



Insurance Quarterly Report

QUARTER 3 2016

Insurance Auto Auctions, Inc. (IAA) helps insurance carriers dispose of total loss vehicles via a dual live and live-online auction format. Insurance vehicles sold through IAA's auctions display a range of loss types, including collision, storm or flood damage, theft recovery and more. These vehicles are purchased by public and professional buyers for a variety of purposes, including dismantling/recycling, resale, exporting and personal use.

The Insurance Quarterly Report provides an analysis of auction results for vehicles in this category, as well as an overview of economic and industry factors that influence auction returns. These include:

- Whole Crushed Auto-Body Prices
- Used-Car Price Index
- Vehicle Parts and Equipment Consumer Price Index
- Metals Prices
- New-Vehicle Sales and Total Miles Driven
- Gasoline Prices



Whole Crushed
Auto-Body Prices



Aluminum



Parts Prices



Palladium



Total Miles
Driven



Platinum

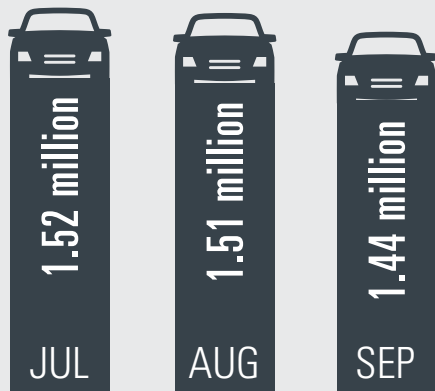


Overview Of The Automobile Industry

Auto sales have enjoyed a steady pace through the past few years, but lost some steam in the third quarter of 2016, with new-vehicle sales dropping 1.2% compared to last year. However, that steady pace culminated in 2015's record-breaking sales figures, so even this quarter's slight dip indicated that sales are historically strong. There's no need to worry about how much time Americans spend behind the wheel either, as a robust economy and low gas prices contributed to a 2% increase in total miles driven from the same quarter a year prior.

Cheap interest rates, longer loan terms and an increase in leasing kept customers coming to the lots.¹ To keep them coming, automakers placed a heavy emphasis on rebates and incentives, and relied heavily on their fleet customers like rental car companies, government agencies and commercial clients.² Sweetened incentives aren't forecast to lighten anytime soon – North American car and light-truck production reached an August record, and the potential supply glut may take a hit on new-vehicle prices. Additionally, automakers had to combat a growing supply of late-model used cars entering the market after their leases expired, as buyers could decide to forego purchasing a new vehicle in favor of paying less for a used vehicle in good condition.³

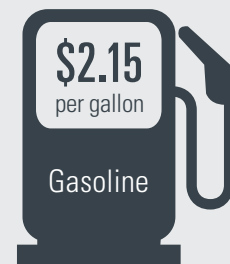
New-Vehicle Sales



Total Miles Driven

Year-over-Year
2.0%

Economic Drivers



Top Movers



6.7%



2.6%



1.8%

Insurance Carrier Vehicles

In the third quarter of 2016, the average actual cash value (ACV) of insurance vehicles rose 1.2% compared to the last quarter, but dropped 0.5% year-over-year. Average ACV, as a representation of a vehicle's estimated value in an undamaged state, serves as a benchmark for the general quality of insurance vehicles that make their way to the auction. The year-over-year slip in ACV is somewhat surprising, considering that average age and mileage fell on a yearly basis, and both typically have an inverse relationship with the ACV measurement.

Average
ACV

Year-Over-Year

0.5% 

Quarter-to-Quarter

1.2% 

Average
Age

Q3 2015

9.3
YEARS

Q3 2016

9.1
YEARS

Average
Mileage

Year-Over-Year

3.0% 

Quarter-to-Quarter

1.5% 

Source: IAA

Scrap Metal: Whole Crushed Auto-Body Prices

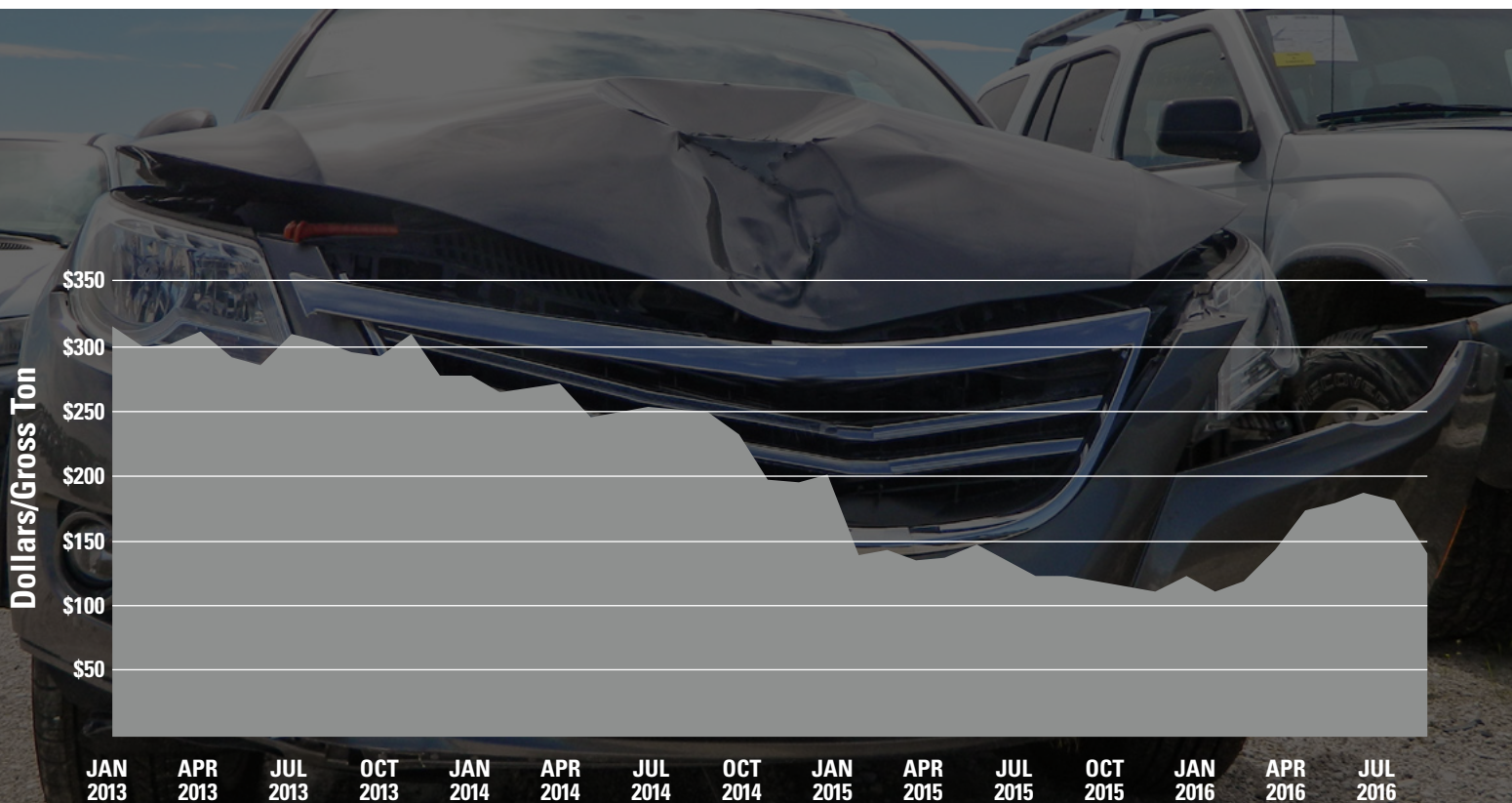
Despite a rally in whole crushed auto-body prices in the first half of the year, the momentum was halted by the third quarter of 2016. On a monthly basis, average prices fell 2.5% in August and then 22.4% in September. China continued to flood the international marketplace with cheap steel, as an increase in output and lackluster demand contributed to fallen prices.⁴ Average whole crushed auto-body prices did rise 33.6% from the same period in the year prior, but obscured the fact that whole crushed auto-bodies saw abnormally low prices in 2015. Even with this increase, average whole crushed auto-body prices remain near historic lows.

Year-Over-Year

33.6% 

Quarter-to-Quarter

3.1% 



Source: American Recycler

Used-Car Price Index

Average used-car prices remained higher on an annual basis in the third quarter, rising sequentially in July, declining seasonally in August and leveling out in September. According to Tom Kontos of ADESA Analytical Services, the 5.7% year-over-year gain for the quarter came on the strength of truck pricing and an inventory mix that favored younger, lower-mileage, higher-priced off-lease supply.⁵ Unlike trucks, the average price of cars was little changed year-over-year and actually declined in August. Retail used-vehicle sales remained strong during the quarter, providing demand-side support for wholesale values, though there was some tapering in retail demand in September.⁶



Source: ADESA Analytical Services

Vehicle Parts And Equipment Consumer Price Index

The vehicle parts and equipment consumer price index was likely influenced by low gas prices and unemployment rates, both of which contributed to the high number of total miles driven and in turn increased the demand for auto parts and equipment.⁷ In both July and August, the index increased from the same period a year ago. However, the index stumbled in September, dropping 0.6% and exhibiting the first time the index has fallen since the U.S. Bureau of Labor Statistics started tracking it in 2006. It's still unknown whether this decrease was a one-time event or indicative of an ongoing trend.



Source: Bureau of Labor Statistics

Gasoline

After a five-month rally, oil and gas prices sank back down. Concerns about oversupply and continued high production pushed U.S. oil prices to a three-month low in July, and continued to be down through August and September as well. Brent crude – a benchmark for international oil prices – hovered above \$40 a barrel in July as global production continued to rise.⁸ The Energy Information Administration expects gasoline prices to sit below \$2 a gallon and perhaps drop even further amidst concerns that refiners produced a glut of oil that could persist despite a strong driving demand.⁹

Year-Over-Year

13.7%

Quarter-to-Quarter

1.4%



Metals

Aluminum

There were predictions that China would ramp up aluminum production in the second half of the year. Well, it hasn't happened yet. In fact, Chinese aluminum saw lower-than-expected production that contributed upward pressure to prices.¹⁰ This was further assisted by healthy Chinese demand for the metal, fueled by increased credit and construction. Additionally, thermal coal prices saw a 60% rise this year. Since this energy accounts for a significant cost for aluminum production, idled plants are unlikely to restart despite the boost in demand, which could lead to a sustained rally for this metal.¹¹

Year-Over-Year
1.7%

Quarter-to-Quarter
3.1%

Source: World Bank

Platinum

In the third quarter of 2016, industrialized nations experiencing lackluster growth saw investors eager to purchase assets like precious metals as an alternative to bonds and stocks.¹² Enter platinum, which saw quite the healthy start to the second half of the year with increases of 8.1% quarterly and 10.2% year-over-year. While demand surged, concerns about a potential mineworkers' strike that could lead to reduced production also pushed up platinum prices.¹³ Not to mention, the value of the South African rand is leading gains in emerging-market currencies and is another contributing factor to the risen value of platinum, as a stronger local currency makes the metal more expensive.¹⁴

Year-Over-Year
10.2%

Quarter-to-Quarter
8.1%

Source: Johnson Matthey

Palladium

Move aside, aluminum and platinum. Palladium soared 19.0% compared to the last quarter and 9.8% year-over-year to become the best-performing precious metal for the third quarter of 2016.¹⁵ Similar to platinum, palladium values rose amidst similar concerns about output production and worker strikes in Russia and South Africa. Palladium is also an option for investors looking for a safe-haven alternative to bonds and stocks. Chinese vehicle sales continue to be robust and are expected to grow as consumers take advantage of a soon-to-expire tax cut.¹⁶ All of these factors added to concerns about a reduction in palladium supply and consequently drove higher palladium prices.

Year-Over-Year
9.8%

Quarter-to-Quarter
19.0%

Source: Johnson Matthey

U.S. Dollar

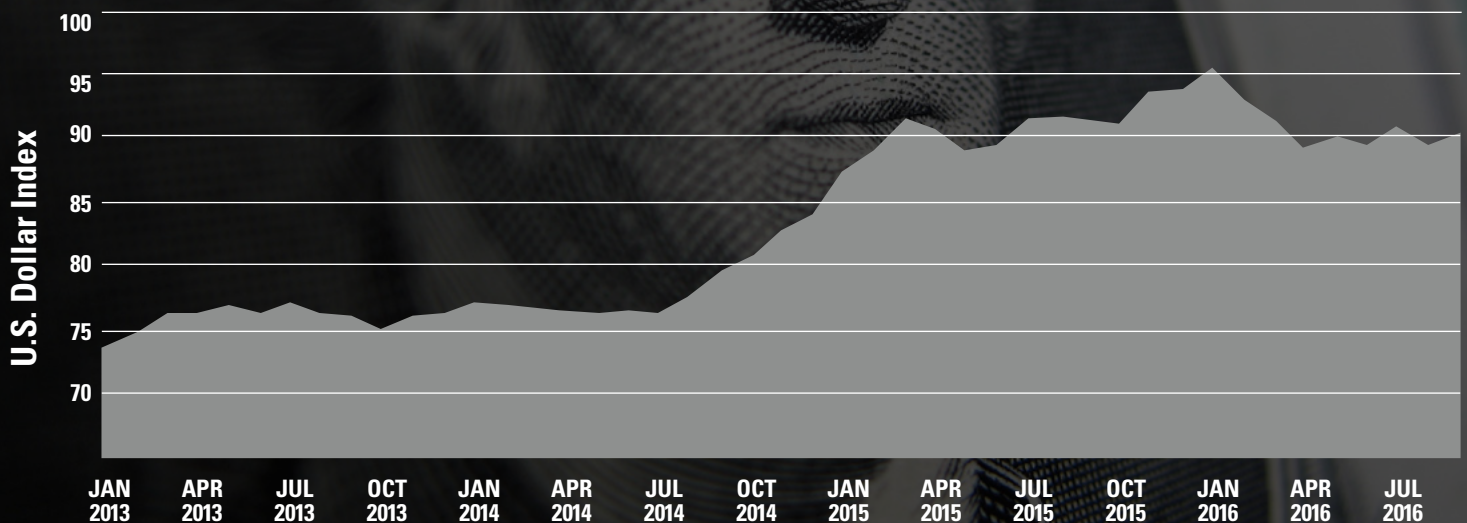
Will they, or won't they? Making the comparison on a quarterly basis, the U.S. dollar rode a slight increase on the backs of investor belief that the Federal Reserve would increase short-term rates at the September Federal Open Market Committee meeting.¹⁷ Since higher rates make dollar-denominated assets more attractive, bets on a stronger dollar were abundant. However, the U.S. dollar slipped 1.7% compared to last year. While the dollar did see a swift appreciation last year thanks to a quicker-than-expected economic recovery and loose monetary policy in Japan and the Eurozone, the current decrease signaled uncertainty surrounding the U.S. presidential election and reduced inflation expectations. With such little pressure of inflation, the Federal Reserve may actually decide to leave interest rates on hold.¹⁸

Year-Over-Year

1.7%

Quarter-to-Quarter

0.8%



Source: Federal Reserve Bank of St. Louis

€ Euro

The value of the euro shrunk this quarter in comparison to a strong U.S. dollar, fighting against the steady performance of the U.S. labor market and economic outlook, as well as the probability of a rate increase in the coming months.¹⁹ Additionally, low interest rates in Europe and quantitative easing has made U.S. dollar-denominated assets more attractive, further decreasing demand for the euro.²⁰

Year-Over-Year
0.3% 

Quarter-to-Quarter
1.2% 

Source: OANDA Corp.

\$ Canadian Dollar

Given that Canada is a significant oil-exporting country, the slide in crude oil values triggered a depreciation of the Canadian dollar against the U.S. dollar.²¹ What's more, uncertainty surrounding a break in or renegotiation of the North American Free Trade Agreement (NAFTA) as well as the Trans-Pacific Partnership weighed on the loonie, as these policies could significantly impact Canadian trade.²²

Year-Over-Year
0.2% 

Quarter-to-Quarter
1.2% 

Source: OANDA Corp.

\$ Mexican Peso

The Mexican peso dropped 14.2% against the U.S. dollar, with indications that the U.S. presidential election had a significant impact on the value of Mexico's currency. Contributing to the depreciation of the peso is the concern surrounding a renegotiation or termination of NAFTA, which could significantly impact the Mexican economy. With a potential raise in tariffs on Mexican imports and a tax set on remittances, investors are wary about Mexico's economic future.²³

Year-Over-Year
14.2% 

Quarter-to-Quarter
3.6% 

Source: OANDA Corp.

¥ Japanese Yen

In early August, the yen benefited after Japan's government – in an effort to boost the economy – announced an additional 4.6 trillion yen (\$45 billion) in fiscal spending by the end of the year. Additionally, the yen appreciated against the dollar as a result of Japan's lower-than-expected ease of monetary policy and sustained economic growth.²⁴

Year-Over-Year
16.2% 

Quarter-to-Quarter
5.2% 

Source: OANDA Corp.

References

1. [Mile Colias and Anna Steele, "Auto Sales Starting to Hit the Brakes," *The Wall Street Journal*, September 1, 2016.](#)
2. [Anna Steele and John D. Stoll, "U.S. Auto Sales Slip in September," *The Wall Street Journal*, October 3, 2016.](#)
3. [John D. Stoll, "North American Light-Vehicle Production Soars in August, But Incentives Are Rising," *The Wall Street Journal*, September 21, 2016.](#)
4. [Anil Mathews, "Chinese steel output rebounds in August; Demand limps," *Scrap Monster*, September 16, 2016.](#)
5. [Tom Kontos, "July 2016 Kontos Kommentary," ADESA.](#)
6. [Tom Kontos, "September 2016 Kontos Kommentary," ADESA.](#)
7. [Dan Moskowitz, "AutoZone Upgraded for 3 Key Reasons \(AZO\)," *Investopedia*, September 27, 2016.](#)
8. [Timothy Puko, "U.S. Oil Prices Hit 3-Month Lows on Growing Oversupply Concerns," *The Wall Street Journal*, July 26, 2016.](#)
9. [Nicole Friedman, "EIA: Gasoline Prices to Fall Below \\$2-a-Gallon Later This Year," *The Wall Street Journal*, August 9, 2016.](#)
10. [Raul de Frutos, "Aluminum Back to \\$1,700 per Metric Ton?" *Shanghai Metals Market*, October 11, 2016.](#)
11. [Yuliya Fedorinova, "Aluminum's Rally Can Last on Higher China Costs, Rusal Says," *Bloomberg Markets*, October 12, 2016.](#)
12. [Meera Shawn, "Reviewing the Spread between Gold and Platinum for Guidance," *Market Realist*, September 20, 2016.](#)
13. [Andrew Topf, "South Africa girding for another platinum strike," *Mining.com*, July 10, 2016.](#)
14. [Eddie Van Der Walt, "Platinum Rises Most in Months as Rand Boots Cost Outlook," *Bloomberg Markets*, September 5, 2016.](#)
15. [Luzi-Ann Javier, "Palladium Tops Precious Metals Gains as Chinese Sales Advance," *Bloomberg*, July 31, 2016.](#)
16. [Bloomberg News, "China Auto Sales Rise 24.5% on Rush to Beat Expiring Tax Cut," *Bloomberg Markets*, September 7, 2016.](#)
17. [Ira Iosebashvili and Chelsey Dulaney, "Traders Bet Dollar Will Keep Climbing," *The Wall Street Journal*, August 29, 2016.](#)
18. [Eric Morath, "U.S. Consumer Prices Unchanged as Inflation Remains Muted," *The Wall Street Journal*, August 16, 2016.](#)
19. [Ira Iosebashvili, "Dollar Gains Against Major Currencies After Yellen Speech," *The Wall Street Journal*, August 29, 2016.](#)
20. [Elaine Moore, "QE purchases near record even as doubts grow," *Financial Times*, October 4, 2016.](#)
21. [Christopher Murphy, "Why the U.S. Dollar Will Continue Marching Higher Vs. The Canadian Dollar," *Seeking Alpha*, August 2, 2016.](#)
22. [Matt Lundy, "How a Trump Presidency Would Impact Canada's Economy," *The Globe and Mail*, August 23, 2016.](#)
23. [Anthony Harrup, "After Turbulent Third Quarter, Mexican Peso Faces Another Stormy Quarter," *The Wall Street Journal*, September 30, 2016.](#)
24. [Rebecca Spalding and Lananh Nguyen, "Currency Traders Had Divergence Bet Backward, Yen's Surge Shows," *Bloomberg Markets*, August 2, 2016.](#)

Overview of IAA

Insurance Auto Auctions, Inc. (IAA) is the leading live and live-online salvage vehicle auction company and a business unit of KAR Auction Services (NYSE: KAR). With 170+ auction facilities — the largest footprint in North America — IAA provides registered buyers from more than 110 countries the opportunity to bid on and purchase vehicles from a comprehensive group of sellers, including insurance companies, fleet and rental companies, financing companies, charitable organizations and the general public. Through its weekly auctions, IAA has sold millions of vehicles, offering towing, financing and titling services. IAA leverages its business model to assist charitable organizations in the U.S. through its One Car One Difference® program. To date, IAA has provided millions of dollars in additional funding to charities by assisting in the processing of donated vehicles. Learn more about the program by visiting 1Car1Difference.com. With a talented team of more than 2,700 employees, IAA is committed to technological innovation and providing its customers the highest level of service in the salvage auto industry. To learn more, visit IAA-Auctions.com, and follow IAA on [Facebook](#), [Twitter](#) and [LinkedIn](#).



About the Author

Meggan O'Malley is manager of sales analysis at Insurance Auto Auctions, Inc. (IAA). Mrs. O'Malley leads the organization's efforts in monitoring and reporting on customer performance and analyzing industry trends. Mrs. O'Malley joined IAA in 2007 and held several positions before assuming her current responsibilities. Prior to joining IAA she served as a financial analyst at Grant Thornton, one of the world's leading organizations of independent audit, tax and advisory firms. Mrs. O'Malley holds bachelor's degrees in finance and marketing from Marquette University, and an MBA with a concentration in management from Argosy University.

The auto salvage industry as discussed in this document refers to the industry as experienced by IAA. IAA does not possess data on the performance of other salvage companies; therefore, the analyses are based on how different economic factors affect the performance of vehicles sold through IAA's auctions.

The statements contained in this report and statements the company may make orally in connection with this report that are not historical facts are forward-looking statements. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from the results projected, expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include those matters disclosed in KAR Auction Services, Inc.'s Securities and Exchange Commission filings. KAR and IAA do not undertake any obligation to update any forward-looking statements.

IAA-Auctions.com