Monro, Inc. presents at UBS 12th Annual Global Consumer and Retail Conference

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Event Participants

Analysts (1)

Michael Lasser

Executives (1)

Brian D'Ambrosia

Michael Lasser

ANALYST

Good morning, everyone. I'm Michael Lasser, the hardline, broadline and food retail analyst from UBS. And welcome to day two of our UBS Global Consumer and Retail Conference. We could not be more excited to have the team from Monro with us. Monro has been a long-standing participant in the UBS Consumer Conference, and we are so glad that you are back this year.

With us from Monro is the company's Chief Financial Officer, Brian D'Ambrosia, and a year into his role? Over a year; Felix Veksler, who runs the Investor Relations function. Monro has made a lot of progress in a transformation effort that it's been executing over the last few years, operates in a very dynamic and interesting area of economy, the auto care industry, which tends to be pretty needs based. And at this time, when the economy is uncertain, it's good to have a need-based offering for consumers.

Michael Lasser

ANALYST

So with that being said, and -- if you could give the group a sense of who the customer is for Monro and what have you seen? What have your observations been about that consumer?

Brian D'Ambrosia

Yes, absolutely. We really appreciate you having us back again, Michael, and good morning, everybody. When we look at our customer, our customer cuts across some different demographics, but they have one thing in common, is they're driving a -- typically, our sweet spot, a 6- to 12-year-old vehicle. And we'll see vehicles certainly newer than that, and we see our fresher vehicles older than 12 years, especially as the car park has been aging. But the one thing in common is that they are driving an older vehicle.

And there's different reasons for that. It may be a single-person household driving, making $50,000 or less, driving it for obvious economic reasons and affordability issues of new vehicles as they look at their overall spend across their categories. And it's the same thing for households $100,000 or lower that are doing that as well. We'll also see some more affluent households that have maybe 2 or 3 free vehicles, the third vehicle may be for a daughter or a son and those create that third vehicle that's aged. And they're likely the customer of both the dealer for their newer vehicles and of the aftermarket.

So it's really based on the vehicle. And that's based on rational economic behavior where, as the vehicle depreciates, you start to look at the cost of servicing that vehicle and look to really kind of shop for value and the aftermarket provides that value against the depreciating asset for the consumer. So I would say, as we look at the behavior of that consumer recently in this economic environment across those income thresholds, we have seen a shop for value. We've seen a good example of that being trade down within tires. And it's not just the lower end of the tire Tier 3 down to opening price point, it's our Tier 1 tires looking for manufacturer rebates, looking for offers, looking even to trade down and see what value they can get maybe from the next brands that are down on the price tier.

We've also seen deferral on the service side. And that's because trade down opportunities are fewer in service. You either do the work or you don't. You don't necessarily have as much ability to trade down on the price point. And so we've seen deferral open up on the service side.

But to your point earlier, Michael, the auto aftermarket, particularly the service and tire business that Monro operates in, which is about 50% tires and 50% service for us, service being underhood, undercar repair, those are nondiscretionary. There's no such thing as a mild. It doesn't include wear and tear on a vehicle. So we're seeing the consumer continue to drive. We're seeing the cars continue to age.

That means the work needs to be done. On tires, it's being done at value price points. On service, it's being elongated, but cannot be put off forever. But we're certainly seeing those trends more pronounced in the lower income levels.

Michael Lasser
ANALYST

That's very helpful. And I have some good news. My 15-year-old daughter, Sydney Lasser, got a learner's permit on Monday. So you may have a future consumer in the not too distant future.

Brian D'Ambrosia

We'll be looking forward to that, pretty sure.

Michael Lasser
ANALYST

Now it's been quite a few days with the events of what's happening in the banking system. Give the crowd a sense for how you see any impact of some disruption in the capital markets or the banking system and your customer or the auto aftermarket in general?

Brian D'Ambrosia

Yes. First of all, we certainly have no exposure to the banking issues that may or may not play out here. But as it relates to the customer, I think that's really the question. And I think that, as you look forward, we think about outcomes of this environment and certainly a policy. And therefore, in one of those outcomes is obviously the possibility of recession.

We don't root for it, we don't root against it. We just know that it's in the possibilities of outcomes. And so for us, we look and say the auto aftermarket, because of its nondiscretionary nature, is very resilient during recessionary periods. It tends to be in environment where consumers continue to invest in their vehicles because of a trade down, ultimately, from a new or a used car purchase to maintaining what's in the driveway. It's a period of time where vehicle miles travels tend to hold up pretty well, as you see consumers trading off of other forms of transportation and driving more for other vacations or other recreation.

And so we've done very well and held up very well during recessionary periods. A good example of that being 2009 through 2011, our business comped about 6.5% during that period of time. So it shows you the resiliency of that. And obviously, that was a disinflationary period of time post Great Recession, and it also was a period of time where -- so it was really led by car count and traffic, those comps. So for us, that's been our outlook that whether it's rate hikes or tightening credit conditions, if that's going to pressure the consumer, maybe tip the economy into a slowdown or a contraction, we operate well in that environment.

Michael Lasser
ANALYST

Yes. That's super helpful. And in the past, have you seen any changes in vehicle miles driven which -- or traveled, which is such an important measure for -- and driver for the aftermarket enduring these recessionary periods?

Brian D'Ambrosia

Yes, I think that it's our -- talk about vehicle miles traveled. It really is the #1 metric -- leading metric that we're going to look at as a company because it's the one item that really helps you get a sense for the demand profile. And vehicle miles traveled have been pretty stable on an upward march as the car park has expanded due to population growth. As the car park is also aged, more miles are being driven within our sweet spot. So the average age of vehicle since I've been at Monro has gone up from about 9, 10 to over 12 now.

And that means that more miles are being driven in that sweet spot of ours as the miles driven also expands. The one shock that happened, obviously, during -- related to vehicle miles traveled was during COVID and the lockdowns. We saw a 50% drop. The good news is right now, we're back to pre-pandemic levels in vehicle miles traveled. We may have foregone some of the growth we would have otherwise seen over the last few years, but at least we're back to pre-pandemic.

And I think, looking back on that ['09 to '11] period, I'd expect continued incremental kind of normal growth trend from Pre-COVID.

Michael Lasser
ANALYST
Before we move on to some of the specific strategies that Monro has been doing, I want to touch on one of the other dynamics within the aftermarket, which has been -- there's been a drop in new cars. It's been difficult to find a lightly used car. And as a result, perhaps folks have been maintaining their vehicles for longer. How do you see the relationship between the demand that the aftermarket has been experiencing and changes in either new or lightly used?

Brian D'Ambrosia

Yes, it's a great question. I think the first thing to anchor on is the U.S. auto aftermarket has over 300 million vehicles in it. So it's not a cohort that changes rapidly. And that's an advantage for the aftermarket in that it's a stable customer base that, over time, has been incrementally aging and incrementally driving more miles in the -- in those serviceable sweet spots of the aftermarket.

So any changes that occur, they occur slowly. So the scrappage rates have been reduced, to your point, as people are holding on to vehicles longer and the new cars coming into that 0 to 5 range have been lower. And so that benefits us to the extent that people are continuing to invest in their vehicles. And we think that, as we talked just a few minutes ago, the recessionary trend, that's a typical recessionary trend and now it's obviously playing out in more of an inflationary environment as well. Over the long term, as we saw after the great financial crisis, it does create sometimes an air pocket that needs to then flow through.

So those -- we benefit from robust new car sales because, ultimately, those new cars become cars in the aftermarket in the next 5 or 6 years. So we saw that after the GFC that out in like maybe '15, '16, '17, you start to see an air pocket from those low sorry years. But again, you're talking about, I think, marginal changes because of the size of the aftermarket.

Michael Lasser
ANALYST
And on gas prices, we've seen some volatility. There's a perception out there that the consumer wants to spend a fixed amount on their cars. So when gas prices go up, they might defer some maintenance. When gas prices come down, because you have this mindset that you only want to spend a fixed amount, maybe you'll go back and do some maintenance. Is that a misperception?

Or is there some truth to the relationship between gas prices and the aftermarket?

Brian D'Ambrosia

I think as we look at gas prices historically, let's go pre one year ago when [indiscernible]. It's been more of a correlation between gas prices and vehicle miles traveled. So the price at the pump influences how much you utilize the car, which means that service cycles might extend if less vehicles are being put on a vehicle -- less miles are being put on a vehicle per day or per week or per month. So that's been the traditional correlation. But I think what we saw beginning a year ago and a little bit previous is gas prices became an overall share of wallet concern because food prices, shelter, transportation, they were all going up at the same time.

So that was causing the consumer to really rationalize their spend as it relates to how much can I afford in this part of my budget, which is auto care, inclusive of gas prices, knowing that the other pieces of the wallet were getting stretched even further. So for us, we saw that dynamic and certainly have seen some relief in that as the gas prices have abated. But I do think, like I said earlier, we're seeing a consumer still shopping for value and still deferring when they're able to.

Michael Lasser
ANALYST

Got it. Speaking of inflation, it's been across the board. The aftermarket tends to deliver an inelastic good. It's a needs-based offering. So give us a sense for, across the industry, how much pricing has been passed through?

What do you think the outlook for pricing is from here? And how has Monro been navigating through this very challenging environment from a pricing perspective?

Brian D'Ambrosia

Yes. It's an important question, and it has been a challenging environment. I'll split it between our two businesses or two main categories: tires 50% and service 50% of our business. On the tire side, the tire cost is -- the actual cost of the tire is the largest input cost for us when we do a tire sale. The installation is a much smaller cost, an hour of a technician's time.

The tire cost is the vast majority of that bill of materials. And so it's very important to make sure that you're passing along any cost inflation that you're seeing on that tire. And we've seen -- we scrape about 100 DMAs across our country and know our competitors' pricing and competitive set across, and we price accordingly to where we want to be positioned against those competitors. And we've seen rational behavior in terms of passing price increases on. Now on the flip side, as that price has moved up, you've seen the consumer trade down to lower options.

So they're clearly reacting to those price increases. On the service side of the business, the part is a much smaller piece and the labor is the larger piece of service. Service comes at higher volumes because it's more labor intensive and less material intensive, but labor is still the largest component in the bill of materials for a service job. We've seen labor wage increases. We've made investments in labor quantity to service and grow our business.

But at the same time, because of the deferral cycle on the service side, I think you've seen less price passed to the consumer and a real -- a much more competitive environment on the service side as companies are trying to really position themselves. So as the consumer does shop in those categories, they're going to be looking for value and they're going to need to make choices, and you want to be priced right there. So I think that's the overall impact. As you look at what that does generally to our margins, it's obviously a trade down in tires pressures margin, not fully passing wage increases pressures margin. And then you see also the fact that in that environment, you're selling more tires than service because of the deferral in service.

So that's also pressures margins. So mix and price have been a headwind for us in FY '23. We haven't captured as much as we've received in terms of cost. And at the same time, we're making labor investments. So I think '23 was a year of some margin contraction for those reasons.

As we look forward to our FY '24, we certainly expect to recapture some of that as we leverage our technicians and also our ability to influence the mix through pricing and assortment.

Michael Lasser
ANALYST

And how is the market for techs right now? It's been a challenge, maybe you'll get some equity research analysts to come and want to be a tech given that there is a shortage of techs in this country, and it can be a nicely lucrative career. Are you seeing any easing in some of those pressures?

Brian D'Ambrosia

The technician or the competition for technician labor has been one that we've been fighting since I came to Monro in 2013 and prior. There's been a multiyear kind of generational trend of less technicians coming to the trade schools and a shortage versus where the demand is, which is a growing aftermarket. And so that's something that we're well versed in attacking that challenge, even pre-COVID. Now COVID certainly exacerbated that. And so what we've been able to do, I think, is very important in terms of adding 650 technicians in this environment where it is a battle for technicians.

And so I think that says a lot about Monro's value proposition to these technicians, the career pathing and training, the investments that we're making in technology and also the productivity of our stores because, ultimately, technicians stay where they're seeing growth, and they're going to get cars to be able to see and money to be made. And ultimately, for us to attract and retain them, we've done a good job across those fronts. And that's, I think, a real important part of our growth has been the ability to add labor to our stores. It's still challenging. Wages have increased, as I just mentioned in the previous question.

But that's something that we need to manage. We're at the end of our technician investment in terms of quantity of techs. We feel good about where we're at there. We're really focused on now the productivity of the technicians we've added. So that takes some pressure off the ability or the need for us to go out and recruit more technicians than we lose.

But at the same time, we continue to expect that wage pressure will continue into '24. And that's our job to manage through productivity improvements and pricing.

Michael Lasser
ANALYST

The mantra in the financial services industry is also do more with less. So we get it. This is a point, I think a good one to turn to some of the strategies that Monro has put into place for a while now. And for those who are a bit less familiar with the story, it seems like Monro has pivoted over the last 5, 6 years under your leadership and the rest of the team where historically, Monro's focus was really on doing acquisitions, M&A. And the old adage was, during tough times, you buy a little bit more.

During good times, the assets that you have would do a little bit better. And I think this is no longer your father's Monro. In the last 5, 6 years, the focus has been on -- it's less about accumulating assets and more bringing together the assets that we have. So a, is that fair? And b, where is Monro in this transformation?

Brian D'Ambrosia

Yes, I would say that's fair. I would say that the company has done a tremendous job of consolidating the auto aftermarket. And I think our previous leadership saw opportunities to do that even before Others. It was in the auto aftermarket and also in the financial sponsor community. I think that Monro was on the leading edge of a lot of that consolidation.

And it's really allowed us to grow to the scale that we're at now, where scale becomes a real competitive differentiator for us to maintain our rock-solid balance sheet, but still make investments in technicians and labor, make investments in price and an assortment with our tire category and investments in our stores and people. So I think the scale that we've achieved through that acquisition strategy is a real competitive advantage for us. At the same time, I think you're right. I think there has been a pivot from a focus maybe of importance on the roll up to, okay, let's look at the assets that we've acquired and make sure that we have scalable standardized processes so that we're not only taking advantage of our scale in terms of price advantage through supplier agreements and assortment and all of that, but also taking advantage of our scale through guest experience and making sure that we're leveraging our collective chain to deliver a consistent and guest experience that leads to repeat business, ultimately, supporting organic growth in addition to the continued opportunity of M&A growth that is there for us. And so that more balanced approach, I think, to operational improvement as well as continued M&A is the philosophy of the business now.

I would say it's not one or the other. We still have an expectation that our unit count will continue to grow and we will continue to invest in M&A. But at this point, in Monro, I think we look at -- our largest opportunity is to really deliver those sustainable mid-single-digit comp store sales and then to recapture some of the margins from FY '23 and continue to expand both gross and operating margins and then generate a lot of cash through our working capital management as well through operations. Those things position us to be a great acquirer going forward.

Michael Lasser
ANALYST

And with that being said, one of the key elements of the strategy has been to focus on some of the stores that had not performed as well. And so, a, why has that been the case? And b, it seems like whatever you're doing, and if you could outline those steps, it's been working because you've seen some improved performance, especially at those underperforming stores.

Brian D'Ambrosia

I agree. I think that what we've done across the chain, we've done nothing different at the underperforming stores. We've just maybe done in a little more concentrated way, in a little of in advance of the chain. So meaning, we started with the underperforming stores, we gave them a concentrated focus of technician staffing, of technician productivity improvements through the training program and also through that standardized in-store execution. So that then scaled throughout the chain.

And I think you saw the benefits for the last three quarters of 10% to 15% top line growth at those underperforming stores. And then last quarter, 5% growth at the rest of the chain. So I think that's all coming together to deliver outsized performance there. It all starts with the staffing. In order to deliver on the in-store experience that leads to a good guest experience but also a rewarding experience for Monro in terms of our ability to grow sales and see more cars, it comes through staffing.

And there's a couple of reasons why I think -- I won't get into maybe all the reasons why those -- these stores may be attrited staffing throughout the years, but I can say post-implementation of the staffing why I think that they've responded very well in terms of comp growth. The first is, you're able to be much more convenient to the guest. So that store manager is able to ask the guests when they would like to come in versus talking about how busy the shop is and I can't get you until next week, all the things that I think we've probably all heard. So it allows us to be much more convenient to that guest appointment. And then on top of that, when they do come in, it allows us to deliver on the promise of getting their car to them when they expect.

But the important thing in between is it allows us to really invest the time and doing a full courtesy inspection of the vehicle. We're not just processing the car for what they came in for, but we're completing, in a thorough and thoughtful way, the inspection of the vehicle, which either leads to more business that day or it doesn't. But it ultimately allows us to have a conversation with the guests about what their car may need now or may need the next time or the time after that. And that builds that trust, especially when those things come true in the future. So that is an important part of what labor in the store can do for you.

Michael Lasser
ANALYST

And has this been a training journey? Is it -- it's a compensation journey? Have you had to change the compensation to incentivize some of these behaviors? Change the metrics that they're focused on? Can you give the audience a bit more insight into that?

Brian D'Ambrosia

Yes. It's been -- it starts as a staffing journey, like many things do. But within staffing, it's not just quantity of staffing, it's also the complement within the store. So we've looked at our models of -- our ratio of higher-level technicians versus our entry-level general service technicians, our ratio of how many people on the front shop, as you know, taking care of the guests at the counter versus those that are doing the work in the bays and really rebalancing that in a lot of these smaller stores to optimize that for -- to be able to see more vehicles and spend more time with each vehicle that we see. So that's been the first part.

And then certainly behind that has been scheduling. We implemented a scheduling software during COVID. It's benefiting us in spades now. It's -- in the past, Monro -- and a lot of these investments Monro made just before and into COVID related to technology in the stores. A big one has been our ability to manage our labor force through an online scheduling tool.

In the past, it was paper-based and now we have visibility to all of our schedules. We know when schedules are efficient or not efficient, optimized or not. And that's allowing us to make sure we have the right tech staffed in the store, but they're scheduled at the right times of the day and on the right days of the week that really are going to optimize the guest experience again. And then finally, it is training. I mean we -- again, during pre-COVID, we launched Monro University.

And we're really leveraging Monro University as well as in-person training from a more filled out field training staff and utilizing Teams and Zoom and all of those things to do remote live trainings as well. Again, some key initiatives, but things such as phone training for our front counter, courtesy inspection training for our in-store teammates, educational selling for our front counter and then things just as technical trainings like how to really utilize our new battery testers and things like that, that bring all of that together in-store. And the focus, like we talked about, has been on those underperforming stores and then that's starting to spread throughout the chain.

Michael Lasser
ANALYST
I might add, you've made an investment in Investor Relations that's been paying off too.

Brian D'Ambrosia

Yes, I would say so.

Michael Lasser
ANALYST
On the subject of the underperforming stores and taking what you've learned to the rest of the chain, is there anything different about the rest of the chain that wouldn't make it relevant for the experience and the good news that you've had at the underperforming stores?

Brian D'Ambrosia

Yes. I think the full chain benefits from everything that we're doing around technician staffing, around the complement optimization, around our scheduling tool, certainly, the training. They just have -- they've had a fairly good comp performance along the way. So their opportunity for outsized comp growth is not as pronounced as the underperforming stores. The underperforming stores have had multiyear declines that we're expecting multiyear outperformance of the chain as they return to sales levels and profitability levels that are much more comparable to look-alike stores in their areas.

Michael Lasser
ANALYST
And how -- what's the size of the cohort of the underperforming stores versus the size...

Brian D'Ambrosia

It's about 300 of our 1,300 [indiscernible]

Michael Lasser
ANALYST

The example you cited about the labor scheduling tool that you put in is a good one. It shows the opportunity to deploy technology to replace tasks that were being done manually and use that to improve the guest experience. Are there other examples of that, that are still on the horizon that can be implemented or other types of strategies that can be implemented that you can use a similar approach?

Brian D'Ambrosia

Absolutely. We have a robust technology road map, some other things in addition to just that we've recently implemented, the scheduling tool. We re-implemented an entire company-wide phone system, which really allows us to capture all of our call data. We're using that to monitor the efficacy of our call conversion into appointments. So that's how it helps us to also give early indications of, do we have a staffing issue at a store that's preventing us from converting calls into appointments at the same ratio as we would expect?

Do we have a selling issue where our store managers need some training on how to better sell the appointment on the phone and follow the scripts that we've have been able to provide? So that technology allows us really full visibility and ability to listen to all those phone calls so we can understand what the guest is asking and how our stores are responding to that. We implemented a category management tool for tires, which in previous to this, we were managing our tire category through spreadsheets and now we're using a Blue Yonder to be able to really manage our largest category. And that's helping to inform a lot of these pricing decisions. And it's also a real point of interaction for planning and forecasting as we partner with ATD, who's now our primary tire distributor as well as our category captains and the branded side, to be able to make sure that we're making the right assortment choices and the pricing accordingly.

So those are examples of recent technology implementations. But as we look forward, we have what we call the Monro Digital Shop. And that's our initiative to really transform the way we execute in-store and then how that ultimately interacts with the guest. And a good example of that is tablet technology. All of our stores are equipped with tablets now.

And that tablet technology is on a road map. The first part of that is, it's basically utilizing technology to allow the tech to be able to look at things on the tablet, look at their engine, wiring diagrams. They have rescue lens, which allows you to get somebody on the tablet with you, while you video, what's going on in the engine. You bring in additional resources to that tech right at the car where he is doing the work, where in the past that would require to go into the office, print out the wiring diagram, so the efficiency of the back shop by putting that technology in the hands of the tech is important. But it also becomes a launching point for further enhancements.

And one of the things that we will be piloting in FY '24 will be the electronic courtesy inspection. So the paper-based form that you currently would receive if you went to Monro, the red, yellow, green on brakes, tires, all the 32 points that we look at will be transformed into the tablet. And so that does a couple of things for us. Similar to with scheduling where when it's paper-based, we didn't know if a schedule is even being posted for that store, when it was being posted, how effective it was. You take now that paper-based DI where we have lower visibility to what's going on at the store, you put it electronically.

Now we can see, making sure every car is getting a courtesy inspection. We can look at the efficacy of the courtesy inspection to make sure it doesn't look like it's being pencil whipped. And we can make sure that those things that are being found on the courtesy inspection are ended up on the invoice to the consumer or at least as items that were rejected by the consumer for further marketing to them later. So it really ties all of it together just by getting that on the tablet, and it's a much better experience for the teammate as well. So there's a lot of things then that branch out from that, but that's really what our road map is, is creating the tablet to really be the backbone of both the back shop and the front shop.

Michael Lasser

ANALYST

And at the risk of being cliche to use the baseball analogy, it does seem like this is all still early innings and the benefit is on the comp. Is that fair? And where is the rollout of the tablets and some of the other initiatives?

Brian D'Ambrosia

Absolutely. It's been within the last year that we rolled out the tablets for purposes of the technician being able to work at the car. It will be in the next year that we move into the more robust tablet-based inspection. And then beyond that, it unlocks a lot in the way we can interact with the guests, both through SMS, text, e-mail. Being able -- a lot of guests don't wait for their vehicle, but you still want to be able to do a show and tell of what they need.

The ability to capture pictures of their vehicle to show them exactly what you're talking about if they're not in the store to be able to walk them out to the bay and point to the issue at hand. So it just provides a more robust framework for us to do that. And ultimately, I think it builds a lot more transparency with the guests, which in an industry that needs trust, that's important.

Michael Lasser

ANALYST

And it seems like the auto aftermarket is an industry that's been a little slower to adopt technology, especially because you have a lot of independents who may not have the resources to make these types of investments. So Monro is going from maybe behind the curve in some of these processes to now seemingly ahead of the curve. So is that a fair characterization?

Brian D'Ambrosia

Yes, I think so. We believe that there are certainly smaller providers and some more not as scaled players that are doing some of these things. But on a scale basis, we believe this would be industry-leading. We think that we've got the partners to be able to accomplish this in a really, I think, cutting-edge way that puts us, like you said, in a lot of regards at the forefront. So there are areas where we're still playing catch up, obviously.

But I think one of the advantages is, we've really leveraged a lot of our -- both technology partners, but we have really -- as Mike talked about, Monro is extremely focused on developing and leveraging strategic relationships. And we see that with our -- with the transaction we did with ATD. We see that with our ability to have divested our distribution assets and now really leveraging our partners through our supply chain. And all of those relationships, they all cumulatively allow us to be more nimble when it comes to trying to do things that are like the tablets.

Michael Lasser

ANALYST

And you made the point earlier, which was a good one that while the focus has been on improving the execution, bringing together this chain and making it an even more powerful platform than it is, there is still an opportunity to consolidate what is a fragmented industry. So can you give us a sense for what the lay of the land looks like in the auto care industry? And then I want to get -- after that, I want to ask a question just around the approach to M&A and doing further deals.

Brian D'Ambrosia

Absolutely. There's over 100,000 service outlets nationally. We're one of the largest, obviously, with 1,300. I think the top 10 have only about 15% market share. You can be less than 10 stores -- about 10 stores as a tire provider and be in the top 100 tire chains in the U.S.

So there's a long tail on the fragmentation. And it -- I think as we -- the primary reason, in addition to the economics for a lot of the roll-up and the consolidation thus far, has been demographics in terms of first and second generation owners without succession plans and looking for other options for their business. I think that continues. At the same time, I think you see some of the acceleration in both technology as well as what's coming in the car park, whether it's electrification or just needed investments in technology for lower-profile tires or different types of technology to really fully service guest vehicle or provide the guest experience you want, that requires capital. And so I think that's where our scale, the cost advantages that we have that smaller chains don't enjoy, they put us in a position to buy really good businesses where those companies have done a really good job of building trust and relationship with their guests that really allow a more capitalized company to come in and make the investments that are needed for what's going to be coming down the pike.

I think that could accelerate some of the consolidation. So we think it's a robust environment moving forward for continued consolidation in the industry. And we believe all the things we're doing now are going to set us up to be a big part of that consolidation.

Michael Lasser
ANALYST
And what do valuations look like? Does some of this disruption in the credit markets impact that make -- create more opportunity?

Brian D'Ambrosia

Yes. As it relates to valuations, there hasn't been a significant change in the valuations of what I would call Monro's traditional roll-up stores, those 5 to 40 store chains. The purchase price on those are more easily financed or a little less sensitive to cost of capital increases. And those multiples have been pretty consistent for a while now. Where maybe you've seen peak multiples pull back has been maybe some of the larger deals that are more sensitive to that financing.

But at the same time, there's been a little less activity in that area as well.

Michael Lasser
ANALYST
And what about from a geographic perspective? Monro kind of was following a continuous state strategy and then found some opportunities in other parts of the country.

Brian D'Ambrosia

Yes, absolutely. We continue to grow and fill in the map. And on the West Coast, we're in California, Nevada. We're up in Idaho. We've just recently did an acquisition that added our presence in Iowa.

And then the bulk of our concentration is certainly in the Northeast, Mid-Atlantic and continuing to fill out Florida and the Southeast. So as we look at that, we have continued opportunities across our existing footprint to continue to build density in a lot of our markets. But at the same time, if we look at our expansion plans, we'd like to continue to build out in the geographies that we've most recently acquired, including the Southwest, the Southeast. And ultimately, to connect them across the South would be logical, given where new vehicle registrations are and certainly population movements.

Michael Lasser
ANALYST
And ultimately, in -- on the distribution side of the aftermarket, we've seen a lot of consolidation, a few big chains to dominate. Would you expect similar outcome on the service side as well where the big are going to become bigger and it just will be a little less difficult -- a little bit more difficult for the smaller independents to keep pace?

Brian D'Ambrosia

Yes. I think in terms of the service, Monro service business...

Michael Lasser
ANALYST
Yes, the service business, the industry will become consolidated. Monro is going to be a leader, but you'll see a few large players.

Brian D'Ambrosia

I think so. I think you could see consolidation throughout the space of the aftermarket. You've seen some larger M&A already. I think you continue to see that. And I think that presents opportunities for well-capitalized players like Monro.

If you look at where we're running right now, we're only about 0.7x levered bank debt to EBITDA. And even though that's our leverage profile right now, we still deployed a lot of capital during the year in terms of returning cash to shareholders through our share repurchase program, in terms of our dividend, our CapEx, getting a couple of smaller deals done. Yes, we still maintain a really attractive leverage profile, and that's because of the cash generation of the business. So for us, that presents a lot of optionality as we look forward on how to use that balance sheet to best drive shareholder returns, and certainly M&A of all sizes are an opportunity for us.

Michael Lasser
ANALYST

And you mentioned that Monro is mindful of the changing dynamics in the vehicle population. It's hard to have a conversation around the aftermarket without talking about the electrification of vehicles. I think the perception is it's going to be negative for the industry. Those that might have an electric vehicle, like some of our friends in the audience, might know that electric vehicles burn through tires pretty quickly. So Monro actually has a really complementary set of assets to service the changing vehicle population.

So can you give us a little bit of your perspective on how, over time, as the vehicle population does change, what does that mean for Monro?

Brian D'Ambrosia

Yes, absolutely. I'll go back to my earlier comment that there are 300 million vehicles in the auto aftermarket. The vast majority, nearly all of those vehicles are internal combustion engines. So as you move into an arrow where certain states are going to be phasing out the ability to purchase internal combustion engines in the future, you could have some consequences where that ICE population ages out even further, meaning you're going to have people wanting to hold on to internal combustion engine vehicles and invest in them, either because of affordability issues on a new EV or just the desire to continue to drive vehicles. So we think there's going to be a long serviceable aftermarket for the 300 million internal combustion engine vehicles and hybrids that include ICE engine going forward.

That being said, there's no doubt that EVs are here. They're in our base as we speak. If you look out to California and Northern Virginia, Florida, we see electric vehicles every day. But there are certain things you need to prepare for as you invest in, as you service electric vehicles, and we've done that across our chain. Any one of our stores can see an internal combustion engine vehicle.

You have to retrofit your lifts with certain spacers to be able to properly lift an electric vehicle so that you don't damage the under -- the battery compartment under it. You have to train your team on how to properly lift the vehicle because there are certain settings, there's some different modes that create some air compression and decompression that allow certain spacing to be achieved so that you don't damage the engine compartment -- the battery compartment. So that has all been rolled out across Monro. All that retrofitting has occurred, all that training has occurred. So we are EV ready for the services that we currently provide.

So what those primarily are coming in for our tires, they are heavier vehicles. They include a lot more torque on the tire, which wear it out faster, but we're seeing it for ride control and also for friction replacement. And all of those services are compatible to our service model. The one area that you get where there is no overlap is fluid exchange, which is oil change, 10% to 15% of our business. That's the area of the 300 million vehicles that will, ultimately, migrate to the point where we'll have to be able to service oil on those ICE engines, but we'll have to be able to be relevant to the battery component, which will ultimately replace -- replaces the oil service.

Usually, those are going to be longer in service duration, but they're going to be at higher ticket. And I'm not talking just battery replacement, which is an opportunity, but it's more battery service. There's a lot of hoses and coolant that goes into keeping those battery compartments cool. There are failure points on those hosing on those valves. And certainly, there is replacement needed on and refresh needed on those coolants to be able to properly function.

So those are all opportunities for us in the future as we start to see the critical mass build in. But currently, we've really just trained our team on how to currently service an electric vehicle on the services that they come to you for.

Michael Lasser
ANALYST

And in a weird way, as there are more electric vehicles, could even be a bigger opportunity for Monro because it's going to come from more players than just those that have maybe had a captive element of their service like Tesla. It's hard to work on -- others to work on a Tesla [so as] the breadth of the electric vehicles that could play well...

Brian D'Ambrosia

Yes. And I would say that if you're in California traveling stores, you'll see mostly Teslas that are the EVs. But you're correct. And I think that -- we talked about rational economic behavior before. That doesn't change in the EV world.

As that vehicle depreciates, there's going to be a big place for the auto aftermarket to deliver value to a depreciating vehicle and a consumer that does not want to pay dealer prices for those -- that aging vehicle.

Michael Lasser
ANALYST

This was awesome. We can't thank you, Brian, Felix, enough for joining us today and telling the Monro story. Please join me in thanking them for delivering a wonderful presentation.

Brian D'Ambrosia

Thank you.