

Consolidation and MSO Growth

You reported that 2014 was a record year for Mergers and Acquisitions (M & A) as the trend is expected to continue, what challenges do you see MSOs experiencing with their record growth?

- Based on MLO-Platform transactions there was \$1.0 B in revenue processed that was acquired in 2014 and 1.6B when 2012 & 2013 are combined with 2014. Does not include single acqs. Brownfields and Greenfields.
- Current YTD 2015 MLO platform acqs. At \$250 M....so close to \$2B in <3.5 yrs. Or about 6.5% of what I call the addressable market size that has fluctuated between \$30 B and \$32 B.
- About \$3 B invested by Private Equity during this time
- One of the 4 independent consolidators intends to expand by about 130 units at \$4.3 M average revenue/location or \$559 M.
- MSO challenges:
 - Constructive Transformation or the inevitable heavy lifting associated with integrating newly acquired multiple repair units simultaneously and how quickly they can adapt and can be assimilated into the acquiring MSO's culture and larger organization structure. The challenge is to do this while performing consistently and systematically to operational, financial, marketing and other functional business area processes.
 - Recruiting, developing, nurturing and retaining employees while providing sustainable competitive jobs or in the case of upwardly mobile employees a career path environment with greater responsibility, pay and opportunity.
 - The ability to consistently and effectively manage a concentrated group of insurer customers and their various DRPs requirements over their large scale repair center network metrics while maintaining high performance results and best in class competitive rankings throughout the Enterprise.

- Sustaining the aggressive expansion and market share growth that was built primarily over the last 3 to 5 years through larger MSO platform transactions. There are still some 200 \$10 M and above annual revenue operators but the pool that are interested in selling at multiples that the MSOs are willing to give is shrinking.

Technology

As consolidation continues, will you share any key trends that have changed how MSOs are managing their technology differently today?

- Their size and scale allows them to centrally purchase, manage, test and implement software, hardware and other innovative technology providing them economies of scale as the roll out and implement their technology across their broad multi-regional network of repair centers.
- Not just a department.....it's an IT group and its capabilities become a strategic advantage when working with suppliers, insurance company customers and other strategic partners
- A strong in house and experienced IT organization allows the MSO to better control their technology destiny while operating more efficiently and effectively than some of their competitors.
- MSOs are able to build centralized databases that produce data rich reports and analytics that help them manage the Enterprise while comparing and contrasting multiregional markets and individual repair centers on a competitive performance basis. Use results to sell/market their enterprise value propositions
- They have developed and implemented call center capabilities that allow them to partner with insurance clients where they can provide a broad range of services or other capabilities including but not limited to FNOL, third party warm transfers between insurers and insureds, glass management. Additionally, they work with strategic partners to provide electronic auditing, centralized repair appointments and management of capacity utilization across broad local and broad market area.

- Technology coupled with an operational integration process model allows for faster and more effective assimilation of new or acquired repair centers.
- Most recently, there is a market example where technology played a significant part in a decision where one of the four independent MSO consolidators was awarded best supplier of the year by USAA across all supplier business segments and not just collision repair.

PARTS PROCUREMENT: REPAIR VS. REPLACE

What procurement/product strategies and processes do you believe our industry needs to focus on and what is changing in the way parts are acquired?

- There still are too many disparate parts companies, by my estimate up to 20 in the US, that are competing for mind and market share within the collision repair industry. I foresee that the number of providers will consolidate in the next 3 to 5 years.
- Parts continue to be primarily focused and purchased on a local market basis instead of a centralized basis.
- Surprisingly, parts procurement is still being done how some might affectingly say is the “traditional way” using phone, email and fax coupled with excessive back and forth communication among repairers, parts suppliers and insurers.
- Today’s collision repair culture needs to focus on electronic procurement involving technology and software that will improve the parts procurement process.
- Parts procurement programs need to integrate with other aspects of the market participant’s work flow. Stand-alone applications over the long term do not add as much value. Integration should be seen as an opportunity to ease a repairer’s/supplier’s pain, not an opportunity to hold those same businesses hostage.
- The industry should be working with companies that attempt on a large scale enterprise basis to bring technology and software which continues to

evolve and move the industry from the traditional phone, fax and email to a more electronify process

- Parts procurement, like all aspects of business, is changing from a 'who do you know?' decision making process, to a performance-based, KPI focused decision making process.
- Larger MSOs are able to develop corporate national programs that provide more significant buyer discounts and economies of scale that benefit the enterprise more so than smaller MSOs and single shop operators. This ultimately becomes a strategic advantage for the MSOs
- Most repairers, including all size MSOs, are still dealt with the same way, instead of customizing parts procurement and distribution based on the profile and needs of the various size MSOs.

CURRENT IMPACTS IN COLLISION REPAIR

Human Resources are a topic that has been a constraint within our industry for quite some time. What are MSOs doing in order to attract and retain employees?

- It starts with executive leadership and/or ownership at the top where it is strategically important. Focus on recruiting, developing, and retaining employees. Providing sustainable competitive jobs, highly visible employee development programs and in the case of upwardly mobile employees, a career path environment with opportunities to be promoted from within the company.
- Creating and identifying a pool of local market, regional and national market prospects identified across a broad spectrum of talent buckets. The senior HR officer or in some cases Chief Talent Officer is working with management at all levels to continually develop those identified as long term keepers who have the ability to be cross trained and want to be considered for jobs outside the current location and might consider moving to other markets.

- Of course, working closely with trade voc-tech schools on a local market basis.
- The military has been and will continue to downsize and this offers large pool of potential technical, administrative and managerial candidates. As you may know, many constituents including a number of MSOs from across our auto physical damage ecosystem have been in long term planning and recent implementation of a two year collision repair school, Fayetteville, NC that draws military personnel from Fort Bragg, North Carolina The school is funded by private and federal government dollars and has the military's backing. Additionally, some companies are currently working with the military at Fort Hood, TX for another pool of candidates. All military locations around the country can offer a source of employee talent.
- BTW, an example of how much of a constraint this area is, one large MSO is short 100 technicians, which by their calculation costs them \$6.0M a month or \$72.0M a year.
- MSOs are going outside the industry.....target the type of person that has no industry experience but can be trained and developed under a formal or informal training program for technicians, administrative and management staff.

CLAIMS PROCESSING

What Impact has the consolidation of MSO's/MLO's had on claims processing

- MSOs are being asked and mostly willing to continue taking over more of what traditionally has been the insurers' role and responsibilities in claims processing. MSO's are willing to test and implement new and hybrid claims management tools and models. The insurers are also open and willing to test these models with them too.
 - self-managed, concierge, SPP DRP programs under SLAs
 - warehousing and building up a sizeable inventory of frequently used parts

- vehicle repair appointment setting through a transparent view of all locations for better capacity management, utilization and customer experience
- expedited/fast lane repair, repair segmentation
- total loss disposition programs
- A number of claims process advantages have been realized through the MSO relationship
 - Increase DRP penetration across multiple markets served. DRP national DRP penetration is currently approximately 55% and expected to grow to between 65% 75% in the next five years
 - Lower severity expense, approximately 8 to 12% lower
 - The Strategic Preferred Programs (SPPs) have added an additional 3 to 5% savings from unallocated LAE
 - Decreases complexity of managing relationships across multiple markets Single point of contact
 - Improved process and metrics including higher touch time, lower cycle time and LOR, competitive peer group operational performance reporting(KPI)
 - Close alignment with information providers' leveraging their software and technology in conjunction with some insurers' and MSOs requirements and requests. A close working relationship among all three. They are teaming up for success and working on common solutions that benefit all of them.

EDUCATION AND WORKFORCE DEVELOPMENT

What are other MSOs doing to meet their staffing needs with their growth?

- One mid-tier MSO starts as a company that it's viewed as employer of choice in the market. Employer of choice is based on a broad range of market activities and behavior, management/owner leadership, brand reputation and awareness as well as market perception and the positive

voice and recommendations of current and past employees as well as a competitive compensation package

- CROP-Collision Repair Opportunity Program
 - Missionary feet on the street marketing and collaboration with local area high schools to create awareness of the job opportunities for 12 grade level students
 - Once the prospects are identified, then there is a 3 month unpaid internship, 20 hours weekly, designated mentors throughout the internship periods with written and hands on testing. Then a 6 month paid probationary period before full time employment is offered.
- Develop your own internal apprentice development program for all levels starting with technicians
- Vote for tax proposals that offer tax credits for every apprentice trained by your business.

LOR, METRICS AND IMPORTANCE OF DATA

- LOR is extremely important to all parties and has become the defacto, if not one of the key metrics for managing the success of the claims process. LOR equates to about \$35 per claim each per savings for an insurance company, so it's easy to see how quickly savings or expense can add up when length of rental increases or decreases.
- Understanding one's mix of vehicles is very important in managing LOR. How to process efficiently the different mix of vehicles, for example: small hit/express repair vs. mid-size or heavy damage plays a crucial role in impacting what one might call yield management or throughput.
- Managing a repair center's WIP is also important. The traditional belief that success for a shop is a function of having a lot of WIP in the yard or shop has morphed to a much more enlightened view of managing WIP based on your mix of vehicles, while taking into consideration other operational constraints; e.g. staffing, weather conditions, a high frequency event like hail, customer priority, etc.

- Modulating the flow of vehicles through the repair center by optimizing and effectively allocating customer appointments, as part of a maximize capacity utilization culture, produces a better LOR and a higher degree of success. Getting the right car to the right place at the right time should be a shop and organizations' mantra.

Given your perspectives on the key trends and current business drivers, what is the one our repairers should focus on to remain competitive in their market?

- Strategic partnering.....Teaming for success.
- Going it alone as an island among countries or solely as an independent business operator is today much less than an optimal model.
 - Better to leverage partners to assist you in gaining insight, knowledge and market specific partner competencies to better insure a competitive edge