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THE TAKE AWAY

MSOS ARE A SIGNIFICANT FORCE IN THE CONTRACTION, CONSOLIDATION AND CONVERGENCE IMPACTING THE PHYSICAL DAMAGE INDUSTRY.

MINDING YOUR BUSINESS



THE EVOLVING EVER MSO MARKET

EXPANSION AND CONSOLIDATION CONTINUE TO SPUR MULTI-SHOP OPERATOR GROWTH

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WE'VE BEEN researching, tracking, analyzing and interpreting data and trends involving the collision repair industry and multiple-location operators, MLOs or MSOs, since the first round of industry consolidation began during the late 1990s through about 2003. This first-round consolidation period saw MSO platform transactions with companies like ABRA, M2, CARA, Car Quarters (Sterling) and Caliber. This consolidation effort eventually lost its momentum for several reasons including:

- An overly-aggressive growth model based on acquisitions that were not properly integrated and a business model that could not be sustained,

- Insurers' less-than-enthusiastic adoption of the MSO model with its promised, but under-developed, operational and performance benefits, and

- Inadequate multi-location information, operations and management systems for an expanding and growing enterprise.

In our annual white paper, A Profile of the Evolving Collision Repair Marketplace, we identify and track the \$20 million or larger MSOs within the U.S. along with multiple-location network operators, also known as MLNs. These MLNs include four franchise and branded network organizations, CARSTAR, which strategically and operationally positions itself as an MSO; Maaco; ABRA (MSO and

U.S. Collision Repair Market Dollars in Millions

	<u>2011</u>	<u>2006</u>	<u>Change</u>
Total Collision Repair Locations	36,800	45,000	-8,200
Total Collision Repair Revenue	\$29,475	\$30,000	-525
Total Number of \$20M MLOs	65	57	8
<u>\$20M MLO Locations</u>			
Total MLO Locations	1,245	959	286
Total MLO Production Locations	1,125	898	227
% of MLO Production Locations to 36,800 Collision Repair Locations	3.1%	2.0%	1.1%
<u>MLO Revenue</u>			
Total \$20M MLO Revenue	\$3,951	\$2,728	\$1,283
\$20M MLO Share of Total Collision Repair Revenue	13.4%	9.1%	4.3%

franchise); and FIX Auto (franchise and branded network). The following charts show the growth that these larger MSOs and MLNs have experienced, along with their segment market share, from 2006 to 2011.

The number of MSO companies generating repair revenue \geq \$20 million annually from 2006 to 2011 grew from 57 to 65, representing approximately \$4 billion in annual revenue in 2011. The market share for these organizations relative to all collision repair industry revenue processed during that time grew from 9.1 percent to 13.4 percent. We estimate that 2012 revenue processed by the \$20 million or larger MSO s/MLOs will be about \$4.4 billion or approximately 15 percent of total annual collision repair industry revenue.

The second wave of collision repair industry consolidation started in 2010 and has picked up momentum in the last two years. Since 2010, we have seen the evolution of two primary MSO expansion strategies begin to reshape the collision repair industry. One strategy, focusing expansion within existing and/or contiguous markets, is being driven by regional MLOs/MSOs such as Collision-Max, Seidners and Car Care Collision Centers. Another strategy utilized by national MSO consolidators such as Boyd/Gerber, ABRA and Caliber, is centering expansion within existing markets coupled with leap-frogging to new markets using platform acquisitions to gain entry. With both strategies, single-location

“tuck ins” are utilized, in the form of single-location or smaller multiple location acquisitions, Brownfields and Greenfields, to fill in market gaps. Unlike the larger, national MSOs, there have been few regional MLOs/MSOs venturing into new markets. These expansion strategies will continue to influence the direction of consolidation and right-sizing within the collision repair industry, and will result in increased MLO market share in the U.S.

The chart below represents four primary MSO franchise and branded network organizations: CARSTAR, Maaco,

ABRA (franchise) and FIX Auto. These organizations have historically been viewed as franchise businesses. Some companies, such as CARSTAR, have positioned and branded their capabilities and value proposition as those of an MSO with geographic scale, a broad range of national, multi-regional and local market capabilities, centralized services, managed KPIs for enterprise performance for owner/operators who actively manage their collision repair businesses. When combined with the \geq \$20.0M MSOs and the franchise and branded networks, MLNs/MSOs represent about 18 percent of the annual repair revenue processed. As with independent and dealer MSOs, we expect this share to continue to grow throughout 2013.

Our early and preliminary numbers for 2013 are reflected in the following chart along with another important segment, those repairers processing \$10 million to \$20 million annually. The \$7.4 billion total for these three segments represents approximately 24 percent of the annual collision repair revenue processed for 2012, indicating a fragmented collision repair industry with much upside for further consolidation.

From 2010 to 2012, the merger and acquisition activity for single and multiple-location operators occurred primarily in 16 state markets, seven of which — Illinois, Colorado, Ohio,

U.S. Collision Repair Market - 2011 Including Franchise and Branded Network (FBN) Dollars in Millions

Total Collision Repair Locations	36,800
Total Collision Repair Revenue	\$29,475
<u>Production Locations</u>	
Total Franchise and Branded Networks	906
Total \$20M MLO Production Locations Including FBN	2,031
Share of \$20M MLO Production Locations, Including FBN, to 36,800 Collision Repair Locations	5.5%
<u>Revenue</u>	
Total Franchise and Branded Networks	\$1,342
Total \$20M MLO Including FBN	\$5,293
Share of \$20M MLO Including FBN to Total Collision Repair Revenue	18.0%

Maryland, North Carolina, Pennsylvania and Indiana — were associated with the largest single platform acquisitions by Boyd/Gerber involving True2Form in 2010 and Cars Collision in 2011. The following is a list of the announced MSO multiple-location platform acquisitions (two or more) occurring between 2010 and 2012.

MSO Multiple Platform Transactions 2010-2012 Boyd/Gerber

- True2Form, Cars Collision, Master Collision, Pearl Auto, Big Sky, Collision Works, Auto Crafters, Recovery Room

Service King

- B&B Collision, Alamo, Auto Body World, Collision Specialists, Wade, Express Auto Body, Auto Body America

Caliber

- 911 Collision, Crown Collision, 101 Collision, Hi Tech Collision

ABRA

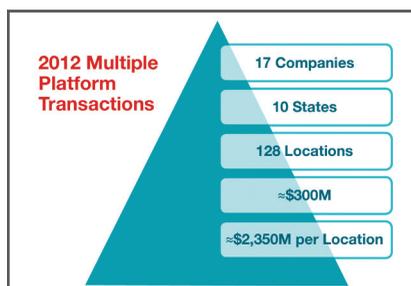
- Bradshaw, Collision Solutions, Collision Plus

Cooks Collision

- Holmes Auto Body

2012 Estimated Market Segments	Annual Revenue
≥ \$20.0 M MLO/MSO	\$4.4 B
Multiple Location Networks – MLN/MSO	\$1.5 B
\$10.0-\$20.0 M MLO/MSO	\$1.5 B
Total	\$7.4 B

In 2012, merger and acquisition activity for multiple-location platform transactions took place in 10 states, involving 17 independent collision repair organizations with 128 locations. These platform transactions shifted approximately \$300 million in revenue during 2012, an average revenue of \$2.35



MLO/MSO	AK	AZ	CA	CO	FL	GA	IN	IL	MA	MI	MD	MO	MS	NC	NM	NV	NY	OH	PA	TN	TX	WA	WI	TOTAL	
ABRA							4	3												5				12	
Boyd/Gerber				6	32																				38
Caliber			15																						15
CARSTAR			4		2	1		1		1							1	1				5	3	1	20
Cooks Collision			6																						6
Service King	3	11											2							15	7				35
Golden State Collision/Bodycraft				19																					19
TOTAL 2012	3	11	44	6	34	1	4	4	1	1	2	2	1	1	1	2	1	1	20	12	3	1	1	148	
Boyd/Gerber				6			8	14																	28
Caliber			5													2									7
CARSTAR									1		1			1				1				7	3		14
Service King																						13			13
TOTAL 2011	5	6	6	8	14	1	1	1	1	2	1	1	2	1	2	1	1	8	5	20	3	1	1	62	
The Boyd Group		4			2					7				17				8	5						43
CARSTAR	7				2	1					1									4	2	1	1		19
TOTAL 2010	7	4	2	3	7	1	7	1	17	8	5	4	2	1	1	10	5	24	34	7	2	1	1	62	
GRAND TOTAL	10	20	44	12	36	4	12	18	1	1	7	2	2	17	1	2	1	10	5	24	34	7	2	272	

million per location acquired. At this time, merger and acquisition activity remains noticeably absent in the upper northeast region, from New Jersey to Maine.

The chart at the top of the page reflects independent MSO multiple-location platform acquisitions and CARSTAR's multiple-location network MSO activities by state from 2010 through 2012.

The short-term profile for existing and emerging MSO models today includes the following:

- Independent, dealership and franchise multiple-region platform MSOs
- Multiple-region combined independent and franchise MSOs
- Large multiple-location, single-market independent and dealership MSOs

▪ Medium size multiple-location single market independent and dealership MSOs

The longer-term will eventually include some nationally recognized independent, franchise and hybrid MSOs.

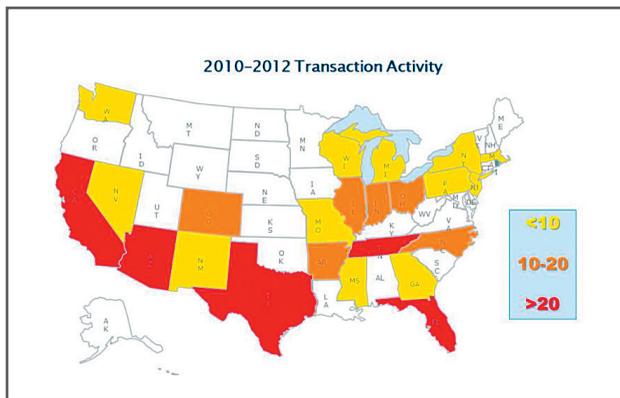
The map, "2010-2012 Transaction Activity," page 20, shows which states had the most independent MSO multiple-location platform merger and acquisition activity from 2010 through 2012.

Determining which companies will ultimately lead the collision repair industry is an evolution and part of a longer-term continuum involving four active and simultaneous industry-changing phases: contraction, consolidation, convergence, and constructive

transformation. The need for constructive transformation has become greater due to the acceleration of MSO platform acquisitions in 2010 through 2012, as well as the anticipated 2013 acquisition activity. Industry contraction and consolidation facilitates an environment where companies converge across both similar and different market segments through mergers and acquisitions. While there are many examples of this throughout all auto physical damage segments, it is especially prevalent with MSOs as seen in both the map and the merger and acquisition chart. Contraction, consolidation and convergence ultimately give way to the inevitable and required phase of constructive transformation.

Constructive transformation within the consolidating and converging collision repair industry involves the necessary heavy lifting associated with the integration of different organizations, business platforms and cultures. It involves determining the best suited or MSO-preferred estimating/management system, technology infrastructure, brand transition, personnel and organizational structure for the merged enterprise and its morphing culture, while simultaneously managing its growth and expansion.

Absent this integration transition phase of construction transformation, MSOs run the high risk of failing to assimilate the acquired companies. This



failure is manifested through poor operational performance, lower customer satisfaction and the under achieving of KPIs that eventually provide lower competitive peer rankings related to insurance company DRPs. An unintended consequence would be a reduction in wholesale business, which is the lifeblood of an MSO's planned revenue and market share position.

When properly executed, constructive transformation delivers both the plan and the promise for MSOs that aggregating capacity can bring accretive financial and operational value, market share dominance and higher business valuation. It also allows the MSO to consistently deliver sustained performance and output, reflecting an increasing benchmark of competitiveness that the MSO leverages for its own advantage. During constructive transformation, MSOs lead and manage with a strategic mindset that embraces both the opportunity and risk associated with new market entrance and expansion while leveraging market uncertainty and ambiguity to their advantage, rather than avoiding it.

In today's competitive and dynamic market, MSOs know that they should not just go it alone. It is important to leverage a strategic partner and alliance ecosystem, which includes a broad number of constituent groups including strong and loyal customers, supportive and flexible suppliers, competitors (frienemies) for benchmarking progress, investors, and business partners. These entities become an integral part of the collaborative brain trust where there is a shared commitment to co-create and change the orga-

nization and its dynamic environment for their individual and mutual benefit. It is through this constructive transformation that successful MSOs will secure their future.

We expect that, as a result of a number of industry-specific and macro-economic conditions, the collision repair landscape will

continue to evolve. This evolution will likely cause a continuation of collision repairers to exit the business or become MSO merger and acquisition targets. Some of the prevailing conditions that support this industry evolution include:

- Continued contraction, consolidation, convergence and constructive transformation of all auto physical damage segments associated with the collision repair industry

- A lackluster economy with uneven and slow growth, prompting repairers to consider exit or strategic alliance options that include being acquired or joining a franchise MSO or branded network

- Globalization and U.S. market entry of foreign companies in the collision repair, property and casualty insurance, and numerous auto physical damage industries, creating both horizontal and vertical channels of distribution influence and disintermediation within the collision repair and property and casualty insurance industries

- Private equity interest and focus on increased investments in MSOs and various auto physical damage segments

- Insurance company strategies related to cost reduction and the adoption of fewer points of contact with a limited number of multiple-location operators. MLOs and MSOs are more aligned during this consolidation phase than in the past.

- The benefits of insurer DRPs and hybrid model DRPs have been accepted and adopted by the once reluctant and uncertain insurance companies

- The insurance company DRP claim-conversion percentage continues to increase, producing a larger volume of business for the emerging end-game MSO winners under contract

- Key performance indicators and peer rankings, coupled with MSO wide-area networks, are becoming the de facto standard used to drive DRP claims utilization and preference for top-tier MSOs

- Innovation and risk-taking by MSOs, prompting a move toward a co-managed or self-managed vehicle repair model, will require more people and infrastructure, with the expected outcome of less insurance company oversight, involvement and disintermediation

- Fluctuating and conflicting market trends are reflected in higher gas prices, fewer miles driven, diminished interest on the part of younger drivers to obtain their driver's license, broader adoption of accident avoidance systems, nascent car sharing models, and numerous other trends are influencing lower accident frequency and eventually fewer repairable claims in the longer term

- Acceleration of aggressive repairer multi-level selling, marketing and branding of their competitive value propositions and performance to current and prospective wholesale and consumer segments

- Development, marketing and implementation of new, innovative services by MSOs as a competitive advantage that others will not have the ability or the inclination to pursue

- Lean production and its business benefits leading to a competitive advantage and long-term business sustainability for some MSOs

- Hybrid claims management and process models that not all repairers are willing or able to accept, adopt or maintain

- Increased technology requirements, with the associated integration and adoption, and its effect on the evolution and movement toward an integrated electronic claims processing model

By themselves, any one or just a few of these prevailing conditions together would have limited impact on MSOs or the collision repair industry. However, all of these conditions are simultaneously in play at some level. As they continue to vertically and horizontally intersect each other, their impact will accelerate the business, market, financial and strategic decisions that drive the future direction of not only MSOs, but all constituent groups in the auto physical damage landscape. ■