MONRO, INC.
Form 10-Q
February 07, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 29, 2018.

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____________ to _____________

Commission File Number: 0-19357

MONRO, INC.

(Exact name of registrant as specified in its charter)

New York	16-0838627
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification #)
200 Holleder Parkway, Rochester, New York	14615
(Address of principal executive offices)	(Zip code)

585-647-6400

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer   Accelerated filer   Non-accelerated filer   Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes   No

As of January 25, 2019, 33,103,468 shares of the registrant's common stock, par value $ .01 per share, were outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

MONRO, INC.

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	December 29, 2018	March 31, 2018
	(Dollars in thousands)	
Assets		
Current assets:		
Cash and equivalents	$ 3,579	$ 1,909
Trade receivables	15,033	11,582
Federal and state income taxes receivable	5,276	4,185
Inventories	158,846	152,367
Other current assets	39,579	37,213
Total current assets	222,313	207,256
Property, plant and equipment	807,230	767,864
Less - Accumulated depreciation and amortization	(376,587)	(351,195)
Net property, plant and equipment	430,643	416,669
Goodwill	548,153	522,892
Intangible assets	50,810	49,143
Other non-current assets	12,756	10,997
Long-term deferred income tax assets	2,406	11,475
Total assets	$ 1,267,081	$ 1,218,432
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt, capital leases and financing obligations	$ 21,361	$ 18,989
Trade payables	95,166	84,568
Accrued payroll, payroll taxes and other payroll benefits	22,570	20,197
Accrued insurance	39,848	36,739

Warranty reserves	12,555	12,381
Other current liabilities	21,123	21,131
Total current liabilities	212,623	194,005
Long-term debt	119,884	148,068
Long-term capital leases and financing obligations	228,877	227,220
Accrued rent expense	4,116	4,530
Other long-term liabilities	12,919	14,141
Long-term income taxes payable	2,528	1,992
Total liabilities	580,947	589,956
Commitments and contingencies		
Shareholders' equity:		
Class C Convertible Preferred Stock, $1.50 par value, $.064 conversion value, 150,000 shares authorized; 21,802 shares issued and outstanding	33	33
Common Stock, $.01 par value, 65,000,000 shares authorized; 39,459,263 and 39,166,392 shares issued at December 29, 2018 and March 31, 2018, respectively	395	392
Treasury Stock, 6,359,871 and 6,330,008 shares at December 29, 2018 and March 31, 2018, respectively, at cost	(108,729)	(106,563)
Additional paid-in capital	216,809	199,576
Accumulated other comprehensive loss	(4,475)	(4,248)
Retained earnings	582,101	539,286
Total shareholders' equity	686,134	628,476
Total liabilities and shareholders' equity	$ 1,267,081	$ 1,218,432

The accompanying notes are an integral part of these financial statements.

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MONRO, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

	Quarter Ended Fiscal December		Nine Months Ended Fiscal December	
	2018	2017	2018	2017
	(Dollars in thousands, except per share data)			
Sales	$ 310,110	$ 285,730	$ 913,027	$ 842,237
Cost of sales, including distribution and occupancy costs	192,144	178,743	557,876	514,426
Gross profit	117,966	106,987	355,151	327,811
Operating, selling, general and administrative expenses	87,256	77,688	256,862	230,943
Operating income	30,710	29,299	98,289	96,868
Interest expense, net of interest income	6,797	6,138	20,180	17,997
Other income, net	(321)	(99)	(809)	(336)
Income before provision for income taxes	24,234	23,260	78,918	79,207
Provision for income taxes	3,703	11,659	15,982	32,755
Net income	20,531	11,601	62,936	46,452
Other comprehensive loss, net of tax:				
Changes in pension, net of tax benefit	(76)	(50)	(227)	(151)
Comprehensive income	$ 20,455	$ 11,551	$ 62,709	$ 46,301
Earnings per common share:				
Basic	$ .62	$ .35	$ 1.90	$ 1.41
Diluted	$ .61	$ .35	$ 1.87	$ 1.39
Weighted average number of common shares outstanding used in computing earnings per share:				
Basic	33,032	32,779	32,932	32,746
Diluted	33,766	33,352	33,605	33,317

The accompanying notes are an integral part of these financial statements.

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MONRO, INC.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(UNAUDITED)

(Dollars and shares in thousands)

	Class C Convertible Preferred Stock Shares	Amount	Common Stock Shares	Amount	Treasury Stock Shares	Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Retained Earnings
Balance at March 31, 2018	22	$ 33	39,166	$ 392	6,330	$ (106,563)	$ 199,576	$ (4,248)	$ 539,286
Net income									62,936
Other comprehensive loss:									
Pension liability adjustment ($302) pre-tax								(227)	
Cash dividends (1): Preferred									(306)
Common									(19,778)
Dividend payable									(37)
Activity related to equity-based plans			293	3	30	(2,166)	14,083		
Stock-based compensation							3,150		
Balance at December 29, 2018	22	$ 33	39,459	$ 395	6,360	$ (108,729)	$ 216,809	$ (4,475)	$ 582,101

(1) First, second and third quarter fiscal year 2019 dividend payment of $.20 per common share or common share equivalent paid on June 14, 2018, September 6, 2018 and December 21, 2018, respectively.

The accompanying notes are an integral part of these financial statements.

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MONRO, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Nine Months Ended Fiscal December	
	2018	2017
	(Dollars in thousands) Increase (Decrease) in Cash	
Cash flows from operating activities:		
Net income	$ 62,936	$ 46,452
Adjustments to reconcile net income to net cash provided by operating activities -		
Depreciation and amortization	41,035	36,477
Gain on bargain purchase	-	(13)
Gain on disposal of assets	(314)	(400)
Stock-based compensation expense	3,150	2,010
Net change in deferred income taxes	10,707	12,183
Change in operating assets and liabilities (excluding acquisitions):		
Trade receivables	(1,777)	(1,367)
Inventories	2,225	118
Other current assets	772	(6,390)
Other non-current assets	1	2,305
Trade payables	10,598	6,802
Accrued expenses	1,596	547
Federal and state income taxes payable	(1,091)	(1,445)
Other long-term liabilities	(1,767)	(780)
Long-term income taxes payable	536	610
Total adjustments	65,671	50,657
Net cash provided by operating activities	128,607	97,109
Cash flows from investing activities:		
Capital expenditures	(30,763)	(29,727)
Acquisitions, net of cash acquired	(46,052)	(16,363)
Proceeds from the disposal of assets	492	2,333
Other	281	-
Net cash used for investing activities	(76,042)	(43,757)
Cash flows from financing activities:		
Proceeds from borrowings	313,875	260,951
Principal payments on long-term debt, capital leases		

and financing obligations	(356,834)	(300,514)
Exercise of stock options	12,148	3,035
Dividends paid	(20,084)	(17,966)
Net cash used for financing activities	(50,895)	(54,494)
Increase (decrease) in cash	1,670	(1,142)
Cash at beginning of period	1,909	8,995
Cash at end of period	$ 3,579	$ 7,853

The accompanying notes are an integral part of these financial statements.

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MONRO, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1 – Condensed Consolidated Financial Statements

The consolidated balance sheets as of December 29, 2018 and March 31, 2018, the consolidated statements of comprehensive income for the quarters and nine months ended December 29, 2018 and December 23, 2017, the consolidated statement of changes in shareholders' equity for the nine months ended December 29, 2018 and the consolidated statements of cash flows for the nine months ended December 29, 2018 and December 23, 2017, include financial information for Monro, Inc. and its wholly-owned subsidiaries, Monro Service Corporation and Car-X, LLC (collectively, "Monro," "we," "us," "our," the "Company"). These unaudited, condensed consolidated financial statements hav been prepared by Monro. We believe all known adjustments (consisting of normal recurring accruals or adjustments) have been made to fairly state the financial position, results of operations and cash flows for the unaudited periods presented.

Interim results are not necessarily indicative of results for a full year. The year-end consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The information included in this Quarterly Report on Form 10-Q should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2018.

We report our results on a 52/53 week fiscal year with the fiscal year ending on the last Saturday in March of each year. The following are the dates represented by each fiscal period reported in these condensed financial statements:

"Quarter Ended Fiscal December 2018"	September 30, 2018 – December 29, 2018 (13 weeks)
"Quarter Ended Fiscal December 2017"	September 24, 2017 – December 23, 2017 (13 weeks)
"Nine Months Ended Fiscal December 2018"	April 1, 2018 – December 29, 2018 (39 weeks)
"Nine Months Ended Fiscal December 2017"	March 26, 2017 – December 23, 2017 (39 weeks)

Fiscal 2019, ending March 30, 2019, is a 52 week year.

Monro's operations are organized and managed in one operating segment. The internal management financial reporting that is the basis for evaluation in order to assess performance and allocate resources by our chief operating decision maker consists of consolidated data that includes the results of our retail, commercial and wholesale locations. As such, our one operating segment reflects how our operations are managed, how resources are allocated, how operating performance is evaluated by senior management and the structure of our internal financial reporting.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued new accounting guidance for the reporting of revenue from contracts with customers. This guidance provides guidelines a company will apply to determine the measurement of revenue and timing of when it is recognized. Additional guidance has subsequently been issued to amend or clarify the reporting of revenue from contracts with customers. The guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2017. Early adoption was permitted. We adopted this guidance and all related amendments during the first quarter of fiscal 2019 using the modified retrospective approach. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements. See Note 7 for additional information.

In February 2016, the FASB issued new accounting guidance related to leases. This guidance establishes a right of use ("ROU") model that requires a lessee to record a ROU asset and lease liability on the balance sheet for all leases with terms longer than twelve months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition. The guidance is effective for financial statements issued for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Additional guidance has subsequently been issued in order to provide an additional transition method as well as an additional practical expedient to be available upon adoption. We are required to adopt the new lease guidance utilizing one of two methods: retrospective restatement for each reporting period presented at time of adoption, or a modified retrospective approach with the cumulative effect of initially applying this guidance recognized at the date of initial application. Under the modified retrospective approach, prior periods would not be restated. Early adoption is permitted, but we have not early adopted this guidance. We expect to adopt using the modified retrospective approach and that the new lease standard will have a material impact on our Consolidated Financial Statements. While we are continuing to assess the effects of adoption, we currently believe the most significant changes relate to the recognition of new ROU assets and lease liabilities on the Consolidated Balance Sheet for operating leases as approximately 50% of our store leases, all of our land leases and all of our non-real estate leases are currently not recorded on our balance sheet. We expect that substantially all of our operating lease commitments will be subject to the new guidance and will be recognized as operating lease liabilities and ROU assets upon adoption. Absent potential acquisitions, we do not anticipate any significant changes in the volume of our leasing activity until the period of adoption.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

In August 2016, the FASB issued new accounting guidance related to cash flow classification. This guidance clarifies and provides specific guidance on eight cash flow classification issues that are not addressed by current generally accepted accounting principles and thereby reduce the current diversity in practice. This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2017. Early adoption was permitted. We adopted this guidance during the first quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In January 2017, the FASB issued new accounting guidance which clarifies the definition of a business, particularly when evaluating whether transactions should be accounted for as acquisitions or dispositions of assets or businesses. This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2017. Early adoption was permitted for certain transactions. We adopted this guidance during the first quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In January 2017, the FASB issued new accounting guidance simplifying the accounting for goodwill impairment by removing Step 2 of the goodwill impairment test, which required the determination of an implied fair value of goodwill. Under this guidance, an entity should perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value. This guidance is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019, and should be applied on a prospective basis. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. We adopted this guidance during the third quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In March 2017, the FASB issued accounting guidance that amends how employers present the net benefit cost in the income statement. The new guidance requires employers to disaggregate and present separately the current service cost component from the other components of the net benefit cost within the Consolidated Statement of Comprehensive Income. This guidance is effective for fiscal years and interim periods beginning after December 15, 2017, and should be applied retrospectively. Early adoption was permitted. We adopted this guidance during the first quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In May 2017, the FASB issued new accounting guidance which clarifies when to account for a change to the terms or conditions of a share based payment award as a modification. Under this guidance, modification is required only if the fair value, the vesting conditions, or the classification of an award as equity or liability changes as a result of the change in terms or conditions. This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2017. Early adoption was permitted. We adopted this guidance during the first quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

In June 2018, the FASB issued new accounting guidance that amends the accounting for nonemployee share-based awards. Under the new guidance, the existing guidance related to the accounting for employee share-based awards will apply to nonemployee share-based transactions, with certain exceptions. This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2018. Early adoption is permitted. We are currently evaluating the potential impact of the adoption of this guidance on our Consolidated Financial Statements.

In August 2018, the FASB issued new accounting guidance which eliminates, adds and modifies certain disclosure requirements for fair value measurements. This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2019. Early adoption is permitted. We are currently evaluating the potential impact of the adoption of this guidance on our Consolidated Financial Statements.

In August 2018, the FASB issued new accounting guidance that aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2019. Early adoption was permitted. We adopted this guidance during the third quarter of fiscal 2019. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

Other recent authoritative guidance issued by the FASB (including technical corrections to the Accounting Standards Codification) and the Securities and Exchange Commission did not, or are not expected to have a material effect on our Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Guarantees

At the time we issue a guarantee, we recognize an initial liability for the fair value, or market value, of the obligation we assume under that guarantee. Monro has guaranteed certain lease payments, primarily related to franchisees, amounting to $2.2 million. This amount represents the maximum potential amount of future payments under the guarantees as of December 29, 2018. The leases are guaranteed through April 2020. In the event of default by the franchise owner, Monro generally retains the right to assume the lease of the related store, enabling Monro to re-franchise the location or to operate that location as a Company-operated store. As of December 29, 2018, no liability related to anticipated defaults under the foregoing leases is recorded. We recorded a liability related to anticipated defaults under the foregoing leases of $.2 million as of March 31, 2018.

Note 2 – Acquisitions

Monro’s acquisitions are strategic moves in our plan to fill in and expand our presence in existing and contiguous markets, and leverage fixed operating costs such as distribution, advertising and administration. Acquisitions in this footnote include acquisitions of five or more locations as well as acquisitions of one to four locations that are part of our greenfield store growth strategy.

Subsequent Events

Subsequent to December 29, 2018, we signed definitive asset purchase agreements to complete the acquisition of 12 retail tire and automotive repair stores located in Louisiana. This transaction is expected to close during the fourth quarter of fiscal 2019 and is expected to be financed through our existing credit facility.

On January 13, 2019, we acquired 13 retail tire and automotive repair stores located in Florida from R.A. Johnson, Inc. These stores operate under The Tire Choice name. The acquisition was financed through our existing credit facility.

Fiscal 2019

During the first nine months of fiscal 2019, we acquired the following businesses for an aggregate purchase price of $45.4 million. The acquisitions were financed through our existing credit facility. The results of operations for these acquisitions are included in our financial results from the respective acquisition dates.

· On December 9, 2018, we acquired two retail tire and automotive repair stores located in Virginia from Colony Tire Corporation. These stores operate under the Mr. Tire name.

· On November 4, 2018, we acquired five retail tire and automotive repair stores located in Ohio from Jeff Pohlman Tire & Auto Service, Inc. These stores operate under the Car-X and Mr. Tire names.

· On October 14, 2018, we acquired one retail tire and automotive repair store located in Illinois from Quality Tire and Auto, Inc. This store operates under the Car-X name.

· On September 23, 2018, we acquired one retail tire and automotive repair store located in South Carolina from Walton's Automotive, LLC. This store operates under the Treadquarters name.

· On September 16, 2018, we acquired one retail tire and automotive repair store located in Illinois from C&R Auto Service, Inc. This store operates under the Car-X name.

· On September 9, 2018, we acquired four retail tire and automotive repair stores in Arkansas and Tennessee from Steele-Guiltner, Inc. These stores operate under the Car-X name.

· On July 15, 2018, we acquired one retail tire and automotive repair store located in Pennsylvania from Mayfair Tire & Service Center, Inc. This store operates under the Mr. Tire name.

· On July 8, 2018, we acquired eight retail tire and automotive repair stores in Missouri from Sawyer Tire, Inc. These stores operate under the Car-X name.

· On May 13, 2018, we acquired 12 retail/commercial tire and automotive repair stores and one retread facility located in Tennessee, as well as four wholesale locations in North Carolina, Tennessee and Virginia, from Free Service Tire Company, Incorporated. These locations operate under the Free Service Tire name.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

- On April 1, 2018, we acquired four retail tire and automotive repair stores located in Minnesota from Liberty Auto Group, Inc. These stores operate under the Car-X name.

These acquisitions resulted in goodwill related to, among other things, growth opportunities, synergies and economies of scale expected from combining these businesses with ours, as well as unidentifiable intangible assets. All of the goodwill is expected to be deductible for tax purposes. We have recorded finite-lived intangible assets at their estimated fair value related to customer lists, favorable leases and a trade name.

We expensed all costs related to acquisitions in the nine months ended December 29, 2018. The total costs related to completed acquisitions were $.1 million and $.4 million for the quarter and nine months ended December 29, 2018, respectively. These costs are included in the Consolidated Statements of Comprehensive Income primarily under operating, selling, general and administrative expenses.

Sales for the fiscal 2019 acquired entities for the quarter and nine months ended December 29, 2018 totaled $14.7 million and $33.4 million, respectively, for the period from acquisition date through December 29, 2018.

Supplemental pro forma information for the current or prior reporting periods has not been presented due to the impracticability of obtaining detailed, accurate or reliable data for the periods the acquired entities were not owned by Monro.

The preliminary fair values of identifiable assets acquired and liabilities assumed were based on preliminary valuations and estimates. The excess of the net purchase price over net identifiable assets acquired was recorded as goodwill. The preliminary allocation of the aggregate purchase price as of December 29, 2018 was as follows:

As of
Acquisition

	Date (Dollars in thousands)
Trade receivables	$ 1,674
Inventories	8,517
Other current assets	230
Property, plant and equipment	12,490
Intangible assets	7,646
Other non-current assets	17
Long-term deferred income tax assets	1,555
Total assets acquired	32,129
Warranty reserves	314
Other current liabilities	