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ORLY.OQ - Q2 2024 O'Reilly Automotive Inc Earnings Call

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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Welcome to the O'Reilly Automotive, Inc., second-quarter 2024 earnings call. My name is Holly, and I will 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 Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

Thank you Holly. Good morning, everyone, and thank you for joining us.

During today's conference call, we will discuss our second-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, guidance, target, 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 Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Thanks, Jeremy. Good morning, everyone, and welcome to the O'Reilly Auto Parts second-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'd like to begin my comments today by thanking our team of over 91,000 hard-working professional parts people across North America for their continued dedication to our customers during a challenging second quarter. As we'll discuss during our call today, our second-quarter results were below our expectations, as we faced broader headwinds to demand in our industry. However, we are pleased with the job our teams did to uphold our commitment to providing top-notch customer service to our customers on both sides of our business.

Despite a sales performance that fell short of what we have come to expect, we continue to outperform the industry. This is the direct result of our team maintaining a high level of attention to detail and doubling down on their efforts to provide even better service to our customers.

We finished the second quarter with a 2.3% comparable store sales increase on top of a 9% in the prior year. The pressure to topline sales also negatively impacted our operating profit and earnings per share results, and we have revised our full-year outlook for these metrics as outlined in our press release last night.

Though our results were below our expectations for the quarter, we were still able to generate increased operating profit and EPS on top of several years of a robust growth. We now expect our full-year EPS to come in within a range of \$40.75 to \$41.25, with the adjustments reflecting our results in the second quarter and revised full-year comparable store sales and operational outlook.

At the midpoint of our updated range, our guidance represents a forecasted 7% increase in full-year EPS, which matches our EPS growth in the first half of 2024. Our ability to generate solid EPS growth in a challenging macro environment, especially in light of the comparison to the 15% growth we delivered in 2023, is a testament to the continued strong execution by Team O'Reilly.

Now, I'd like to dig in further to our results in the second quarter by walking through the details of our sales performance, starting with our cadence of sales in the quarter. As we discussed on our last call, our quarter started off with sluggish results in April as we faced headwinds from cool, wet weather during the spring selling season. The softness in our business persisted into May, which we believe reflected broad-based pressure throughout the industry.

As we entered June, we saw improved trends driven by strong performance in hot weather-related categories. On a week-to-week basis, relative to our original guidance expectations, June represented the strongest performance for our quarter. So far in July, sales trends have remained solid, with weather benefit we saw in June moderating somewhat as we compared to similar favorable hot weather in July of last year.

Our comparable store sales growth in the second quarter was driven by continued strength in our professional business, where we delivered yet another quarter of mid-single-digit comps. While increases in average ticket values were positive contributors to comps on both sides of our business, the majority of our professional sales growth was fueled by robust growth in ticket counts.

Our results in the second quarter came on top of prior year comparisons to mid-teens professional comps in 2023, and we attribute our robust two-year stack performance to our industry-leading customer service and inventory availability. We continue to be excited by our team's ability to leverage the momentum we've created in our professional business, and we remain bullish on our prospects to compound our share growth in what remains a highly fragmented professional market.

The strength in our professional business was partially offset by headwinds in DIY comparable store sales, which were down just shy of 1% for the quarter from pressure on ticket counts. Average ticket values on both sides of our business benefited from modest same-SKU inflation of less than 1%.

From a category perspective, our results for the quarter were highlighted by the strong performance in hot weather categories, including batteries and HVAC, as well as solid performance in maintenance categories like brakes, oil changes, and spark plugs, which we believe reflects the ongoing priority our customers are placing on keeping their vehicles on the road and running well.

The sales softness we experienced in the quarter was more pronounced in the discretionary appearance and accessory categories. These categories comprise of a small percentage of our business and typically are not primary drivers of our comparable store sales results. However, demand for these products is more susceptible to volatility in periods where consumers are pressured, and that dynamic contributed to our sales shortfall in the second quarter.

We also saw some sluggishness on both sides of our business in certain undercar hard part categories, which performed below the company average. These types of repair parts are impacted by cumulative wear and tear and have been key contributors to our professional sales growth and share gains over the past two years. While we still believe we are performing well in these categories relative to the industry, our results in the second quarter may be indicative of temporary pressure across the broader industry.

Against this backdrop of mixed results in our business for the first half of 2024, we continue to have confidence in the long-term fundamental drivers of demand for our industry, but also remain cautious about the current market environment. We still view the average consumer as relatively healthy, with strong employment and wage rates underpinning the ability of our customers to invest in the repair and maintenance of their vehicles. However, we also believe we're seeing some level of conservatism in how consumers are managing their spend as they face the cumulative impact of elevated price levels and uncertainty about the broader macroeconomic conditions.

Historically, more challenging periods in our industry are characterized by this type of short-term adjustment on the part of economically constrained DIY consumers. That said, we are cognizant of the potential that demand could be impacted during the back half of the year if this economic uncertainty persists, particularly during an election year. Given this outlook and the trends we have seen in the first half of 2024, we are lowering our full-year comparable store sales guidance to 2% to 4%, which reflects both our second-quarter results and our updated expectations for the third and fourth quarter.

We believe the pressure that our industry is experiencing will prove to be a short-term headwind. Our experience through multiple similar cycles in our company's history gives us confidence that the core drivers of demand for the automotive aftermarket remain very solid. The size and growth of the car park in North America, coupled with the quality of vehicles and a continually rising average vehicle age, drive resilient demand in our industry.

We expect to see continued steady growth in total miles driven, underpinned by population growth and the critical nature of the daily transportation needs of vehicle owners. We also believe that the value proposition for continued investment in an existing vehicle has never been higher and that consumers will continue to prioritize funding the cost of repair and maintenance of older, higher mileage vehicles.

Ultimately, the macroeconomic conditions we face do not affect our company's philosophy for how we execute our business model. We have instilled an ownership mentality throughout our organization. Our run-it-like-you-own-it philosophy does not accept external pressures as an excuse when there is still market share to gain in every local market, simply by outthrusting and outservicing our competition. Even though we believe we gained market share in the first half of 2024 in a tough environment, I can guarantee that none of our teams in our stores, distribution centers, and offices are satisfied with a 2.8% year-to-date comparable store sales increase.

Our teams are committed to putting in the work it takes to win every day in every one of our markets and remain hungry to achieve performance that matches the high bar we have set as a company. As I wrap up my prepared comments, I would like to once again thank Team O'Reilly for your commitment to our customers, our company, and to your fellow team members.

Now, I'll turn the call over to Brent.

Brent Kirby - *O'Reilly Automotive Inc - President*

Thanks, Brad. I would also like to join Brad in thanking Team O'Reilly for their continued dedication to our company's success and their steadfast commitment to excellent customer service. Our team's ability to gain market share in a challenging industry environment is a testament to their professionalism and dedication to our customers.

Today, I would like to begin my comments by discussing our second-quarter gross margin results. For the quarter, our gross margin of 50.7% was down 53 basis points from the second quarter of 2023, with approximately 35 basis points of the decrease driven by the acquisition of our Canadian business.

As a reminder, the acquired Vast-Auto business operates a higher mix of distribution sales to independent parts stores at substantially lower gross margins. As we have worked to align their financial reporting, we now expect the headwind to gross margin from the addition of their results to be slightly higher than our original expectations, with 30 to 35 basis points of dilution anticipated for the remainder of 2024. However, our outlook for the net impact of the acquired business is unchanged, and we still expect only a 15-basis-point headwind to operating profit in 2024.

Excluding the impact of the Canadian business in the second quarter, our gross margin results came in below our expectations, driven by a few different factors. First, the category composition of our sales that Brad outlined earlier resulted in a product mix margin headwind, as some of the solid results we saw in maintenance products carried a lower margin than the pressured undercar categories.

We also saw some pressure to distribution costs in our gross margin from the deleverage of fixed costs on the below planned second quarter sales. Finally, our second-quarter results include a slightly larger-than-anticipated headwind from the mix of DIY and professional business, as the headwinds we saw to sales were more significantly felt in our higher-margin DIY business.

While we are cognizant that we can experience these types of puts and takes in any given quarter, our outlook on the core drivers of our gross margin performance is unchanged. We continue to be confident in the stability of both acquisition costs and selling prices of our business and believe we have the ability to incrementally improve gross margins by delivering on premium value proposition we create for our supplier partners and customers.

In the second quarter, we saw a stable acquisition cost environment with the anticipated mix of incremental cost improvements and modest inflation pressure. Pricing remains rational in the industry, and we expect it to remain so in the future. Based on our results for the first half of 2024 and our outlook for the remainder of the year, we are maintaining our full-year gross margin guidance range of 51% to 51.5%.

Turning to SG&A, our second-quarter results reflect prudent and appropriate expense management by our teams against the softer sales backdrop. On an average per store basis, our SG&A grew 2.8% in the second quarter, with approximately 10 basis points of that growth driven by the inclusion of Canada's operating results.

Our SG&A spend was below our original outlook for the second quarter, as our teams effectively balanced our unwavering commitment to deliver industry-leading customer service while also prudently dialing in the appropriate staffing levels to match our business. While we are certainly not pleased with the deleverage of our operating expenses resulting from pressure to comparable store sales, we remain committed to maintaining a high standard of customer service and will not make dramatic adjustments to our SG&A spend that would negatively impact our ability to serve our customers.

One of the greatest resources as an organization is the professionalism and experience of our store team leaders. An excellent example of the strength of our leadership bench is the quality and tenure of our group of over 600 district managers, who each have responsibility for an average of 10 stores. Our district manager group averages more than 14 years of service with Team O'Reilly. And each of these leaders is actively engaged on a daily basis to identify and capitalize on opportunities to enhance the service we provide to our customers while also optimizing the productivity of the dollars we spend in each of our stores.

Our ability to execute our business model at a high level and over 6,000 stores is the direct result of the broad-based experience and industry knowledge across the company. We believe that our consistency in delivering excellent customer service in all market conditions, driven by this experienced leadership team, has been critical to our long-term success.

Ultimately, our customers require and deserve a high level of service regardless of the broader market conditions. Our commitment to work that much harder to earn their business in a challenging environment simply represents another opportunity for us to develop strong long-term relationships and grow our share of the business over time.

As we look to the back half of 2024, we are cognizant of the sales volatility we could face, as Brad discussed earlier, and expect to continue to judiciously manage SG&A expenses to match the business environment. Based on our results thus far in 2024 and updated outlook for the remainder of the year, we now expect full-year SG&A per store to grow between 3.5% to 4%, down from our previous guidance of 4.5% to 5%. This guidance range assumes a more moderate impact from the addition of our Canadian business of approximately 0.2% of per store SG&A growth, which is revised from our previous expectation of one half of 1%.

While our updated SG&A range reflects our current expectation for the rest of 2024, we will continue to adjust as appropriate. Based on our first-half performance and our outlook for the remainder of the year, we are updating our operating margin guidance and now expect the full year to come in within a range of 19.6% to 20.1%, which is a 10-basis-point reduction from our previous guidance.

Before I conclude my comments, I would like to provide an update on our inventory and capital expenditure and expansion results. Inventory per store finished the quarter at \$767,000, which was up just under 1% from this time last year and 1.4% from the end of 2023. We continue to be pleased with the health of our supply chain, and our store and stock position remains strong.

We are leaving unchanged our 2024 target of 4% growth in inventory per store within our existing chain, excluding the impact of the acquired Vast-Auto inventory. We plan to opportunistically add inventory in the back half of the year to supplement our store, hub, and DC level inventories, ensuring that we are offering the best inventory availability in all of the markets that we serve.

We opened a total of 27 stores during the second quarter and remain on track to open 190 to 200 new stores in 2024. During the first half of the year, 7 of our 64 new store openings have been in Mexico, bringing our store count in Mexico to 69 stores, with an expectation to open an additional 15 to 20 stores in the back half of 2024. While our footprint in Mexico is still relatively small and we are still only in the early innings of our growth, we continue to be excited about the attractiveness of the Mexican market and our prospects to grow a strong and profitable business there over time.

We are also very excited about our new business in Canada and continue to be pleased with the partnership that we have formed with our Canadian team. Capital expenditures for the first six months of 2024 were \$475 million, which is in line with our expectations, with a heavy weighting towards our ambitious plans to invest in new store and distribution expansion projects.

To close my comments, I want to once again thank Team O'Reilly for their continued dedication to our customers. Our success is dependent upon providing the best customer service in our industry, and I'm confident in our team's ability to maintain this very high standard and deliver a strong finish to 2024.

Now, I will turn the call over to Jeremy.

Jeremy Fletcher - O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President

Thanks, Brent. I would also like to add my thanks to all of Team O'Reilly for their continued dedication to our company's long-term success.

Now, we will cover some additional details on our second-quarter results and outlook for the remainder of 2024. For the quarter, sales increased \$203 million, driven by a 2.3% increase in comparable store sales and a \$70 million non-comp contribution from stores opened in 2023 and 2024 that have not yet entered the comp base. For 2024, we now expect our total revenues to be between \$16.6 billion and \$16.9 billion.

Our second-quarter effective tax rate was 23.3% of pre-tax income, comprised of a base rate of 23.9% reduced by a 0.6% benefit for share-based compensation. This compares to the second quarter of 2023 rate of 22.5% of pre-tax income, which was comprised of a base tax rate of 24.3% reduced by a 1.8% benefit for share-based compensation.

For the full year of 2024, we continue to expect an effective tax rate of 22.4%, comprised of a base rate of 23.2% reduced by a benefit of 0.8% for share-based compensation. We expect the fourth-quarter rate to be lower than the other three quarters due to the totaling of certain tax periods. And variations in the tax benefit from share-based compensation can create fluctuations in our quarterly tax rate.

Now, we will move on to free cash flow and the components that drove our results. Free cash flow for the six months of 2024 was \$1.2 billion, in line with the first half of 2023, with growth in income offset by a lower benefit from reduction in net inventory this year versus 2023. For 2024, our expected free cash flow guidance remains unchanged at a range of \$1.8 billion to \$2.1 billion.

Our AP as a percentage of inventory finished the second quarter at 130%, down from 131% at the end of 2023. This ratio was slightly above our expectations, driven by the timing of inventory investments in the first half of the year. We continue to expect to see moderation in our AP to inventory percentage in the back half of 2024 and expect to finish the year at a ratio of approximately 127%.

Moving on to debt, we finished the second quarter with an adjusted debt to EBITDAR ratio of 1.97 times, as compared to our end of 2023 ratio of 2.03 times, with the decrease driven by a reduction in borrowings under our commercial paper program. We continue to be below our leverage target of 2.5 times 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 second quarter, we repurchased 784,000 shares at an average price of \$1,012 for a total investment of \$794 million. Year to date, through our press release yesterday, we repurchased 1.3 million shares at an average share price of \$1,020 for a total investment of \$1.3 billion.

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 Brad outlined earlier includes the impact of shares repurchased through this call, but does not include any additional share repurchases.

Before I close my comments today, I have one final item to cover as it relates to our investor relations function at O'Reilly and the change we will be making to our team. After more than 15 years as our Head of IR, Mark Merz will be transitioning into another key role with our company.

Many of you who have interacted with Mark closely over the years understand that in addition to his duties managing our investor engagement and communications, Mark is also a senior leader in our finance team and a key partner to business leaders across our company. Beginning in a few months, Mark will be leveraging that deep experience and knowledge of our business as he takes on a new role as an in-country leader in our Mexican operation. As we continue to grow our business in Mexico, we have an opportunity to build on a strong foundation for success and growth in what we believe will be a large and important market for our company.

In this new position, Mark will be taking on a key senior leadership role, working in tandem with our growing leadership team in Mexico. We plan to make this transition at the end of our third quarter, so Mark will continue to serve in his current role and be available to answer your questions about our business and second-quarter results.

During that process, he will also be managing the handoff of our primary investor relations contact function to Leslie Skorick. Leslie is a tenured O'Reilly team member with over nine years of experience with our company and currently heads up our tax function as Senior Director of Tax, but will now be adding investor relations to her duties. Mark and Leslie will be managing this handoff over the next couple of months, including the opportunity for you to meet Leslie at our upcoming Analyst Day in August in Chicago.

In addition, many of you have interacted with Eric Bird, another senior leader on our finance team, and he will continue to serve in his same role as an additional point of contact to support engagement with our investor community.

This concludes our prepared comments. At this time, I would like to ask Holly, the operator, to return to the line, and we will be happy to answer your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Scott Ciccarelli, Truist.

Scott Ciccarelli - Truist Securities, Inc. - Analyst

Good morning, guys. Scott Ciccarelli. Two quick ones, hopefully. You talked about softness in your discretionary goods. Can you provide more color on what percent of mix you consider discretionary and how negative those sales were down mid-single digits, high single digits, low double digits, et cetera?

And then secondly, I may have missed it or misunderstood it, but I thought you said you expect Canada to be more dilutive to gross margins than originally expected, but that you're maintaining your full-year gross margin guide. Can you just help reconcile that? Thank you.

Jeremy Fletcher - O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President

Yeah. Scott, thanks. This is Jeremy. I'll jump in on the first part of the question, and the guys might be able to help me on the other one.

On the discretionary categories, we mentioned in our prepared comments, and it's pretty common, those, even accumulated, are a smaller portion of our overall company chain. It's not typically a big driver. They were down more significantly than the rest of our group. We don't really quantify individual category comments, but we're pretty substantially pressured versus where we saw the rest of the chain. And because of that, even though it's a small piece, was enough to be, I think, a mover of the overall comp when typically they don't have that impact. But overall, it's still, I would tell you, a minor part of our overall business.

Brad Beckham - O'Reilly Automotive Inc - Chief Executive Officer

As we think about your second question, from a gross margin perspective, we did see, just as we lined out how we would roll Canada's numbers in and got more familiar with their operations to roll in, do expect that there would be a little bit more dilutive than what we've normally seen, but had a decent amount of that obviously already built into our guidance range. So it becomes one of the puts and takes as we think about what gross margin looks like in the back half of the year.

Similarly, some of the things that Brent pointed out in his prepared comments are also things that we view as more transitory items over a longer period of time. Things like mix between our categories and how our teams are able to manage our DC cost of leverage are things that typically we can see level out and don't think will create as much pressure.

We continue to think for the back half of our year that being able to be a favored partner for a lot of our suppliers gives us opportunities from a cost perspective. And as we've built that into the plan, we expect that that accumulates some benefit over the year.

And while we've seen some amount of that so far in our year, our outlook, as we think about that, is an offsetter that we think will be a contributor in the back half of the year. And those kind of all move into how we think broadly about our gross margin outlook being in a position to be relatively stable for how we've thought about the full year with some just kind of more short-term items here in the quarter.

Scott Ciccarelli - *Truist Securities, Inc. - Analyst*

Understood. Thank you.

Operator

Greg Melich, Evercore ISI.

Greg Melich - *Evercore ISI - Analyst*

Hi. Thanks. I wanted to follow up on the July trends. I think you guys said it remained solid, but it sounds like it might have been not as good as June. Would that be fair?

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Well, hey, good morning, Greg. This is Brad. I think what we want to balance on just kind of the exit rate coming out of June and heading into July, like we mentioned, when we look back at our original guidance and our internal plan kind of week by week, as we said it at the beginning of the year, June was the best performer from that aspect in the quarter. And like I mentioned earlier, we feel solid about the trends as they rolled into July.

I think what we want to balance that with a little bit, Greg, is just making sure when we say -- when I say solid, that's relative how the year's gone so far, as well as how we feel about our adjusted guidance for the remainder of the year, which we feel really good about. There's been a couple of moving pieces in July that make it a little bit of a tough read.

We're a few weeks in, still a lot of quarter to go, and the way that July -- the Fourth of July holiday layered in that first week, it's always a little bit hard to tell just from a category mix and a business mix. But overall, we feel really good about how we started the quarter.

Jeremy Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

The other thing to keep in mind there too, Greg, is that the timing of the weather benefit that we've seen so far this year compared to prior year saw really a shift in the second quarter. We're probably up against some of our more challenging comparisons in all of the back half here as we work through July because that's when, if you remember in 2023, we saw the hot weather come on and the benefits you got.

And it's always a challenge. We're always reluctant to try to draw in too many conclusions and extrapolate off of a two-, three-year period when that hot weather just impacts in a different way every year as it comes in. To Brad's point, we feel confident in what we think the read is just broadly across our business, outside of some of these fluctuations, and that's really what's informed how we think about the back half of the year, not just kind of a short look at a week or two.

Greg Melich - *Evercore ISI - Analyst*

Got it. That's great. And then my follow-up was, you mentioned certain undercar parts were weak, but you're still gaining share there. I guess, what do you think's going on? Are people deferring doing some of these larger ticket undercar things, or is there some trade down going on there?

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Yeah. Hey, Greg. This is Brad again. Great question. We called that out. When we look at our business, really on both sides of the business, but we look at professional, especially these last two or three years, we have really taken a lot of share.

When we look at the data we look at from a share perspective in those undercar, underhood, but specifically undercar hard part category lines, we're going up against some unbelievable compares. And then you start to think about maybe a little bit of mild winter the last couple of years, and you look at those categories. I think what we're seeing is, to answer your question directly, some deferral. So I think there is some deferral with those high-ticket service items on both sides of the business, but especially in the repair shops.

What we're still not seeing, Greg, and Brent may want to help me here, is the trade-down that you asked about. A little bit of deferral, but not trade-down in our line design.

Brent Kirby - *O'Reilly Automotive Inc - President*

And Greg, just to kind of build on Brad's comments, when we look, and that's something we've obviously watched closely with some of the pressure on the consumer that's been in the news, at our good, better, best progression across our product lines, we still, as we've reported in prior quarters, see actually a migration to best and out of good and better, which is interesting given the consumer backdrop.

But to Brad's point, I think where we're -- part of what's driving some of that is higher-end batteries, AGM requirements. There's some different things in the industry that are driving, we feel like, some of that migration up the continuum in terms of getting into the better and best categories. Some of it is also, for us, anyway, has been driven by our proprietary brands.

When we look at the growth there with SYNTEC, our synthetic oil proprietary brand, the growth there in units and courts as it continues to penetrate. We launched BrakeBest Select Pro. Import Direct Brakes continue to grow there in that best category. So we continue to see customers migrate there. They see value and they see quality in the box.

Where we have seen a little bit of -- we talked about -- Jeremy talked about discretionary categories a minute ago, but think about wipers for your car. We did see units were fairly consistent in Q2, but dollars showed some trade down there; people moving more down to the middle, lower level. And if you think about it, your wipers are more of a nuisance than something that's really critical to having your car on the road. But if it's streaking, you're going to replace it, and we did see some evidence in a category like that where people were looking for maybe an option that was a little bit more in the good or better range. But generally speaking, that's kind of what we're seeing.

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

And Greg, I may, just one more thing, cap that, just back to the root of your question. On some pressure we've seen on the undercar categories, we still feel good about our share and our share gains when we look at the data we look at.

Greg Melich - *Evercore ISI - Analyst*

Well, that's great. A lot of great color there, guys. Thanks. Congrats, Mark, on the new role, and have a good quarter.

Operator

Michael Lasser, UBS.

Michael Lasser - *UBS - Analyst*

Good morning. Thank you so much for taking my question. Congratulations, Mark Merz. Do you think another round of either price or expense investment is necessary in order to maintain or perhaps even accelerate your market share gains from here, especially if the industry goes through a period of protracted softness, as we've seen in the last couple of quarters? Thank you.

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Yeah. Hey, great question, Michael. Thank you so much. The short answer to the first part of your question there on pricing is no. We feel really good about the decision we made. It's been almost 2.5 years ago now to make the strategic investments into our professional pricing initiative.

And as we've said many times, we felt so good about those investments, not because of just the competitiveness of our on-the-street price compared to the independents, but the way that we, as a company, backed that up with our professional parts people -- our best-in-class delivery service in terms of turning bays and getting cars off the rack for a customer, all the work our territory sales managers have done in the last many years, as we've always done, just to make that price that's always third and fourth down the list, to really make those things pay, we had to do the other things that much better, from a service relationship and then all the work that our supply chains and teams have done to continue to keep us best in class in inventory availability. And we feel like all that has paid off greatly.

But like we've said many times, we don't feel that that is necessary to continue our share gains. I think what we're seeing right now is simply some pressure on the consumer. We don't feel like anything has really materially changed from the way we compete. The way that our investments are paying off, not seeing a lot different. We have tough competitors out there, but we're a \$16 billion-plus company operating in an almost \$150 billion industry and we don't see any other price investments necessary to take us to the next level. When we see times like we're seeing this year, where things are a little bit tough, we see unique opportunities to take share in other ways.

And I just maybe -- with the second part of your question in terms of other investments, we continue to invest. We continue to invest in staffing, though our teams did a phenomenal job managing SG&A this quarter based upon the sales results. We haven't backed off our investments and initiatives. And those initiatives are really centered around taking the friction out for our team members and our customers. And so really, we're going to continue to invest in all the strategic initiatives, but don't feel like there's another round of price initiative necessary.

Michael Lasser - *UBS - Analyst*

Okay. My follow-up question is, what do you think the catalyst is to accelerate growth across the industry? Is it just getting into the fourth quarter with comparison fees and then flipping the calendar to get into next year? And if this period of softness persists into next year, just as the industry gives back some of the gains from the last few years, what's a minimum level of growth in SG&A per store that O'Reilly can manage through just so we can properly calibrate our model? Thank you.

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Great. A couple other great questions, Michael. Well, as far as the catalyst for -- I'll take the first part, and then I'll let Jeremy help me out on the back part. I think on the first part, Michael, I think we have done such a great job controlling our own destiny the last many years. And obviously, we've had some amazing share gains and we're not resting on our laurels.

I mean, I also don't want to hide from the fact that, yeah, as we continue to comp the comp and lap all these share gains, the fact of the matter is we've decelerated some in terms of the overall continue to take the same amount of share year after year. But I don't think -- I think it's still yet to be seen how others will report for the next quarter or two, but we're seeing nothing that says that we're still not continuing to take share.

When we look at category data, when we look at market data, we still feel really good about our share gains. And again, I think time will tell based upon how others report how we're doing on that front. It's always a little bit hard to tell, obviously, with the independents and the OE dealers and things like that. But we see a constant catalyst to continue to build our teams better, give better service, and just continue to do what we do.

When I think back, Michael, to the toughest years we've had from a macro perspective in my 28-year career with O'Reilly, some of our toughest years are the biggest opportunities we have to kind of build our own catalyst going into 2025. There's times that when things get tough, there's certain competitors, not always our public competitors, that overreact on the expense front and they don't do as good a job of staffing their stores, staffing their delivery vehicles. They can overreact on inventory levels and things like that.

And so I actually believe the biggest catalyst we have is just being our own worst critic internally, looking ourselves in the mirror in terms of our execution. And our team is fully committed to putting the things in place that it's going to take to drive continued share gains.

Jeremy Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

Yeah. Maybe, Mike, just to add a little bit to also what Brad said, if we think about just the broader dynamics in the industry, we've seen periods of time like this in the past before. But we have a lot of conviction around the long-term strength of the core fundamentals that drive our business. And having been through many of these cycles, we know that our industry is very much supported by the ability to support a consumer that's economically constrained and give them an option to conserve part of their monthly budget that needs to go into other areas because they can keep their cars on the road.

The question around what the right SG&A spend is or where we leverage, it's always a challenging one for us to answer. We don't put a fine point on it because it depends on the markets and the circumstances we're in, what broader level of inflation looks like overall. And obviously, we don't provide that long-term outlook or guide into 2025 versus where we're at today.

I think what's more important for us is what Brent touched on in his prepared comments, in that we've got a team that very effectively manages how we think about the cadence and pace of the business and appropriately dialing in our operations to address the business when it gets a little bit soft, but to do so in a way that does not sacrifice really the value proposition, the relationships, the service that -- where the needs of the consumer do not change in these type of environments. So we're always going to be able to balance that well while making sure that we're investing in the long term for our business and feel confident that -- whether we're in a higher inflation environment, lower inflation, whatever that might look like, that we can manage well the productivity of our spend to support our results.

Michael Lasser - *UBS - Analyst*

Thank you very much, and welcome, Leslie.

Operator

Steven Forbes, Guggenheim Securities.

Steven Forbes - *Guggenheim Securities, LLC - Analyst*

Good morning. I wanted to follow up on the -- I wanted to ask about the cadence of store openings this year. I was curious if it's being impacted by any of your initiatives, distribution related, or so forth. And then given the expected number of openings in the back half implied, any reason for us to think that the number of openings could increase into sort of the out years here, especially given your commentary around growth in Mexico? Thank you.

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Yeah. Thanks, Steven. I'll say a few things and let Brent jump in. But no, nothing's changed on the store front -- on the store growth front in the US nor Mexico or Canada. We still feel really good about the pace of our new store openings.

First half of the year has gone really well; still feel good about the back half. So nothing out there to slow us down or speed us up necessarily. We really still feel like we have the right number in terms of store openings, domestically and internationally, and feel good about how we're going to end the year.

Brent Kirby - *O'Reilly Automotive Inc - President*

Yeah. The only thing I would add, Steven, to everything Brad just said is we continue to invest in our distribution infrastructure as well to support that store growth. We've got the three active DC projects out there that we've talked about, the relocation of two existing, and then one brand new there in the mid-Atlantic that we're working on. So we're continuing to -- that pipeline is going to continue, in the foreseeable future, at the same pace we're seeing now.

Steven Forbes - *Guggenheim Securities, LLC - Analyst*

And then maybe just a quick follow-up to Michael's question, maybe asked a different way, we think about how the employee mix has shifted sort of full-time versus part-time over the past few years. And would it help us frame up sort of what that has done to the fixed versus variable cost structure of the business, as we potentially may be entering a period of more moderate growth? Another way of asking Michael's question, but it does appear that there could be some pressure on expenses. And so any way to sort of frame up how we think about the fixed cost structure versus variable cost structure of the business?

Jeremy Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

Yeah. Thanks, Steven, for that question, and it's an interesting one. We still feel like we've got a solid amount of flexibility in how we manage the process to dial in our staffing levels to take care of customers.

The potential flexibility headwinds that you might talk about because of the higher full-time mix of our business, we think, really becomes offset by the productivity in the high service levels that those team members provide. And we still have, with the large chain in lots of different locations and just the normal turnover of our business, it gives us opportunities to dial in those levels as we need to.

But over the course of the last few years, as we have invested, not just in how we think about what the right full-time, part-time mix is in our business, but as we've thought about how we compensate our teams and how we manage our managers' work schedules as we've invested in benefits and those types of items, the overall quality of our store teams continues to, we believe, operate at a very high level and operate at a high level that's effectively managed by a lot of very seasoned team members and leaders within our company, as Brent pointed out in his comments. And that allows us on a very distributed basis to know that we're executing the playbook, running our business model in the right way, and can manage through these periods of time with a solid amount of flexibility.

Clearly, we've talked about it this quarter. We've talked about it several times over the course of the last years. We're not going to overcompensate there, we're not going to overadjust and do something that would create a service shortfall at all. We're not -- when we talk about softness in our industry from a sales perspective, these are not huge movements, and candidly, they don't matter to our customers.

If sales are a little bit soft, they still need a high level of service and we won't sacrifice that. So there are limits to how you manage that broader cross-structure. But for sure, we feel comfortable we've got a great leadership team in place to dial that into the right level.

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Yeah. And maybe, Steven, just to build on what Jeremy said or maybe just put a point on it is that we feel really good about the work that Jason Tarrant and our store operations leaders have done as we came out of COVID and we kind of drew a line in the sand as we increased that full-time mix, as well as just made our retention an even higher focus. It's always been a huge focus at O'Reilly. You can't have professional parts people if you have turnover on the counter; it just doesn't work.

And so we feel really good about those investments we made, and not only full-time, but all our initiatives come out of COVID to slow down that store turnover. And we've made a lot of progress. We feel really good about the progress. We feel like it's paying off in productivity, customer

service levels, and the stability of our business. Still work to be done; it's an ongoing thing to continue to work on that retention, but really feel good about those investments and the work that the store operations teams have done.

Steven Forbes - *Guggenheim Securities, LLC - Analyst*

Thank you.

Operator

Christopher Horvers, JPMorgan.

Christopher Horvers - *JPMorgan - Analyst*

Thanks. Good morning, guys. So my first question is maybe turn the industry growth question around a little bit. Do you think that weather was a net benefit or a net headwind to the category in your growth in the second quarter here? Because I know June got a weather benefit, but you had a pretty late spring in the north. So as you're trying to disaggregate the underlying trend of the business, how do you think about the influence of weather? And then related to that, as you saw about July's solid performance, are you also seeing that on the DIY side of the business being better than what you experienced in the second quarter?

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Yeah. Chris, on the question around -- I would say it's probably a net positive in the second quarter just because the hot weather comes on. And oftentimes, that first round of extreme weather gives you a little bit of a boost because it gets the first piece of the failures there.

As we look over the balance of the first half of the year, candidly, that's probably informed more how we think through where the overall industry has been because it has been choppy. There's been lots of different puts and takes that you'd attribute to weather. But as we've said multiple times over the course of time, a lot of that stuff evens itself out as you put periods on top of periods. And so we think it's likely to have been more neutral there, although for sure, lots of puts and takes.

And we'll see the balance of the back half of the year as you move further out of summer and you have a little bit less of those impacts, obviously, until you get into the winter. And our compare is a little bit softer at the end of the fourth quarter as it relates to that. But that's really how we would kind of frame out that broader question.

Christopher Horvers - *JPMorgan - Analyst*

And then on the DIY into July versus what you experienced in the second quarter?

Jeremy Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

Yeah. We don't want to parse July too much for all the reasons that Brad talked about a lot. I would tell you the composition of the business -- really, the thought process between DIY and professional has been pretty consistent as we move through the year. So a lot of those categories that we talk about that are benefited from a hot weather perspective, we saw solid performance on both professional and DIY side.

Christopher Horvers - JPMorgan - Analyst

Got it. And then following up on an earlier gross margin question, so just to clarify, did 2Q benefit from lower product acquisition costs? And I guess if it didn't, it sounds like you're expecting that to happen in the back half of the year. So is there some sort of accounting waiting for the inventory turn? Was there anything unique in the second quarter on that side that turns that to a benefit as the year progresses?

Brent Kirby - O'Reilly Automotive Inc - President

Yeah. I can start on that one, Chris. When we think about product acquisition costs, as we've continued to move past COVID and into a more normalized environment, we've got some suppliers out there that are still facing wage pressure, labor production pressures, raw materials, those kind of things. We've got some that aren't, some that are getting more efficient, getting better. So I would tell you it's been what I would say back to a normal version of some puts and takes with acquisition costs, navigating through all the typical things that are out there in that environment.

As we think about how we planned the year, we planned the back half of the year to be probably even more normal than the first half of the year when you think about how we built the plan. So we anticipate that to continue to play out the way we see it now. So that's what I would tell you there on the acquisition cost side. I would tell you it's not, and we're not in a point where we're seeing a bunch of deflation there, but we are seeing a normalization there.

Jeremy Fletcher - O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President

Yeah. And Chris, there's nothing unique from an accounting perspective. There was a net benefit in second quarter. We just think incrementally, to Brent's point, we can add to that as we move through the back half of the year.

Christopher Horvers - JPMorgan - Analyst

Got it. So year on year, gross margin should be pretty similar in the back half of the year?

Jeremy Fletcher - O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President

Yeah. I mean, we feel comfortable with where our guide is at and obviously what that implies for the back half of the year.

Christopher Horvers - JPMorgan - Analyst

Understood. Thanks, guys.

Operator

Brian Nagel, Oppenheimer.

Brian Nagel - Oppenheimer & Co., Inc. - Analyst

Hi. Thanks for slipping me in here. So some shorter-term questions, I apologize, but maybe just a follow-up on Chris's question as well, but can you help us understand better -- you talked about the business solidifying or strengthening in June. Now, how much stronger June was than the prior two months in the quarter?

And then my second question, with the moderation of the guidance, does that reflect primarily the weakness in the first half of the year? Or are you actually also moderating expectations for the second half of the year?

Jeremy Fletcher - *O'Reilly Automotive Inc - Chief Financial Officer, Executive Vice President*

Yeah. No, thanks for the questions, Brian. I think maybe the second one first. It reflects both. Just as it works out, our back half will be pretty similar within our implied guidance to our first half of that, just based upon -- if you think about it from a midpoint perspective. So it's not just the flow through of our results so far, but how those have informed what we think our outlook for the remainder of the year is, along with, obviously, what we see in the business and how we and how we perceive that to be.

As we think about the cadence of the quarter, I think that Brad said it well in his prepared comments, April and May were both softer than both our expectations. As the heat came on June, June performed better and more in line with what we would have looked for as we entered into the quarter, certainly not a situation where we significantly outperformed our kind of longer-term expectations for the year in the quarter. It was a little bit more of just a normalization back towards what our expectations would have been. But that's sort of the right way to think about the cadence of the impact month to month.

Brian Nagel - *Oppenheimer & Co., Inc. - Analyst*

Okay. That's helpful. I appreciate it. Thank you.

Operator

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

Brad Beckham - *O'Reilly Automotive Inc - Chief Executive Officer*

Thank you, Holly. We would like to conclude our call today by thanking the entire O'Reilly team for your continued hard work and dedication to our customers in the second quarter. I would like to thank everyone for joining our call today, and we look forward to reporting our third-quarter results in October. Thank you.

Operator

Thank you. 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.

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