REFINITIV STREETEVENTS

EDITED TRANSCRIPT

ORLY.OQ - Q1 2024 O'Reilly Automotive Inc Earnings Call

EVENT DATE/TIME: APRIL 25, 2024 / 3:00PM GMT

OVERVIEW:

Company Summary

REFINITIV

CORPORATE PARTICIPANTS

Brad W. Beckham *O'Reilly Automotive, Inc. - CEO*

Brent G. Kirby *O'Reilly Automotive, Inc. - President*

Jeremy Adam Fletcher *O'Reilly Automotive, Inc. - Executive VP & CFO*

CONFERENCE CALL PARTICIPANTS

Christopher Michael Horvers *JPMorgan Chase & Co, Research Division - Senior Analyst*

Gregory Scott Melich *Evercore ISI Institutional Equities, Research Division - Senior MD*

Michael Lasser *UBS Investment Bank, Research Division - MD and Equity Research Analyst of Consumer Hardlines*

Michael Allen Baker *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Seth Mckain Basham *Wedbush Securities Inc., Research Division - MD of Equity Research*

Simeon Ari Gutman *Morgan Stanley, Research Division - Executive Director*

PRESENTATION

Operator

Welcome to the O'Reilly Automotive, Inc. First Quarter 2024 Earnings Call. My name is Matthew, and I'll be your operator for today's call. (Operator Instructions)

I will now turn the call over to Jeremy Fletcher. Mr. Fletcher, you may begin.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Thank you, Matthew. Good morning, everyone, and thank you for joining us. During today's conference call, we will discuss our first quarter 2024 results and our outlook for the remainder of the year. After our prepared comments, we will host a question-and-answer period.

Before we begin this morning, I would like to remind everyone that our comments today contain forward-looking statements, and we intend to be covered by and we claim the protection under the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You can identify these statements by forward-looking words such as estimate, may, could, will, believe, expect, would, consider, should, anticipate, project, plan, intend or similar words. The company's actual results could differ materially from any forward-looking statements due to several important factors described in the company's latest annual report on Form 10-K for the year ended December 31, 2023, and other recent SEC filings. The company assumes no obligation to update any forward-looking statements made during this call.

At this time, I would like to introduce Brad Beckham.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Thanks, Jeremy. Good morning, everyone, and welcome to the O'Reilly Auto Parts first quarter conference call. Participating on the call with me this morning are Brent Kirby, our President; and Jeremy Fletcher, our Chief Financial Officer. Greg Henslee, our Executive Chairman; and David O'Reilly, our Executive Vice Chairman, are also present on the call.

I'll begin our call today by thanking our over 90,000 team members for their relentless dedication to providing the knowledge and expertise our customers have come to expect and rely on from the professional parts people at O'Reilly Auto Parts. We are truly in a people business where relationships and customer service are paramount, and Team O'Reilly continues to demonstrate their ability to outhustle, (inaudible) and, in turn, outperform our competition. We finished the first quarter with a 3.4% comparable store sales growth on top of a 10.8% in the prior year. Our continued strong top line sales results are dependent on and driven by consistent daily execution across all of our 6,200-plus stores in the U.S., Mexico, Puerto Rico and now Canada.

Driving continued growth in our store volumes does not get easier as our company gets bigger, especially as we build on the significant market share gains we have captured over the last few years. Our single greatest challenge as a company and the driving factor to our success is our ability to build and develop teams and leaders who will be the standard bearers of our culture far into the future.

Our leaders across our stores, distribution centers and corporate offices are relentlessly dedicated to perpetuating our culture and investing in our people. Thank you, Team O'Reilly for your commitment to our customers, our company and your fellow team members.

Now I'd like to start our discussion of the first quarter by walking through the details of our sales performance. Starting with comparable store sales, our growth of 3.4% in the quarter was within our full year guidance range, but slightly below our expectations as we saw some volatility I will discuss in more detail in a moment. We drove solid performance and positive comps in both our DIY and professional businesses in the quarter with the mid-single-digit comps in Professional being the larger driver of our results, consistent with our expectation and ongoing trends. Increases in average ticket values and ticket counts were both contributors to comp growth on both sides of our business with inflation at about 1%, in line with our full year expectations.

Next, I want to provide some color on the cadence of our sales results in the first quarter. As we have discussed in the past, our first quarter can be volatile as we see variability in our business from both the type and severity of winter weather and from the timing of the onset of spring. We were pleased to generate positive comparable store sales results in each month of the quarter. However, we did experience the choppiness that can be characteristic of first quarter, especially as we exited with a slow start to spring. As we reported on last quarter's earnings call, we produced solid results in January, which benefited from harsh winter weather in many of our markets.

Moving past the winter weather in January, our business was negatively impacted through much of February by the timing of individual income tax refunds. Typically, we see a benefit starting early in February and ramping through the month that coincides with the distribution of tax refunds. However, there was a noticeable delay in the processing of refunds this year that pressured both sides of our business. These pressures moderated as the cumulative amount of refunds begin to catch up to the prior year, and we saw improved trends at the end of February in the first half of March. However, we also experienced unseasonably cool wet weather throughout March across many of our markets. As a result, March and the full quarter finished slightly below our expectations. The trends we saw as we exited the first quarter, have continued into April as we still really haven't seen the uptick in our business that typically accompanies sustained favorable spring weather.

The choppiness we saw in the first quarter more significantly impacted DIY business, which is in line with what we have seen historically. Our DIY customers are often working on their vehicles in their driveways, so weather conditions can impact their ability and willingness to perform repair, maintenance and tune up items that may have been on hold during the winter. While our DIFM business was also impacted by the delayed timing of tax refunds, our professional customers tend to be more insulated from weather pressures and the volatility on this side of our business was more muted during the quarter.

We continue to be pleased with the performance of our professional business even as we face very challenging comparisons. As we outlined in our full year guidance on last quarter's earnings call, we are seeing an expected moderation in professional comps as we calendar significant share gains that drove a professional comp performance that exceeded 20% in the first quarter of last year. Against these challenging comparisons, we believe our professional results in the first quarter of this year reflect continued share gains. We are excited by our team's ability to leverage the momentum we have created in our professional business and continue to grow our share of what remains a highly fragmented professional market across all of North America.

Now I'd like to provide some comments as to how we are thinking about the sales outlook for the balance of the year. As I noted previously, the volatility we have seen so far in 2024 is not uncommon for our business in the first quarter. As many of you listening today have heard us say before, we are cautious not to overreact to choppiness at this point in the year. As we move forward, we expect any weather-driven variability will moderate and business will normalize into the summer selling season. Given this outlook, we are maintaining our full year comparable store sales guidance of 3% to 5% and would also expect our quarterly comp results to fall within the same range.

Inherent in our guidance expectations is our belief that demand for our industry is resilient and our end consumer continues to be reasonably healthy. In situations of heightened economic pressures, we believe consumers will continue to prioritize investing to maintain their vehicles, particularly given the significant cost and monthly payment burden of a new or replacement vehicle. We believe the composition of our sales results support this view of the consumer in the current environment.

We are encouraged to see broad-based performance across our category mix with continued strength in categories such as oil and filters as consumers continue to prioritize recurring maintenance jobs. Additionally, we are not seeing notable evidence of trade down within our categories, rather we are seeing better and best level value spectrum products continue to perform well as consumers prioritize higher-quality products that carry extended warranties and in turn, provide long-term value to their investment in transportation.

However, we still remain cautious of the potential deterioration in the broader macro environment that could push consumers to begin more carefully considering where and how they spend their money. Our experience gives us confidence that these demand headwinds are short term. And over time, the consumer will continue to prioritize their transportation needs given the value proposition that is present. All of this being said, we will not settle for industry average growth or allow our teams to accept macroeconomic pressures as an impediment to growth. We know there is substantial opportunity to gain a bigger piece of the pie in our industry and the mission we have set before our team is to be the leader in all of our markets and on both sides of our business.

Before I move on from our sales discussion, there are a few items I would like to call out as discrete impacts to our sales. First, the Easter holiday shifted into our first quarter this year, which was built into our plan and met our expectations as a headwind of approximately 20 basis points to comparable store sales on the quarter.

Next, we received the benefit of an additional selling day as a result of leap day in the first quarter of 2024. We exclude the impact of leap day from our comparable store sales calculation, but this benefit was included in our total sales guidance and came in as expected, representing 125 basis points of our total sales increase of 7.2% on the quarter.

Last, we closed on the acquisition of Groupe Del Vasto on January 22, and their operating results from that point forward are included in our reported numbers. The first quarter total sales increase benefited by approximately 70 basis points from the inclusion of Vast-Auto sales results, which are also excluded from our comparable store sales like Mexico.

Moving on to diluted earnings per share. We are increasing our full year EPS guidance to a range of $41.35 to $41.85. Our lift in EPS guidance is driven by the gross margin and SG&A results that Brent will cover next as well as a lower-than-planned tax rate and the impacts of shares repurchased through the date of our earnings release today. As Brent will share with you here in a moment, we have been pleased with our team's ability to manage costs while still making steady progress on the numerous initiatives and projects we have in motion to further enhance our competitive position. As I wrap up my prepared comments, I would like to once again thank Team O'Reilly for their hard work and dedication to start 2024.

Now I'll turn the call over to Brent.

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

Thanks, Brad. I would also like to begin my comments this morning by thanking Team O'Reilly for their incredible hard work to ensure a solid start to 2024. We are proud to say that Team O'Reilly now extends across the United States, Mexico, Puerto Rico and Canada. Regardless of the market we operate in, we know that the absolute key to our success is a team of professional parts people dedicated to the O'Reilly culture of excellent customer service.

Today, I will cover our first quarter gross margin and SG&A results and provide a quick update on our expansion and capital investments thus far in 2024. Starting with gross margin. Our first quarter gross margin of 51.2% was an 18 basis point increase from the first quarter of 2023 and slightly better than our expectations for the quarter. As Brad previously noted, this was the first quarter to include the operating results from the acquisition of the Vast-Auto business. And the incremental dilution to our first quarter gross margin was in line with the full year 25 basis points we guided to at the beginning of the year. We have continued to see a stable supplier and supply chain environment, and experienced the anticipated mix of acquisition cost puts and takes in the first quarter.

On a net basis, improved acquisition costs benefited gross margins driven by incremental buying improvements as well as market-driven reductions in freight cost. To the extent that we have seen modest inflation pressure in certain categories, we have been successful in passing those cost increases along in a continued rational pricing environment. Given our solid performance in the first quarter, we continue to expect our quarterly gross margin performance to land within our full year gross margin range of 51% to 51.5%.

Turning to SG&A. We are pleased with our SG&A management in the first quarter results in line with expectations as a percentage of sales. Our first quarter average SG&A per store growth of 5.7% included an anticipated 100 basis point increase from the additional business day as a result of leap day. Additionally, the SG&A per store growth includes a 15 basis point increment on the quarter from the inclusion of Canada's operating results, which was in line with our expectations based on the portion of the quarter since we have owned that business.

Our spend in the first quarter keeps us on pace for our full year plan of growing average SG&A per store by 4.5% to 5%. As we noted on our last call, the cadence of growth in average SG&A per store will moderate as we move throughout the year as a result of beginning to compare against the impact of 2023 investments that we made in the business. While we continue to move forward as planned on our growth initiatives, some of the investments we have been making in technology capabilities as well as enhancements to our vehicle fleet and the image and appearance of our store will begin to layer into our SG&A comparisons as we incurred ramping incremental expenses throughout 2023 in these areas.

The impact of these comparison headwinds in our first quarter SG&A spend drove the planned deleverage of SG&A, which we also anticipate to moderate throughout the balance of this year. Given the top line choppiness we experienced during the first quarter, we believe our teams effectively balanced the incremental investments we are deploying in our business with prudent expense control. The decisions we make concerning the staffing levels within our stores remain the most significant driver of our SG&A spend in total.

Our team is focused on judiciously managing our expenses as appropriate for the current conditions in our business, while also ensuring that we are delivering excellent customer service that develops and maintains long-term customer relationships. We feel that our consistency in delivering excellent customer service in all market conditions has been critical to our long-term success and reflects the high level of professionalism demonstrated by our team. We are confident that the investments we have made and are continuing to make position Team O'Reilly to provide industry-leading customer service at high levels of productivity.

With the solid gross margin and SG&A performance we saw in the first quarter, our operating margin outlook is unchanged, and we continue to expect the full year to come in within the range of 19.7% to 20.2%, which includes the anticipated dilution of 15 basis points from the inclusion of Vast-Auto's results.

Inventory per store finished the quarter at $773,000, which was up 2.5% from this time last year and 2.2% from the end of 2023. The addition of Vast-Auto's inventory and store count provided the 1% incremental increase we had anticipated, and we continue to target a range of 4% growth within our existing chain by the end of 2024. Inventory turnover has remained at 1.7x, and we are pleased to see strong inventory productivity as we have continually enhanced and refined the inventory deployment in each of our stores while also expanding hub and DC level inventories. Our store in-stock position remains strong, and our teams are working hard to ensure O'Reilly Auto Parts offers the best inventory availability in all of our markets.

Turning to our progress on store growth and capital investments. We opened a total of 37 stores across the U.S. and Mexico during the first quarter. Additionally, we were pleased to officially bring the 23 Canadian stores into the fold. Our annual net new store opening guidance of 190 to 200 excludes the addition of the 23 Canadian stores. Capital expenditures for the quarter were $249 million, and we are on track for our annual goal of $900 million to $1 billion.

Our DC relocation projects in Springfield, Missouri and Atlanta, Georgia, are making great progress, and we are excited to bring those new, larger and more efficient facilities online later this year to further enhance service levels within those markets. We are also excited about the progress made so far on our Mid-Atlantic, D.C. in Stafford, Virginia, that is slated to be operational in the middle of 2025.

As I finish my comments, I would like to thank Team O'Reilly for their commitment to delivering excellent customer service one customer at a time. I look forward to the opportunities we have ahead and taking on that challenge as a team.

Now I will turn the call over to Jeremy.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Thanks, Brent. I would also like to congratulate Team O'Reilly on a solid start to the year. Now we will fill in some additional details on our first quarter results and outlook for the remainder of 2024.

For the quarter, sales increased $268 million, driven by a 3.4% increase in comparable store sales and a $73 million noncomp contribution from stores opened in 2023 and 2024 that have not yet entered the comp base. For 2024, we expect our total revenues to be between $16.8 billion and $17.1 billion. Our first quarter effective tax rate was 21.9% of pretax income, comprised of a base rate of 24.2%, reduced by a 2.3% benefit for share-based compensation. This compares to the first quarter of 2023 rate of 23.7% of pretax income, which was comprised of a base tax rate of 24.3%, reduced by a 0.6% benefit for share-based compensation.

Our first quarter effective tax rate was below our expectations as a result of the timing and amount of benefit we realized from share-based compensation. For the full year of 2024, we now expect an effective tax rate of 22.4% comprised of a base rate of 23.1%, reduced by a benefit of 0.7% for share-based compensation. We expect the fourth quarter rate to be lower than the other 3 quarters due to the tolling of certain tax periods. Also, variations in the tax benefit from share-based compensation can create fluctuations in our quarterly tax rate as we saw in the first quarter.

Now we will move on to free cash flow and the components that drove our results. Free cash flow for the first quarter of 2024 was $439 million versus $486 million in 2023.

The decrease of $47 million was the result of a larger increase in net inventory in 2024, partially offset by an increase in earnings. For 2024, our expected free cash flow guidance remains unchanged at a range of $1.8 billion to $2.1 billion. Our accounts payable as a percentage of inventory finished the first quarter at 127%, down from 131% at the end of 2023. This moderation was in line with expectations, including the impact from our Canadian acquisition and we would anticipate finishing the year in line with these levels.

Moving on to debt. We finished the first quarter with an adjusted debt-to-EBITDA ratio of 1.95x as compared to our end of 2023 ratio of 2.03x with the decrease driven by a reduction in borrowings under our commercial paper program. We continue to be below our leverage target of 2.5x and plan to prudently approach that number over time. We continue to be pleased with the execution of our share repurchase program. And during the first quarter, we repurchased 262,000 shares at an average share price of $1,029 for a total investment of $270 million. We remain very confident that the average repurchase price is supported by the expected discounted future cash flows of our business, and we continue to view our buyback program as an effective means of returning excess capital to our shareholders. As a reminder, our EPS guidance, Brent outlined earlier, includes the impact of shares repurchased through this call, but does not include any additional share repurchases.

Before I open up our call to your questions, I would like to thank the entire O'Reilly team for their dedication to our company and our customers. Your hard work and commitment to excellent customer service continues to drive our outstanding performance. This concludes our prepared comments.

At this time, I'd like to ask Matthew, the operator, to return to the line, and we will be happy to answer your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Chris Horvers from JPMorgan.

Christopher Michael Horvers - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Can you talk about, since the beginning of February, can you talk about the geographic performance that you've seen? And how correlated has that been to the arrival of spring? So markets where you have seen spring arrive, what is the performance of the comps look like versus markets that haven't?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Chris, thanks for the question. Well, there was a lot of moving pieces in the quarter really directly to your question there. And really, what we saw just kind of walking through the quarter again is January, we were really pleased with January. And in a lot of the markets, you're really true winter markets where harsh weather really drives that demand, we felt like that really exactly played out that way in January.

As we got into February, it definitely kind of more normalized from a kind of a weather standpoint or early on in the month. And then not too long after that, we felt like there was a little bit of volatility more from lack of seeing some of the tax money roll in, Chris. And then kind of what we saw as things started to kind of stay cool and get a little bit more wet in the markets you don't necessarily want to see it, that kind of matched up with what we saw geographically in certain regions, in certain divisions, and it really kind of made sense to us, kind of what was happening with some unfavorable weather, especially on the DIY business for people to get out and work on stuff. So there was a lot of moving pieces there. When we looked at our regional performance versus our plan by region and you looked at the kind of the comparison from this time last year, everything was really fairly consistent, and it pretty much made sense based upon what the weather was doing.

Christopher Michael Horvers - *JPMorgan Chase & Co, Research Division - Senior Analyst*

So does the -- I guess, in markets that where you've seen spring break, have the comps been consistent with the 3% to 5% outlook for the quarters in the year?

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. I think one of the challenges -- this is Jeremy. I think one of the challenges we've had is we just haven't really seen consistency in how our business would perform on a sustained normalized spring business. I think, as Brad described on the call, the choppiness that we've seen has been exactly that. We'll see pockets of improved performance as we move through. But there's not anything that's been consistent and sustained. And for sure, the areas that have been more volatile are the ones where we can see the impact of that. But at this stage, with a few of the different factors that we saw impact us during the quarter, especially as we move through that period of time when tax refund money shifted around, it's been harder to get a more consistent rate just week to week on the underlying businesses. There's just been a lot of the choppiness that's characterized the quarter.

Christopher Michael Horvers - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Understood. And I know you mentioned that you're seeing -- as a follow-up question, I know that you mentioned that you're seeing consumers trade up, haven't seen trade down. And I also understand that you have a low mix exposure to national accounts. And even within that, you're not selling to the A and B SKUs like brake pads or something like that. But in that channel or any other parts of the business, are you seeing any evidence of deferral of some bigger ticket type repairs or even oil change or anything else?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Yes, great follow-up question, Chris. The answer is no. When we look at kind of our book of business and you look at the general independent garage versus strategic accounts, whether it be a regional account or whether it be a national account. As you know, we have a smaller portion of our business that is the national account business and some of our competitors. And -- but when we look at the mix of business, when you look at the category of customer and then you really break it down to the last part of your question, we're just -- we're not seeing that. Especially when you look at our nondiscretionary categories, the needs-based categories when Brent and I, when we look at our (inaudible) categories, when we look at our maintenance categories, we're extremely pleased with how those categories are performing.

And kind of like we said earlier, that when we look at good, better, best, our better and best of the value spectrum has been very encouraging. The only area that I would say that we have seen some softness, Chris, would be more with our discretionary categories. When you think about things like truck and towing accessories, maybe performance or something like that, that's where we want to just be a little bit cautious that we have seen some pressure in Q1, and we're going to watch that closely.

The thing that I would balance that with is some of those categories only perform really well when people can get out and do those things in their driveway. So it's a little bit of a challenging answer that we are seeing some pressure due to discretionary. Some of that may have to do with some of the weather. But really, when you think about our failure and maintenance categories, nondiscretionary needs based, we're extremely encouraged.

Operator

Your next question is coming from Seth Basham from Wedbush Securities.

Seth Mckain Basham - *Wedbush Securities Inc., Research Division - MD of Equity Research*

My first question is just on SG&A per store growth. You anticipate some moderation through the year here, and that's despite the fact that you expect comps to likely accelerate a little bit from here. Is that simply due to the investment comparisons or anything else?

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

Yes. Seth, this is Brent. I'll start and then Jeremy can jump in, I'm sure on some of that on the back end of it. But yes, as I talked about in the script, biggest driver of our SG&A per store really is our store payroll. And our teams have been very focused on balancing that with the demand and the opportunity that they see in their markets, and they manage through a period in Q1 where we did have some of that choppiness that we've talked about. But really proud of the job overall that the teams did there, and we're obviously approaching any kind of choppiness with an eye to expense control, but we do have some of that investment depreciation pressure that I mentioned in my script that we're going to see as we move through the year. That's why our plan was not a peanut butter spread on SG&A for this year. So -- and Jeremy, you may have a couple of other thoughts on that.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. No, I think, Brent, I think you said it well. Seth, I think we previewed a little bit on last quarter's call, but it's kind of hard to get the cadence quarter-to-quarter. As we just think like in particular about the timing of the impact of some of last year's investments and not to get too far down in the weeds here, but our depreciation headwind in first quarter was kind of high teens year-over-year growth there. And that's the number that through the balance of the year starts to moderate as we move down through. So more broadly speaking, especially as you think about the dollars, you also had impacts in the quarter with leap day.

So it does create a little bit of noise in terms of the cadence. But against that broader backdrop, feel solid about the management SG&A. It's in line with where we would have expected to be. And as we work through the balance of the year, feel comfortable with how we think the teams are balancing both the investments that we continue to talk through and we'll execute on while also just being responsive to what we're seeing in the business.

Seth Mckain Basham - *Wedbush Securities Inc., Research Division - MD of Equity Research*

That's helpful. And as my follow-up, just thinking about the DIY segment and the softness you called out discretionary categories, recognizing that some of that might be weather-driven. Is this a change in trend that you've seen with more pressure in the discretionary categories in recent months?

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. I can probably talk to that. And maybe the first caution that I would say is we're still within a relatively tight end of what we thought from expectations and I know Brad mentioned it within his response. The confidence that we feel is just from the broader mix of our business, the ability to see solid performance really across the core categories that we know are indicative of how the consumer is thinking about the backdrop has been good.

The entry into first quarter, both the tax refund money and with the weather backdrop, it tends to be a quarter that can be more volatile just generally on discretionary categories. Often, we're in the position like others within our industry of -- of hoping that we've got both good weather and tax refund money hitting at the same time. So that's -- there's a reason why that can be volatility. We wouldn't call it out as a sea change. And for sure, in the broader sense of our business, it's a smaller piece, but it is just one area that we pay attention to as we're trying to make sure we've got a good read on what the consumer looks like.

Operator

Your next question is coming from Michael Lasser from UBS.

Michael Lasser - *UBS Investment Bank, Research Division - MD and Equity Research Analyst of Consumer Hardlines*

While the indications are still coming in about the performance of the overall aftermarket and it's still pretty early. It does seem like O'Reilly's outperformance versus the rest of the industry is moderating versus where it's been. Why is that the case?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Michael, thanks for the question. I don't see it that way. Number one, I've been in this business here at O'Reilly for 27 years this year and been through challenging years, been through great years and been through election years and years that we get off to a little bit of a choppy start, and I've learned every time not to necessarily overreact that we all -- we take any potential slowdown or anything like that very seriously. We want to make sure we control what we can control. But it's always hard for us to base exactly where the share gains are coming from and it's sure hard to base it here short term on just a competitor reporting or something like that. We don't spend a lot of time internally trying to dissect that. What we do internally here is, we focus on our revenue versus the $147 billion, we believe, is being sold in the United States, and that just gets even bigger. Obviously, now that we're expanding to the rest of North America.

So we stay focused on that total addressable market versus what we do today. And Michael, I don't see anything that's materially changed in the way that we're competing. We have tough competitors out there. We have really great competitors that we have a ton of respect for both the big close-in competitors that are public companies as well as the solid WD operators, the independent operators. And we still feel really good. I'm so proud of what our teams have accomplished the last few years, but I believe our share gains continue.

Michael Lasser - *UBS Investment Bank, Research Division - MD and Equity Research Analyst of Consumer Hardlines*

Got you. Brad, you mentioned that you did see a bit of a slowdown in March, and that's continued into the first part of the quarter. Can you provide some frame of reference for that? And what does the P&L look like? How is the sensitivity of the P&L? If this is just one of those years where it's a bit of a slower backdrop for the aftermarket and the ultimate comp ends up at the low end or maybe even slightly below your guidance?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Thank you, Michael. I'll start out and answer your question on just kind of the cadence of the exit and kind of how we're feeling about the last few weeks, and then I'll let Jeremy talk to the last part of your question there on SG&A. So Michael, really, the thing I want to be a little careful of is, even though we have a few weeks, it is just 3 weeks, and we have a lot of quarter left and I think the reason that we're trying to balance the choppiness with not knowing what the future holds, all with the fact that we have had some of this weather that it's just not ideal. It's a different weather story than like in January, where we love harsh winters, and we love hot summers. The stuff that's in the middle can just be a little bit not conducive to what our DIY customers want and need to get out and work on their stuff. I'm sitting here in Springfield, Missouri this morning, looking out the window, 50-something degree weather and it's raining out there.

And our operational teams absolutely did not spend any time focusing on things that they can't control like weather. But we don't want to say too much about the choppiness because there has been some, but there's also just been this weather factor, and we feel like that we got a lot of quarter left and we just want to see how that plays out. But we just want to balance those things, and I'll let Jeremy take the SG&A.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. Just from the -- I guess, further down the income statement as we think through the balance of the year, Michael, I'd tell you, nothing really changes about our expectation on how and the degree to which we can respond to different market conditions than really we've had for a long time within our business. From our history that -- that we really do truly manage the business from a long-term perspective and will not overreact in short periods of time to fluctuations and cognizant of the volatility we've seen in the first quarter, but also understanding that we're in an election year and there's just a little bit more uncertain backdrop that we could face some puts and takes as we move through the year. It's important for us to maintain a high level of service and to prioritize that as we move through the business. While at the same time, we've got a pretty long-standing expense control culture, and we will address how we manage the business, we think, appropriately to the right market environment and feel good about how the teams have performed in that way, as Brent mentioned, during the course of this year so far.

Operator

Your next question is coming from Greg Melich from Evercore ISI.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

I wanted to circle back on the inflation commentary and also the decline in acquisition costs. So (inaudible) all the unusual parts of inflation where that now we pretty much expect that to be steady, the cadence each quarter going forward. And on the cost side, can we still get some acquisition cost relief if interest rates start to back up? And how does that come into the equation?

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

Yes. Greg, this is Brent. I'll start and then let the other guys jump in. But in terms of the cost environment, as I mentioned in the script, we kind of saw what we'd expect some typical puts and takes on cost. But I mean, in terms of inflation and what's out there, I think we kind of guided and felt like going into this year is going to be around 1%. It's kind of what we saw in Q1, kind of what we anticipate for the rest of the year. So we don't really see that changing a whole lot. Now with that said, the good news is we continue to be able to diversify our supply chain. Our merchandise team has done a fantastic job with that.

We've done a fantastic job with our proprietary brand portfolio and continue to grow that. It's resonating with our customers. So that gives us an ability to control cost in some respects by dual sourcing and multi-sourcing different lines. And we continue to see that as a competitive strength of where we are and how we're positioned. But that's kind of the outlook we have in terms of cost and where we are going into this year.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Great. And I'd love to just make sure I got the comp trend correct there. The traffic in the first quarter, was that positive or negative or kind of flat if you look at the whole quarter?

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

It was positive.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

It was a contributor.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

It was a contributor to comp. And so if presumably where that would have been negative in DIY by the exit rate, and that the gap between do-it-for-me and DIY that happened through the quarter at the end was basically traffic and therefore, weather-driven. I just want to make sure I'm interpreting what you guys are seeing.

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. Yes. I would tell you the traffic even on the DIY side of the business was still positive for the quarter (inaudible) that was pretty significantly impacted by the strength that we saw in January, which we've talked about that side of the business is more volatile around the refund and just the spring impacts. But yes, we were positive, both sides of -- in both traffic and ticket.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

And so now as consumer -- as DIYers come in, you mentioned, I think there's no trade down. It's actually still a trade up. But I'm curious, are items in basket under pressure. Is that a sign of any pressure on the consumer there?

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes. Again, volatility there, Greg, as we saw in the first quarter. Some of that is similar to what we've seen from an accessory perspective and oftentimes, those are the add-on type things that hit when somebody is coming in to change brakes or to do that type of oil change. Not having a perfect read on how tax refund money flows through, that can also affect size in certain instances. But a little bit choppy there to be able to draw any really strong conclusions. But for sure, some of the -- some of what we've seen is that number not being a contributor, a little bit of a headwind for us in the quarter.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Greg, maybe just to build on that basket question a little bit, kind of parse it out a little bit. An example of what we're not seeing is any issue with -- if somebody is doing a great job, we still feel with that something they need to do. They're still -- our teams are still able to work that customer from a DIY standpoint through having everything they need to do the job right. We don't see any basket issues in terms of not buying the hard parts they need to do the job and normally the things that go along with that.

An example, it may be what we're seeing a little bit was some of the discretionary is maybe like tools, for example, on the DIY side is the customer where they normally may have bought that specialty tool they need to do that break job.

They may be renting it from us, which they can do for free through our loaner tool program. So that would be an example of some of the things that we're seeing a little bit of pressure to, but not necessarily on the hard parts side.

Gregory Scott Melich - *Evercore ISI Institutional Equities, Research Division - Senior MD*

That's great color. And good luck guys, and we'll be praying for some sunshine.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

We appreciate it, Greg.

Operator

Your next question is coming from Simeon Gutman from Morgan Stanley.

Simeon Ari Gutman - *Morgan Stanley, Research Division - Executive Director*

Everyone. Brad, and Jeremy, you've mentioned that it's been choppy, and there isn't a clean weather and nonweather market spread. Can I ask, is that because of tax refund season or there's -- we're lapping used cars, the consumers under pressure. Are you thinking it's possible there are other variables at play? Or how (inaudible) weather and weather turns and we're in the clear?

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes, Simeon, great question, really is. I would tell you, we're as confident in our read right now as we ever are after first quarter. Brad mentioned it within the context of his comments, we think it's appropriate to not overreact to the things that we see in first quarter. For certainly a couple of things we know, the range of our -- the band of our performance has still been relatively tight even though we've seen choppiness move throughout. So we're not seeing the types of serious fluctuations in our business that come on where you do see things like oil changes being pushed back or brakes moving around more significantly. What we are seeing is what we often will see from a variability in business around choppiness of tax refunds.

So whether those are -- can be significant impacts as you just try to get a perfect week to week on the business. As we step back from that, we remain cautious about the consumers in our prepared comments and it's a focus of our business. Often we get a much clearer read on that as we move forward past some of the volatility. So we're cognizant of where that is. We understand some of the broader commentary that exists within broader retail. Often, we see the impacts of some of those things as they flow through on a more delayed basis for our business, understand we're in an election year. Those things we're cautious about. But as we sit here today, there's just not the clear indicators that we're seeing that more sustained pressure that we would normally expect to see.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Yes, Simeon, what I would say, it's a fair question. And I think maybe just on the tax refunds, for example, there's no doubt that the delay impact of this, to some degree, there in February. I think the reason that we want to just be cautious with how that will play out is just the fact that we are in election year. There's a lot going on in the world. We have this weather that no doubt has played in to some extent. But we also know that the reality is when people get their tax refunds, it's normally pretty clear when we get that and how much of it we get. But we know our lower-end consumer. They're spending money, first and foremost, on groceries, their homes, insurance rates personally, things like that, that are a pressure to them right now. And we just want to -- we want to balance that. We know that is some of it, but we also know this weather is some of it as well.

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

I was just going to say maybe just one other thing to add on your question, and it is a good one. But when -- just like the guys talked about, when you think about maintenance categories and obviously, failure categories (inaudible) maintenance categories, there is some discretion in those. And even on the DIY side, again, a lot of confidence still in the backdrop knowing that we still saw strength in motor oil filters in the category. I mean we didn't see any reason to believe that people were putting off the oil change to pay for groceries that we -- when we looked at it at a product level. So that was underlying in all of this, too. So just wanted to mention that.

Simeon Ari Gutman - *Morgan Stanley, Research Division - Executive Director*

My follow-up, if you take the PPI initiative and you look at the products that were impacted where price was lowered, it looks like the payoff was especially strong last year to that -- maybe to that market share question. Is -- are you still seeing growth in those PPI products? And are there any opportunities as you look across your pricing and your catalog where there may be some price differences where you can take advantage of that again?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Yes. Thanks, Simeon. So yes, I mean, when you talk about PPI, that's over 2 years old now. Basically, we're lapping at 24 months in. We feel extremely good about that investment we made. When you look at those categories, not only those categories, but kind of the halo categories that revolve around those (inaudible) underhood categories, and it was very broad. It was a very (inaudible) approach, but it was very broad by SKU, by line. We feel really good about what we've done there. We -- when I look at it, especially versus some of the WDs and the independent 2 separate type players, we feel really good about what we've done, and we haven't seen really any other reactions to any large degree out of our big competitors nor those other competitors. The reason that I feel like that we have made those investments pay, Simeon, is because our team has gotten out there and this just hasn't been a one-pronged approach.

The investments were one thing, but we knew going into it, the only way we were going to make that pay was to do what we already did well even better, being out there calling on customers, building relationships with those customers that had traditionally bought from some of the independents through relationships, through service, et cetera, and some of that being price. Our teams have got out there and done all the other things that matter more than pricing, calling on customers, building relationships, the most efficient delivery service in the aftermarket, right part, right place, right time, the work our supply chain teams have done in the last couple of years have all made that pay off.

But really to the last part of your question, we feel really good about where our pricing matrix is. We moved it down to that level that you know we did on the professional side, but we're always within that new matrix. We're always tweaking and optimizing within that new matrix. But we feel like that matrix is where it needs to be for now in the foreseeable future and don't see anything competitively that would tell us we need to ever do that again.

Brent G. Kirby - *O'Reilly Automotive, Inc. - President*

And Simeon, maybe to just further add to what Brad said on that, on the professional side. I mean when you look at the -- by category, when you look at some of the categories, brakes, chassis, driveline, ride control, all the big category, a lot of big categories, dollar categories that we're not seeing that growth stagnate, which I think is kind of where your question is going (inaudible) running out of gas in those categories. We're not seeing that. We're seeing continued growth even on top of big comparisons year-over-year.

Operator

Your next question is coming from Mike Baker from D.A. Davidson.

Michael Allen Baker - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Two quick ones. One, with April -- end of March, April being a little bit slower because of the weather, does that -- are those sales off? Or does that get made up if and when the weather turns better?

Jeremy Adam Fletcher - *O'Reilly Automotive, Inc. - Executive VP & CFO*

Yes, Michael, it's always a little bit of a tough question to answer. Often that is the case with spring business that it's just a shift in demand. I think more broadly, the way that we view that is that none of the timing of what we're seeing or none of the impacts affect kind of core fundamental underlying demand within the industry. So it's always a little bit tough to know, will you get it rebound? How much can you really measure it when you do -- but more broadly speaking, as we move further into the quarter, that becomes less important of a dynamic, it's just the broader strength in our business will kind of prove out as we move into the balance of the quarter.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Yes, Mike, there could be some of the discretionary. There could be some of the short-term stuff that could potentially be lost. But I think as we always say, and we still believe this as much as we ever have that the underlying drivers of our business are absolutely there. When you look at vehicle's miles driven, you look at all the things that we look at to drive our business, average age of vehicles, not only in the U.S. but in North America, we still feel really good that demand is going to continue to be there.

Could it be one of those years that the lower-end consumer is pressured? Very potentially. But as you know, Mike, when in tough years or when customers go through tough times, our industry is not immune to that, but it's more short term. And then as things move on, people hold on to their cars longer, they're working on their cars more often. And mid- to long-term, we couldn't feel better about how we're set up from a demand standpoint.

Michael Allen Baker - *D.A. Davidson & Co., Research Division - MD & Senior Research Analyst*

Perfect. That makes sense. The other question I want to ask is a much more bigger picture, longer term, have you ever -- or could you ever talk about what you see as the potential size of your business down in Mexico? I think you have about 63 stores according to the press release here. What can that be over time? One of your competitors, I think, as close to 1,000? Any thoughts on where Mexico could be for you longer term?

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Sure, Mike. Absolutely. Well, we're really excited about the Mexican market. We acquired Mayasa back in 2019 and we had our eyes on that market for a long time. And to your point, one of our toughest competitors has done an amazing job down there for several decades and has a tremendous business down there. That said, it is so fragmented down there, Mike. When you look at the average age of vehicles in the U.S. at 12.5, but then you look at the Mexico market at over 16 years of age on the average vehicle and how fragmented the independent market still is down there, we see a tremendous runway. I mean that's why it was our first international venture. We have a great team down there. The timing of when we acquired Mayasa back in 2019, we acquired a lot of great team members. We acquired a base of people and distribution.

Since then, we got our -- we had our state-of-the-art O'Reilly prototype distribution center opened last summer. And so that enables that growth that you're asking about. I don't want to put a number on revenues or store count over time. But what I can tell you is that's going to be -- it has the opportunity to be a good portion of our growth over the next many years. And there's no reason that we can't get after Mexico, no different than we have in the U.S. from coast to coast.

Operator

We have reached our allotted time for questions. I'll now turn the call back over to Mr. Brad Beckham for closing remarks.

Brad W. Beckham - *O'Reilly Automotive, Inc. - CEO*

Thank you, Matthew. We would like to conclude our call today by thanking the entire O'Reilly team for your unwavering dedication to our customers and the outstanding results you produced in the first quarter. I would like to thank everyone for joining our call today, and we look forward to reporting our second quarter results in July. Thank you.

Operator

This does conclude today's conference call. You may disconnect your phone lines at this time, and have a wonderful day. Thank you for your participation.
