



Consolidation Trends in the Automotive Aftermarket Industry

July 21, 2014



What is Axial?

- Axial is the largest business development network for professionals who run, advise, finance, or acquire private companies.
- Private companies join Axial to meet the advisors and partners who can help them grow, finance, or exit their business

The screenshot displays the Axial platform interface. At the top left, a callout box states: "Axial instantly generates a list of advisors and buyers relevant to your company". The main content area is titled "OPPORTUNITY > RECOMMENDATION LIST" and features a table with the following columns: "Name", "Transaction Profile", and "Contact".

	Name	Transaction Profile	Contact
<input checked="" type="checkbox"/>	 David Polack Lion Capital Partners	Industrials Investments	 
<input type="checkbox"/>	 Peter Rooke Star Group, LLC	Manufacturing Opportunities	 
<input type="checkbox"/>	 Jen Weldon Larson Capital	Materials Investments	 

A second callout box on the right side of the table states: "Before reaching out, research a recommendation's team and past transactions".



Meet the panelists



David Roberts,
**Managing
Director,**
FOCUS
Investment
Banking

Dave leads the automotive practice at FOCUS and brings over 25 years of combined transactional and operational experience in the automotive space. As co-founder of Caliber Collision, he raised more than \$125M in capital while leading 37 acquisitions. Over 15 years as a deal professional, he has represented buyers and sellers of middle-market companies in over \$500M of transactions.



Brian
Devening, **Vice
President,** The
Fred Jones
Companies

Brian leads M&A for The Fred Jones Companies, a third-generation family business with a 90-year track record of operating automotive businesses in the U.S. Brian brings over 15 years of funding businesses as both an entrepreneur and a transaction professional, and led TFJC's sale of Global Parts Distributor's in 2009 and sale of Industrial Specialties in 2012.



Vincent
Romans,
**Founding
Partner,** The
Romans Group

Vincent is the Principal of The Romans Group, a firm providing strategic advisory services to the collision repair, property and casualty auto insurance, and auto physical damage aftermarket supply ecosystem. Vincent brings four decades of operating and consulting experience working with domestic and global companies.



Agenda

- Overview
- Manufacturing
- Case Study: Collision Repair Consolidation
- Q&A



Consolidation, Contraction, Convergence Industry Transformation



Industry Transformation

- Simultaneous activities:
 - Contraction
 - Consolidation
 - Convergence
- Results
 - Industry Transformation
 - Structural change

Transformation Impacts:

- Manufacturers
 - OEM manufacturing & parts, aftermarket parts, paint
- Services
 - Collision repair, distributors, dealerships, software vendors
- Insurers
- Investors



Distribution and Services Consolidation

- **Rental - Technology**

- Enterprise acquires National and Alamo
- Clayton Venture Group acquires CynCast
- Avis buys Zip Car
- Hertz acquires Dollar-Thrifty
- Enterprise acquires I-go car service, Mobileye

- **Parts**

- LKQ acquires Keystone
- LKQ acquires Greenleaf
- LKQ acquires Euro Parts
- LKQ acquires AKZO Distribution locations
- LKQ acquires Pro Body Parts Canada
- Solera/Audatex acquires APU Solutions
- LKQ acquires Keystone Automotive Operations Inc.

- **Glass-Networks**

- Belron acquires Safelite
- Kohlberg acquires LYNX Services
- Solera/Audax acquired LYNX APD
- Boyd Group acquires Glass America

- **Data - Information**

- IHS acquires I.L. Polk & Company (CARFAX)
- Hellman & Friedman invests in CarProof
- Solera/Audatex acquires New Era Software, See Progress, Inc., Hyperquest
- CCC Acquires Injury Sciences, Auto Injury Solutions
- KKR acquires Mitchel

- **PBE**

- Uni-Select acquires several companies 2014
 - Lakeland Auto Paint and Supply, January 7, 2 locations Florida
 - Metro Paint Supply, February 17, 5 locations, Illinois and Colorado
 - J. K. Distributors, March 4, 9 locations Virginia



The Romans Group LLC

Deals are Getting Done in All Segments of the Aftermarket

(\$ in millions)

SELECT STRATEGIC BUYER TRANSACTIONS SINCE JANUARY 1, 2013

Date	Target	Buyer	TEV	Target Description
1/2/2014			\$450	Distributor of specialty aftermarket equipment and accessories
1/2/2014			\$2,040	Distributor of replacement automotive parts, supplies, and tools
9/13/2013			NA	Designer, manufacturer, and supplier of exhaust products
4/1/2013			\$1,019	Reseller and supplier of automotive parts and accessories in Australia and New Zealand



The Romans Group LLC

SELECT PRIVATE EQUITY TRANSACTIONS SINCE JANUARY 1, 2013

Date	Target	Buyer	Seller	TEV	Target Description
11/20/2013	 *			NA	Operator of auto body, paint, dent, and collision repair centers
10/24/2013	 *			NA	Supplier of high-performance auto parts
10/14/2013				\$1,000	Supplier of information solutions to collision repair operators and insurers
2/1/2013				\$4,900	Manufacturer, marketer, and distributor of coating systems primarily for the transportation industry
1/15/2013				NA	Leader in collision repair and insurance estimating software solutions and analytical tools
1/7/2013				NA	Manufacturer of automotive air conditioning products

*Denotes transactions where BB&T Capital Markets served as financial advisor



Insurers Concentration

2013 Rank	Insurance Company	Market Share Percent				13-Year Change
		2013	2009	2004	1999	
1	State Farm	18.5	18.1	18.6	19.5	-1.0
2	GEICO	10.3	8.4	4.9	3.8	6.5
3	Allstate	10.0	10.7	10.5	12.5	-2.5
4	Progressive	8.5	7.6	6.6	4.4	4.1
5	Zurich/Farmers	5.5	6.5	5.4	5.8	-0.3
6	USAA	5.1	4.1	3.9	3.5	1.6
7	Liberty Mutual	5.0	4.4	2.7	2.2	2.8
8	Nationwide	4.0	4.6	4.4	4.1	-0.1
9	American Family	1.9	2.1	2.5	2.1	-0.2
10	Travelers	1.8	2.1	2.6	2.0	-0.2
	Total Share - Top 5	52.8	51.3	46.0	46.0	6.8
	Total Share - Top 10	70.6	68.6	62.1	59.9	10.7

- Over half of all auto insurance is handled by just five companies
- The top 10 insurance companies combined increased market share by almost 10 points in 13 years
- State Farm and Allstate, while down slightly during this time, still command almost 30% of the market
- GEICO passed Allstate's market share in 2013



Investors Focused on Consolidation

- Private Equity investors are driving investment, even in consolidating & contracting industries
- Huge pools of idle money chasing limited number of attractive return targets
- Recent success of ONCAP exit from Caliber at 5.5-7x initial investment over 5 years was catalyst in collision repair
- Large, \$30 B + industry opportunity
 - Recurring revenue, free cash flow and attractive returns on invested capital
- High barriers to entry for MSO model
 - Business complexity, performance model and required competitive performance
 - Brand recognition
 - Mature management teams
 - Operational excellence and economies of scale
- Insurance industry strategy aligned with MSO strategy



S&P CASH BALANCES

(\$ billions)

Strategic buyers remain flush with cash as a result of more conservative cash management following the downturn and are again actively participating in acquisitions



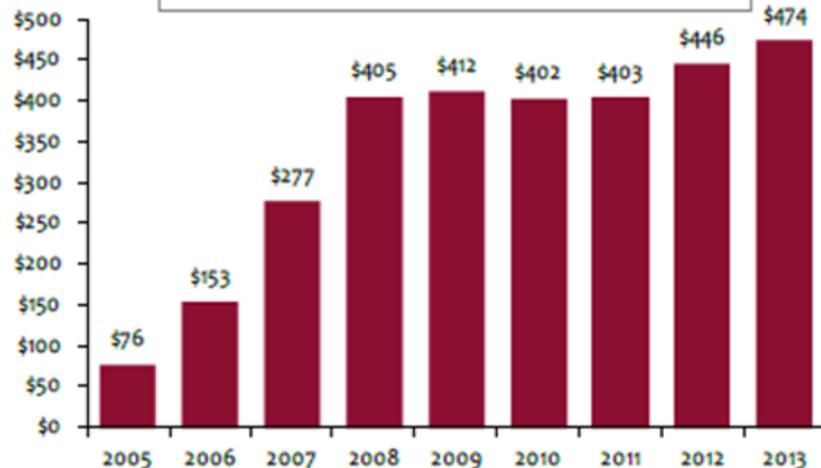
Source: FactSet; Buyouts Magazine

*2013 as of Q3

PRIVATE EQUITY DRY POWDER

(\$ billions)

Funds available for investment now stand at \$470 billion, which equates to nearly \$950 billion in purchasing power when factoring in current borrowing availability



Major Trends in the U.S. Automotive Industry



The Manufacture of Light Vehicles is Changing Dramatically...

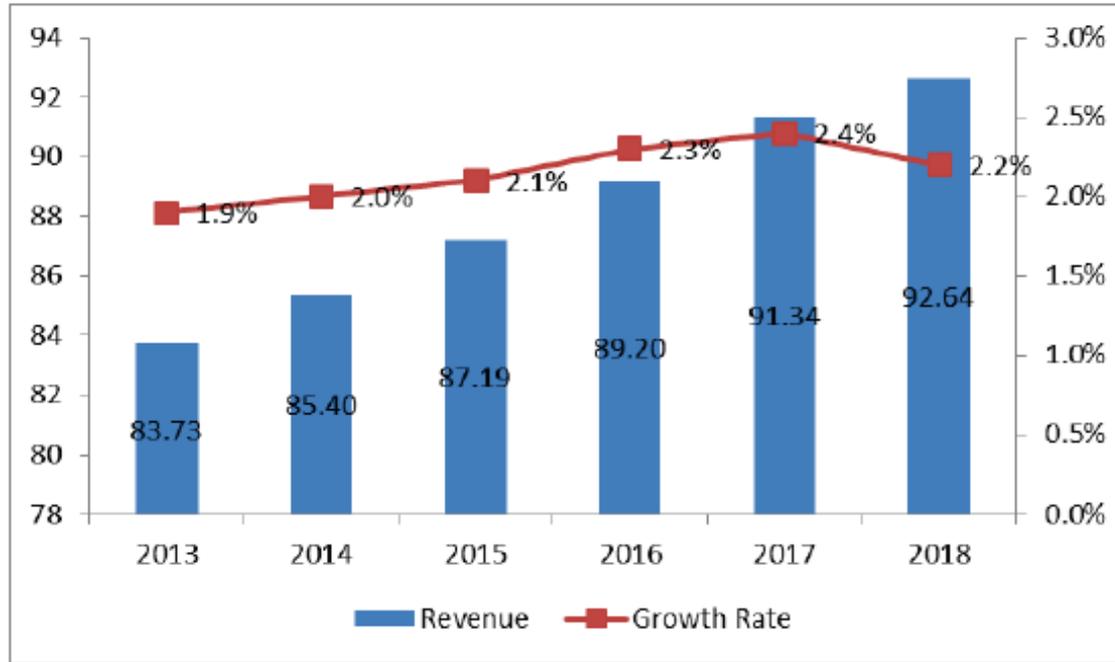
And so it will for aftermarket parts and services



- Remanufactured Engines and Transmissions
- Wiper Blades
- Exterior Accessories
- Audio Receivers
- Interior Accessories
- Suspension Components
- Waxes/Polishes
- Collision/Body
- Steering/Linkage Components
- Oxygen Sensors
- Tires and Wheels
- Exhaust Components
- Lighting
- Batteries
- Antifreeze/Performance Chemicals
- Brakes
- Switches
- Starters/Alternators
- Spark Plugs
- Motor Oil



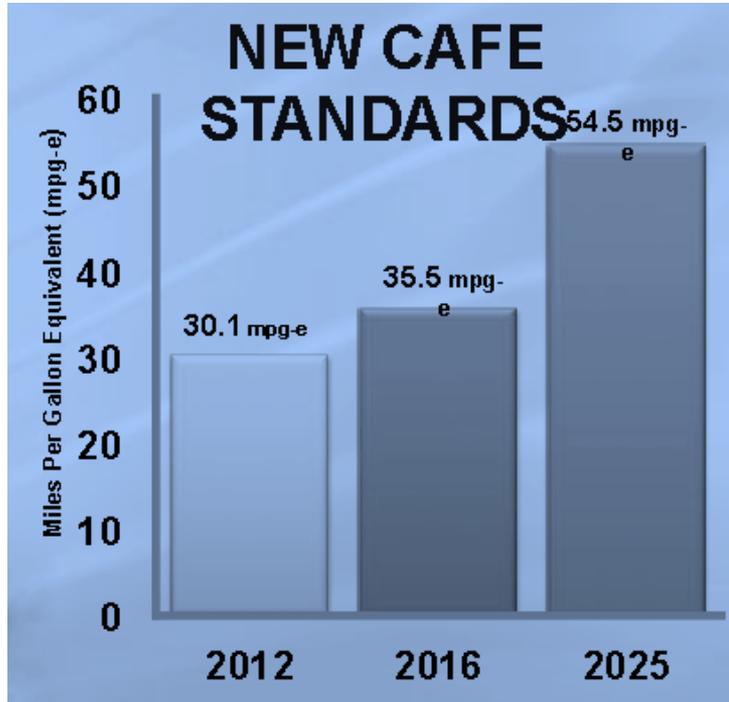
Automotive Parts Aftermarket in the U.S. 2013-2018 (\$US Billion)



Source: TechNavio Analysis

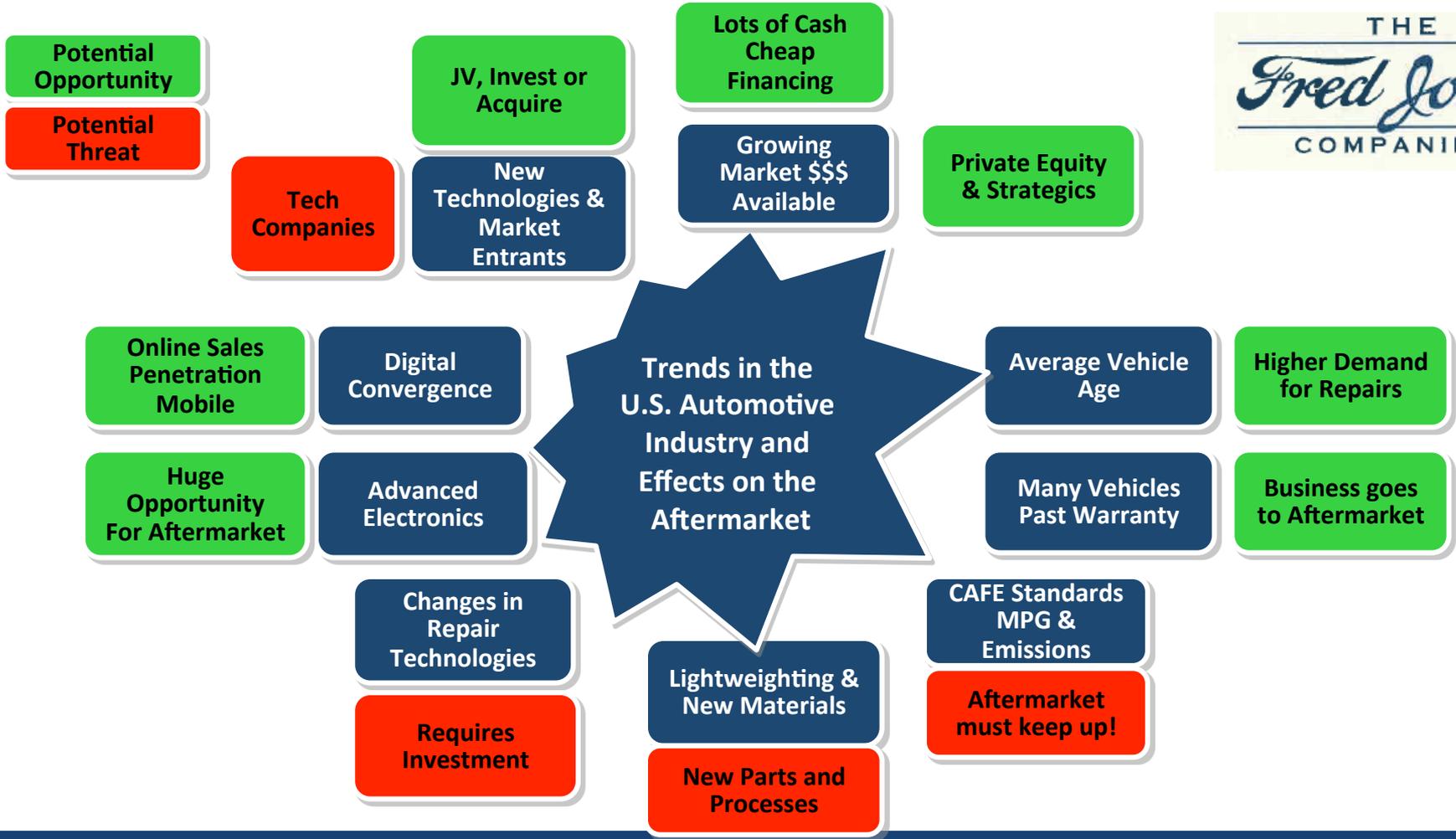


Automotive Industry Megatrends



- Driving OEMs to Innovate and Lightweight
- New materials, Engine Downsizing, Alternative Powertrains
- Fuel economy and emissions reduction efforts favor vehicle lightweighting
- Every 10 percent reduction in vehicle mass leads to a 5 to 7 percent decrease in fuel consumption.
- Aftermarket must adjust to new materials, parts, manufacturing processes and new technologies faster than ever before





Raw Materials Used in Major Segments of Automotive Industry



Structural (30%)



- Chassis
- Body in White
- **Steel**
- **HSS**
- **Carbon Composites**

Power Train (22%)



- Engine
- Suspension
- Transmission
- **Steel**
- **Aluminum**
- **Magnesium**
- **Carbon Composites**
- **Titanium**

Interior (23%)



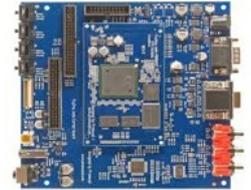
- Dashboard
- Floor
- Door panel
- Steering
- Seat
- **Plastics**
- **Steel**
- **Glass Composites**
- **Carbon Composites**
- **Magnesium**

Exterior (11%)



- Door modules
- Hood
- Trunk lid
- Bumper
- **Steel**
- **Aluminum**
- **Plastics**
- **Glass Composites**
- **Carbon Composites**

Electrical/Electronic & Others (14%)



- Switches & Modules
- Wiring and lamps
- **Plastics**
- **Rubber**
- **Glass Composites**
- **Magnesium**

% represents weight distribution of total vehicle weight



Mechanics Must be Technicians

New Market Entrants



Electronics
<ul style="list-style-type: none">• Engine controllers and sensors• Safety systems• Chassis control• Measurement and diagnostics• Entertainment• Navigation systems• Emissions monitoring

Body Parts
<ul style="list-style-type: none">• Materials• Adhesives & Fasteners• Joining• Dissimilar Materials• Repair or Replace

Connectivity
<ul style="list-style-type: none">• Infotainment• Telematics• V2V• V2I• Autonomous Vehicles• Big Data

Alternative Powertrains
<ul style="list-style-type: none">• BEV• PHEV• FEV• CNG• LNG• Hybrids

Software & Hardware
<ul style="list-style-type: none">• Over 100M lines of code• Over 60 microprocessors• Over mile of wiring• Updates & Recalls



Shift from DIY to DIFM
Increasing Complexity of Vehicles

OEMs innovating Rapidly-Lightweight, Alt. Powertrain, Electronics, Connectivity



Key Aftermarket Demand Drivers

Lower Cost Better Quality	<ul style="list-style-type: none"> ▪ Generally cheaper than OE ▪ Aftermarket suppliers can improve upon OE quality
Variety of Options	<ul style="list-style-type: none"> ▪ Consumers have multiple brands to choose from for same parts ▪ Aftermarket products and services are available through multiple channels
Advanced Parts	<ul style="list-style-type: none"> ▪ Innovation and technology driven by CAFE and Connectivity is driving demand for replacement parts and new service technologies
Vehicle Age and UIO	<ul style="list-style-type: none"> ▪ Average vehicle age is over 11 years ▪ Units in Operation in the U.S. will increase annually and exceed 300M by 2018
Economic Factors	<ul style="list-style-type: none"> ▪ U.S. Automotive Industry is right-sized and sales are at pre-recession levels ▪ Strategic and financial buyers still have excess cash for consolidation



Key Aftermarket Challenges

Low Cost Foreign Parts	<ul style="list-style-type: none"> ▪ Chinese supplies can often undercut pricing ▪ Large U.S. trade deficit on auto parts
Competition from OEMs	<ul style="list-style-type: none"> ▪ Products becoming more complex, OEMs want to capture more aftermarket \$ ▪ OEMs are creating proprietary processes and materials
OEMs bypassing Channel	<ul style="list-style-type: none"> ▪ Many parts mfgs are set up to drop-ship individual parts to consumers ▪ E-Commerce is gaining traction for auto parts and will increase competition
Keeping up w/ Repair Education	<ul style="list-style-type: none"> ▪ Collision repair centers must invest in new equipment and provide training on new materials and parts ▪ Electronics, software, and hardware require sophisticated technicians
Choosing the Winners	<ul style="list-style-type: none"> ▪ Many competing technologies, only some will survive



Case Study: Collision Repair Industry



Collision Repair Industry today

- Over 34k shops, \$31B revenue
- Market Segments
 - 4 consolidators (largest multi-shop operators, or MSOs)
 - ABRA, Caliber, Gerber, Service King
 - 160 other MSOs > \$10M
 - 24 Dealer MSOs > \$20M
 - 4 multi-location networks (MLNs)
 - CARSTAR, FixAuto, MAACO, ABRA franchisees
 - Remainder of industry



Consolidation

- Consolidation – big are getting bigger:
 - Larger, more productive/efficient, better managers/systems, higher margins, organized
 - Insurers reward scale and performance with more volume, which improves margins
 - Higher margins = more investment in management, systems, training, marketing, acquisitions
 - Result = virtuous cycle of greater scale
- Consolidation Drivers:
 - Availability of targets (more sellers, esp. smaller ones)
 - Low cost of capital (large consolidators own by large PE firms or public)
 - Attractive investment returns (medium MSOs are expanding with new capital from PE investors and lenders)
 - Attractive exit opportunities (smaller MSOs and independents are merging and selling to large MSOs)



Consolidators Focus on Top 125 Markets

Unconsolidated
market examples:

– Philadelphia, PA -
\$650 million

– Washington, DC -
\$800 million

Consolidating market
examples:

– Chicago, IL - \$1.2
billion

– Charlotte, NC -
\$200 million

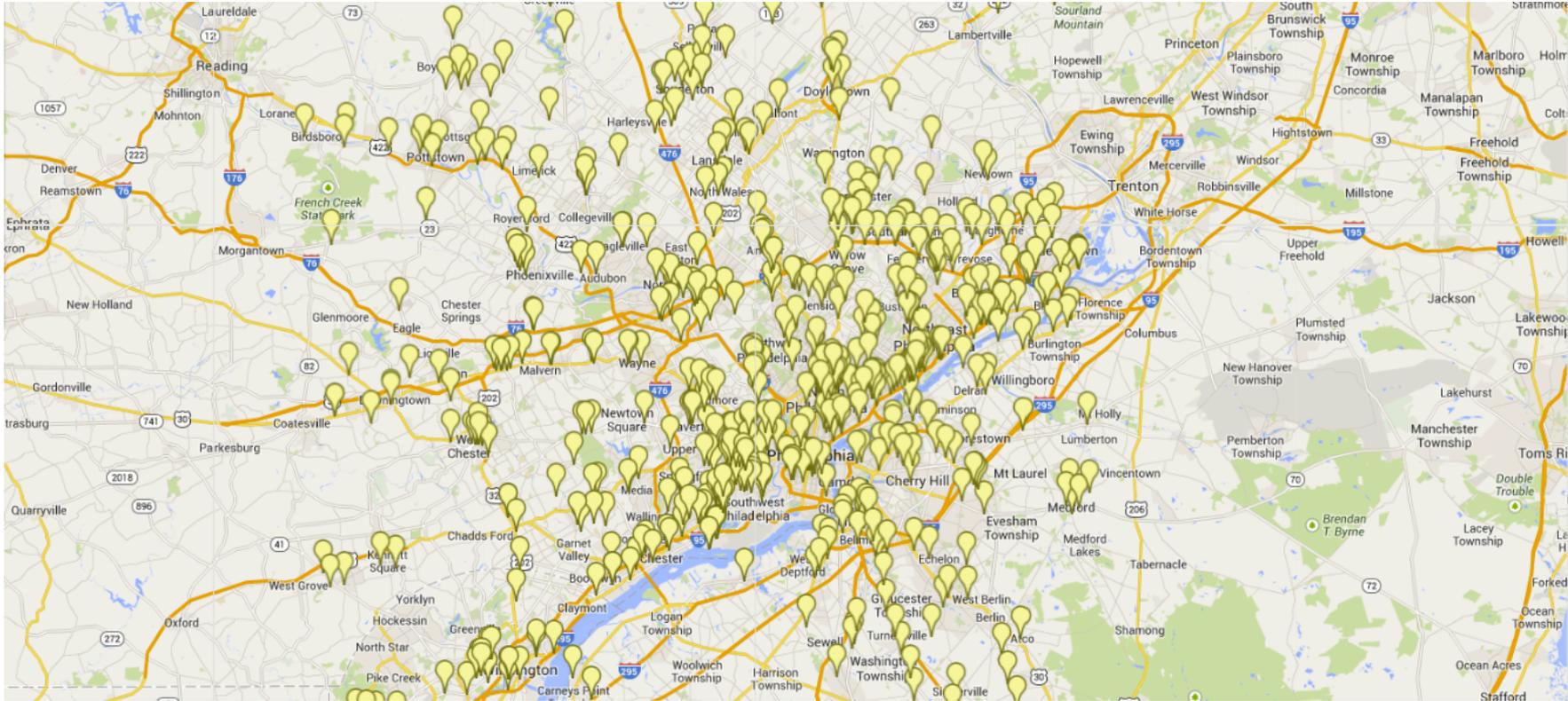
Consolidated market
examples:

– Denver, CO - \$220
million

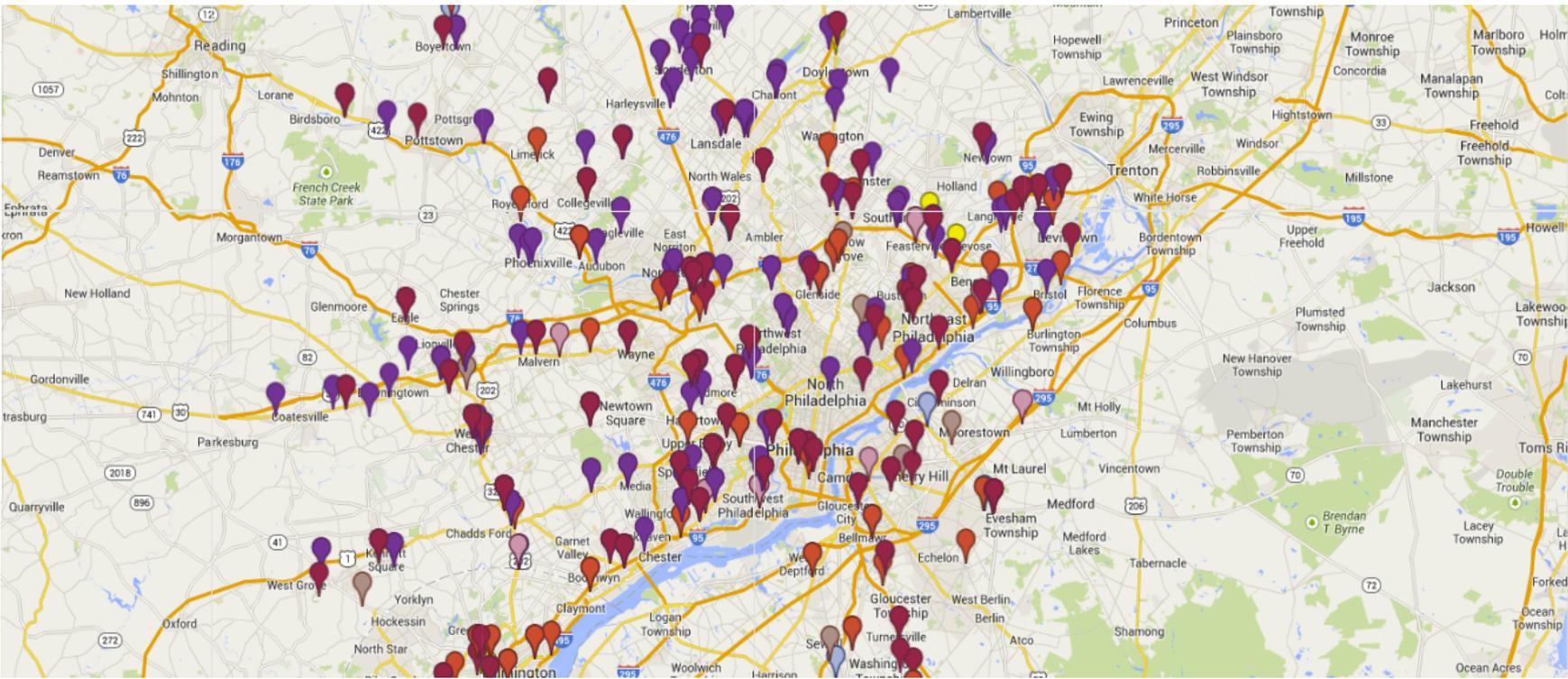
– Phoenix, AZ - \$400
million



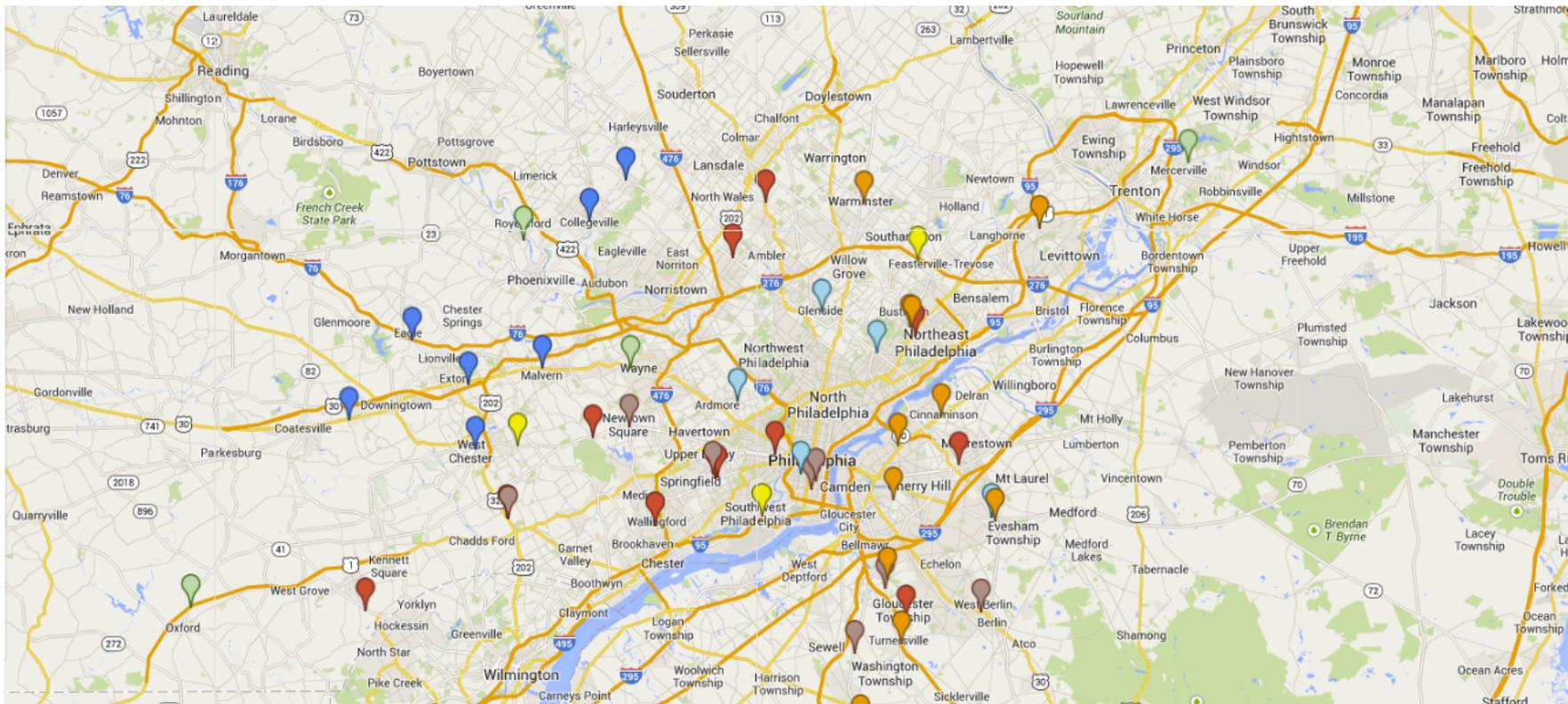
622 Independent Shops in Philadelphia Market



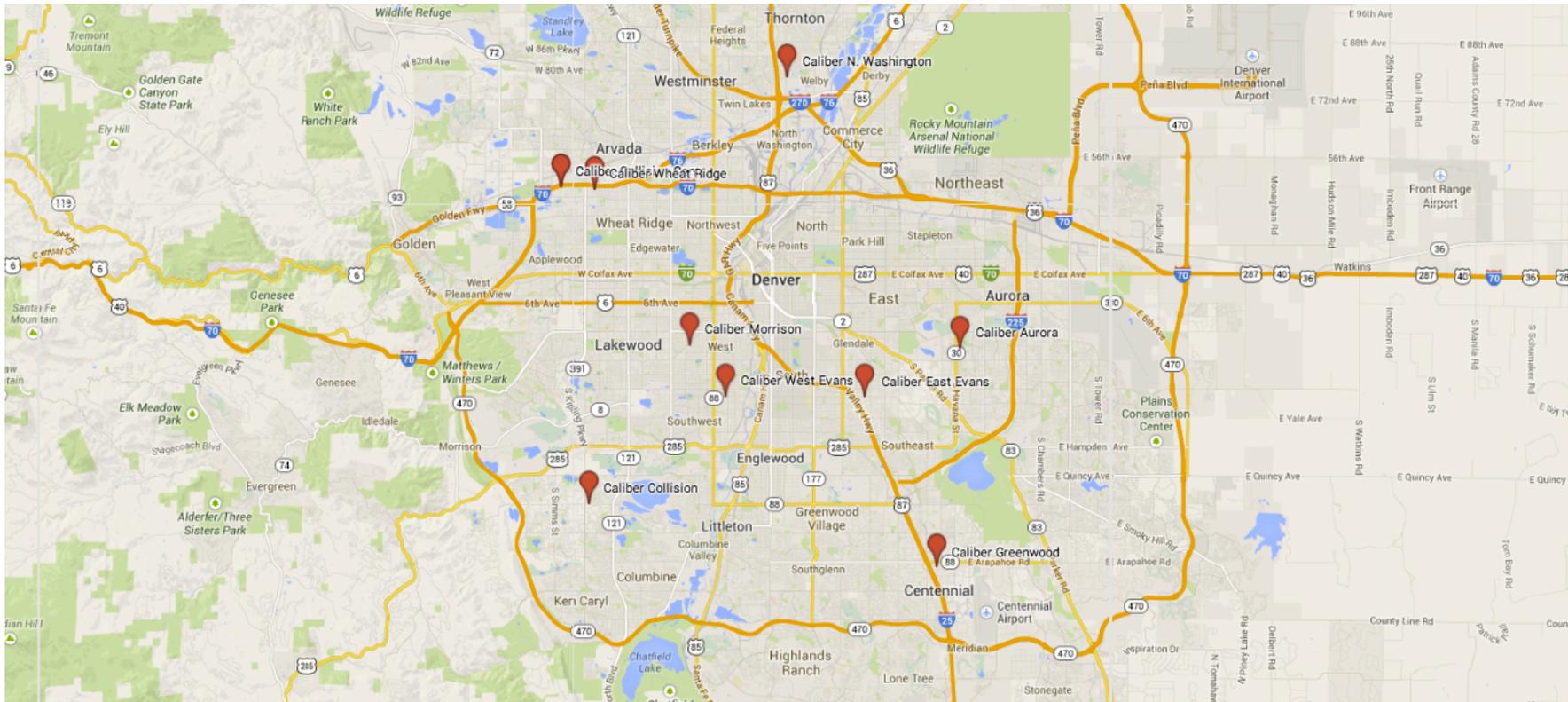
250 DRP Shops in Philadelphia Market



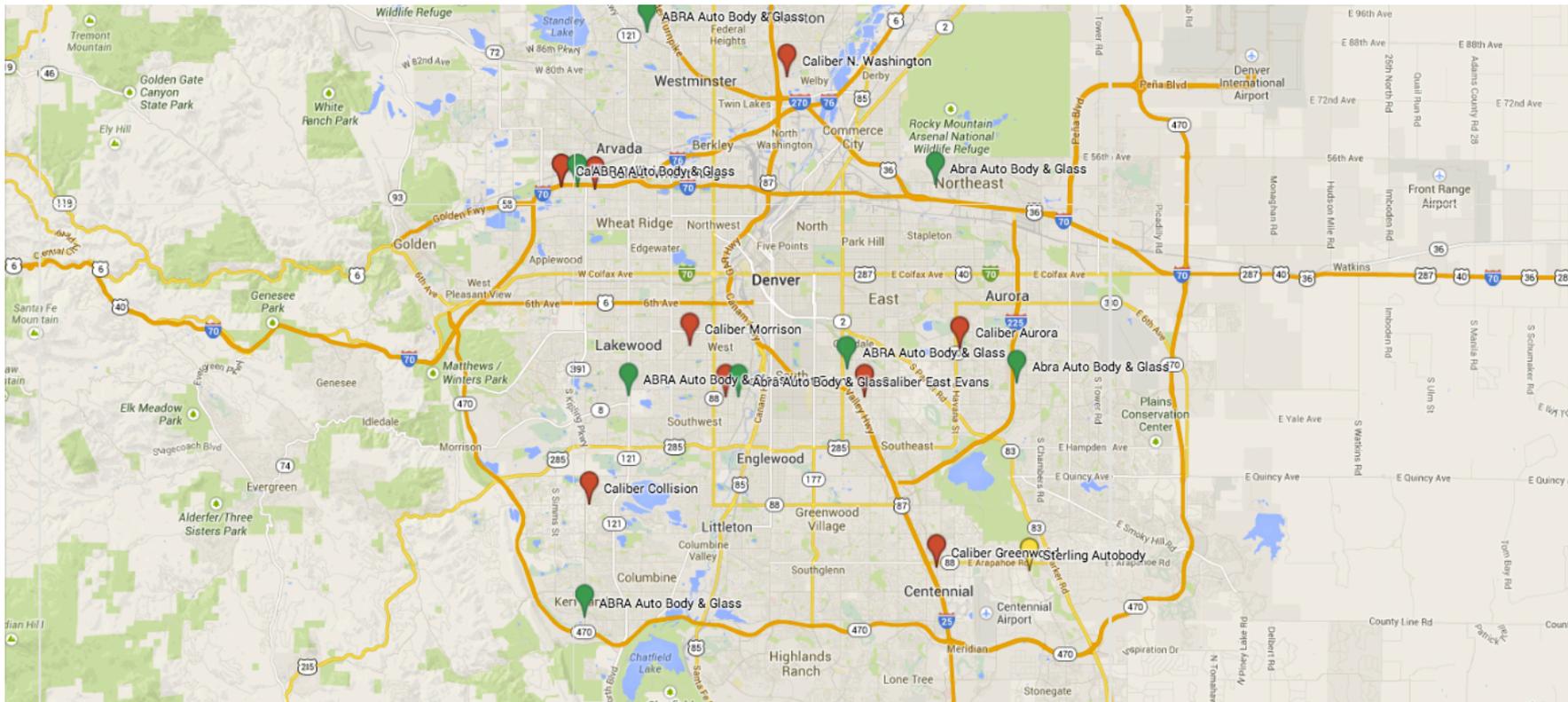
54 MSO shops in Philadelphia Market Including only 3 Consolidator shops



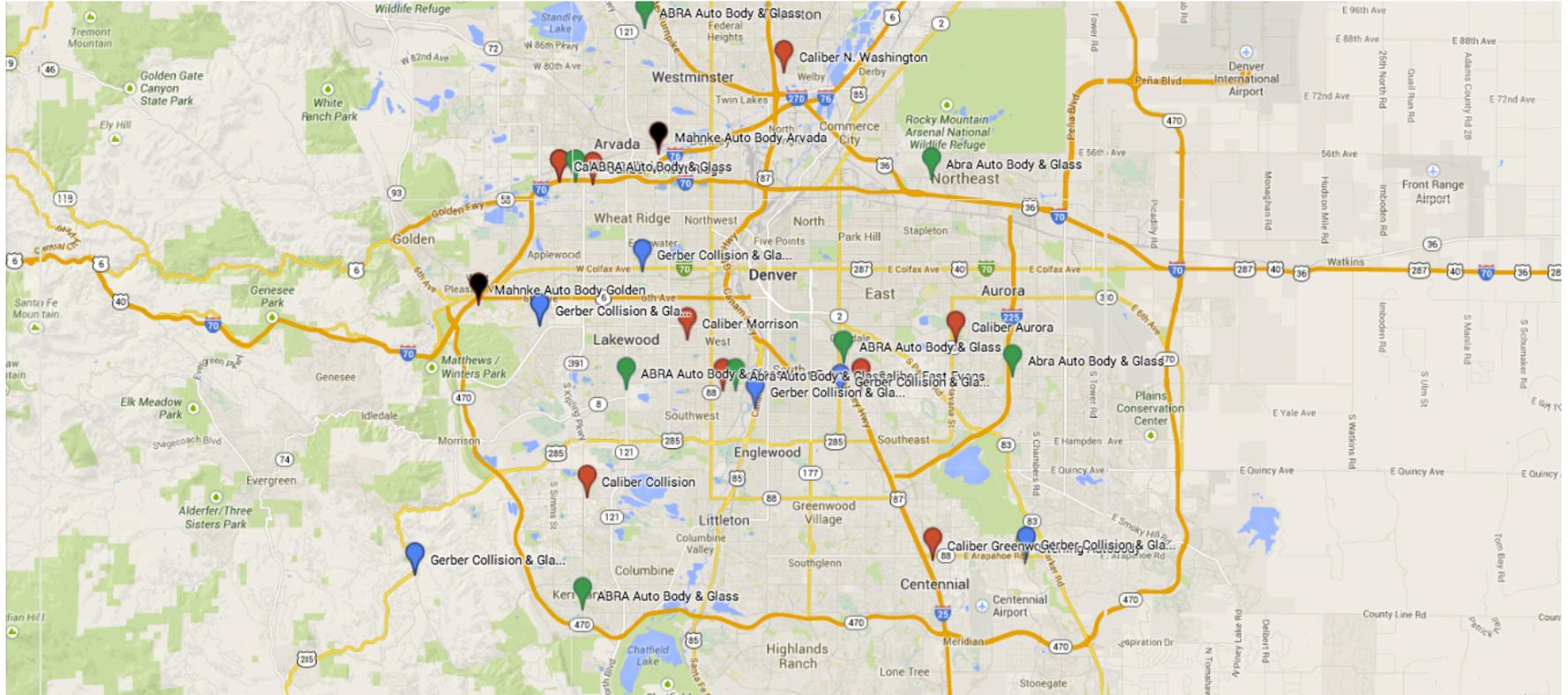
13 Caliber Shops in Denver



Plus 9 ABRA Shops, 2 Service King Shops



Plus 9 Gerber Shops and 4 shops in one remaining independent MSO



Convergence

- Insurers with larger market shares are concentrating repairs with MSOs
- Best insurance company DRP networks utilize MSOs that have proven their capabilities across entire markets
- MSOs are expanding to meet insurers desires for market coverage/capacity



Benefits and Risks for MSOs

Benefits

- Competitive
 - Improved market share
 - Improved positioning with insurers
- Operational
 - Improved processes, improved quality
 - Improved management, better staffing
 - More efficient utilization of fixed assets
- Financial
 - More income, less risk
 - Lower parts, paint, materials costs
 - Preserves or improves margins

Risks

- No long-term commitments from insurers
- MSOs give guarantees to insurers (discounts, cycle time, CSI penalties)
- Only real commitments from insurers is promise to bring all MSO shops onto their DRPs
- May use volume leverage to extract more concessions
- Risky investment decisions – does expansion, investments, and improved performance have long-term ROI or do insurers just keep raising the bar



Alternatives for MSOs

- Larger MSOs (the consolidators)
 - Continued rapid growth through acquisitions
 - Possible public offerings to access expansion capital and reward investors
- Other large MSOs have different choices
 - Grow bigger and attempt to thrive in markets where they compete with consolidators
 - Sell out now to consolidators
 - Grow bigger then sell to consolidators
- Smaller MSOs and independents have fewer choices
 - Consolidation in their markets may outpace their ability to grow and diminish their value
 - Selling sooner may be best alternative
- Defensible opportunities - depends on market sizes, degree of consolidator penetration, specialization by MSO
- Tertiary and rural markets
 - Markets where consolidators are less likely to expand
- Special expertise and focus
 - Aluminum
 - Restoration
 - High end brand repairs



Benefits and Opportunities for Insurers

Benefits

- Improved retention: CSI, quality, communication
- Reduced ULAE and LAE: single point of contact, management by KPIs and reduced field staffing
- More predictable outcomes
- Better data for underwriting
- Possibilities for future savings, process changes

Opportunities

- Continuing improvement in performance across MSOs (quality, coverage, self-management capabilities, discounts)
- Better alignment with MSOs for future changes in tech, communication
- Market leading insurance creates unique competitive advantages by using MSOs to deliver on marketing promises
- Higher-performance provider networks can enable new offerings (HMO type offering w/ restricted networks, capitation possibilities with MSOs willing to take risk)



Thank you for attending

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Contact Information & Questions



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