrysler | 1998 | Y |
| Grande Prairie, Alberta | Grande Prairie Hyundai | Hyundai | 2005 | Y |
| Grande Prairie, Alberta | Grande Prairie Subaru | Subaru | 1998 | Y |
| Grande Prairie, Alberta | Grande Prairie Mitsubishi | Mitsubishi | 2007 | Y |
| Grande Prairie, Alberta | Grande Prairie Nissan | Nissan | 2007 | Y |
| Grande Prairie, Alberta | Grande Prairie Volkswagen | Volkswagen | 2013 | Y |
| Ponoka, Alberta | Ponoka Chrysler Jeep Dodge | Chrysler | 1998 | Y |
| Sherwood Park, Alberta | Sherwood Park Hyundai | Hyundai | 2006 | Y |
| Saskatoon, Saskatchewan | Dodge City Chrysler Jeep Dodge Ram | Chrysler | 2014 | Q3 2016 |
| Winnipeg, Manitoba | Audi Winnipeg | Audi | 2013 | Y |
| Winnipeg, Manitoba | St. James Volkswagen | Volkswagen | 2013 | Y |
| Winnipeg, Manitoba | Eastern Chrysler Jeep Dodge | Chrysler | 2013 | Y |
| Cambridge, Ontario | Cambridge Hyundai | Hyundai | 2008 | Y |
| Mississauga, Ontario | 401 Dixie Hyundai | Hyundai | 2008 | Y |
| Toronto, Ontario | Toronto Chrysler Jeep Dodge Ram | Chrysler | 2014 | Q1 2017 |
| Moncton, New Brunswick | Moncton Chrysler Jeep Dodge | Chrysler | 2001 | Y |
| Dartmouth, Nova Scotia | Dartmouth Chrysler Jeep Dodge | Chrysler | 2006 | Y |
| **Equity Investments:** | | | | |
| Duncan, British Columbia | Island Chevrolet Buick GMC | General Motors | 2013 | Q4 2016 |
| Kelowna, British Columbia | Don Folk Chevrolet | General Motors | 2015 | Q4 2017 |
| Edmonton, Alberta | Lakewood Chevrolet | General Motors | 2014 | Q4 2016 |
| Sherwood Park, Alberta | Sherwood Park Chevrolet | General Motors | 2012 | Q4 2016 |
| Sherwood Park, Alberta | Sherwood Buick GMC | General Motors | 2012 | Q4 2016 |
| Spruce Grove, Alberta | Grove Dodge Chrysler Jeep | Chrysler | 2015 | Q1 2018 |
| North Battleford, Saskatchewan | Bridges Chevrolet Buick GMC | General Motors | 2014 | Q1 2017 |
| Prince Albert, Saskatchewan | Mann-Northway Auto Source | General Motors | 2014 | Q4 2016 |
| Saskatoon, Saskatchewan | Saskatoon Motor Products | General Motors | 2014 | Q4 2016 |
| Winnipeg, Manitoba | McNaught Cadillac Buick GMC | General Motors | 2014 | Q4 2016 |
| Laval, Quebec | BMW Laval and MINI Laval | BMW / MINI | 2014 | Q1 2017 |
| Montreal, Quebec | BMW Canbec and MINI Mont Royal | BMW / MINI | 2014 | Q3 2016 |
| Ottawa, Ontario | Hunt Club Nissan | Nissan | 2015 | Q1 2018 |
| Ottawa, Ontario | 417 Nissan | Nissan | 2015 | Q1 2018 |
| Ottawa, Ontario | 417 Infiniti | Infiniti | 2015 | Q1 2018 |
| **Dealership Loan Financing:** | | | | |
| Whitby, Ontario | Whitby Honda[2] | Honda | 2015 | N/A |
| Edmonton, Alberta | Southview Acura[2,3] | Acura | 2016 | N/A |

1 *Same store means the franchised automobile dealership has been owned for at least 2 full years since acquisition. The dealership is then included in the quarter thereafter, for same store analysis.*

2 *See "GROWTH, ACQUISITIONS, RELOCATIONS AND REAL ESTATE" for more information related to this dealership loan financing arrangement.*

3 *On May 1, 2016, the Company provided financing for Southview Acura in Edmonton, Alberta.*

### Seasonality

The results from operations historically have been lower in the first and fourth quarters of each year, largely due to consumer purchasing patterns during the holiday season, inclement weather and the reduced number of business days during the holiday season. As a result, our operating results are generally not as strong during the first and fourth quarters than during the other quarters of each fiscal year. The timing of acquisitions and the common control business combination may have also caused substantial fluctuations in operating results from quarter to quarter.

**Management realignment**

Effective April 1, 2016, Steven Landry was appointed Chief Executive Officer, and Tom Orysiuk shall continue as President. In addition, effective May 6, 2016, Pat Priestner shall assume the role of non-executive Chair of the Board of Directors, which he shall hold with a target retirement date at the Annual General Meeting in May 2017.

Steven Landry was most recently the Chief Development Officer for ATCO Ltd & Canadian Utilities Limited in Calgary, and previously the Managing Director & Chief Operating Officer for ATCO Australia. Prior to that, Steven Landry spent 27 years at the Chrysler Group where he held various global and executive positions including: Chief Executive Officer and President of DaimlerChrysler Canada, President of Chrysler Europe and Executive Vice President of North America at Chrysler LLC. Steven holds an MBA from Michigan State University and a Bachelor's Degree in Business from Saint Mary's University in Halifax, Nova Scotia.

Steve Rose, Chief Operating Officer, shall retire from his position effective September 30, 2016. Christopher Burrows, Chief Financial Officer and Erin Oor, Vice-President, Corporate Development & Administration, continue in their current positions.

# 6. RESULTS OF OPERATIONS

### First Quarter Operating Results

EBITDA attributable to AutoCanada shareholders for the three month period ended March 31, 2016 increased by $5.6 million or 44.3% to $18.3 million, from $12.7 million when compared to the results of the Company for the same period in the prior year.

The increase in EBITDA attributable to AutoCanada shareholders for the quarter can be mainly attributed to the increase in number of dealerships due to acquisitions since Q1 2015.

Adjusted EBITDA attributable to AutoCanada shareholders for the quarter ended March 31, 2016 increased by $6.8 million or 52.4% from $12.9 million to $19.7 million when compared to the results of the Company for the same quarter in the prior year.

The following table illustrates EBITDA and adjusted EBITDA attributable to AutoCanada shareholders for the three month period ended March 31, for the last three years of operations:

| (in thousands of dollars) | 2016 | 2015 | 2014 |
|---|---|---|---|
| **Period from January 1 to March 31** | | | |
| Net earnings attributable to AutoCanada shareholders | 7,272 | 4,969 | 8,296 |
| Income taxes | 2,477 | 1,707 | 2,881 |
| Depreciation of property and equipment | 4,687 | 3,932 | 2,512 |
| Interest on long-term indebtedness | 3,876 | 2,079 | 764 |
| **EBITDA attributable to AutoCanada shareholders[1]** | 18,312 | 12,687 | 14,453 |
| Add back: | | | |
| Share-based compensation attributed to changes in share price | 59 | (330) | 565 |
| Revaluation of redemption liabilities[2] | 1,262 | 323 | – |
| Unrealized loss on embedded derivative | 20 | 214 | – |
| **Adjusted EBITDA attributable to AutoCanada shareholders[1]** | 19,653 | 12,894 | 15,018 |

1 *This financial measure is identified and defined under the section "NON-GAAP MEASURES."*

2 *Redemption liabilities relate to put options held by certain non-controlling interests and are measured at fair value. Adjustments to fair value are recognized as income or expense through profit and loss.*

Pre-tax earnings attributable to AutoCanada shareholders increased by $3.0 million or 46.0% to $9.7 million for the three month period ended March 31, 2016 from $6.7 million in the same period of the prior year.

Net earnings attributable to AutoCanada shareholders increased by $2.3 million or 46.3% to $7.3 million in the first quarter of 2016 from $5.0 million when compared to the prior year. Income tax expense attributable to AutoCanada shareholders increased by $0.8 million to $2.5 million in the first quarter of 2016 from $1.7 million in the same period of 2015.

Adjusted net earnings attributable to AutoCanada shareholders increased by $3.3 million or 63.4% to $8.6 million in 2016 from $5.3 million in the prior year.

The following table reconciles net earnings to adjusted net earnings for the three month period ended March 31:

| (in thousands of dollars) | 2016 | 2015 | 2014 |
|---|---|---|---|
| **Net earnings attributable to AutoCanada shareholders** | 7,272 | 4,969 | 8,296 |
| Add back: | | | |
| Share-based compensation attributed to changes in share price, net of tax | 43 | (245) | 419 |
| Revaluation of redemption liabilities[2] | 1,262 | 323 | – |
| Unrealized loss on embedded derivative | 20 | 214 | – |
| **Adjusted net earnings attributable to AutoCanada shareholders[1]** | 8,597 | 5,261 | 8,715 |
| Weighted average number of shares - Basic | 27,362,440 | 24,409,574 | 21,685,876 |
| Weighted average number of shares - Diluted | 27,427,695 | 24,520,694 | 21,685,876 |
| **Adjusted net earnings per share attributable to AutoCanada shareholders - Basic[1]** | 0.31 | 0.22 | 0.40 |
| **Adjusted net earnings per share attributable to AutoCanada shareholders - Diluted[1]** | 0.31 | 0.21 | 0.40 |

1 *This financial measure is identified and defined under the section "NON-GAAP MEASURES."*

2 *Redemption liabilities relate to put options held by certain non-controlling interests and are measured at fair value. Adjustments to fair value are recognized as income or expense through profit and loss.*

**Revenues**

Revenues for the three month period ended March 31, 2016 increased by $33.5 million or 5.3% as compared to the same period of the prior year. This increase was driven by increases in new vehicle, used vehicle, and parts, service and collision revenue streams as a result of acquisitions since Q1 2015. New vehicle sales increased by $17.7 million or 5.1% for the three month period ended March 31, 2016 to $363.2 million from $345.5 million in the same period of the prior year. Used vehicle sales increased by $16.9 million or 10.3% for the three month period ended March 31, 2016 compared to the same period of the prior year. Finance and insurance revenue decreased by $2.8 million or 8.9% in the three month period ended March 31, 2016 compared to the same period of the prior year. This decrease is driven by reduced commissions earned on financing products. Parts, service and collision repair revenue increased by $1.8 million or 1.9% for the three month period ended March 31, 2016 compared to the same period of the prior year.

*Revenues - Same Store Analysis*

Same store revenue decreased by $10.6 million or 3.1% in the three month period ended March 31, 2016 when compared to the same period in 2015. Same store new vehicle revenues decreased by $13.3 million or 7.0% for the first quarter of 2016 over the prior year due to a decrease in new vehicle sales of 949 units or 18.5% offset by an increase in the average revenue per new vehicle sold of $5,250 or 14.1%.

Same store used vehicle revenues increased by $9.1 million or 10.1% for the three month period ended March 31, 2016 over the same period in the prior year due to an increase in the average revenue per used vehicle sold of $6,186 or 18.3% offset by a decrease in used vehicle sales of 182 units or 6.9%.

Same store parts, service and collision repair revenue decreased by $2.8 million or 6.6% for the first quarter of 2016 compared to the prior period and was primarily a result of an increase in overall repair orders completed of 4,885 offset by a $53 or 11.4% decrease in the average revenue per repair order completed.

Same store finance, insurance and other revenue decreased by $3.6 million or 19.5% for the three month period ended March 31, 2016 over the same period in 2015. This was due to a decrease in the average revenue per unit retailed of $189 or 7.0% and a decrease in the number of new and used vehicles retailed, that had finance and insurance related products, of 909 units.

**Gross Profit**

Gross profit increased by $6.3 million or 5.9% for the three month period ended March 31, 2016 when compared to the same period in the prior year. As with revenues, gross profit increased due to increases across new vehicle, used vehicle, and parts, service and collision revenue streams as a result of acquisitions since Q1 2015. Gross profit on the sale of new vehicles increased by $1.5 million or 5.8% for the three month period ended March 31, 2016. The increase in new vehicle gross profit for the three month period ended March 31, 2016 can be attributed to an increase in the average gross profit per new vehicle sold of $323 or 11.2% offset by a decrease in the number of new vehicles sold of 431 or 4.8%. Used vehicle gross profit increased by $2.1 million or 24.7% for the three month period ended March 31, 2016. The Company's finance and insurance gross profit decreased by $1.1 million or 3.8% during the first quarter of 2016. This decrease can mainly be attributed to decreases in the total number of vehicles retailed of 407 or 3.3% ended March 31, 2016. Parts, service and collision repair gross profit increased by $3.8 million or 8.6% in the first quarter of 2016.

*Gross Profit - Same Store Analysis*

Same store gross profit decreased by $3.1 million or 5.5% for the three month period ended March 31, 2016 when compared to the same period in the prior year. New vehicle gross profit decreased by $1.3 million or 9.3% in the three month period ended March 31, 2016 when compared to 2015 as a result of a decrease in new vehicle sales of 949 units or 18.5% offset by an increase in the average gross profit per new vehicle sold of $322 or 11.4%.

Used vehicle gross profit increased by $0.6 million or 12.4% in the three month period ended March 31, 2016 over the prior year. This was due to an increase in the average gross profit per used vehicle retailed of $391 or 20.7% offset by a decrease in the number of used vehicles sold of 182 units.

Parts, service and collision repair gross profit increased by $1.0 million or 4.8% in the three month period ended March 31, 2016 when compared to the same period in the prior year as a result of an increase in the number of repair orders completed of 4,885 offset by a decrease in the average gross profit per repair order completed of $1 or 0.4%.

Finance and insurance gross profit decreased by $3.4 million or 20.0% in the three month period ended March 31, 2016 when compared to the prior year as a result of a decrease in the average gross profit per unit sold of $188 and a decrease in units retailed that had finance and insurance related products of 909 units.

**Operating expenses**

Operating expenses consist of four major categories: employee costs, administrative costs, facility lease costs and depreciation of property and equipment. A significant portion of the Company's operating costs are employee costs which are largely variable in nature. There is a balance between reducing staffing levels as a result of business contraction, and maintaining high-performing staff. Due to the competitive nature of the retail automotive industry, additional measures are employed to ensure that the high performing staff are maintained during downtimes, as a result any decrease in gross profit may not be met with a matched decrease in operating expenses. The Company operates a centralized marketing department and information technology department both of which provide services to the dealerships in order to leverage the size of the group as a means to lower the operating costs of the dealerships.

The following tables summarize operating expenses as a percentage of gross profit. When evaluated, operating expenses are broken into their fixed and variable components. Fixed expenses are costs that do not fluctuate with changes in sales volume while variable expenses are costs that vary depending on sales volume.

| | Three month period ended March 31, 2016 | Three month period ended March 31, 2015 | Change |
|---|---|---|---|
| Employee costs | 52.9% | 54.9% | (2.0)% |
| Administrative costs – Variable | 18.2% | 19.5% | (1.3)% |
| **Total variable expenses** | 71.1% | 74.4% | (3.3)% |
| Administrative Costs – Fixed | 5.2% | 5.3% | (0.1)% |
| Facility lease costs | 5.3% | 4.8% | 0.5% |
| Depreciation of property and equipment | 4.4% | 3.9% | 0.5% |
| **Total fixed expenses** | 14.9% | 14.0% | 0.9% |
| **Total operating expenses** | 86.0% | 88.4% | (2.4)% |

Operating expenses increased by 3.1% or $2.9 million during the three month period ended March 31, 2016 as compared to the same period in the prior year. Since many operating expenses are variable in nature, Management considers operating expenses as a percentage of gross profit to be a good indicator of expense control. Operating expenses as a percentage of gross profit decreased to 86.0% in the first quarter of 2016 from 88.4% in the same period of the prior year due to the impact of the variable portion of these expenses. As a percentage of gross profit, the variable portion of operating expenses has decreased from 74.4% to 71.1% while the fixed portion has increased slightly from 14.0% to 14.9% due to increased facility costs.

The increase in the fixed portion of operating expenses is due to the growth of the Company since the first quarter of 2015, resulting in an increase in facility lease costs, depreciation of property and equipment, and the fixed portion of administrative costs. While the fixed costs would typically remain steady as a percentage of gross profit, the slowdown in the economy in the current year has caused this to rise. As the economy, and gross profit, improves, the fixed costs as a percentage of gross profit are also expected to improve.

As evidenced by the variable costs as a percentage of gross profit, Management continues to be successful in controlling operating costs for the Company and have been able to show improvement over the prior year as a result of integration efforts of new dealerships.

*Employee costs*

During the three month period ended March 31, 2016, employee costs increased by $1.2 million to $59.1 million from $57.9 million in the prior year period. Employee costs as a percentage of gross profit stayed consistent compared to the same period of the prior year. Employee costs as a percentage of gross profit for the three month period ended March 31, 2016 decreased to 52.9% from 54.9% for the same period in the prior year. Our dealership employee pay structures are tied to meeting sales objectives, maintaining customer satisfaction indices, as well as improving gross profit and net income.

*Administrative costs*

During the three month period ended March 31, 2016, administrative costs stayed consistent at $26.0 million. The variable portion of administrative costs as a percentage of gross profit decreased to 18.2% in the first quarter from 19.5% in the comparable period of 2015. The fixed portion of administrative costs as a percentage of gross profit decreased to 5.2% in the first quarter from 5.3% in the comparable period of 2015.

*Facility lease costs*

During the three month period ended March 31, 2016, facility lease costs increased by 16.4% to $5.9 million from $5.1 million. primarily due to the acquisitions completed since Q1 2015 as they are fully represented in the expenses during the current period. Facility lease costs are 5.3% of gross profit for the three month period (2015 - 4.8%) ended March 31.

*Depreciation of property and equipment*

During the three month period ended March 31, 2016, depreciation of property and equipment increased to $5.0 million from $4.2 million in the same period of the prior year. The increase in depreciation of property and equipment can be primarily attributed to the acquisitions completed since Q1 2015 as they are fully represented in the expenses during the current period. Depreciation expense makes up 4.4% of gross profit for the three month period (2015 - 3.9%) ended March 31.

**Income Taxes**

Income tax expense for the three month period ended March 31, 2016 increased by $1.1 million to $3.1 million from $2.0 million in 2015.

During the first quarter of 2016, the Company paid $6.3 million of cash taxes which relates to the fiscal 2015 taxation year and installments toward the 2016 taxation year. The payment of cash taxes will have an impact on adjusted free cash flow.

**Finance costs**

The Company incurs finance costs on its revolving floorplan facilities, long term indebtedness and banking arrangements. During the three month period ended March 31, 2016, finance costs on our revolving floorplan facilities decreased by 15.4% to $3.0 million from $3.6 million in the first quarter of 2015, mainly due to increased inventory as a result the acquisitions completed since Q1 2015 as they are fully represented in the expenses during the current period. Finance costs on long term indebtedness increased by $1.8 million in the first quarter of 2016 due to the increase in the Company's revolving term facility for acquisitions completed since Q1 2015 as they are fully represented in the expenses during the current period.

During the quarter ended March 31, 2016, the net income of certain dealerships exceeded the quarterly net income from the comparative quarter, resulting in an increase in cumulative net income for the purposes of revaluing the redemption liabilities. Consequently, a $1,262 increase to the fair value was recorded on the balance sheet with a corresponding expense charged to financing costs in the first quarter.

Some of our manufacturers provide non-refundable credits on the finance costs for our revolving floorplan facilities to offset the dealership's cost of inventory that, on average, effectively provide the dealerships with interest-free floorplan financing for the first 45 to 60 days of ownership of each financed vehicle. During the three month period ended March 31, 2016, the floorplan credits earned were $3,274 (2015 - $3,305). Accounting standards require the floorplan credits to be accounted for as a reduction in the cost of new vehicle inventory and subsequently a reduction in the cost of sales as vehicles are sold.

Management believes that a comparison of floorplan financing costs to floorplan credits can be used to evaluate the efficiency of our new vehicle sales relative to stocking levels. The following table details the carrying cost of vehicles based on floorplan interest net of floorplan assistance earned:

| | **For the Three Months Ended** | |
|---|---|---|
| **(in thousands of dollars)** | **March 31, 2016** | **March 31, 2015** |
| Floorplan financing | 3,030 | 3,581 |
| Floorplan credits earned | (3,274) | (3,305) |
| **Net carrying cost of vehicle inventory** | (244) | 276 |

# 7. GROWTH, ACQUISITIONS, RELOCATIONS AND REAL ESTATE

The Company operates 53 automotive dealerships (60 franchises) comprised of 38 dealerships (43 franchises) which are wholly owned, as well as investments in nine General Motors dealerships (nine franchises), two BMW dealerships (four franchises), one Chrysler dealership (one franchise), and three Nissan dealerships (three franchises), which the Company controls and consolidates for accounting purposes.

**Growth**

Due to the economic slowdown that has occurred in Alberta, Management anticipates that there will continue to be attractive buying opportunities, further enhancing long term shareholder value, however, Management is not yet seeing a change in acquisition multiples. Additionally, the Company shall continue to seek opportunities elsewhere in Canada, where appropriate, so as to provide continued diversity. The Company is in a position to patiently pursue its acquisition strategy thereby maximizing its ability to take advantage of anticipated buying opportunities that times of economic uncertainty generally provide. Management and the Company have excellent relationships with our manufacturer partners and believe that if we can continue to perform well, we can build upon our current brand portfolios and gain the acceptance of other new manufacturers over time.

**Dealership divestiture**

On February 25, 2016, the Company sold substantially all of the operating and fixed assets, including the land and facilities, of Newmarket Infiniti Nissan, located in Newmarket, Ontario for cash consideration. Net proceeds of $10,077 resulted in a pre-tax gain on divesture of $3,206.

**Dealership Loan Financing**

On May 1, 2016, the Company made a second loan, for $2,835 to PPH Holdings Ltd ("PPH"). The Company holds no ownership interest in PPH, which is a company controlled, and formed, by Mr. Patrick Priestner ("Priestner"). The Company has no participation in the equity of PPH or Southview Acura. PPH's principal place of business is Alberta, Canada. Although the Company holds no voting rights in PPH, the Company exercises significant influence by virtue of the existence of its loan and the provision of essential technical information required for operations, as well as through the relationship with Priestner, as AutoCanada's Executive Chair. However, the Company does not have the power to make or block key decisions under the terms of the underlying agreements. As a result, the Company accounts for its loan to PPH under the effective interest method and it is carried at amortized cost.

**Integration of New Dealerships and Investments**

Since April 1, 2015, the Company has acquired six dealerships, and has been dedicating resources to ensure a successful integration of its newly acquired dealerships. As noted in our same store analysis, experience has shown that it takes a minimum of two full years in order to successfully integrate a store and achieve its anticipated performance objectives.

The dealerships acquired in 2014 are integrating well into their respective platforms and within the Company. It is expected that these dealerships will be fully integrated in 2016. The dealerships acquired in 2015 are still fairly new and are being integrated into their respective platforms and within the Company. Management continues to work diligently on the integration of these dealerships and is very satisfied with the progress being made.

The investments in dealerships that we made in the third and fourth quarters of 2015 are very recent. As a result, we are still relatively early in the process of integrating these investments.

We will continue to dedicate significant resources to newly acquired dealerships in order to successfully integrate acquisitions in an efficient manner. As a result, we expect to incur additional selling and administrative costs in the future in order to successfully integrate new dealerships into our model.

**Dealership Open Points**

*Volkswagen – Sherwood Park, Alberta*

In February 2014, the Company announced that it had been awarded the right to a Volkswagen Open Point dealership in Sherwood Park, Alberta. The Company intends to construct an approximately 45,000 square foot facility in Sherwood Park, designed to Volkswagen Canada image standards, with construction anticipated to be completed in the fourth quarter of 2016. The Volkswagen Open Point has a planning potential of 800 new vehicles annually which the Company anticipates achieving in two to three years of operation.

*Nissan – Calgary, Alberta*

On July 1, 2014, as part of the Company's purchase of the Hyatt Group, the Company acquired the exclusive right to build and operate a Nissan dealership on a designated property in southeast Calgary. The purchase price for transfer of the right was $1.5 million, which was satisfied by the issuance of 18,753 common shares of AutoCanada at a deemed price of $79.99. The dealership construction is expected to begin late 2016 with anticipated opening in late 2017. The dealership will be constructed by a third party and subsequently leased by the Company.

*North Winnipeg Kia*

In March 2015, the Company announced that it has signed a Letter of Intent with Kia Canada Inc. ("Kia") which, subject to the completion of requirements contained in the Letter of Intent, will award AutoCanada an Open Point Kia dealership in North Winnipeg, Manitoba. AutoCanada intends to operate the dealership out of a new facility, designed to Kia image standards, with construction anticipated to commence in early 2017.

*Nissan - Ottawa, Ontario*

On November 1, 2015, as part of the purchase of Hunt Club Nissan, the Company acquired the exclusive right to build and operate a Nissan motor vehicle franchise on a designated property in southwest Ottawa. AutoCanada intends to operate the dealership out of a new facility, designed to Nissan image standards, with construction anticipated to commence in second quarter of 2016 and anticipated opening in early 2017.

**Capital Plan**

The Company maintains a capital plan for contemplated future capital projects. Details of the capital plan are described below:

*Dealership Relocations*

Management estimates the total capital requirements of additional potential planned dealership relocations to be approximately $133.0 million by the second quarter of fiscal 2019, $83.5 million of which is to be financed. As noted above, the Company expects dealership relocations to provide long term earnings sustainability and result in significant improvements in revenues and overall profitability. Management continually updates its capital plan and as such the estimates provided may vary as delays occur or projects are added or removed.

*Current Dealership Expansion and Imaging Requirements*

The Company has identified approximately $35.1 million in capital costs that it may incur in order to expand or renovate various current locations by the end of of fiscal 2019, $13.0 million of which is to be financed. The Company is required by its manufacturers to undertake periodic imaging upgrades to its facilities. Included above are the estimated costs and timing related to the re-imaging requirements by Hyundai Canada. The Company expects re-imaging to attract more customers to its dealerships.

*Open Point Opportunities*

Management regularly reviews potential open point opportunities. If successful in being awarded these opportunities, Management would then estimate additional capital costs in order to construct suitable facilities for open points. The Company estimates approximately $18.0 million in capital costs that it may incur by the end of fiscal 2017 related to currently awarded Open Points, $5.4 million of which is to be financed. If awarded in the future, Management will provide additional cost estimates and timing of construction. In order to be successful in some opportunities, Management may be required to secure appropriate land for the potential open points, in which case, additional land purchase costs may be incurred in the future.

The following summarizes the capital plan for contemplated future capital projects as at March 31, 2016:

| (in millions of dollars) | 2016 | 2017 | 2018 | 2019 | Total |
|---|---|---|---|---|---|
| **Same Store** | | | | | |
| Dealership Relocations | 22.9 | 56.3 | 16.5 | – | 95.7 |
| Current Dealership Expansion and Imaging Requirements | 2.2 | 4.8 | 5.2 | 7.8 | 20.0 |
| **Capital Plan** | 25.1 | 61.1 | 21.7 | 7.8 | 115.7 |
| **Expected to be financed** | 14.1 | 39.8 | 13.3 | – | 67.2 |
| **Non Same Store** | | | | | |
| Dealership Relocations | – | 12.0 | 11.3 | 14.0 | 37.3 |
| Current Dealership Expansion and Imaging Requirements | 10.4 | 4.7 | – | – | 15.1 |
| Open Point Opportunities | 9.6 | 8.4 | – | – | 18.0 |
| **Capital Plan** | 20.0 | 25.1 | 11.3 | 14.0 | 70.4 |
| **Expected to be financed** | 12.1 | 8.4 | 7.9 | 6.3 | 34.7 |
| **Total Capital Plan** | 45.1 | 86.2 | 33.0 | 21.8 | 186.1 |
| **Total Expected to be financed** | 26.2 | 48.2 | 21.2 | 6.3 | 101.9 |

Notwithstanding the capital plan laid out above, expected capital expenditures are subject to deferral due to issues in obtaining permits, construction delays, changes in reimaging requirements or other delays that are normal to the construction process. The above is considered to be a guide for when the Company expects to perform capital expenditures, however, significant deferral may occur in the future. Management closely monitors the capital plan and adjusts as appropriate based on Company performance, Manufacturer requirements, expected economic conditions, and individual dealership needs. Management performs a robust analysis on all future expenditures prior to the allocation of funds. Timing of dealership relocations is determined based on the dealership's current performance, the market, and expected return on invested capital. It is expected that a dealership relocation will result in improved performance and increased profitability.

# 8. LIQUIDITY AND CAPITAL RESOURCES

Our principal uses of funds are for capital expenditures, repayment of debt, funding the future growth of the Company and paying dividends to Shareholders. We have historically met these requirements by using cash generated from operating activities and through short term and long term indebtedness.

The Company maintains working capital in excess of manufacturer requirements which may be used for capital expenditures. The Company's analysis of its available capital based on the balance sheet at March 31, 2016 is as follows:

- The Company had drawn $111.0 million on its $250.0 million revolving term facility.

As a result of the above, as at March 31, 2016, the Company currently has approximately $139.0 million in readily available liquidity, not including future retained cash from operations, that it may deploy for growth expenditures including acquisitions.

### Cash Flow from Operating Activities

Cash flow from operating activities (including changes in non-cash working capital) of the Company for the three month period ended March 31, 2016 was $6.8 million (cash provided by operating activities of $8.7 million less negative net change in non-cash working capital of $1.9 million) compared to $(0.8) million (cash used by operating activities of $5.2 million less net increase in non-cash working capital of $4.4 million) in the same period of the prior year.

### Cash Flow from Investing Activities

For the three month period ended March 31, 2016, cash flow from investing activities of the Company was a net inflow of $2.2 million as compared to a net outflow of $25.2 million in the same period of the prior year. The change was primarily due to the proceeds on divestiture of Newmarket Infiniti Nissan and substantial reduction in capital expenditures.

### Cash Flow from Financing Activities

For the three month period ended March 31, 2016, cash flow from financing activities was a net outflow of $1.6 million as compared to a net inflow of $20.0 million in the same period of 2015. The change was primarily due to reduced usage of long-term indebtedness, $37.0 million compared to $63.7 million in Q1 2015.

### Credit Facilities and Floor Plan Financing

There have been no significant changes to credit facilities or our floorplan financing facilities since described in the annual managements' discussion and analysis for the year ended December 31, 2015.

### Key Financial Covenants

The Company is required by its debt agreements to comply with several financial covenants. The following is a summary of the Company's actual performance against its financial covenants as at March 31, 2016:

| Financial Covenant | Requirement | Q1 2016 Actual Calculation | Q4 2015 Actual Calculation |
|---|---|---|---|
| **Syndicated Revolver:** | | | |
| Senior Secured Leverage Ratio | Shall not exceed 2.75 | 1.42 | 1.38 |
| Adjusted Total Leverage Ratio | Shall not exceed 5.00 | 4.19 | 4.09 |
| Fixed Charge Coverage Ratio | Shall not be less than 1.20 | 1.99 | 1.72 |
| Current Ratio | Shall not be less than 1.05 | 1.15 | 1.18 |
| **Syndicated Floorplan:** | | | |
| Current Ratio | Shall not be less than 1.10 | 1.15 | 1.15 |
| Tangible Net Worth | Shall not be less than $40 million | $90.6 million | $89.4 million |
| Debt to Tangible Net Worth | Shall not exceed 7.50 | 4.95 | 4.67 |

The covenants above are based on consolidated financial statements of the dealerships that are financed directly by the lender. As a result, the actual performance against the covenant does not necessarily reflect the reported performance of AutoCanada. The Company is required to comply with other covenants under the terms of its remaining credit agreements. The Company stress tests all covenants on a monthly and quarterly basis and notes that a significant drop in performance would be necessary to breach the covenants.

As at March 31, 2016, the Company is in compliance with all of its financial covenants.

**Financial Instruments**

Details of the Company's financial instruments, including risks and uncertainties are included in Note 25 of the annual audited consolidated financial statements for the year ended December 31, 2015. There have been no significant changes to the Company's financial instruments since that time.

**Growth vs. Non-Growth Capital Expenditures**

Non-growth capital expenditures are capital expenditures incurred during the period to maintain existing levels of service. These include capital expenditures to replace property and equipment and any costs incurred to enhance the operational life of existing property and equipment. Non-growth capital expenditures can fluctuate from period to period depending on our needs to upgrade or replace existing property and equipment. Over time, we expect to incur annual non-growth capital expenditures in an amount approximating our amortization of property and equipment reported in each period.

Additional details on the components of non-growth property and equipment purchases are as follows:

| (in thousands of dollars) | January 1, 2016 to March 31, 2016 | January 1, 2015 to March 31, 2015 |
|---|---|---|
| Leasehold improvements | 1,980 | 965 |
| Machinery and equipment | 338 | 419 |
| Furniture and fixtures | 225 | 412 |
| Computer equipment | 176 | 398 |
| Company & lease vehicles | – | 5 |
| | 2,719 | 2,199 |

Amounts relating to the expansion of sales and service capacity are considered growth expenditures. Growth expenditures are discretionary, represent cash outlays intended to provide additional future cash flows and are expected to provide benefit in future periods. During the three month period ended March 31, 2016, growth capital expenditures of $4.1 million were incurred. These expenditures related primarily to land and buildings that were purchased for future dealership operations during the first quarter of 2016. Dealership relocations are included as growth expenditures since they contribute to the expansion of sales and service capacity of the dealership.

The following table provides a reconciliation of the purchase of property and equipment as reported on the Statement of Cash Flows to the purchase of non-growth property and equipment as calculated in the free cash flow section below:

| (in thousands of dollars) | January 1, 2016 to March 31, 2016 | January 1, 2015 to March 31, 2015 |
|---|---|---|
| Purchase of property and equipment from the Statement of Cash Flows | 6,864 | 25,279 |
| Less: Amounts related to the expansion of sales and service capacity | (4,145) | (23,080) |
| **Purchase of non-growth property and equipment** | 2,719 | 2,199 |

Repairs and maintenance expenditures are expensed as incurred and have been deducted from earnings for the period. Repairs and maintenance expense incurred during the three month period ended March 31, 2016, was $1.6 million (2015 - $1.6 million).

**Planned Capital Expenditures**

Our capital expenditures consist primarily of leasehold improvements, the purchase of furniture and fixtures, machinery and equipment, service vehicles, computer hardware and computer software. Management expects that our annual capital expenditures will increase in the future, as a function of increases in the number of locations requiring maintenance capital expenditures, the cost of opening new locations and increased spending on information systems.

For further information regarding planned capital expenditures, see “GROWTH, ACQUISITIONS, RELOCATIONS AND REAL ESTATE” above.

**Financial Position**

The following table shows selected audited balances of the Company (in thousands) for December 31, 2015 and December 31, 2014, as well as unaudited balances of the Company at March 31, 2016, September 30, 2015, June 30, 2015, March 31, 2015, September 30, 2014 and June 30, 2014:

| (in thousands of dollars) | March 31, 2016 | December 31, 2015 | September 30, 2015 | June 30, 2015 | March 31, 2015 | December 31, 2014 | September 30, 2014 | June 30, 2014 |
|---|---|---|---|---|---|---|---|---|
| Cash and cash equivalents | 72,878 | 62,274 | 77,071 | 77,676 | 66,351 | 72,462 | 64,559 | 91,662 |
| Trade and other receivables | 116,092 | 90,821 | 118,853 | 124,683 | 104,753 | 92,138 | 115,074 | 85,837 |
| Inventories | 628,641 | 596,542 | 581,258 | 620,837 | 625,779 | 563,277 | 471,664 | 324,077 |
| **Assets** | 1,578,225 | 1,532,182 | 1,508,028 | 1,517,978 | 1,449,213 | 1,354,755 | 1,211,527 | 910,715 |
| Revolving floorplan facilities | 600,578 | 548,322 | 550,857 | 607,694 | 601,432 | 527,780 | 437,935 | 313,752 |
| Non-current debt and lease obligations | 293,273 | 285,759 | 313,703 | 287,202 | 241,929 | 223,009 | 179,447 | 294,289 |

**Net Working Capital**

The automobile manufacturers represented by the Company require the Company to maintain net working capital for each individual dealership. At March 31, 2016, the aggregate of net working capital requirements was approximately $92.6 million. At March 31, 2016, all working capital requirements had been met by each dealership. The working capital requirements imposed by the automobile manufacturers’ may limit our ability to fund capital expenditures, acquisitions, dividends, or other commitments in the future if sufficient funds are not generated by the Company. Net working capital, as defined by automobile manufacturers, may not reflect net working capital as determined using GAAP measures. As a result, it is possible that the Company may meet automobile manufacturers’ net working capital requirements without having sufficient aggregate working capital using GAAP measures. The Company defines net working capital amounts as current assets less current liabilities as presented in the interim consolidated financial statements. At March 31, 2016, the Company had aggregate working capital of approximately $107.4 million.

The net working capital requirements above restrict the Company’s ability to transfer funds up from its subsidiaries, as each subsidiary dealership is required to be appropriately capitalized as explained above. In addition, our VCCI Facilities require our Volkswagen and Audi dealerships to maintain minimum cash and equity, which also restricts our ability to transfer funds up.

**Off Balance Sheet Arrangements**

The Company has operating lease commitments, with varying terms through 2037, to lease premises and equipment used for business purposes. The

Company leases the majority of the lands and buildings used in its franchised automobile dealership operations from related parties and other third parties.

The minimum lease payments over the upcoming fiscal years will be as follows:

| (in thousands of dollars) | $ |
|---|---|
| Reminder of 2016 | 15,009 |
| 2017 | 18,723 |
| 2018 | 16,232 |
| 2019 | 14,233 |
| 2020 | 12,279 |
| Thereafter | 134,015 |
| **Total** | 210,491 |

Information regarding our contractual obligations with respect to long-term debt, capital lease obligations and other long-term obligations is included in the Liquidity Risk section of Note 25 of the Company's annual consolidated financial statements.

**Related Party Transactions**

Note 22 of the condensed interim consolidated financial statements of the Company for the period ended March 31, 2016 summarizes the transactions between the Company and its related parties.

*Administrative support fees*

The Company currently earns administrative support fees from companies controlled by the Executive Chair of AutoCanada. The administrative support fees consist of a portion of human resource and fixed costs associated with providing technological and accounting support to these companies. The Company believes that providing support services to these companies provides value to both the companies supported and AutoCanada. By providing support, AutoCanada is able to reduce its overall fixed costs associated with accounting and information technology.

Related party transactions are measured based on the proportionate allocation of actual costs incurred multiplied by the number of resources and/or hours provided to or used by the related party. There are no ongoing or continuing obligations of the Company to provide these services or for the related parties to utilize these services.

*Loan to related parties*

The Company structured the loan to PPH with the associated terms and conditions in order to satisfy the requirements of the manufacturer. It is the Company's belief that this loan investment will provide future opportunities to finance further acquisitions thereby acquiring additional revenue and income streams from this manufacturer.

## 9. OUTSTANDING SHARES

As at March 31, 2016, the Company had 27,459,683 common shares outstanding. Basic and diluted weighted average number of shares outstanding for the three month period ended March 31, 2016 were 27,362,440 and 27,427,695, respectively. As at March 31, 2016, the value of the shares held in trust was $3.6 million (2015 – $3.3 million) which was comprised of 133,093 (2015 - 100,643) in shares with a nil aggregate cost (2015 - nil). As at May 5, 2016, there were 27,459,683 shares issued and outstanding.

## 10. DIVIDENDS

Management reviews the Company's financial results on a monthly basis. The Board of Directors reviews the financial results periodically to determine whether a dividend shall be paid based on a number of factors.

The following table summarizes the dividends declared by the Company in 2016:

| Record date | Payment date | Per Share $ | Total $ |
|---|---|---|---|
| February 29, 2016 | March 15, 2016 | 0.25 | 6,840 |
| May 5, 2016 | June 15, 2016 | 0.10 | 2,735 |

In light of the continued economic uncertainty that exists in Canada, the reduction in the dividend from $0.25 to $0.10 allows AutoCanada to maintain our policy of returning a portion of funds from operations to shareholders while also retaining sufficient capital for acquisitions and growth projects. A reduction in the dividend also allows us to continue effectively employ our five point strategy implemented to deal with the current downward pressure.

As per the terms of the HSBC facility, we are restricted from declaring dividends and distributing cash if we are in breach of financial covenants or our available margin and facility limits or if such dividend would result in a breach of our covenants or our available margin and facility limits. The Company is currently within its covenants.

# 11. FREE CASH FLOW

The Company has defined free cash flow to be cash flows provided by operating activities (including changes in non-cash operating working capital) less capital expenditures (excluding capital assets acquired by acquisitions or purchases of real estate).

| (in thousands of dollars, except unit and per unit amounts) | Q1 2016 | Q4 2015 | Q3 2015 | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 | Q2 2014 |
|---|---|---|---|---|---|---|---|---|
| Cash provided by operating activities | 6,831 | 12,420 | 20,139 | 21,004 | (810) | 42,276 | 9,093 | 10,918 |
| **Deduct:** | | | | | | | | |
| Purchase of property and equipment | (2,786) | (3,354) | (5,144) | (3,228) | (2,352) | (2,454) | (2,834) | (1,057) |
| **Free cash flow[1]** | 4,045 | 9,066 | 14,995 | 17,776 | (3,162) | 39,822 | 6,259 | 9,861 |
| Weighted average shares outstanding at end of period | 27,362,440 | 25,016,637 | 24,440,080 | 24,424,598 | 24,409,574 | 24,410,169 | 24,103,670 | 21,832,777 |
| **Free cash flow per share** | 0.15 | 0.36 | 0.61 | 0.73 | (0.13) | 1.63 | 0.26 | 0.45 |
| **Free cash flow - 12 month trailing** | 45,882 | 38,675 | 69,431 | 60,695 | 52,780 | 63,723 | 32,256 | 33,137 |

[1] *This financial measure is identified and defined under the section "NON-GAAP MEASURES."*

Management believes that the free cash flow (see "NON-GAAP MEASURES") can fluctuate significantly as a result of historical fluctuations in our business operations that occur on a quarterly basis as well as the resulting fluctuations in our trade receivables and inventory levels and the timing of the payments of trade payables and revolving floorplan facilities.

Changes in non-cash working capital consist of fluctuations in the balances of trade and other receivables, inventories, finance lease receivables, other current assets, trade and other payables, vehicle repurchase obligations and revolving floorplan facilities. Factors that can affect these items include seasonal sales trends, strategic decisions regarding inventory levels, the addition of new dealerships, and the day of the week on which period end cutoffs occur.

The following table summarizes the net increase (decrease) in cash due to changes in non-cash working capital for the three month periods ended March 31, 2016 and March 31, 2015.

| (in thousands of dollars) | January 1, 2016 to March 31, 2016 | January 1, 2015 to March 31, 2015 |
|---|---|---|
| Trade and other receivables | (25,254) | (12,615) |
| Inventories | (32,601) | (63,296) |
| Finance lease receivables | (600) | 583 |
| Other current assets | (2,030) | (4,278) |
| Trade and other payables | 6,438 | 10,156 |
| Vehicle repurchase obligations | (132) | 209 |
| Revolving floorplan facilities | 52,256 | 73,652 |
| | (1,923) | 4,411 |

### Adjusted Free Cash Flow

The Company has defined adjusted free cash flow to be cash flows provided by operating activities (before changes in non-cash operating working capital) less non-growth capital expenditures.

| (in thousands of dollars, except unit and per unit amounts) | Q1 2016 | Q4 2015 | Q3 2015 | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 | Q2 2014 |
|---|---|---|---|---|---|---|---|---|
| Cash provided by operating activities before changes in non-cash working capital | 8,754 | 11,242 | 23,082 | 22,386 | (5,221) | 19,125 | 23,192 | 16,497 |
| **Deduct:** | | | | | | | | |
| Purchase of non-growth property and equipment | (2,719) | (3,164) | (4,131) | (3,199) | (2,199) | (2,003) | (1,079) | (996) |
| **Adjusted free cash flow**[1] | 6,035 | 8,078 | 18,951 | 19,187 | (7,420) | 17,122 | 22,113 | 15,501 |
| Weighted average shares outstanding at end of period | 27,362,440 | 25,016,637 | 24,440,080 | 24,424,598 | 24,409,574 | 24,410,169 | 24,103,670 | 21,832,777 |
| **Adjusted free cash flow per share** | 0.22 | 0.32 | 0.78 | 0.79 | (0.30) | 0.70 | 0.92 | 0.71 |
| **Adjusted free cash flow - 12 month trailing** | 52,251 | 38,796 | 47,840 | 51,002 | 47,316 | 62,082 | 56,891 | 49,404 |

1 *This financial measure is identified and defined under the section "NON-GAAP MEASURES."*

Management believes that non-growth property and equipment is necessary to maintain and sustain the current productive capacity of the Company's operations and cash available for growth. Management believes that maintenance capital expenditures should be funded by cash flow provided by operating activities. Capital spending for the expansion of sales and service capacity is expected to improve future free cash and as such is not deducted from cash flow provided by operating activities before changes in non-cash working capital in arriving at adjusted free cash flow. Adjusted free cash flow is a measure used by Management in forecasting and determining the Company's available resources for future capital expenditure, repayment of debt, funding the future growth of the Company and dividends to Shareholders.

In the three month period ending March 31, 2016, the Company paid approximately $6.3 million in corporate income taxes and tax installments. Accordingly, this reduced our adjusted free cash flow by this amount. The Company expects the payment of corporate income taxes to have a more significant negative affect on free cash flow and adjusted free cash flow. See "RESULTS FROM OPERATIONS – Income Taxes" for further detail regarding the impact of corporate income taxes on cash flow.

### Adjusted Return on Capital Employed

The Company has defined Adjusted Return on Capital Employed to be EBIT (EBITDA, as defined in "NON-GAAP MEASURES", less depreciation and amortization) divided by Average Capital Employed in the Company (average of shareholders' equity and interest bearing debt, excluding floorplan financing, for the period, less the comparative adjustment defined below). Calculations below represent the results on a quarterly basis, except for the adjusted return on capital employed – 12 month trailing which incorporates the results based on the trailing 12 months for the periods presented.

| (in thousands of dollars, except unit and per unit amounts) | Q1 2016 | Q4 2015 | Q3 2015 | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 | Q2 2014 |
|---|---|---|---|---|---|---|---|---|
| EBITDA[1,2] | 21,010 | 23,524 | 29,487 | 30,730 | 13,890 | 26,043 | 31,895 | 21,702 |
| **Deduct:** | | | | | | | | |
| Depreciation of property and equipment | (4,954) | (5,176) | (5,063) | (4,461) | (4,160) | (4,423) | (4,139) | (2,550) |
| **EBIT[1,2]** | 16,056 | 18,348 | 24,424 | 26,269 | 9,730 | 21,620 | 27,756 | 19,152 |
| Average long-term debt | 300,520 | 312,471 | 314,443 | 277,571 | 239,251 | 204,514 | 240,799 | 211,903 |
| Average shareholder's equity | 510,595 | 481,112 | 447,774 | 439,711 | 436,262 | 440,513 | 326,410 | 205,613 |
| **Average capital employed[1]** | 811,115 | 793,583 | 762,217 | 717,282 | 675,513 | 645,027 | 567,209 | 417,516 |
| **Return on capital** | 2.0% | 2.3% | 3.2% | 3.7% | 1.4% | 3.4% | 4.9% | 4.6% |
| Comparative adjustment[3] | (13,191) | (13,191) | (17,264) | (17,264) | (17,264) | (17,264) | (15,951) | (15,951) |
| **Adjusted average capital employed[1]** | 797,924 | 778,354 | 744,953 | 700,018 | 658,249 | 628,418 | 551,258 | 401,565 |
| **Adjusted return on capital employed[1]** | 2.0% | 2.4% | 3.3% | 3.8% | 1.5% | 3.4% | 5.0% | 4.8% |
| **Adjusted return on capital employed - 12 month trailing** | 11.7% | 11.2% | 12.7% | 15.5% | 16.5% | 18.6% | 19.3% | 20.7% |

1 *These financial measures are identified and defined under the section "NON-GAAP MEASURES."*

2 *EBITDA and EBIT used in the calculation of Adjusted Return on Capital Employed is calculated using the financial results including non-controlling interests.*

3 *A comparative adjustment has been made in order to adjust for impairments and reversals of impairments of intangible assets. Due to the increased frequency of impairments and reversals of impairments, Management has provided an adjustment in order to freeze intangible assets at the pre-IFRS amount of $43,700. As a result, all differences from January 1, 2010 forward under IFRS have been adjusted at the post-tax rate at the time the adjustment to the intangible asset carrying amount was made. Management believes that the adjusted return on capital employed provides more useful information about the return on capital employed.*

Management believes that Adjusted Return on Capital Employed (see "NON-GAAP MEASURES") is a good measure to evaluate the profitability of our invested capital. As a corporation, Management of AutoCanada may use this measure to compare potential acquisitions and other capital investments against our internally computed cost of capital to determine whether the investment is expected to create value for our shareholders. Management may also use this measure to look at past acquisitions, capital investments and the Company as a whole in order to ensure shareholder value is being achieved by these capital investments. The decrease in adjusted return on capital employed - 12 month trailing over the past two years results from the increase in land and facility ownership, compounded by the reduced economic activity in 2015. Management expects this measure to return to normal as the economy improves and acquisitions are further integrated.

## 12. CRITICAL ACCOUNTING ESTIMATES AND ACCOUNTING POLICY DEVELOPMENTS

A complete listing of critical accounting policies, estimates, judgments and measurement uncertainty can be found in Notes 3 and 5 of the annual consolidated financial statements for the year ended December 31, 2015; there has been no significant change in our critical accounting policies, estimates, judgments and measurement uncertainty in Q1 2016.

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the IASB or International Financial Reporting Interpretations Committee ("IFRIC") that are not yet effective for the period ended March 31, 2016. A listing of the standards issued which are applicable to the Company can be found in Note 4 of the annual consolidated financial statements for the year ended December 31, 2015. No new standards or amendments were adopted for the period ended March 31, 2016.

## 13. DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

During the quarter ended March 31, 2016, there were no changes in the Company's disclosure controls or internal controls over financial reporting that materially affected, or would be reasonably likely to materially affect, such controls.

## 14. RISK FACTORS

We face a number of business risks that could cause our actual results to differ materially from those disclosed in this MD&A (See "FORWARD LOOKING STATEMENTS"). Investors and the public should carefully consider our business risks, other uncertainties and potential events as well as the inherent uncertainty of forward looking statements when making investment decisions with respect to AutoCanada. If any of the business risks identified by AutoCanada were to occur, our business, financial condition, results of operations, cash flows or prospects could be materially adversely affected. In such case, the trading price of our shares could decline. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also adversely affect our business and operations. A comprehensive discussion of the known risk factors of AutoCanada and additional business risks is available in our 2015 Annual Information Form dated March 17, 2016 available on the SEDAR website at www.sedar.com.

## 15. FORWARD LOOKING STATEMENTS

Certain statements contained in the MD&A are forward-looking statements and information (collectively "forward-looking statements"), within the meaning of the applicable Canadian securities legislation. We hereby provide cautionary statements identifying important factors that could cause our actual results to differ materially from those projected in these forward-looking statements. Any statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as "will likely result", "are expected to", "will continue", "is anticipated", "projection", "vision", "goals", "objective", "target", "schedules", "outlook", "anticipate", "expect", "estimate", "could", "should", "plan", "seek", "may", "intend", "likely", "will", "believes", "shall" and similar expressions are not historical facts and are forward-looking and may involve estimates and assumptions and are subject to risks, uncertainties and other factors some of which are beyond our control and difficult to predict. Accordingly, these factors could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements. Therefore, any such forward-looking statements are qualified in their entirety by reference to the factors discussed throughout this document.

In particular, material forward-looking statements in the MD&A include:

- the belief that, as the Company continues to grow, operating expenses as a percentage of gross profit should continue to improve as the Company achieves greater economies of scale;
- the impact of an increase or decrease of one new retail vehicle sold on estimated free cash flow;
- expectations to incur additional selling and administrative costs in the future to successfully integrate new dealerships;
- the belief that, if the Company can perform well, it will be able to build upon its current brand portfolios and hopefully gain the acceptance of other new manufacturers over time;
- commitments regarding future investments in additional GM dealerships;
- expectations to incur additional selling, general, and administrative costs in the future to facilitate the growth anticipated by the Company due to increased acquisition activity;
- estimates, intentions, and expectations regarding the capital plan, potential relocation of certain dealerships, dealership expansion needs, and Open Point opportunities;
- our belief that relocation of certain dealerships may provide incremental long-term earnings growth and better align some of our dealerships with the growth expectations of our manufacturer partners;
- the impact of dealership real estate relocations and purchases and its impact on liquidity, financial performance and the Company's capital requirements;
- our belief that under a high growth scenario, cash from operating activities may not be sufficient to meet future capital needs and the potential need to seek additional capital in the form of debt or equity;
- our belief that our available liquidity is sufficient to complete our current capital expenditure commitments and to execute on additional dealership acquisitions;
- the impact of a significant decline in sales as a result of the inability to procure adequate supply of vehicles and/or lower consumer demand on cash flows from operations and our ability to fund capital expenditures;
- our expectation to incur annual non-growth capital expenditures in an amount approximating our amortization of property and equipment reported in each period;
- our expectation that growth expenditures will provide additional future cash flows and future benefit;
- our expectation to increase annual capital expenditures and the reasons for this expected increase;
- the impact of working capital requirements and its impact on future liquidity;
- our belief that free cash flow can fluctuate significantly and the impact of these fluctuations on our operations and performance;
- our belief that maintenance capital expenditures should be funded by cash flow provided by operating activities;
- our potential use of Adjusted Return on Capital Employed as a measure for comparison and analysis;
- guidance with respect to future acquisition and Open Point opportunities;
- our assumption on the amount of time it may take for an acquisition or Open Point to achieve normal operating results;
- expectations and estimates regarding income taxes and their effect on cash flow and dividends;
- assumptions over non-GAAP measures and their impact on the Company;

- management's assumptions and expectations over the future economic and general outlook;
- the impact of economic stress on our compensation costs;
- belief that the recession experienced during fiscal 2008 and 2009 should not be used as a proxy to forecast an impact in 2016;
- the impact of economic uncertainty on the Company's acquisition opportunities;
- the impact of seasonality on financial performance;
- outlook regarding vehicle sales in Canada in 2016;
- the impact of the decline in the exchange rate of the Canadian dollar to the US dollar;
- expectations of capital costs related to currently awarded Open Points;
- expectations that re-imaging will attract more customers to its dealerships;
- our belief that improvements in technology and process in its parts and service departments will continue to produce increasingly positive results;
- estimates regarding additional legal and administration expense for each acquisition; and
- the impact on the Company as a result of the lower oil prices and any related expectations.

Although we believe that the expectations reflected by the forward-looking statements presented in this release are reasonable, our forward-looking statements have been based on assumptions and factors concerning future events that may prove to be inaccurate. Those assumptions and factors are based on information currently available to us about ourselves and the businesses in which we operate. Information used in developing forward-looking statements has been acquired from various sources including third-party consultants, suppliers, regulators, and other sources. In some instances, material assumptions are disclosed elsewhere in this release in respect of forward-looking statements. We caution the reader that the following list of assumptions is not exhaustive. The material factors and assumptions used to develop the forward-looking statements include but are not limited to:

- no significant adverse changes to the automotive market, competitive conditions, the supply and demand of vehicles, parts and service, and finance and insurance products;
- no significant construction delays that may adversely affect the timing of dealership relocations and renovations;
- no significant disruption of our operations such as may result from harsh weather, natural disaster, accident, civil unrest, or other calamitous event;
- no significant unexpected technological event or commercial difficulties that adversely affect our operations;
- continuing availability of economical capital resources; demand for our products and our cost of operations;
- no significant adverse legislative and regulatory changes;
- stability of general domestic economic, market, and business conditions;
- assumptions regarding other automobile manufacturer agreements; and
- assumptions regarding provincial government regulations.

Because actual results or outcomes could differ materially from those expressed in any forward-looking statements, investors should not place undue reliance on any such forward-looking statements. By their nature, forward-looking statements involve numerous assumptions, inherent risks and uncertainties, both general and specific, which contribute to the possibility that the predicted outcomes will not occur. The risks, uncertainties and other factors, many of which are beyond our control, that could influence actual results include, but are not limited to:

- rapid appreciation or depreciation of the Canadian dollar relative to the U.S. dollar;
- a sustained downturn in consumer demand and economic conditions in key geographic markets;

- adverse conditions affecting one or more of our automobile manufacturers;
- the ability of consumers to access automotive loans and leases;
- competitive actions of other companies and generally within the automotive industry;
- our dependence on sales of new vehicles to achieve sustained profitability;
- levels of unemployment in our markets and other macroeconomic factors;
- our suppliers' ability to provide a desirable mix of popular new vehicles;
- the ability to continue financing inventory under similar interest rates;
- our suppliers' ability to continue to provide manufacturer incentive programs;
- the loss of key personnel and limited management and personnel resources;
- the ability to refinance credit agreements in the future;
- changes in applicable environmental, taxation and other laws and regulations as well as how such laws and regulations are interpreted and enforced;
- risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; and
- the ability to obtain automotive manufacturers' approval for acquisitions.

The Company's most recent Annual Information Form and other documents filed with securities regulatory authorities (accessible through the SEDAR website www.sedar.com) describe the risks, material assumptions and other factors that could influence actual results and which are incorporated herein by reference.

Further, any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by applicable law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for Management to predict all of such factors and to assess in advance the impact of each such factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statement.

# 16. NON-GAAP MEASURES

Our MD&A contains certain financial measures that do not have any standardized meaning prescribed by Canadian GAAP. Therefore, these financial measures may not be comparable to similar measures presented by other issuers. Investors are cautioned these measures should not be construed as an alternative to net earnings (loss) or to cash provided by (used in) operating, investing, and financing activities determined in accordance with Canadian GAAP, as indicators of our performance. We provide these measures to assist investors in determining our ability to generate earnings and cash provided by (used in) operating activities and to provide additional information on how these cash resources are used. We list and define these "NON-GAAP MEASURES" below:

### EBITDA

EBITDA is a measure commonly reported and widely used by investors as an indicator of a company's operating performance and ability to incur and service debt, and as a valuation metric. The Company believes EBITDA assists investors in comparing a company's performance on a consistent basis without regard to depreciation and amortization and asset impairment charges which are non-cash in nature and can vary significantly depending upon accounting methods or non-operating factors such as historical cost. References to "EBITDA" are to earnings before interest expense (other than interest expense on floorplan financing and other interest), income taxes, depreciation, amortization and asset impairment charges.

### Adjusted EBITDA

Adjusted EBITDA is an indicator of a company's operating performance and ability to incur and service debt. The portion of share-based compensation related to changes in the share price and its impact on the Company's cash-settled portions of its share-based compensation programs, the revaluation of redemption liabilities, and the unrealized gain or loss on embedded derivatives are added back to EBITDA to get to adjusted EBITDA. The Company considers these expenses to be non-cash in nature. The Company believes adjusted EBITDA provides improved continuity with respect to the comparison of our operating results over a period of time.

### Adjusted net earnings and Adjusted net earnings per share

Adjusted net earnings and adjusted net earnings per share are measures of our profitability. Adjusted net earnings is calculated by adding back the after-tax effect of impairment or reversals of impairment of intangible assets, impairments of goodwill, the revaluation of redemption liabilities, the unrealized gain or loss on embedded derivatives, and the portion of share-based compensation related to changes in the share price and its impact on the Company's cash-settled portions of its share-based compensation programs. The Company considers these expenses to be non-cash in nature. Adding back these amounts to net earnings allows Management to assess the net earnings of the Company from ongoing operations. Adjusted net earnings per share is calculated by dividing adjusted net earnings by the weighted-average number of shares outstanding.

### EBIT

EBIT is a measure used by Management in the calculation of Return on capital employed (defined below). Management's calculation of EBIT is EBITDA (calculated above) less depreciation and amortization.

### Free Cash Flow

Free cash flow is a measure used by Management to evaluate its performance. While the closest Canadian GAAP measure is cash provided by operating activities, free cash flow is considered relevant because it provides an indication of how much cash generated by operations is available after capital expenditures. It shall be noted that although we consider this measure to be free cash flow, financial and non-financial covenants in our credit facilities and dealer agreements may restrict cash from being available for distributions, re-investment in the Company, potential acquisitions, or other purposes. Investors should be cautioned that free cash flow may not actually be available for growth or distribution of the Company. References to "Free cash flow" are to cash provided by (used in) operating activities (including the net change in non-cash working capital balances) less capital expenditure (not including acquisitions of dealerships and dealership facilities).

### Adjusted Free Cash Flow

Adjusted free cash flow is a measure used by Management to evaluate its performance. Adjusted free cash flow is considered relevant because it provides an indication of how much cash generated by operations before changes in non-cash working capital is available after deducting expenditures for non-growth capital assets. It shall be noted that although we consider this measure to be adjusted free cash flow, financial and non-financial covenants in our credit facilities and dealer agreements may restrict cash from being available for distributions, re-investment in the Company, potential acquisitions, or other purposes. Investors should be cautioned that adjusted free cash flow may not actually be available for growth or distribution of the Company. References to "Adjusted free cash flow" are to cash provided by (used in) operating activities (before changes in non-cash working capital balances) less non-growth capital expenditures.

### Absorption Rate

Absorption rate is an operating measure commonly used in the retail automotive industry as an indicator of the performance of the parts, service and collision repair operations of a franchised automobile dealership. Absorption rate is not a measure recognized by GAAP and does not have a standardized meaning prescribed by GAAP. Therefore, absorption rate may not be comparable to similar measures presented by other issuers that operate in the retail automotive industry. References to ''absorption rate'' are to the extent to which the gross profits of a franchised automobile dealership from parts, service and collision repair cover the costs of these departments plus the fixed costs of operating the dealership, but does not include expenses pertaining to our head office. For this purpose, fixed operating costs include fixed salaries and benefits, administration costs, occupancy costs, insurance expense, utilities expense and interest expense (other than interest expense relating to floor plan financing) of the dealerships only.

### Average Capital Employed

Average capital employed is a measure used by Management to determine the amount of capital invested in AutoCanada and is used in the measure of Return on Capital Employed (described below). Average capital employed is calculated as the average balance of interest bearing debt for the period (including current portion of long term debt, excluding revolving floorplan facilities) and the average balance of shareholders equity for the period. Management does not include future income tax, non-interest bearing debt, or revolving floorplan facilities in the calculation of average capital employed as it does not consider these items to be capital, but rather debt incurred to finance the operating activities of the Company.

### Adjusted Average Capital Employed

Adjusted average capital employed is a measure used by Management to determine the amount of capital invested in AutoCanada and is used in the measure of Adjusted Return on Capital Employed (described below). Adjusted average capital employed is calculated as the average balance of interest bearing debt for the period (including current portion of long term debt, excluding revolving floorplan facilities) and the average balance of shareholders equity for the period, adjusted for impairments of intangible assets, net of deferred tax. Management does not include future income tax, non-interest bearing debt, or revolving floorplan facilities in the calculation of adjusted average capital employed as it does not consider these items to be capital, but rather debt incurred to finance the operating activities of the Company.

**Return on Capital Employed**

Return on capital employed is a measure used by Management to evaluate the profitability of our invested capital. As a corporation, Management of AutoCanada may use this measure to compare potential acquisitions and other capital investments against our internally computed cost of capital to determine whether the investment shall create value for our shareholders. Management may also use this measure to look at past acquisitions, capital investments and the Company as a whole in order to ensure shareholder value is being achieved by these capital investments. Return on capital employed is calculated as EBIT (defined above) divided by Average Capital Employed (defined above).

**Adjusted Return on Capital Employed**

Adjusted return on capital employed is a measure used by Management to evaluate the profitability of our invested capital. As a corporation, management of AutoCanada may use this measure to compare potential acquisitions and other capital investments against our internally computed cost of capital to determine whether the investment shall create value for our shareholders. Management may also use this measure to look at past acquisitions, capital investments and the Company as a whole in order to ensure shareholder value is being achieved by these capital investments. Adjusted return on capital employed is calculated as EBIT (defined above) divided by Adjusted Average Capital Employed (defined above).

**Cautionary Note Regarding Non-GAAP Measures**

EBITDA, EBIT, Free Cash Flow, Absorption Rate, Average Capital Employed, Return on Capital Employed, Adjusted Average Capital Employed and Adjusted Return on Capital Employed are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP. Investors are cautioned that these non-GAAP measures should not replace net earnings or loss (as determined in accordance with GAAP) as an indicator of the Company's performance, of its cash flows from operating, investing and financing activities or as a measure of its liquidity and cash flows. The Company's methods of calculating EBITDA, EBIT, Free Cash Flow, Absorption Rate, Average Capital Employed, Return on Capital Employed. Adjusted Average Capital Employed and Adjusted Return on Capital Employed may differ from the methods used by other issuers. Therefore, the Company's EBITDA, EBIT, Free Cash Flow, Absorption Rate, Average Capital Employed, Return on Capital Employed, Adjusted Average Capital Employed and Adjusted Return on Capital Employed may not be comparable to similar measures presented by other issuers.

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