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# EDITED TRANSCRIPT

CDK.OQ - Q3 2021 CDK Global Inc Earnings Call

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**OVERVIEW:**

Co. reported 3Q21 revenue of $433m and non-GAAP adjusted EPS of $0.69. Expects 2021 revenues to be $1.66-1.70b and non-GAAP adjusted EPS to be $2.50-2.65.



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## PRESENTATION

**Operator**

Good day, and thank you for standing by. Welcome to the Q3 2021 CDK Global, Inc. Earnings Conference Call. (Operator Instructions)

I would now like to hand the conference over to your speaker today, Julie Schlueter, Director of Investor Relations. Please go ahead.

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**Julie Schlueter** - *CDK Global, Inc. - Director of IR*

Thank you, and good afternoon. I'd like to welcome you to our Third Quarter Fiscal '21 Earnings Call. Joining me on today's call are CEO, Brian Krzanich; Chief Operating Officer, Joe Tautges; and our CFO, Eric Guerin. Following their prepared remarks, we'll be taking questions. Our earnings press release was issued after the close of the market today and is posted on our Investor Relations website at investors.cdkglobal.com, where this call is being simultaneously webcast.

In addition, our website also includes an updated Excel schedule of supplemental financial information and a copy of our results presentation that we will be referencing during our prepared remarks. Throughout today's call, we will be discussing our continuing operations only, which do not include the International business, which is presented as discontinued operations. Unless otherwise noted, all references to financial amounts during our call are on a non-GAAP adjusted basis.

Reconciliations of adjusted amounts to the most directly comparable GAAP amounts are included in this afternoon's press release. Please also note that all growth percentages refer to the year-over-year change for that period, unless otherwise specified. I would like to remind everyone that remarks made during this call may contain forward-looking statements. These statements involve risks and uncertainties as further detailed in our filing with the SEC, which could cause the actual results to differ materially from those mentioned in the forward-looking statements.

With that, it is my pleasure to turn the call over to Brian.

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Thank you, Julie, and welcome, everybody. I'd like to start today by saying that I'm very pleased with the execution and performance of the organization during our fiscal third quarter. The revenue for the quarter was $433 million, up $7 million year-over-year. And EBITDA for the quarter was $166 million at a margin of 38.4% and an EPS of $0.69. And these results matched our forecast and reflect the successful addition of new customers as well as existing customers rewarding us with more of their business.

Now looking at some of the trends within the industry. We continue to see heightened consolidation activity in the retail automotive market, where the larger dealers are continuing to get bigger, and that plays to our strength. While we expect this tailwind to continue into 2022, led by some of our top customers who have announced record expansion plans and dealers are facing tight inventory levels for new retail vehicles due to reduced production caused by a part of a chip shortage, but they are working through these, and as a result, are seeing a lot more activity in used vehicle sales, with both sales and prices of used vehicles up in the quarter. The overall sales activity can be seen on Slide 4 of our results presentation, which shows the recent quarter had the highest average sales over the 5-quarter period. Our execution for the quarter was strong, and many of the important indicators of the health of our company and customers' confidence in our future direction were positive.

In particular, we saw significant site growth, exceeding 9,000 auto sites for the first time since 2017 and the largest quarterly increase since 2016. The site growth was up 94 sites for auto, 9 straight quarters of year-over-year growth and up 137 in adjacencies. Equally as important, revenue per site reached all-time highs for both auto and adjacencies, up 2% and 4%, respectively. And this is based on the strength of our DMS and core solutions like Service and CRM. And as we continue to grow each quarter, we expect to achieve more record highs.

As you are aware, we successfully closed the $1.45 billion sale of our International business during the third quarter, and I'm pleased with the recognition of the value we received, which equated to a 15x multiple. The finance team has done a great job at putting the proceeds of the sale to work for our shareholders. We've taken our debt down by $1.1 billion and have lowered our leverage ratio and interest expenses. We are reserving some of the cash for potential investment opportunities, which could include acquisitions or other strategic activities. We're planning on returning capital to our shareholders in the form of stock purchases. And Eric will provide more details about this in his remarks.

We believe this balanced approach will provide our shareholders with continued value well into the future. And with a view of the future, I'd like to announce that we plan to host an investor event sometime after our fiscal year-end results, where we can go into detail about our growth plans and investment strategy. But I'd like to touch on a few important initiatives here today.

As you know, our transformation journey started 2 years ago as we launched a dramatic, more customer-focused approach to our service and support. At the same time, we directed our investment efforts on modernizing our products and underlying technology with a focus on building a modern platform for integrations via Fortellis and a platform of managing and providing insights from the wealth of data across our industry. Together with our customer-focused approach, our unique combination of domain expertise, our market leadership, workflow enablement through Fortellis and data insights from our Neuron platform distinguish us in the industry.

Our 3-year strategic investment program is on track, and we're now starting to see the results of these efforts in the growth of the business. We've made significant progress in modernizing our software and expect the continued rollouts of our more customer-focused enhancements in 2022, such as new user interfaces, enhanced workflows and the use of data-driven insights to deliver truly differentiated value. Our Fortellis Automotive Commerce Exchange platform had over 27 million transactions during the quarter and is on track to reach our goal of over 100 million transactions for the full year. Next year, we're setting our expectations at significant multiples of this level. And as more developers and independent software vendors embrace Fortellis, we anticipate a compounding network effect through this connected community.

We've seen the pace of innovation from our Neuron platform further increase as a result of our Square Root acquisition during the quarter. The integration of the company is going well, and we're already seeing benefits of the larger team of data scientists.

But beyond our current investments, we're always studying and anticipating the longer-term trends impacting our industry. And as a market leader, we have both a responsibility and an opportunity to help guide dealers and OEMs through all the industry shifts that are occurring and provide the tools they need. I'm especially excited about the evolution of the car buying experience and the trends toward modern digital retailing. Dealers



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are realizing that their true competitive advantage lies in providing a meaningful customer experience, one that is personalized, easy and cohesive across all channels and interactions.

We see this trend extending to all touch points a dealer has with their customers, from marketing and sales to service and repair. We believe we are uniquely positioned to connect all of the pieces together. And with our industry-leading DMS and CRM, along with our digital retailing solutions and enhancements to products like CDK Service, we have the building blocks to win big in this market. We have ambitious plans for the rest of the fiscal year and through 2022.

We continue to invest in our products, our platforms and people to support our customers. We're excited about the trends in the industry and our ability to capture more of this attractive market. While no one can predict when the world will completely return to normal, we see upside opportunities for our customers and for our business. We're cautiously optimistic in our outlook for next quarter, and Eric will provide more details on our full year guidance.

And before turning it over to Joe, I'd like to personally thank the employees of CDK for their dedication and flexibility through this year.

Their high level of performance and successful management of our business has never been more important, and I'm truly grateful for all their hard work, commitment and enthusiasm.

So now I'll turn it over to Joe for the business highlights.

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Thanks, Brian. Now that I've completed my first 90 days in the COO role, I'd like to share how excited I am about the momentum that we're building across both sales and operational execution and how we continue to lean in to our focused and disciplined approach to the business. We're winning because our customers are at the center of everything we do. And as Brian highlighted, we are investing heavily in technology to help both dealers and OEMs drive success in their businesses.

Let me first start with sales and a view into our customer base and where we are seeing progress in what solutions are resonating with our customers. This quarter, we're seeing continued momentum in sales to larger dealer groups, primarily arising from 3 different avenues.

First, we are gaining net new business as a result of additional dealership wins, coupled with the highest retention level we've had in several years across our book of business. Second, we're seeing accelerated consolidation activity within the dealership industry with some of our largest customers leading the way, and they're selecting CDK as their integration partner of choice. And third, our sales team, as the trusted partner of our dealerships, is bringing our key strategic applications to help dealers improve their business and further increase our penetration.

As proof points of our commitment to provide the best capabilities and service to our customers, we won back several dealers this quarter, including a 20-plus group that returned to CDK after 18 months on a competitive system and a 5-plus site group from 2 years ago. In April, we also renewed a 60-month contract with one of our largest enterprise-class dealerships, who has been working with CDK on integrating even more sites through their consolidation strategy.

Now let me talk about what I am seeing in our portfolio as it relates to the 1 to 2 dealer sites. Our customer-first orientation is resulting in the highest retention we've seen in that portion of the portfolio over the last year and is attracting many new dealers to adopt our solutions. We've been able to put together quite compelling software offerings that are tailored to the small franchise dealer groups and include our fit-for-purpose Drive DMS solution. And it's resonating with that group, and we're winning.

Moving on to our installation and customer support operations. We've been laser-focused on improvements in installation quality, customer service, tech support and resolution wait times. My leadership team and I are committed to be #1 in this industry for providing the highest quality delivery and support for our solutions. This quarter, we achieved a significant increase in our customer delivery NPS score due to install quality improvements, such as providing dealers with the ability to recreate and view deals from prior systems and to take multiple test drives throughout the install





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process. We had a very good quarter for installation. And across our core strategic products, we installed over 10% more than a year ago, driven by significant increases in Service and Doc Cloud solutions.

Now I'd like to move on to a deeper dive into the Q3 business highlights of our portfolio of products. As you know, we have a large portfolio of products, several technology targets going on at CDK. And my focus is on how we take the best of what we are building and what items are moving the needle the most for our dealers and OEMs. Then we're prioritizing successfully launching those new products, enhancements and capabilities, such as the next versions of our key solutions and new apps launched as part of Fortellis and Neuron, like CDK OnePay. The outcome of all of this is delivering better results for our OEM and dealer partners as well as accelerating revenue and profit growth for CDK.

I'm talking more about our strategy and priorities for execution at our upcoming investor event. But I'd like to highlight a few of the product enhancements we made recently. As Brian mentioned, we're investing in Fortellis and Neuron to provide value-added integrations and intelligence within our products (technical difficulty) which are then allowing dealers to better serve consumers and increase their profitability.

We've also made investments in our core software to improve ease of use. For example, we're introducing enhancements to our service application, focusing on the most used functions. We've upgraded to a new modern user interface, the majority of workflows technicians use each day to manage a repair order and that their customers use to make appointments with the dealerships.

By modernizing these key functions, we are making it easier and more time-efficient for dealers and customers to complete the entire repair order process. Our #1 focus across our software portfolio is to make it easy to use with a modern experience and seamless workflows. And in fiscal year '22, you will see much more coming out across our portfolio. All these innovations are helping to further strengthen our core business and, together with our customer-centric focus, are resulting in solid performance.

Focusing on the current quarter. I'd like to walk through the results of our core products, starting with the DMS. Auto DMS sites for the quarter were up 94, the strongest increase since Q1 of 2016 and represents over 1% growth, our ninth straight quarter of year-over-year growth. It also represents a 45-site increase over last quarter and reflects the acceleration of our Drive DMS product, improvements in our customer satisfaction scores, which are yielding strong retention rates, the highest level we've seen in several years. This momentum, combined with our Q3 sales performance, gives us confidence that this cycle of trend will continue into Q4.

As I said earlier, we continue to see robust growth from our larger dealers. And while we are seeing improvements in the 1 to 2 sites, they are declining, and I believe this is reflective of the broader industry trend. Auto revenue per site rose 2%, with solid growth in 3-plus auto site dealers that is partially offset by modest declines in revenue from 1 to 2 site auto dealers. We think our strong sales performance will help us continue to build on this progress.

Moving on to our applications business. We believe our core applications provide a strong path to sustain growth within our business. Our penetration rates offer ample opportunities to work with our customers to provide more value-added solutions that will help their workflow efficiency and profitability. Our CRM solution continues to do well, both within our DMS dealer base as well as agnostically with non-CDK dealers. Penetration rates are in the mid- to high 30s within our auto DMS dealer base. Our Service solutions showed solid improvements during the quarter. And given the recent technology enhancements that are currently in the early stages of rollout, we believe our penetration rates will continue to demonstrate meaningful growth.

My discussion of our performance wouldn't be complete without highlighting our successful adjacency business, which delivered another excellent quarter of results. Sites and revenue per site were both at an all-time record high levels again this quarter. Sites were up 137, or 3%, and revenue per site was up 4%, fueled in part by improvements in the heavy equipment space. As you can see in the presentation charts, both the marine and power sports industry sales have outpaced last year.

We also recently announced that we'll be making our ELEAD CRM solution available to heavy equipment dealers in the construction and agricultural space, and we expect continued healthy growth contributions from the adjacency business as we move into next year. With this strong foundational subscription base, we continue to look beyond our own current capabilities to see what's next on the horizon for all of our customers. Our digital





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retailing initiatives and focus on CRM and Service, coupled with our technology enhancements, provide a formidable bundle of solutions to capitalize on developing industry trends.

Our priorities going forward reflect our goal to remain the leader -- the leading provider of solutions to our dealer and OEM customers and to accelerate upon the solid foundational drivers of cycle and penetration levels as we head into 2022.

I'll now turn it over to Eric for the financial results.

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**Eric Guerin** - *CDK Global, Inc. - Executive VP & CFO*

Thanks, Joe, and good afternoon, everyone. As Brian and Joe mentioned, our customer-centric strategies are driving real improvement in the underlying health of the business. Some of the improvement is reflected in our financial performance but our results continue to be influenced by the lingering impacts of COVID and the investments we are making to support our customers.

I'll walk you through the details of the quarter and our outlook for the remainder of the year. I'd like to remind everyone that results are for continuing operations only and do not include the International business, which is presented as discontinued operations.

In the third quarter, our revenue was $433 million, up 2% versus the prior year. Subscription revenue was $332 million, up just slightly from 2020. Subscription revenue benefited from strong growth in site and revenue per site for both auto and adjacency, which, as Joe noted, saw a solid year-over-year and sequential growth. We're pleased that the underlying metrics continue to improve as they provide good insight into the long-term growth potential of our core subscription business.

There are, however, some near-term headwinds in reported subscription revenue. In particular, we continue to see the impact of ASC 842, the new lease accounting rules adopted last year. Under these rules, a portion of our monthly fee for certain products attributed to hardware is deemed to be lease revenue and is recognized upfront in other revenue. While there is no impact on our underlying economics, this transition will remain a headwind in reported subscription revenue until the entire book of business renews and transitions to the new accounting treatment.

Subscription revenue also continues to be affected by the amortization of the onetime discounts we extended to support our customers during the depth of the COVID lockdowns in April of 2020. This impact is spread over the life of the associated contract and will continue in the fourth quarter and into '22 at declining levels. While our partner program remains an important offering, we continue our transformation of the program to realign value, and our progress is advancing as expected.

Transaction revenue rose 14% to $43 million. This was partially attributable to higher transaction volume as we start to lap the significant impact on auto sales of the initial COVID lockdown. The increase also reflects the pass-through of higher credit bureau charges for credit checks. Other revenue grew 4%, driven by higher deemed hardware leases under ASC 842 as we continue to see strong installations of our Cloud Connect products. This was offset by COVID-related headwinds in our consulting and call center businesses.

Now turning to earnings. Third quarter EBITDA was $166 million, down 6% versus last year and reflecting a 38.4% margin. Lower EBITDA was driven by higher employee-related costs, including those associated with our $20 million incremental investment for the year but also higher benefit-related costs and higher bonus attainment. We also saw higher costs for outside services, which were a mix of investment-related items as well as some onetime project work. These impacts were partially offset by lower travel costs.

Our effective tax rate was 22.7% in the quarter, down just slightly from last year. Quarterly earnings per share were $0.69 versus $0.76 in the prior year. Free cash flow continues to be strong at $182 million year-to-date. Our balance sheet and liquidity position was strengthened significantly by the sale of the International business. Cash at quarter end was $1.1 billion after repaying $566 million of term loans in the quarter. As a result, net debt-to-EBITDA fell to 1.5x.

I'd like to spend a few minutes on our capital allocation strategy. Our priority is to increase value of our shareholders through the sustained profitable growth of our company, while balancing the return of excess capital to shareholders. We are doing this through, first, strengthening our balance



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sheet in order to provide financial flexibility for the pursuit of strategic investments in growth opportunities. In addition to the repayment of our term loan, we also retired the $500 million of 5.875% bonds due in 2026 during April. This will lower our interest expense and improve profitability, while further reducing our net debt-to-EBITDA leverage ratio.

Our long-term target leverage ratio remains in the 2.5 to 3x range, and we expect to manage within that range over time. We'll continue to bring a disciplined approach to our pursuit of potential acquisition targets to supplement our existing businesses and drive profitable growth. Given our current level of financial flexibility and strong cash flow generation, we expect to return $200 million to $250 million to shareholders via share repurchase over the next 12 to 18 months. We believe this represents the right balance of investment and capital return and will provide our shareholders with continued value well into the future.

Now turning to our annual guidance. We are tightening our guidance ranges for revenue, EBITDA and earnings per share. We now expect revenue of $1.66 billion to $1.7 billion; EBITDA of $640 million to $660 million and EPS of $2.50 to $2.65. Our tax rate for the full year is anticipated to be 26% to 27%.

In summary, we continue to see solid progress in our underlying business that positions us well for long-term growth. And I look forward to the opportunities ahead. Thank you, and we will now open the line for questions. Operator?

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) And our first question comes from Josh Baer with Morgan Stanley.

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**Joshua Phillip Baer** - *Morgan Stanley, Research Division - Equity Analyst*

Congrats on the site adds and the strong KPIs. I guess I wanted to start just asking like how the quarter went for you versus your own expectations as far as revenue and EBITDA?

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Sure. I can start. This is Brian. For me, I think the quarter went pretty much right as expected in both cases. It's -- we are ending out of the quarter very strong. You saw the site adds and all. The installations have gone well. I tell you the business is strong, and it was right in line with what we were forecasting in.

I'll let Joe and Eric add more detail but it was right in where I thought we would end up for the quarter.

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Yes. Nothing to add, BK. I think that, that's right. I think we saw more momentum on the site front. I think the strength in our customer satisfaction scores and, quite frankly, the retention and all the work that the sales team is doing, our customer delivery teams and our customer care teams, that came in a bit ahead of where we expected it, but everything else in line.

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**Joshua Phillip Baer** - *Morgan Stanley, Research Division - Equity Analyst*

Okay. Great. Yes, that's helpful. And so like with that in mind, just trying to get a sense for, excuse me, for the full year guide, with the midpoint and the high end coming down, is there something that you're seeing about Q4 that's changed versus a quarter ago?





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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Yes. I'll start and then Eric can chime in. I would tell you, the one thing you heard in Eric's prepared remarks is just timing. When you look at revenue recognition and a few things there, it's more timing of 606 and how those revenues come through. Otherwise, we are seeing a bit of more investment. And quite frankly, we're seeing so much progress on what we talked about with our larger customers driving consolidation within implementations and a strong backlog. We had a very successful sales quarter in Q3. And so I think if you look at quarter-to-quarter, we continue to think about the long term and growth acceleration as we head into FY '22.

Anything, Brian or Eric that you guys would add?

**Eric Guerin** - *CDK Global, Inc. - Executive VP & CFO*

No. I think, Joe, you touched on the key points.

**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

The only thing I would add or just kind of comment on is there are 2 things that I use to measure the strength of the business, the site growth and the revenue per site. And that's what I really use, Josh, to understand.

**Joshua Phillip Baer** - *Morgan Stanley, Research Division - Equity Analyst*

Yes. That's helpful. And both of those were super strong, I think, ahead of my expectations, too. Is it -- with that in mind and like the strong performance there, is it possible to break out what revenue would have been, like the size of the discounts, the impact from the discounting on this quarter's revenue? And then also from the revenue recognition change, the upfront rev rec change?

**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

I'll start out again. Eric can add in. What I would say is what Brian said. I think the best read when you look at the fundamental business is revenue per site and site growth combined together. So we're seeing a better underlying growth and really instead of going through all the different pieces, the delta is really the items you just described.

**Operator**

Our next question comes from David Robinson with William Blair.

**David Charles Robinson** - *William Blair & Company L.L.C., Research Division - Associate*

I guess I was just curious if you could provide a little more color around kind of the maybe the size of the opportunity within the adjacencies base and attaching the ELEAD CRM solution. I know you saw some good attach rates within the existing DMS base in auto. And I guess, with kind of the success you've seen in growing the revenue per site for adjacencies as well, I'm just trying to get a sense of kind of how large that opportunity will be overall and then with the kind of ELEAD solution as well.



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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Sure. I'll start out, and this is a common theme you're going to hear from us. Like we're very focused within our core businesses, both the auto side as well as the adjacency side, of expanding solutions that help dealers and OEMs. Specifically in the adjacency business, the team there has just done a very strong job around execution, both in terms of more customers adopting our solutions with sites growing 2-plus percent this quarter as well as revenue per site and then buying more.

And the heavy equipment space is quite attractive also. And that's where you heard us bring the ELEAD CRM to play. So while we don't disclose the exact number, what I would tell you is that business is growing in the high single digits now, and we continue to expect it to perform very well going forward.

I would say more broadly, David, you bring up a good point, which is I think what we're spending a lot of our time now with the -- is significant improvement in the foundational base of our subscription business, being able to look at ways to enhance the workflow integrations, bring value-added solutions that really help our dealers and OEMs sell more vehicles at a better profit level as well as service customers better in their service lane and create this digital retail and interconnected opportunity. There's a lot of opportunities we see as we're laser-focused on execution.

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**David Charles Robinson** - *William Blair & Company L.L.C., Research Division - Associate*

Got it. That's helpful. And then I guess just a quick follow-up on adjacencies as well. I mean, I know you saw some kind of favorable trends last summer, I believe, just around the pandemic, particularly in like powersports and different segments there. I guess, are you expecting kind of similar trends, maybe not as drastic to continue this year? Or how are you viewing that?

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**Eric Guerin** - *CDK Global, Inc. - Executive VP & CFO*

Yes. I mean, everything we see so far, whether it's in unit sales at our customers, because we actually see an insight into that, right, to our own growth. And there's, again, consolidation occurring here and growth. It tells us that, like you said, it may slow down a little bit, but we're seeing strong growth. And we don't see it changing dramatically over the next several quarters.

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**Operator**

Our next question comes from Charles Nabhan with Wells Fargo.

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**Charles Joseph Nabhan** - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

It's good to see the pickup in rev per site this quarter. But I was hoping you could parse that out between the 1- to 2-site segment and the larger dealer segment. I know there's not as much growth in the smaller dealers but given the potential for Drive Flex and I was hoping you could just talk about the penetration rate and the consumption of various apps within that segment for us.

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

So I can start. Let's just talk about it in broader terms and then we can pin it down is. If you take a look at, I'd say, first, let's just talk about site count. We've really seen -- probably the thing that's changed the most over the last few quarters is that we really turned the tide of decline on those 1 and 2 rooftop sites. And we're starting to actually see it return back to growth and winning sites in that area. We still have work to do.

But we -- that's one of the big shifts you've seen. So our site retention in that space is much better. Our new site growth is up much better. And that's really been about us really going out and serving that business segment much better than we did in the past. That said, then we are also seeing growth in our layered applications in that space. And mainly, it's things like CRM where those sites are looking for ways to get in contact





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better with their customers and build relationships with their customers. And they're competing with larger organizations, and ELEAD CRM really helps in that range.

So I tell you it's split pretty equally between those 2, layered applications and just site growth. But definitely we're seeing growth back into that 1 and 2 site area again.

Joe, do you want to comment?

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

No. I thought that was well covered, Brian. I think the retention levels have been the highest this quarter across both groups, not -- and really for 3-plus has performed well, and retention performed well in 1 to 2. And as Brian said, revenue per site grew in both portions of the portfolio pretty equally. So we're seeing just this robustness of the customer care team, the installation team, and the relationship of our sales team as well as the tech and what the tech teams are bringing to market is a great collaborative effort that's resonating well with our dealers.

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**Charles Joseph Nabhan** - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

Got it. And just as a quick follow-up. A few months ago, you announced a partnership with Global Payments to process payments through Fortellis. And I was wondering if you had any updates on that initiative.

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Yes. I'll start. Listen, we're quite excited about it. We are very near general release. We have a couple of dozen dealers that we have ramped up at this point and to pilot and it's working successfully -- very successfully. I think our goal here is to really leverage the Fortellis platform to modernize payments across automotive with this partnership. We're tied together with the highest levels of leadership at Global Payments. And we certainly have strong expectations for this as we head into fiscal year '22 and are quite excited about it.

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**Operator**

Our next question comes from Rayna Kumar with Evercore.

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**Millie Wu** - *Evercore ISI - Analyst*

This is Millie Wu for Rayna Kumar. So I'm wondering if you could talk about some early thoughts on fiscal '22 revenue and EBITDA growth prospects, I think given you guys also guided to, I guess, strong transaction growth for Fortellis. And how is that going to translate into revenue for the coming years?

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Sure. So I'll...

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**Eric Guerin** - *CDK Global, Inc. - Executive VP & CFO*

Yes, thanks. Go ahead, Brian.

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Let me start, and then I'll let Eric talk more. First, we're not going to talk about fiscal '22 until the end of next quarter. We'll give you really clear guidance. And part of our goal of -- you saw us, we also announced that we'd be doing an investor meeting early part of fiscal year '22 as well. And that's really to -- we feel like we haven't essentially really started on this journey of improvement in execution that we haven't had a chance to really go into depth with you guys. So that's the intention of that.

I can tell you that we are seeing all signs that the fourth quarter is going to -- starting off well and we're -- we've given you our projections for the fourth quarter. Clearly, we don't expect any kind of a slowdown as we move into '22, but we're not going to do forecast.

Fortellis, we expect to do the same kind of growth we did this year. So we went from roughly 10 million or so transactions last year to 100 million transactions this year. We expect that same kind of growth as we go through next year. And Fortellis is, there's -- you really need to think of it as an API kind of marketplace and transaction ecosystem. And so it really is dependent. It's really built for ease of use, developer ecosystem that allows people to write APIs and to use our APIs. And it has everything from very simple applications where people are just using data access, APIs, it's read-only. Those aren't going to generate revenue, and they really shouldn't be generating a lot of revenue.

We're not a marketplace of data where we're going to sell other people's data. There are other low areas like with our Repair Order, where there are several APIs, there's read, write, there's calculations. We manage all of the warranty credits. There's a lot of real value-added to the data that we're pushing back and forth as a Repair Order goes through, and we get paid for that. And so we're generating revenue now on those types.

You're going to see more and more of those. You'll see more and more of them from CDK. You'll see more and more of them from third parties as well that are starting to write applications that really add value against whatever the dealer is trying to do. So that's really the purpose of Fortellis.

And then what you're also going to see is what -- Fortellis feeds Neuron. Neuron then feeds insights. So one of the other places you're going to see kind of a side benefit of Fortellis is that we'll start dropping over the next several quarters insights that come out of the Neuron database and Neuron analytics, which we talked about Square Root, our acquisition really adds a lot of value to.

And what those will do, those insights will start to do things like adding propensity to purchase a vehicle into our CRM or how to manage your inventory and suggestions on pricing or what type of inventory to be out looking for on the used market. All of those kinds of things are going to start becoming add-ons to our software, which brings, again, stickiness, value and will help us retain our customers, which then translates into revenue growth as well. So it's not always going to be a one-to-one in Fortellis.

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**Operator**

Our next question comes from Gary Prestopino with Barrington Research.

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**Gary Frank Prestopino** - *Barrington Research Associates, Inc., Research Division - MD*

A couple of questions here. And hoping you can answer some of this. In terms of the automotive revenue per site that you're generating, which keeps going up every quarter, which is great. Can you maybe parse that out as to what percentage of that 9,042 is actual DMS charges versus layered applications?

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Gary, to be honest, our bias would be not to get into details of each product. I think, listen, and how you split that out, given how much we're bundling it's quite difficult. I would just tell you, on average, we're penetrating with our applications with about anywhere from 30-ish percent of our application portfolio combined with our DMS. And we do so much bundling, I think the 9,000 is very fairly representative of the full suite of solutions we're bringing. And we're seeing a lot of momentum, quite frankly, in our dealer IT collaboration, networking, security space offering,





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momentum in the CRM and Service space and our document storage with Doc Cloud in addition to DMS. So it's very tightly coupled and bundled, I don't think it would be helpful to go to try and split the pieces.

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**Gary Frank Prestopino** - *Barrington Research Associates, Inc., Research Division - MD*

Okay. Can we assume that most of the growth that we're seeing, though, is a function of deeper penetration on the layered app side?

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

I think you're seeing growth across the portfolio, to be honest. I think you're seeing growth around DMS sites. I think you're -- and you're also seeing growth in the application space. So I think, when we look across, it's very healthy, whether it's 1 to 2 or 3-plus, whether it is applications or DMS, it's pretty healthy, foundational, consistent growth.

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**Gary Frank Prestopino** - *Barrington Research Associates, Inc., Research Division - MD*

Okay. Can you give us any idea of how Repair Order and Hailer are doing within the Fortellis platform?

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

They're doing quite well. We have groups of -- in Hailer, as an example, we have several hundred dealers who are actively using that application. It's interesting. It originally started as an application to provide transportation service. You bring your vehicle in for service. You can use -- it gives you a onetime credit for getting a ride back to your office or home. And then another one to maybe come pick up your vehicle. We're also seeing dealers start to use it to deliver parts between shops and things like that or go pick up parts from warehouses. So it's -- we're starting to see a broader application of Hailer.

Repair Order is doing quite well. I'd tell you, it is the #1 application from a revenue standpoint on Fortellis right now. Again, several dozens of third parties using it, including some of our biggest competitors that, in this space, we actually think of as partners, are using the Repair Order application on Fortellis. And so it's going quite well. And as I said, it's the largest revenue generator on the system.

Because we had -- remember, Repair Order, like I said earlier, it's several APIs. I think it's like 5, if I remember correctly. I could be off by 1 or 2 there. And many of those APIs, behind them, there's quite a bit of calculation going on, a lot of value-add around -- is it a warranty part and how do you send back the warranty credit, it's read and write. All of that is occurring in that application.

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**Gary Frank Prestopino** - *Barrington Research Associates, Inc., Research Division - MD*

Okay. And then lastly, with the APIs you're developing for developers to put their products into Fortellis. Is that something that you're contemplating? Or are you allowing that to occur free of charge? Or is it something that you are charging these developers for putting their products into Fortellis through the APIs??

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

So there are multiple kinds of APIs. So if you wanted to go write an API tomorrow and post it to Fortellis, you can do that free of charge. Some of our developers aren't capable of doing that, and they're asking for help. And in which case, we'll do a small fee to sometimes offset engineering expenses and things like that. But there's no profit in posting an API to Fortellis. So we post our APIs, most of them are accessible for no cost. Some like the Repair Order ones, where there's a lot of value add, they have a charge to them.



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And then you need to think of APIs as there's our APIs, where if you want to get into the DMS or one of our layered applications or something like that. There are APIs that third parties are posting that then read into ours and/or we read into for our operations. And then there are some APIs that could be from third party to third party.

So somebody might be doing a parts inventory for service applications that then goes into Xtime or something, one of our competitive products, and it never actually passes through our system. But we allow that, right? This is meant to be an agnostic open ecosystem. That's how this will thrive. And they can do that, and it's not a problem to post those types of APIs.

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

Yes. And Gary, the only other thing I would add, I mean, you look at Hailer, Brian talked about, we've seen over 200% growth in that alone this year. And so while it's small numbers still, it certainly is building this ecosystem, and we're quite happy with the work the team has done to build momentum there in the integrations. So you're going to see it. When we talk about modernizing payments within automotive, the connectivity and integration that's going to provide dealers seamlessly in a workflow value within their dealership, leveraging Fortellis with our DMS and everything else is going to be great when it goes to general release later this quarter. So lots of good stuff going on there.

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**Operator**

Our next question comes from Ian Zaffino with Oppenheimer.

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**Ian Alton Zaffino** - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

I just wanted to kind of follow up on the Fortellis side of it. And I know you talked about transactions, but if you could maybe like disaggregate the transactions a little bit. Like how much is actually coming from existing big customers? How much is coming from newly onboarded customers? Or maybe what's sort of like the developer/customer count as a driver of transactions versus existing developers? Yes, and just them increasing their own transactions.

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Okay. So those are good questions, right? So remember, this is an ecosystem that we -- when you build an ecosystem, so if you think of things like the Android ecosystem or some of the ecosystems that are out there with other companies and software platforms, they typically take years to really continue to grow and develop. And when you're doing that, you're really figuring out how do you best attract and make it easy for developers to build on to your product? And then how do you get the usage? And that's why we track transactions.

That's, for us, right now, is even more important than quote revenue or revenue per transaction or something like that because this is really about growing -- the last thing you want to do is have people write a bunch of APIs, and those APIs don't get used. So that's why even more important than API count is transactions because that says people are not only writing APIs, but those APIs are getting used. Data is flowing through them.

I tell you the biggest users today are both us internally, so CDK internally, and some of the big applications that were done by some of the larger developers. So Hailer was a good example of one. Repair Order is a good example of one. There are several hundred developers developing APIs now external to CDK, developing APIs on Fortellis now.

So the tide is coming.

You've seen our partnership with Microsoft. It's going quite well. We're now putting tools and APIs into things like GitHub that allows people to more quickly develop their own APIs. So we're trying to build it easier and easier for people to build on to the Fortellis platform. But I'd tell you, right now, it is mostly the big guys that have the -- several of the big APIs.





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And internally, we are using the tool right and eat your own dog food is kind of the software developers credo when your developing platforms like this. If you're not using it and not making it easy for yourself, you're not definitely making it easier for others either. So we use it ourselves for our own applications.

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**Joseph A. Tautges** - *CDK Global, Inc. - Executive VP & COO*

And Ian, the comments that I would say, when you listen to what BK just said, it is -- all those values are about helping dealers and OEMs sell more vehicles. And we're just focused on adding value. And it's not like the stand-alone product. It's about the whole enabling -- and that's where you're seeing the strength, in our core DMS, in our core applications because the stitched together value of the experiences that we will be able to connect with OEMs, whether it's with the digital retailing experience or within Hailer and how it helps a dealer on profitability of their loaner fleet, there's -- everything's about how you add that value to the dealer, OEM, and Fortellis helps provide the interconnectivity.

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**Ian Alton Zaffino** - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

Okay. Good. And congratulations on punting International and before that, DM. How are we thinking now about the business and what you need to maybe acquire as far as filling in some gaps, right? Like where would it be? And even your appetite just in general to do anything?

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Sure, I'll start and then Eric and Joe can comment. I tell you the digital marketing sale and then the international sale, just to give you some insight, especially the international one, into the strength of our business, right? The international business sold at a 15x multiple, which is again, when we look at our core business, we should look at something even more valuable from that perspective. We're really -- we really like the business we have right now. We did these sales to really focus down. You can't be good at everything. You can't distribute your efforts across too many platforms. You really need to narrow things down. And we really like what we have right now.

That said, as we took the proceeds, Eric talked a bit about it in more detail in his comments, we took the proceeds, the first thing we did was buy down some debt, and that really did a couple of things. One, some of the debt had, in today's market, higher interest rates than when -- are available out there. So relieving that was good. Getting our debt ratio down was quite good. That lowers our expenses of debt. And then we also announced that we'd be doing buybacks over the next several quarters. And that is, again, I look at those 2 things as we can take this money and do some return to investors and really give the money back to the investors in that case.

We did hold back some money that would allow us to do acquisitions. I'm pretty careful about acquisitions. I think that you first have to make sure that they fit into your strategy, that there's a good reason to put them into your core because otherwise, what happens is you do these investments, you don't invest back into them because no investment comes perfect forever. You have to keep investing. And if you're not willing to do that investment because they're not core, you don't see them as your -- one of your growth engines, then that really hurts.

And I think ELEAD is a great example. We did that investment. We've doubled the number of sites since we got ELEADs. It's growing really, really well. It's a combination of growing within our DMS and outside of our DMS. So it's grown equally as much with other companies' DMSs. So that's a good investment. We bought it. We have invested in it. You see us now pushing it down into the rec heavy business. We're going to go push ELEAD across the board.

I'm open to others. They need to have that same kind of characteristic. They need to have a reason to be a part of our core. Something that we're going to willing to continue to invest in and something that we think can really add to our growth measure. And so that's what we're looking for when we think about those. There's nothing on our short-term horizon that says, okay, I've got something in the next 2 quarters necessarily going to add something, but we're constantly looking, and there are certainly some things out there that are potential for us.

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**Operator**

Thank you. This concludes the question-and-answer session. I would now like to turn the call back over to Brian Krzanich for closing remarks.

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**Brian Matthew Krzanich** - *CDK Global, Inc. - President, CEO & Director*

Yes. I would just like to close with. First, thank you, everybody, for taking the time and asking. These were really good questions, and I hope you got better insight into our business and why we're excited. We see really a great quarter in the third quarter. We are excited about the future, and we're showing you where we're really gaining momentum.

As I said, we really look at 2 things that give us insights into the future. That's site count and the revenue per site. That really talks about are we really providing, as Joe said, the solutions that our customers need. And if we are, those things are growing. If we're not, those things won't grow, and it's as simple as that.

And then I'd just like to thank all the CDK employees for just a great quarter. We're continuing to do really well in a COVID environment. We're starting to get back into the offices and a lot of the sites, and we're really excited. And so thank you, everyone, and we will see you next quarter.

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**Operator**

This concludes today's conference call. Thank you for participating. You may now disconnect.

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