CarGurus Edited Transcript

Fourth Quarter and Full Year 2023 Earnings Call

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CORPORATE PARTICIPANTS

Kirndeep Singh, *Vice President, Head of Investor Relations*

Jason Trevisan, *Chief Executive Officer*

Elisa Palazzo, *Chief Financial Officer*

Samuel Zales, *President and Chief Operating Officer*

CONFERENCE CALL PARTICIPANTS

Marvin Fong, *BTIG*

Rajat Gupta, *JPMorgan*

Logan for Brad Erickson, *RBC Capital Markets*

Tom White, *D.A. Davidson*

Ryan for Naved Khan, *B. Riley Securities*

Jed Kelly, *Oppenheimer*

Chris Pierce, *Needham & Company*

Ron Josey, *Citigroup*

John Calantuoni, *Jefferies*

Doug Arthur, *Huber Research Partners*

Jason for Kunal Madhukar, *UBS*

PRESENTATION

Operator

Good day and welcome to the CarGurus Fourth Quarter and Full Year 2023 Earnings Results Conference.

At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. (Operator instructions). As a reminder, this conference is being recorded.

It is now my pleasure to introduce you to your host, Kirndeep Singh, Head of Investor Relations. Thank you, Kirndeep. You may begin.

Kirndeep Singh

Thank you Operator, and good afternoon. I am delighted to welcome you to CarGurus' Fourth Quarter and Full Year 2023 Earnings Call.

With me on the call today are Jason Trevisan, Chief Executive Officer; Sam Zales, President and Chief Operating Officer; and Elisa Palazzo, Chief Financial Officer.

During the call, we will be making forward-looking statements which are based on our current expectations and beliefs. These statements are subject to risks and uncertainties which could cause our actual results to differ materially from those reflected in such statements. Information concerning those risks and uncertainties is discussed in our SEC filings, which can be found on the SEC's website and in the Investor Relations section of our website. We undertake no obligation to update or revise forward-looking statements except as required by law.

Further, during the course of our call today, we will refer to certain non-GAAP financial measures. A reconciliation of GAAP to comparable non-GAAP measures is included in our press release issued today, as well as in our updated Investor Presentation, which can be found on the Investor Relations section of our website. We believe that these non-GAAP financial measures provide useful information about our operating results, enhance the overall understanding of past financial performance and future prospects, and allow for greater transparency as it relates to metrics used by our management in their financial and operational decision making.

With that, I'll now turn the call over to Jason.

Jason Trevisan

Thank you, Kirndeep, and thank you to all those joining us today.

As I shared at the beginning of last year, the theme of 2023 was monetization across our platform, and I am pleased to report that we delivered outstanding results. Throughout the year, we expanded our product offering to enrich our value proposition and meet dealers' and consumers' evolving needs. This further strengthened our partnership with dealers and drove accelerating revenue growth in our foundational Listings business. While smaller in size, the International operations also contributed to the strength of our results: revenue growth accelerated in Canada, and we achieved profitability in the UK, marking a significant milestone for CarGurus achieving profitability in every market.

In December, we completed the acquisition of CarOffer, which will allow us to accelerate the connectivity between our retail and wholesale product offerings. This acquisition, coupled with our Digital Retail efforts, has expanded and diversified the range of monetizable transaction activities that holistically serve our dealer partners. Collectively, we believe that the expansion of product offerings, ongoing innovation, and data-driven insights fortify our ability to attract new dealer customers, increase the wallet share of the existing customer base, and progress toward our ultimate vision of an end-to-end transaction-enabled platform. As a result of our tremendous progress, I am pleased to share that we ended the year exceeding our forecasted EBITDA guidance for the fourth quarter.

In 2023, the Marketplace business significantly outperformed our expectations, exiting the year with approximately 10% revenue growth and meaningfully contributing to our EBITDA beat. In a challenging environment for our customers characterized by weak consumer demand, lack of affordability, and heightened expenses linked to floor plan financing, our foundational Listings business exhibited remarkable resiliency, pricing power, and growth acceleration. In fact, we ended the year growing US QARSD approximately 12% year-over-year to $6,532. This is our strongest year-over-year growth on record since introducing QARSD as a KPI, excluding pandemic-related concessions, and marks the 13th consecutive quarter of increase.

In the fourth quarter, the largest drivers of QARSD growth came from adding on new dealers at market rates, package upgrades, and price increases. We also experienced robust adoption of add-on products, and multiproduct attach rates increased by 36% year-over-year as dealers continue to look for additional channels to attract high-intent, ready-to-purchase shoppers to their inventory. By providing dealers with greater value in our product offerings and simultaneously growing leads per paying dealer year-over-year, in Q4 we experienced the strongest MRR acquisition in 10 quarters.

Evaluating the Marketplace strategy for 2024, our approach consists of two key aspects. As we highlighted on the last earnings call, our number one priority is optimizing all drivers of QARSD. This commitment includes adding new dealers at market rates, expansion of existing dealer wallet share through listings upgrades, product innovation and adoption, and lead quantity and quality. This commitment will allow us to deepen the value we provide our dealers and drive increased monetization.

Secondly, our renewal strategy involves evaluating dealers and executing renewals to align terms with the ROI we provide, simultaneously exploring new product cross-sell and upsell opportunities as we enhance the value proposition of our premium packages. For underpriced dealers that fall below market rates, we will conduct ABRs leveraging their proven success in 2023, as dealers recognize the ROI of our platform.

Throughout 2023 and carrying forward into 2024, we have invested in our QARSD lever of product innovation, aimed at fostering enhanced value creation and strengthening dealer engagement throughout our platform. This commitment to innovation involves leveraging the power of artificial intelligence and data insights to elevate our platform and introducing new products to further enhance the ROI for our customers. Our strategic emphasis on AI centers around three key areas: internal platform efficiencies, elevating the consumer experience, and delivering actionable insights for our dealers. In relation to the first two key areas, our latest development is a Listings' Content Generator. This tool produces an easily digestible list of vehicle features, and streamlines the consumer experience by making it easier to locate keywords and features of relevance during the vehicle shopping journey.

As for greater data insights, we continue to focus on our Dealer Data Insights Initiative. Last October we released Next Best Deal Rating, a powerful report that helps dealers understand the least amount of price reduction needed to achieve the next best deal rating on CarGurus. Since launching in October, we have already signed up over 10% of our dealers for daily or weekly reports to support their price analysis to improve VDP views and inventory turn times. In under three months, over 100,0000 price adjustments were made as a result of the insights provided by Next Best Deal Rating.

We have also developed yet another powerful tool that recommends inventory based on a dealer's turn-time objectives. This early access tool allows each dealer to set a specific turn time goal and we utilize the CarGurus' listings scale to analyze turn time trends at a detailed level, in local and adjacent markets. Additionally, we will leverage CarGurus' site data to examine consumer trends, foreseeing changes in preferences as we look ahead. By combining consumer and inventory data, we generate personalized reports for dealers, predicting vehicles that align with their turn-time objectives. Our aim is for dealers to integrate these insights into their wholesale strategies, optimizing operations and achieving their goals, while fostering synergies with our CarOffer wholesale business. As we develop an end-to-end transaction-enabled platform, we are a leading provider of real-time retail and wholesale insights, empowering dealers' decision making and helping them run a smarter business.

As we merge retail with wholesale from a product development perspective, we are able to offer dealers even more ways to access consumer inventory and give consumers even more choice in how they sell their vehicles. Sell My Car presents consumers with two types of offers: a 100% online offer, as well as offers from local dealers known as Top Dealer Offers. Since launching Top Dealer Offers we have seen conversion rates more than double as consumers value the ability to choose how they sell their vehicle. The primary focus during this early access phase is to guarantee an outstanding customer experience while also catering to the needs of our dealer partners. While we have achieved remarkably high seller Net Promoter Scores, we aim to uphold the quality of the offering as it expands. To achieve this, we are testing with select dealers an intake tool designed to establish trust between consumers and dealers while providing us with a valuable feedback loop of real-time insights for each transaction. The goal is to further scale Top Dealer Offers in 2024 and, as an added benefit, Top Dealer Offers is powered by CarOffer's matrix technology, creating inherent synergies by introducing CarGurus' dealers to the CarOffer wholesale platform.

In 2021, we chose to acquire a stake in CarOffer as it stood as a unique offering, enabling dealers to efficiently buy and sell wholesale inventory programmatically. This decision was driven by our vision to build a distinctive end-to-end wholesale-to-retail transaction-enabled platform that is unavailable elsewhere. Our enthusiasm for this opportunity is greater than ever since accelerating the acquisition and appointing Zach Hallowell as CEO. Our platform is ideal for large players who continue to find programmatic buying to be an efficient and effective way to source and sell inventory. In 2024, our primary focus lies in refining the product capabilities, advancing the CarOffer technology through predictive analytics, and incorporating CarGurus' consumer and retail data to further differentiate our platform.

Despite the tremendous advancements in CarOffer's operational efficiency over the past year, particularly in mechanical inspections, title transfers, and transportation, we will look to enhance our capabilities even further to optimize the dealer experience and drive cost efficiencies. We plan to use the next few quarters to drive our strategic and operational initiatives while applying financial discipline to strengthen our business, and it may take several quarters before the business returns to profitable growth.

Similar to advancing our Digital Wholesale capabilities, we have also been investing strategically in building our Digital Retail platform, where our products allow dealers to serve a broad array of consumers with varying degrees of readiness to purchase their cars.

Since beginning our journey, we have developed two product offerings: the first is Digital Deal. As of year-end, we had 4,667 dealers on Digital Deal growing approximately 200% year-over-year and nearly doubling our digitally-enabled vehicle listings to approximately 400,000.

A component of the accelerated sequential growth is the unique bundling and packaging opportunities we have created with the two highest listing tiers. As of October, dealers upgrading to the Featured Plus or Featured Priority Plus listings tiers receive Digital Deal included in their package.

Another product that has performed well from a bundling and packaging standpoint is Digital Deal with Geographic Expansion. Since bundling Digital Deal and Geographic Expansion, we have seen an approximately 30% increase in adoption year-over-year. With more digitally-enabled listings available than any other online retailer, we are providing consumers with a convenient, self-selective purchasing journey, all while providing trust, transparency, and the best pricing from the largest selection of inventory among major online automotive marketplaces in the U.S. As consumers look to do more of the shopping journey at home, we are seeing digitally enabled leads continue to increase as a percentage of a dealer's overall leads. Digital Deal leads now account for 20% of a dealer's email leads or 30% for top-performing dealers and are up to 5 times more likely to close than traditional email leads.

Our second offering in Digital Retail further advances our digitally-native transaction capabilities and is formally known as CG Buy Online. This pilot is an asset-light, end-to-end solution that empowers dealers to sell cars to out-of-market shoppers entirely online and boost online sales by providing dealers with the marketing, technology, and logistics needed to support these transactions. We are currently live with a small subset of dealers and our goal in 2024 is to collaborate closely with pilot dealers, further validating the product-market fit and developing an outstanding experience for both consumers and dealers alike. Through our digital retail initiatives, we aim to equip dealerships with a broad range of tools and capabilities, enabling them to effectively compete and streamline vehicle sales to digitally savvy or out-of-market shoppers.

In a landscape where consumers increasingly opt for online channels in their car buying and selling journey, it's essential to convey to shoppers that our platform is specifically designed to meet their needs, giving them the flexibility to handle as much or as little as they prefer online. As we progress further down the sales funnel and guide consumers toward completing transactions entirely online—a task that requires a considerable amount of trust when sharing sensitive personal information—it becomes crucial to amplify our brand awareness. In pursuit of this objective, we kicked off an extension of our 2023 campaign called "Your Car, Your Way" in January, spotlighting the gratifying experience of everything falling into place just as desired. As we persist in our efforts to drive direct and own-channel traffic, we've placed a strong emphasis on enhancing brand awareness. Notably, CarGurus ended 2023 as the number one automotive app in terms of downloads on both iOS and Android with an average rating of 4.8 stars. This achievement represents a significant milestone for us, considering that our app plays a crucial role as a source of organic traffic that converts at a higher rate than traditional leads. Our app accounted for a quarter of leads in 2023, growing from only 10% in 2020. As we drive more organic traffic and amplify our brand, we are building a platform that creates consumer loyalty.

In 2023, our accomplishments strengthened our market and product leadership, re-accelerated revenue growth, and drove significant progress toward our vision of being the only end-to-end automotive transaction-enabled platform where dealers can source, market, and sell, and consumers can shop, finance, buy, and sell vehicles.

Looking ahead to 2024, we expect to further build on this momentum. We are very excited about our areas of opportunity, including capturing more value in the Marketplace business, integrating and expanding CarOffer while increasing our share of the growing digital wholesale market, and continuing to invest in innovative growth initiatives such as Digital Retail. Through it all, we plan to offer our dealer customers even greater insights and value by linking the wholesale and retail process together in one seamless platform.

While we will continue to invest in our business, we do so by maintaining financial discipline and prioritizing operational excellence and efficient capital allocation. We believe this will allow us to enhance our profitability and create shareholder value as we continue to expand in both existing and new growth opportunities. We are very pleased with our 2023 accomplishments and financial results. We look forward to accelerating our momentum in 2024.

Now, let me turn it over to Elisa to discuss our financial results.

Elisa Palazzo

Thank you Jason, and good afternoon everyone. Before I dive into the fourth quarter results, I would like to express my excitement about joining CarGurus. Our Marketplace business is a unique asset with the largest network of dealers and the broadest selection of inventory in the U.S., unrivaled product innovation and ROI leadership. It represents an enviable foundation to build a digital platform that captures the full lifecycle of a vehicle transaction.

I am joining the company at a pivotal moment in its growth journey, as our highly profitable Listings business re-accelerates and we continue to enhance and integrate existing and new transaction capabilities and product features. We are in the early innings of building our vision and unlocking what we believe to be the full potential of our franchise.

I will now turn to our results.

Since our business mix has changed substantially versus last year, in my commentary I will highlight both year-over-year and sequential trends.

We experienced exceptional momentum in our Marketplace business, which continued to accelerate and achieved the fastest year-over-year revenue growth rate in nearly three years, while we continued to gain leverage in our cost base and expanded our non-GAAP margins across all our business segments and geographies. As the CarOffer transaction closed and we now have full control of the asset, we plan to focus on achieving operational efficiencies and maintaining financial discipline as we look to return the business to profitability. While we expect this process to take several quarters, we are encouraged by the operational progress to date.

Total fourth quarter revenue was $223 million, down 22% year-over-year, driven by lower wholesale and product revenue, and up 2% sequentially as we continued to expand our monthly recurring revenue base.

Marketplace revenue was $182 million for the fourth quarter, up approximately 10% year-over-year and 2% sequentially, driven by the largest quarterly expansion in MRR in 10 quarters, as well as stable advertising revenue.

Consolidated QARSD grew 12% year-over-year, driven primarily by the addition of new active dealers at current market rates and existing dealers migrating to higher subscription tiers. In the fourth quarter, our Listings business added approximately $17 million year-over-year in revenue, nearly twice as much as the average quarterly expansion we achieved in nearly three years.

Wholesale revenue was $22 million for the fourth quarter, down 7% year-over-year and up 1% sequentially, driven by a modest increase in dealer-to-dealer transaction volume. In the fourth quarter we continued to prioritize operational improvements, while overall market conditions remained muted as wholesale prices are on a path to normalization but remain elevated.

Lastly, product revenue was $19 million for the fourth quarter, down 81% year-over-year and down 5% sequentially, reflecting our decision to continue limiting transaction volume and lower ASPs, as well as meaningfully reduced arbitration revenue.

Instant Max Cash Offer, our consumer-to-dealer product, generated $16 million in revenue in the fourth quarter, down 78% year-over-year and 12% sequentially, as a growing number of dealers continue to opt-in for our highly profitable subscription-based product, Top Dealer Offers.

I will now discuss our expenses and profitability on a non-GAAP basis.

Fourth quarter consolidated non-GAAP gross margin was 78% compared to 50% in the prior-year quarter and 77% in the third quarter. The meaningful expansion in non-GAAP gross margin was due to the shift in revenue mix towards our high margin Marketplace business, which represented 82% of our revenue in the fourth quarter, up from 58% in the prior year and 81% in the third quarter.

Within the individual business segments, Marketplace non-GAAP gross margin expanded 155 basis points year-over-year and approximately 50 basis points sequentially, driven by favorable product mix. Our Digital

Wholesale non-GAAP gross margin was up 130 basis points sequentially, driven by the early operational improvements I referenced earlier, as well as one-time and prior-period favorable items.

Fourth quarter non-GAAP operating expenses were relatively flat year-over-year and fell 5% sequentially to $119 million, predominantly driven by lower sales and marketing spend, which was down 3% year-over-year and 7% sequentially. The sequential decrease in sales and marketing expense reflects our typical fourth quarter cadence as well as our decision to limit marketing investment for Instant Max Cash Offer in 2023.

Our fourth quarter non-GAAP product, technology and development expenses grew 3% year-over-year but were down 3% sequentially to $29 million as we slowed our pace of hiring in the fourth quarter.

As a result of sequentially lower non-GAAP operating expenses, we generated consolidated Adjusted EBITDA of $61 million in the fourth quarter, up 120% year-over-year and 26% sequentially. Consolidated Adjusted EBITDA margin was 27%, and expanded approximately 1,800 basis points year-over-year and was up approximately 500 basis points sequentially. Fourth quarter margin year-over-year expansion was primarily driven by favorable segment mix, as well as improved wholesale margins and some one-off items.

Marketplace Adjusted EBITDA grew 27% year-over-year and 21% sequentially to approximately $62 million. Digital Wholesale Adjusted EBITDA loss was approximately $1 million in the fourth quarter, including approximately $2 million in prior-period and one-off favorability. Excluding these items, Digital Wholesale Adjusted EBITDA would have been approximately flat sequentially.

Non-GAAP diluted earnings per share attributable to common shareholders was $0.35 for the fourth quarter, reflecting the increase in Adjusted EBITDA as well as a reduction in shares outstanding.

I will now discuss a few GAAP metrics that include one-time items related to the purchase of the remaining stake in CarOffer in the fourth quarter.

We incurred total GAAP operating expenses of $190 million, up 77% year-over-year, which includes approximately $50 million of share-based compensation incurred in connection with redeeming the remaining units of CarOffer.

Fourth-quarter GAAP operating loss was $22 million, down $52 million compared to operating income of $30 million in the prior-year period. Fourth-quarter GAAP consolidated net loss was $23 million, down $46 million year over year.

We ended the fourth quarter with $312 million in cash, cash equivalents and short-term investments, a decrease of $135 million from the end of the third quarter. The lower cash balance was primarily driven by the $75 million cash consideration paid for the CarOffer acquisition in December, as well as share repurchases in the fourth quarter.

During the fourth quarter we repurchased 4.8 million shares for an aggregate purchase price of $100 million. Since the beginning of our buyback program in December 2022, we repurchased $223 million in shares, equivalent to approximately 10% of our outstanding capital as of December 2022. In November 2023, we announced that our Board authorized an additional $250 million share repurchase program, expiring in December 2024.

I will close my prepared remarks with our outlook for the first quarter.

We expect our first quarter consolidated revenue to be in the range of $201 to $221 million. We expect the momentum in our Marketplace business to continue in the first quarter, with quarterly revenue expected to be in the range of $182 to $187 million, up between 9% and 12% year-over-year.

Moving to EBITDA, we expect our first quarter non-GAAP consolidated Adjusted EBITDA to be in the range of $41 million to $49 million, with wholesale transaction volumes sequentially lower in the first quarter. On a non-GAAP basis, we expect operating expenses to increase sequentially in the first quarter, primarily driven by marketing spend as we launched our new brand campaign, "Your Car, Your Way". In addition, we typically ramp back our marketing spend by several million dollars in the first quarter, after a seasonal reduction in the fourth quarter.

Going forward for the rest of 2024, we expect quarterly marketing costs and operating expenses to remain roughly in line with the first quarter, but to progressively decline as a percentage of revenue as we continue to grow our business throughout the year.

Finally, we expect non-GAAP earnings per share to be in the range of $0.24 to $0.29.

With that, I would like to open the call for Q&A.

Operator

Thank you. We will now be conducting a question-and-answer session. (Operator instructions).

Thank you. Our first question comes from the line of Marvin Fong with BTIG. Please proceed with your question.

Marvin Fong

Good evening. Thanks for taking my question. I thought I'd just ask about CarOffer. I think you mentioned a couple of times that you're focused on continuing the operational efficiencies and maintaining financial discipline in that segment. I guess maybe if you could maybe just add a little more detail to that, maybe some of the guideposts or thresholds that you're looking to achieve kind of on the way to getting to where you want to be that we, as investors, could observe in your disclosure? Maybe (inaudible).

Elisa Palazzo

Thanks for the question, Marvin. So let me preface that we are incredibly excited about the long-term opportunity in Digital Wholesale. It's an underpenetrated space with sustained secular demand tailwinds, very strong synergistic potential with our foundational listing business and there is an opportunity for us to gain market share in this space over the long term.

We have a number of initiatives underway and we are in the process of rebuilding our leadership. Therefore, we estimate the business to return to profitable growth in the next several quarters.

Now I will focus on my commentary on the first quarter. We have continued our efforts to drive operational efficiencies and enhance our products before we shift our focus externally to intensify our go-to-market efforts. We have improved our inspection, title transfer and transportation capabilities, which have driven lower arbitration rates and better transportation margin. (Inaudible) initiatives, we have also reduced our fixed cost base in dollar terms for the last several quarters. and we are in the process of creating a shared service center with CarGurus as it relates to our support functions. We believe we are executing well against our strategy, and we are confident that we will return to profitable growth in the next few quarters.

Sam, do you want to add anything?

Samuel Zales

I think you nailed it. Thank you.

Marvin Fong

That's terrific, Elisa. Thanks for that color. Maybe a follow-up on you didn't provide full year guidance, which is understandable, but you did provide some commentary about sales and marketing for the year. I just wanted to understand what gives you the confidence that you could kind of provide that outlook for sales and marketing spend? Should we take what you are saying about it being relatively flat for the rest of the year, kind of tying to what you were saying before that we shouldn't expect any major advertising push behind IMCO for this year?

Elisa Palazzo

Marketing spend is fully in our control, and we have visibility and so let me take a step back and comment on the main factors that we believe will affect the OpEx sequentially between Q4 and Q1. The first one is the seasonality of media spend. If you look, typically, we take down our media spend in Q4, we're going to step it back up in Q1 and we expect to keep it constant for the year, as per my prepared remarks.

The second one is a planned investment in sales and marketing, which is partially driven by our new branding campaign, which I also mentioned in my prepared remarks. The second portion of it is really Digital Wholesale. So we said that in Q4, we had a one-off favorability of approximately $2 million; we don't expect that to be repeated in Q1. These are the key drivers of OpEx going forward.

Now, it's important to also point out again, as I mentioned in my prepared remarks, that while we expect OpEx and marketing spend to remain pretty much constant throughout the year or at least until the third quarter, we expect OpEx to decline progressively as a percentage of revenue as we continue to expand our franchise and we expect the marketplace momentum to continue throughout the year.

Jason Trevisan

Just to reiterate that, Marvin. As a result, sales and marketing as a percent of gross profit or as a percent of revenue, we expect to decline over the year.

Marvin Fong

Understood. Okay. That's terrific color everyone. Thanks so much.

Operator

Thank you. Our next question comes from the line of Rajat Gupta with JPMorgan. Please proceed with your question.

Rajat Gupta

Great. Thanks for taking the questions. I just wanted to follow up on Marvin's question earlier on the first quarter guidance. If I look at the low end of the guidance on revenue and EBITDA, it's down roughly $20 million sequentially, but the Marketplace revenue guidance is kind of flattish to up sequentially, even if we exclude the $2 million onetime CarOffer's offer adjustment in the fourth quarter, it would imply something like OpEx going up between $15 million to $20 million for the Marketplace business. Firstly, do you think that's accurate or in the ballpark? If it is, what's driving such a material pickup? Is all of that driven by just the marketing spend that you referred to? Or is there anything else with respect to CarOffer seasonality or you mentioned transaction volumes down; maybe that's driving EBITDA even further lower in the first quarter. I have a quick follow-up, thanks.

Jason Trevisan

Sure. Rajat, it's Jason. Yes, the drivers that Elisa just talked about from largely a marketing perspective, there's a seasonality element. There's a brand element. There are the nonrecurring benefits to Q4 that we don't expect in Q1. There's a small element of lease expense; it was not full quarter. And there's ad revenue seasonality as well, and so those would be offset by the midpoint of the guide and Marketplace has growth and so we would expect growth there at the mid- to high end.

Rajat Gupta

Got it. Got it. Then just on the international businesses, both Canada and U.K. are now profitable. Is there like a ramp in some sales and marketing efforts in those markets as well to improve the profit contribution going forward? Just curious how we should think about the profitability there for this year relative to the fourth quarter exit rate? Thanks.

Jason Trevisan

Yes. The international businesses are both doing quite well and also doing well from a lead volume and quality perspective, both organically as well as paid. We've also introduced some new products and so the momentum there is strong. We are building on that momentum with some reinvestment or elevated investment in marketing, although we're also conscious to make sure that much like you may remember in our U.S. business several years ago, if we grow lead volume too quickly, it's tough to monetize it in a short enough period of time. So we are being reasonably prudent in how much we're investing there, given all the strength in the organic lead growth.

It's a really good story having crossed into profitability, but also being able to reap those margins without having to fuel them or feed them with increased marketing spend.

Rajat Gupta

Understood. Great. Thanks for the color and good luck.

Jason Trevisan

Thanks.

Operator

Thank you. Our next question comes from the line of Brad Erickson (phon) with RBC Capital Markets. Please proceed with your question.

Logan

Good evening. This is Logan on for Brad. Thanks for taking the question.

Given that the off-cycle or off-lease cycle was a little bit light because of just OEM production over the past couple of years, just curious, how does that sort of play out with your dealers' inventories between franchise and independent? Just curious on how you guys are positioned between those two subsets of used car dealers? Then just as a follow-up of the marketing comments through the year, how does affordability changes in used car pricings potentially decline sort of impact your expectations for marketing spend and margins throughout the year? Thanks.

Jason Trevisan

Sure. Thanks, Logan. It's Jason. From an inventory perspective, the biggest changes that we're seeing are growth in new car inventory, as you would expect. We have seen a slight increase, continued increase in used car inventory, but it's not nearly as pronounced as new car, which hit far lower depths and is now growing back much faster, still not even close to pre-pandemic levels for new car. And also, I don't believe not yet back to pre-pandemic levels for used car, although much closer.

Rising inventory tends to be a good thing for our Marketplace business. Dealers—as does higher turn times on lots—dealers feel understandably compelled to want to market more to move the cars quicker, especially if floor plan financing rates are high, which they are. Specifically, as it relates to off-cycle lease returns, it means that dealers are also looking for not only ways to sell those cars retail but also wholesale and so that should be a tailwind to CarOffer.

In terms of affordability, yes, that was the headline challenge, one of the headline challenges in 2023. Dealers typically have one of two ways to help combat that; one is to lower the price of the car. The other is to market more aggressively. We tend to think that marketing more with platforms like ours is a better ROI for them than lowering price, but we also know that they do have to lower price and so we give them insights and tools to help with that as well. We do think that affordability will help in '24, better than it did in '23.

There continues to be though an interesting dynamic between new and used, where with a lot of the OEM incentives on new, used car pricing still does need to come down quite a bit to make sense relative to new car. So we think it's generally going to be better. We think demand as a result, consumer demand will be up, but again, regardless of whether prices are rising or falling or inventories are rising or falling, we're trying to give our dealers more and more insights and actionable tools to help them manage their businesses better.

Logan

Got you. Super helpful. Thanks guys.

Operator

Thank you. Our next question comes from the line of Tom White with D.A. Davidson. Please proceed with your question.

Tom White

Great. Thanks for taking my questions. Just a couple on the Sell My Car Top Dealer Offer product. Jason or whomever, I'm just curious if you guys have any stats about maybe how dealers are converting on the foot traffic element of that offering in terms of turning sellers into buyer customers on their next car. And just curious whether you think the value that they get there is priced into the offering the way you guys are pricing that product today? Then could you just give a little bit more color on the intake tool you mentioned for this? Just kind of what's the impetus for adding that? What will it look like exactly? Thanks.

Samuel Zales

I'm happy to take it. Sam Zales. Thanks for asking. We're seeing really tremendous results from our customer base on conversion rates and they're comparing them—reminder that they have mentioned in the last couple of quarters. We built the product based on customers asking us to do so. They saw products in the market, in KBB and Accu-Trade and said, “We’d like something different, something better.” We're offering something completely unique to consumers, which is the choice of a white glove service with IMCO, as you know, in the combination with this top dealer offers, which means over the two thirds or so of consumers who are saying, "I am going to sell a car, but I might be buying a car as well,” I'm coming into the dealership and that dealership has an advantage to have a buy-sell. We talked about earlier with wholesale inventory as low as it is and high priced as it is, this is gold to dealers, having the opportunity to buy a consumer's vehicle.

So we're seeing tremendous conversion rate. We are in still a limited market launch. We're in 18 markets, as you know, 40% of the country. So we're able to work with every one of our customers that's involved so far, and the feedback I've heard from customers is conversion rates beating those other products in the marketplace.

You asked about the intake tool. We're using that for a number of reasons. One is to create more consistency for the consumer experience. We want every dealer to use the same type of inspection capabilities to be able to say this is the fair market value for that vehicle. It leaves the consumer feeling great about their experience, but importantly it creates the consistency between each of our dealers to have the same experience as others so that it creates a universal objective and strong experience on both sides of the marketplace.

What that's led to is great results. We're looking forward to continuing that as we go forward. We're in early access still, but we're very, very encouraged by the launch of this program that we started in fourth quarter of last year and has already expanded and we look to further expand as the year goes on.

Tom White

Okay. Thanks. It's a subscription offering, so does it show up in your marketplace segment, or is it in CarOffer?

Samuel Zales

It does. It does, Tom. It's a Marketplace subscription product. It's an add-on. It's now going to a dealer set and saying, “We're already talking about a listings product that lets you sell vehicles. Here's another subscription product with high gross margin that allows you to join and get more out of buying cars from consumers,” which as we said is gold in the marketplace because it's the hardest to find today without those off-lease returns.

Tom White

Great. Appreciate the color, Sam. Thank you.

Operator

Thank you. The next question comes from the line of Naved Khan with B. Riley Securities. Please proceed with your question.

Ryan

Hi. This is Ryan on for Naved. Thanks for taking my question. Just two from me, if I may. First, you had mentioned further price changes through ABRs in 2024. Can you discuss the scope and percentage of dealerships that may see significant changes? Then secondly, in terms of CarGurus' ad revenue, it seems like spending is improving across the industry, so how are you guys thinking about the opportunity there? Thanks.

Samuel Zales

Hi Ryan, it's Sam Zales. On price changes, I want to remind you that our QARSD success, our highest-ever year-over-year QARSD growth came because we have three or four major levers we use. One is just pricing dealers at market rates when they come in. Second is upselling dealers to a higher or premium package. The third is core unit pricing growth with our ABRs, and then also the product attachment rates, which are very, very strong.

On the pricing side, we're seeing the continued success of dealers recognizing our ROI that is working tremendously for them and going in with an annual business review and offering a couple of different things. It's not just a straight price increase. It's saying, "Here's a package that may be better serving you to grow your ROI as a customer and in your retail business, and that might require just a higher spend to get more value." But in many cases, we're taking the below-market priced dealers, understanding that they're below market and saying, “This is where the rest of the market is paying for that program you're on. If you want to stay in there, here's the price point to get into it. Here's a lower-level product if you want that.” And you could choose to leave the program if those products, that pricing isn't working. So we're offering multiple options that work tremendously to grow as one of the levers to grow our QARSD. And as you've heard before, when dealers say, “I don't want to take that program,” more than 50% of them come back onto the program within two quarters.

We hit about 20% of our customers last year with the ABR process. We'll continue to be aggressive on that as our results continue to work as well as they are. I'm not going to give a specific number, but we see the same kind of trajectory as we started the new year and we're going to take any underpriced customers that are below market rates, and because we have the confidence in that ROI to offer them the packages that meet the ROI thresholds that they'll still be positive about, but that give a fair share of that leverage to CarGurus.

We're excited to continue that process and hopefully that we'll continue to see the successes you're seeing in our QARSD and our Marketplace business growing as quickly as it has.

From an ad revenue perspective, we are cautiously optimistic that this is a year of strong performance in our business. Incentives are out there with OEMs spending more. Our year-end upfront advertising interest is strong, and so we believe that will be a business that returns to solid performance for us in 2024.

Ryan

Got it. Thank you.

Operator

Thank you. Our next question comes from the line of Jed Kelly with Oppenheimer. Please proceed with your question.

Jed Kelly

Great. Thanks for taking my question. Just following up on the last one, sort of around as you said 20% of ABR. Just as we think about the trajectory of QARSD in the back half and as comps get tougher, are you expecting the same amount of pricing pressure? Then my second question is, as sort of the potential cut of interest rates keeps getting pushed out, how should we view the pace of interest rates impacting consumer demand and your conversations with dealers? Thank you.

Samuel Zales

Jed, I'll take the first on ABR. It's Sam Zales. Thanks. I'm going to keep leaning for QARSD on the multiple levers that we use there. I think this is a really important message. ABRs worked really successfully last year; we're going to continue to do that for underpriced customers, and that is all fueled by our continued growth in our audience, by the way. Terrific to see our audience growing, which means we're providing more connections and more closed sales for our customers. But it's pricing new dealers, and we're continuing to succeed on that front.

It's upselling the premium tiers. Remember now, we've launched the Digital Deal product, which is working so effectively for our customers to close a down funnel consumer into our premium packages. So as we upsell our dealers into the premium packages, they're subscribing to Digital Deal to get access to those very low funnel shoppers who are closing at two times to five times our general leads.

And then we'll continue to work on pricing. We're continuing to product attach. Top Dealer Offer gives us another product in the arsenal to go to those dealers and add more subscription revenue. I think it will be the combination of those and not just pricing pressure to get us there. But I'll give you examples of a customer coming into our revenue kick off just a couple of weeks ago and saying, "I'm closing 46% of your leads." That tells us we know there's more opportunity to continue managing the value between what we're providing to our dealer customers to what we're reaping on our side of the business. We think even though we're going against comps that will be bigger, we do feel very strongly about this trajectory you're seeing. and Elisa's remarks mentioned the growth of our Marketplace business makes us feel very confident going forward.

Jason Trevisan

Then I can add, Jed, just on your third part there on interest rates and impact with consumers. As I mentioned a few minutes ago, two factors that do help our Marketplace business that are a tailwind are rising inventory and rising turn times. That tends to spur most dealers to want to market more. I would also say that it's not necessarily adding marketing budget dollars for a dealer, but it's reallocating how they spend their dollars. Remember that they're spending a reasonably small fraction in marketplaces today, and yet it remains one of the highest ROIs for them. And within marketplaces, we are often cited as the strongest ROI for dealers. So it's a pretty safe place for them to spend.

If interest rates were to come down and consumer demand were to increase, that tends to have a mixed impact on our marketplace and so there's not a high correlation between interest rates and our ability to sign new dealers. If you look at SAAR, for instance, if the SAAR expectations change by 5% or 10%, we don't see a discernible impact on our bookings either and so it's fairly immune from that.

One thing that we are doing, though, to help insulate even further is we're trying to add a lot more value to our marketplace—to our dealer customers and marketplace with insights and data and other tools that are independent from just simply the leads, the quantity and quality of leads that we deliver to them and the connections that we deliver to them, which we're very confident in the volume and growth of that.

The one final area I would say is finance in advance or consumer finance revenue stream of buyers, which is small on a relative basis, but it’s high margin and it's not insignificant. As interest rates have risen, those approval rates have gone down and so that business has suffered a little bit from it. If interest rates were to come down, then we would see higher growth than we're currently forecasting.

Jed Kelly

Thank you.

Operator

Thank you. Our next question comes from the line of Chris Pierce with Needham & Company. Please proceed with your question.

Chris Pierce

Good evening. Can you guys talk about the dealers you're adding back on to the marketplace? Are they 100% new to the platform or had they went away? I just want to get a sense of what's happening under the surface on the dealer side given kind of the detail you've shared around QARSD in the future? Thanks.

Samuel Zales

Thanks Chris. Sam here. It's a mix. I mentioned the ABR outcomes, which is a percentage of dealers who say, "I'm not going to take that price point,” that's a small percentage, but more than 50% are coming back on within two quarters. We are getting dealers who look and will say, as Jason was just mentioning, “The market's changed a little bit.” The consumer demand is down, particularly for the small independent dealer who is living off of, in some cases, credit card payments for the marketing that they do. They're very price-sensitive, so they'll come in, get off the program during the ABR process, stay off for four months and then say, “My gosh, my business is shrinking. Let me get back on again.” So we see the most turnover in that small independent segment, which doesn't make the biggest difference to our MRR overall, but you want to keep those customers because they're important to the consumer mix that they're getting all different types of vehicles to purchase from.

But we're still winning new business. And it's hard to believe. When you look at our TAM out there, there is still a significant number of franchise dealers and independent dealers who are on the sidelines for one reason or another. Jason mentioned, they may be spending more money on local advertising, radio, TV, other forms of media that are not even trackable and to get them converted over there's still a lot of them saying, "I have not been on the third-party marketplace. Let me go to the one with the biggest audience driving the biggest ROI." That's our opportunity to continue growing and fulfilling that new dealer adds segment you're asking about.

Chris Pierce

Okay. Cool. Then on the turn time data that you referenced, is this data that you already have because you have the dealers' inventory or a dealer has to send you new information? I'm sort of asking because, like you led into that can help with CarOffer adoption, helping dealers know what cars to restock their lot with. Is this something that exists right now or the plumbing has to be put in place or dealers have to send you more data to kind of really hone this product?

Samuel Zales

It's a great question, Chris. We have the data. The inventory feeds we get from our dealers are ones in which we then look at how quick those inventories are turning. We see when vehicles are on our site and go off of our sites. We're able to look at that information of the turn time. What dealers have asked us is two things. Jason pointed out, we don't have to just provide leads and connections to provide value to our dealers. They want the consultative feedback to help them run their retail operations more effectively.

What they're saying is combined consumer demand data, which is—and they all say it's the same way. "You have the largest audience. You can tell us where consumer demand is by geographic area down to a local market. Tell us what vehicles consumers are searching for and looking for, what turns I have on those vehicles today, how are my competitors turning their inventory and then tell me what vehicles I should be sourcing." So the great opportunity here is to combine the retail and wholesale capability that no other marketplace can provide with our combination of CarGurus and CarOffer.

You go to CarOffer's offer and you say, "You have a matrix setup to buy these vehicles. Did you realize consumer demand is up in these other types of vehicles? You should be building your matrix around that vehicle acquisition strategy," and helping them become more successful in a consultative way.

On the dealer side—on the retail side of the business is, "Which vehicle should I be planning for?" And as Jason mentioned in his remarks, Next Best Deal Rating. What price point allows me to get to the highest opportunity of winning consumer eyeballs on the CarGurus platform but not giving away too much gross profit. The entire process is looking at the synergies between CarOffer and CarGurus to maximize dealer profits, and that's what they're asking for.

The feedback at our kickoff meeting, our sales kickoff meeting this year from dealers was, "The price of entry is I need your leads and connections. I have to have those because they're the best in the market. But can you also provide me with this data that helps me run my business more efficiently as a marketer and a sourcer of vehicles?" and we think we have the only platform in the market to do so.

Chris Pierce

All right, appreciate it. Thank you.

Operator

Thank you. Our next question comes from the line of Ron Josey with Citi. Please proceed with your question.

Ron Josey

Great. Thanks for taking the question, guys. I have two. Maybe Jason and Sam, with the multiproduct attach increasing 36% year-over-year, talk to us more about the specific products just driving that growth and any insights on overall attach rate of the dealers would be helpful.

Then a quick clarification on the Sell My Car Top Dealer Offer. I know we're live in 18 metro areas and covering 40% of the U.S. population. Talk to us about what needs to happen to go live in more metro areas. What's the unlock here to maybe go nationwide? Thank you.

Jason Trevisan

Hey Ron, it's Jason. Yes, the multiproduct attach rate, I mean examples of other products would be Digital Deal is a key one. Highlight is another product that has been particularly attractive to dealers lately, Geographic Expansion is another as well. A lot of it actually dovetails with what Sam was just saying, which is that as we have multiple products, but then give more insights to help them know how to use some of these products for more specific purposes, whether it's to help or source cars smarter or market certain types of cars differently, it all comes down to their volume and their margin. So the portfolio of products we're building, coupled with the insights we're giving them are helping them to optimize that.

We're also, I think, being much smarter about how we think about the package levels. That's not exactly multiproduct attach, but that's a cousin of it because we are providing some of these insights for higher level packages for dealers who are just much deeper into our platform and getting much more out of it.

Samuel Zales

And Ron, it's Sam. I think you'll have heard this as a repetitive theme over the years we've talked. The Top Dealer Offer expansion to the rest of the country, which we're excited about, but we'll always be deliberate about is based first on consumer experience. We've said that about everything we've built here. You knew what our NPS scores were. Many of our products—IMCO being one of them—we're measuring that, we're watching that to ensure optimal consumer experience in this process.

Remember, a consumer is choosing to bypass a white glove experience and saying, "I'm going to get more money at that local dealership, but I want the experience to be high quality, high integrity and consistent." Hence, the use of this new intake tool that we're out there in the market with right now which creates a seamless and consistent experience between all the dealers who use it. It allows the consumer to say, “I understand why the price point might be different than what you first offered me,” if something is found at the local dealership and using the same consistent tool set.

So one is consumer experience in making as high as possible. Number two is the dealer experience. Earlier question was what kind of close rates are we getting? Now what we're seeing is tremendously high close rates from those dealers who have a consistent intake process for consumer acquisition of vehicles. There are a set of dealers who joined the program who don't have as consistent a regional approach. One dealer retail location might have a different intake process than another one, so your close rates will be different by each. We want to make sure those are as consistent as possible. We’re consulting and helping those dealers to be as successful as possible and the consistent results will say, “Okay, that ROI is high on your subscription program from Top Dealer Offer.”

The last part I would say to you is our economics. We've gone out with pricing in the market that we think is reasonable, but if the close rates continue as successfully as they are, we might change the pricing. The subscription might be too low right now before we head to the rest of the market. I'm not saying it is right now, but as we do that going forward it's going to be really important for us to think about the economics of balanced ROI between the dealer's access and what we get on our side at CarGurus. So we're thinking about that pricing point and making sure when we do roll out nationally, it's maximized for the win-win for both sides of that effort.

Operator

Thank you. Our next question comes from the line of John Colantuoni with Jefferies. Please proceed with your question.

John Colantuoni

Thanks so much for the questions. I wanted to ask about Digital Deal. When thinking about the addressable market for Digital Deal, are there any technical barriers or product investments that you're still working to address before expanding the offering across more dealerships? And when thinking about the opportunity set for Digital Deal, are there certain types of dealerships that are less likely to adopt the product, or could you see every dealership partner adopting it over time? Thanks.

Jason Trevisan

Thanks, John. We're always working to continue to make Digital Deal a better consumer experience, better dealer experience but no, there's not really a—there's no structural technical barrier to faster adoption there. There is some, I would say modest onboarding required at the dealer and for really sort of optimal results at the dealer, they do need to embrace things like hard pull financing, and they really need to, I would say, change the sort of flow of leads and how their sales team handles the leads. For instance, it's not a good consumer experience if the consumer does this work on our site and then walks into the dealership and the salesperson is not familiar with Digital Deal, and is not leveraging all the information that that consumer has given. None of what I've mentioned is a big hill to climb at all – it's not even a big lift for the dealer, but it does require a little bit of change.

Aside from that, there's not really consistent reasons why a dealer wouldn't adopt. It does cost money so some may be price sensitive to it (audio dropout) where consumers say they want the process to be. They say they want to do more and more and in a lot of cases most of the transaction online, and so consumer sentiment is there and we think that's where the market is headed.

On the consumer side, we do have more work to do to make it a more obvious and seamless flow on our site and so we are going to put more resources there so that it's easier to find, it's easier to do, and it's just more part of the central flow.

John Colantuoni

Great. Thanks so much.

Operator

Thank you. Our next question comes from the line of Doug Arthur with Huber Research Partners. Please proceed with your question.

Doug Arthur

Yes, thanks. A lot of questions so I'll just keep it to one. Just on a GAAP basis, is the true-up with the CarOffer close, is that done now, or are we going to see some lingering true-ups in the GAAP numbers, say in Q1?

Elisa Palazzo

We don't expect to see any true-ups going forward. The transaction is closed and so we recorded approximately $50 million in share-based compensation in the fourth quarter related to the transaction, but that should be it. We don't expect anything going forward.

Doug Arthur

Okay. Great. Thank you very much.

Operator

Thank you. Our next question comes from the line of Kunal Madhukar with UBS. Please proceed with your question.

Jason for Kunal

Thanks a lot. This is Jason on for Kunal from UBS. Thanks for squeezing me in. I have a couple of questions. First, could you please double-click into the recent trends you've seen within the dealer-to-dealer whole space, and also unpack a little bit more the value proposition and differentiation of CarOffer compared to the competitor offerings? For instance, I was curious to hear more about what's driving your pricing power with CarOffer (inaudible) your customer base? And I have a follow-up.

Samuel Zales

Sure, Jason. It's Sam Zales. The value proposition is very simple, and that is we've completely pioneered the industry in that, as you know, the wholesale market relies on an auction model for most of its business transactions today. That's moving more digitally and there are some players out there who are offering digital auctions. What CarOffer provides is a digital instant trade platform, which is very different, almost a stock exchange of vehicles a dealer would like to purchase and the price point, and the vehicles that a dealer would like to sell and their price points, creating a light capital model that brings a digital transaction and capability. It doesn't require a wholesale buyer or seller to sit at a timed auction and watch the vehicles go by. It's a completely different and new and innovative solution in the marketplace. We've said that it works perfectly for larger-scale acquirers of vehicles. It works for the larger players in the commercial space as well.

In a down market, it's a new adoptive tool because it requires in a price point market that's going down a dealer community to utilize and watch the vehicles and make sure they're inspected to the levels we're inspecting them and to reduce the arbitration potential of those programs.

We talked about our operational improvements with CarOffer. We've done phenomenally on that front. What we're seeing though is a business that Elisa mentioned upfront; we're going to keep that business with a new leader intact. The reason we're so excited about owning the CarOffer business eight months before we were going to is that we are now running the business from the headquarters of CarGurus and with Zach Hallowell, a veteran digital wholesale leader in place running that business. We're looking at product enhancements. We're looking at continued operational improvements that we've already succeeded at, but are going to push further on. And then a go-to-market focus, which is we're turning our team from sellers into consultants, providing the inventory management tools, the consultation, the AI-based predictive tools to help dealers engage in this platform more than they have over the last few quarters. That's going to take us a couple of quarters to turn around. We're excited about it because you've got a unique tool set with the value proposition no one else has. We just have to operate that business with new leadership to take it forward.

Operator

Thank you. There are no further questions at this time. I'd like to turn the floor back over to Jason Trevisan for closing comments.

Jason Trevisan

Thank you very much and thanks to everyone who joined us this evening, and for the thoughtful questions.

I just want to wrap up by sharing how proud we are of our exceptional performance in Q4 and throughout 2023, and probably most importantly how well we think we're positioned for 2024. I want to thank all of our employees globally who have contributed so much to helping us become the number one digital destination for consumers and dealers to confidently and conveniently buy and sell any vehicle. Thank you very much everyone. Have a good evening.

Operator

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.