

MONRO MUFFLER BRAKE INC

Form 10-Q

October 29, 2010

[Table of Contents](#)

## FORM 10-Q

### SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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

For the quarterly period ended September 25, 2010.

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 No. 0-19357

## MONRO MUFFLER BRAKE, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification #)

200 Holleder Parkway, Rochester, New York  
(Address of principal executive offices)

14615  
(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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files).  Yes  No

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
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 October 23, 2010, 20,135,419 shares of the Registrant's Common Stock, par value \$.01 per share, were outstanding.

**Table of Contents**

MONRO MUFFLER BRAKE, INC.

INDEX

	Page No.
Part I. Financial Information	
Item 1. Financial Statements	
<u>Consolidated Balance Sheets at September 25, 2010 and March 27, 2010</u>	3
<u>Consolidated Statements of Income for the quarters and six months ended September 25, 2010 and September 26, 2009</u>	4
<u>Consolidated Statement of Changes in Shareholders' Equity for the six months ended September 25, 2010</u>	5
<u>Consolidated Statements of Cash Flows for the six months ended September 25, 2010 and September 26, 2009</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	12
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	16
Item 4. <u>Controls and Procedures</u>	16
Part II. Other Information	
Item 1. <u>Legal Proceedings</u>	17
Item 1A. <u>Risk Factors</u>	17
Item 4. <u>Removed and Reserved</u>	17
Item 6. <u>Exhibits</u>	17
<u>Signatures</u>	18
<u>Exhibit Index</u>	19

**Table of Contents**

## MONRO MUFFLER BRAKE, INC.

## PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

## MONRO MUFFLER BRAKE, INC.

## CONSOLIDATED BALANCE SHEETS

	(Unaudited) September 25, 2010	March 27, 2010
	(Dollars in thousands)	
<b>Assets</b>		
Current assets:		
Cash and equivalents	\$ 4,346	\$ 11,180
Trade receivables	1,991	1,922
Inventories	95,526	85,817
Deferred income tax asset	8,812	7,800
Other current assets	19,258	17,373
Total current assets	129,933	124,092
Property, plant and equipment	390,621	386,238
Less Accumulated depreciation and amortization	(191,126)	(183,492)
Net property, plant and equipment	199,495	202,746
Goodwill	96,632	90,372
Intangible assets	13,498	13,888
Other non-current assets	11,479	13,045
Total assets	\$ 451,037	\$ 444,143
<b>Liabilities and Shareholders Equity</b>		
Current liabilities:		
Current portion of long-term debt	\$ 3,144	\$ 2,933
Trade payables	47,632	43,229
Federal and state income taxes payable	4,230	4,169
Accrued payroll, payroll taxes and other payroll benefits	13,429	16,730
Accrued insurance	15,758	15,595
Warranty reserves	5,978	5,510
Other current liabilities	10,143	11,211
Total current liabilities	100,314	99,377
Long-term debt	72,529	96,427
Accrued rent expense	6,568	6,473
Other long-term liabilities	4,629	4,551
Deferred income tax liability	760	560
Long-term income taxes payable	4,410	4,085

Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

Total liabilities	189,210	211,473
Commitments		
Shareholders' equity:		
Class C Convertible Preferred Stock, \$1.50 par value, \$.096 conversion value, 150,000 shares authorized; 32,500 shares issued and outstanding	49	49
Common Stock, \$.01 par value, 45,000,000 shares authorized; 23,811,317 and 23,646,460 shares issued at September 25, 2010 and March 27, 2010, respectively	238	236
Treasury Stock, 3,685,734, and 3,682,429 shares at September 25, 2010 and March 27, 2010, respectively, at cost	(70,719)	(70,590)
Additional paid-in capital	94,640	88,377
Accumulated other comprehensive loss	(2,047)	(2,237)
Retained earnings	239,666	216,835
Total shareholders' equity	261,827	232,670
Total liabilities and shareholders' equity	\$ 451,037	\$ 444,143

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

**Table of Contents****MONRO MUFFLER BRAKE, INC.****CONSOLIDATED STATEMENTS OF INCOME**

(UNAUDITED)

	Quarter Ended		Six Months Ended	
	Fiscal September 2010	2009	Fiscal September 2010	2009
	(Dollars in thousands, except per share data)			
Sales	\$ 162,102	\$ 136,634	\$ 320,341	\$ 264,679
Cost of sales, including distribution and occupancy costs	95,736	77,781	187,976	149,417
Gross profit	66,366	58,853	132,365	115,262
Operating, selling, general and administrative expenses	43,138	41,148	86,199	80,306
Intangible amortization	296	198	591	331
Loss (gain) on disposal of assets	231	(20)	250	119
Total operating expenses	43,665	41,326	87,040	80,756
Operating income	22,701	17,527	45,325	34,506
Interest expense, net of interest income for the quarter of \$20 in 2010 and \$16 in 2009, and year-to-date of \$31 in 2010 and \$29 in 2009	1,208	1,442	2,679	3,338
Other income, net	(73)	(75)	(140)	(117)
Income before provision for income taxes	21,566	16,160	42,786	31,285
Provision for income taxes	8,242	6,158	16,251	11,872
Net income	\$ 13,324	\$ 10,002	\$ 26,535	\$ 19,413
Earnings per share:				
Basic	\$ .66	\$ .51	\$ 1.33	\$ .99
Diluted	\$ .63	\$ .49	\$ 1.26	\$ .95

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

**Table of Contents****MONRO MUFFLER BRAKE, INC.****CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

(UNAUDITED)

(Dollars in thousands)

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Loss (3)	Retained Earnings	Total
Balance at March 27, 2010	\$ 49	\$ 236	\$ (70,590)	\$ 88,377	\$ (2,237)	\$ 216,835	\$ 232,670
Net income						26,535	26,535
Other comprehensive loss:							
Unrealized gain on derivatives contracts (\$307 pre-tax)					190		190
							26,725
Cash dividends: Preferred (\$.18 per CSE) <sup>(1) (2)</sup>						(91)	(91)
Common (\$.18 per share) <sup>(2)</sup>						(3,613)	(3,613)
Tax benefit from exercise of stock options				2,106			2,106
Exercise of stock options		2	(129)	2,597			2,470
Stock option compensation				1,560			1,560
Balance at September 25, 2010	\$ 49	\$ 238	\$ (70,719)	\$ 94,640	\$ (2,047)	\$ 239,666	\$ 261,827

(1) CSE Common stock equivalent

(2) Includes first and second quarter fiscal 2011 dividend payments of \$.09 per CSE paid on both June 18, 2010 and September 17, 2010.

(3) The balance related to the derivative contracts was \$(190) at March 27, 2010. There was no amount related to the derivative contracts at September 25, 2010. The balance related to the pension liability was \$(2,047) at both September 25, 2010 and March 27, 2010.

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

**Table of Contents****MONRO MUFFLER BRAKE, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(UNAUDITED)

	<b>Six Months Ended Fiscal September</b>	
	<b>2010</b>	<b>2009</b>
	<b>(Dollars in thousands)</b>	
	<b>Increase (Decrease) in Cash</b>	
<b>Cash flows from operating activities:</b>		
Net income	\$ 26,535	\$ 19,413
<b>Adjustments to reconcile net income to net cash provided by operating activities -</b>		
Depreciation and amortization	11,053	10,610
Loss on disposal of property, plant and equipment	250	119
Stock-based compensation expense	1,560	1,184
Excess tax benefits from share-based payment arrangements	(2,289)	(1,020)
Net change in deferred income taxes	(930)	105
Decrease (increase) in trade receivables	331	(252)
Increase in inventories	(9,511)	(4,332)
Increase in other current assets	(2,047)	(1,825)
Decrease in other non-current assets	1,027	870
Decrease in intangible assets	191	332
Increase in trade payables	4,325	2,721
Decrease in accrued expenses	(3,892)	(841)
Increase in federal and state income taxes payable	2,167	8,117
Increase in other long-term liabilities	197	37
Increase in long-term income taxes payable	325	228
<b>Total adjustments</b>	<b>2,757</b>	<b>16,053</b>
<b>Net cash provided by operating activities</b>	<b>29,292</b>	<b>35,466</b>
<b>Cash flows from investing activities:</b>		
Capital expenditures	(6,600)	(8,223)
Acquisitions, net of cash acquired	(7,106)	
Acquisition of Midwest Tire, net of cash acquired		(1,959)
Acquisition of Autotire, net of cash acquired		(7,348)
Proceeds from the disposal of property, plant and equipment	98	464
<b>Net cash used for investing activities</b>	<b>(13,608)</b>	<b>(17,066)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from borrowings	88,321	65,251
Principal payments on long-term debt and capital lease obligations	(111,894)	(82,414)
Exercise of stock options	2,470	2,711
Excess tax benefits from share-based payment arrangements	2,289	1,020
Dividends to shareholders	(3,704)	(4,006)



Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

Net cash used for financing activities	(22,518)	(17,438)
(Decrease) increase in cash	(6,834)	962
Cash at beginning of period	11,180	3,336
Cash at end of period	\$ 4,346	\$ 4,298

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

**Table of Contents**

MONRO MUFFLER BRAKE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Condensed Consolidated Financial Statements

The consolidated balance sheets as of September 25, 2010 and March 27, 2010, the consolidated statements of income for the quarters and six months ended September 25, 2010 and September 26, 2009, the consolidated statements of cash flows for the six months ended September 25, 2010 and September 26, 2009, and the consolidated statement of changes in shareholders' equity for the six months ended September 25, 2010, include Monro Muffler Brake, Inc. and its wholly owned subsidiary, Monro Service Corporation (the Company). These unaudited condensed consolidated financial statements have been prepared by the Company. In the opinion of management, all known adjustments (consisting of normal recurring accruals or adjustments) have been made to present fairly the financial position, results of operations and cash flows for the unaudited periods presented.

Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended March 27, 2010. The results of operations for the interim periods being reported on herein are not necessarily indicative of the operating results for the full year.

The Company reports its 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 September 2010 :	June 27, 2010	September 25, 2010 (13 weeks)
Quarter Ended Fiscal September 2009 :	June 28, 2009	September 26, 2009 (13 weeks)
Six Months Ended Fiscal September 2010 :	March 28, 2010	September 25, 2010 (26 weeks)
Six Months Ended Fiscal September 2009 :	March 29, 2009	September 26, 2009 (26 weeks)

During the fourth quarter of fiscal 2010, the Company substantially completed the purchase price allocation for the fiscal year 2010 acquisitions. Some of the amounts previously estimated changed during the measurement period. The significant changes in estimates included an increase in deferred income tax assets of \$1.1 million for the second quarter; an increase in property, plant and equipment of \$2.0 million and \$2.5 million for the first and second quarters, respectively; an increase in intangible assets of \$1.1 million and \$1.7 million for the first and second quarters, respectively; and an increase in long-term debt of \$3.9 million and \$4.6 million for the first and second quarters, respectively. The measurement period adjustments represent updates made to the purchase price allocation based on revisions to valuation estimates in quarters subsequent to the quarter of acquisition and initial accounting. There were no significant adjustments to the Company's Consolidated Statement of Income.

Note 2 Acquisitions

The Company's acquisitions are strategic moves in its plan to fill in and expand its presence in its existing and contiguous markets, and leverage fixed operating costs such as distribution and advertising.

In the first quarter of fiscal 2011, the Company added seven retail tire and automotive repair stores located in Pennsylvania and Maine through two acquisition transactions. Collectively, these stores produced approximately \$11.3 million in sales annually based on unaudited pre-acquisition historical information. The total purchase price of these stores was approximately \$7.1 million in cash and the assumption of certain liabilities. The acquisitions were financed through the Company's existing bank facility. The results of operations of these acquired stores are included in the Company's results from their respective acquisition dates.

The Company has recorded its initial accounting for these acquisitions in accordance with accounting guidance on business combinations. The acquisitions resulted in goodwill related to, among other things, growth opportunities and unidentified intangible assets. All of the goodwill is expected to be deductible for tax purposes.

## Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

The Company has recorded finite-lived intangible assets at their determined fair value related to customer relationships. However, the Company has not completed its final purchase price accounting of these acquisitions due to the timing of the acquisitions. As the Company completes its final accounting for these acquisitions, there may be changes, some of which may be material, to this initial accounting.

**Table of Contents**

## MONRO MUFFLER BRAKE, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In accordance with accounting guidance on business combinations, the Company expensed all costs related to these acquisitions in the first quarter of fiscal 2011. The total costs related to these acquisitions were not material to the Consolidated Statement of Income. These costs are included in the Consolidated Statement of Income under operating, selling, general and administrative expenses.

The purchase price of the acquisitions have been preliminarily allocated to the net tangible and intangible assets acquired, with the remainder recorded as goodwill on the basis of estimated fair values, as follows:

	As of September 25, 2010 (Dollars in thousands)	
Other current assets	\$	599
Intangible assets		393
Other non-current assets		209
Current liabilities		(362)
<b>Total net identifiable assets acquired</b>	<b>\$</b>	<b>839</b>
Total consideration transferred	\$	7,107
Less: total net identifiable assets acquired		839
Goodwill	\$	6,268

Intangible assets consist of customer lists which are being amortized over their estimated useful life of ten years.

**Note 3 Earnings Per Share**

Basic earnings per common share (EPS) amounts are computed by dividing earnings after the deduction of preferred stock dividends by the average number of common shares outstanding. Diluted EPS amounts assume the issuance of common stock for all potentially dilutive equivalents outstanding.

The following is a reconciliation of basic and diluted EPS for the respective periods:

	Quarter Ended Fiscal September		Six Months Ended Fiscal September	
	2010	2009	2010	2009
	(Dollars in thousands, except per share data)			
<b>Numerator for earnings per common share calculation:</b>				
Net income	\$ 13,324	\$ 10,002	\$ 26,535	\$ 19,413
Less: Preferred stock dividends	45	35	91	102
<b>Income available to common stockholders</b>	<b>\$ 13,279</b>	<b>\$ 9,967</b>	<b>\$ 26,444</b>	<b>\$ 19,311</b>
<b>Denominator for earnings per common share calculation:</b>				

Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

Weighted average common shares, basic	20,083	19,568	19,937	19,504
Effect of dilutive securities:				
Preferred stock	507	507	507	507
Stock options	554	471	550	476
Weighted average number of common shares, diluted	21,144	20,546	20,994	20,487
<b>Basic earnings per common share:</b>	<b>\$ .66</b>	<b>\$ .51</b>	<b>\$ 1.33</b>	<b>\$ .99</b>
<b>Diluted earnings per common share:</b>	<b>\$ .63</b>	<b>\$ .49</b>	<b>\$ 1.26</b>	<b>\$ .95</b>

**Table of Contents**

## MONRO MUFFLER BRAKE, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENT

The computation of diluted EPS excludes the effect of the assumed exercise of approximately 180,000 and 181,000 stock options respectively, for the three and six months ended September 25, 2010, and 120,000 and 171,000 stock options respectively, for the three and six months ended September 26, 2009. Such amounts were excluded as the exercise prices of these options were greater than the average market value of the Company's common stock for those periods, resulting in an anti-dilutive effect on diluted EPS.

**Note 4 Income Taxes**

In the normal course of business, the Company provides for uncertain tax positions and the related interest and penalties, and adjusts its unrecognized tax benefits and accrued interest and penalties accordingly. The total amount of unrecognized tax benefits were \$5.9 million and \$5.6 million, respectively at September 25, 2010 and March 27, 2010, the majority of which, if recognized, would affect the effective tax rate. As of September 25, 2010, the Company had approximately \$.6 million of interest and penalties accrued related to unrecognized tax benefits.

The Company is currently under audit by certain state tax jurisdictions for the fiscal 2001 to 2009 tax years. It is reasonably possible that the examination phase of the audit for these years may conclude in the next 12 months, and that the related unrecognized tax benefits for tax positions taken regarding previously filed tax returns may change from those recorded as liabilities for uncertain tax positions in the Company's financial statements as of September 25, 2010. However, based on the status of the examinations, it is not possible to estimate the effect of any amount of such change to previously recorded uncertain tax positions.

The Company files U.S. federal income tax returns and income tax returns in various state jurisdictions. The Company's fiscal 2007 and fiscal 2009 U.S. federal tax years and various state tax years remain subject to income tax examinations by tax authorities.

**Note 5 Derivative Financial Instruments**

The Company reports derivatives and hedging activities in accordance with accounting guidance on disclosures about derivative instruments and hedging activities. This statement requires that all derivative instruments be recorded on the balance sheet at fair value. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether the derivative is designated as part of a hedge transaction, and if it is, depending on the type of hedge transaction.

At March 27, 2010, the notional amount of derivative financial instruments, which consisted solely of three interest rate swaps used to minimize the risk and/or costs associated with changes in interest rates, was \$30.0 million. These swaps matured in July 2010.

The effect of derivative financial instruments in cash flow hedge relationships on the financial statements for the three months ended September 25, 2010 and September 26, 2009 were as follows:

Derivatives in Cash	Amount of Gain or (Loss)		Location of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)	Amount of Gain or (Loss)	
	Recognized in Other Comprehensive Income on Derivatives (Effective Portion)			Reclassified From Other Comprehensive Income into Income (Effective Portion)	
Flow Hedging Relationships	2011	2010	(Effective Portion)	2011	2010
	(Dollars in thousands)		(Effective Portion)	(Dollars in thousands)	
Interest rate contracts	\$ 47	\$ 84	Interest income (expense)	\$ (38)	\$ (228)



**Table of Contents**

## MONRO MUFFLER BRAKE, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENT

The effect of derivative financial instruments in cash flow hedge relationships on the financial statements for the six months ended September 25, 2010 and September 26, 2009 were as follows:

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in Other Comprehensive Income on Derivatives (Effective Portion) 2011      2010 (Dollars in thousands)		Location of Gain or (Loss) Reclassified from Accumulated Other Comprehensive Income into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified From Other Comprehensive Income into Income (Effective Portion) 2011      2010 (Dollars in thousands)	
	2011	2010		2011	2010
Interest rate contracts	\$ 190	\$ 181	Interest income (expense)	\$ (268)	\$ (443)

**Note 6 – Supplemental Disclosure of Cash Flow Information**

The following transactions represent non-cash investing and financing activities during the periods indicated:

**SIX MONTHS ENDED SEPTEMBER 25, 2010:**

In connection with the fiscal 2011 acquisitions (Note 2), liabilities were assumed as follows:

Fair value of assets acquired	\$ 1,200,000
Goodwill acquired	6,268,000
Cash paid, net of cash acquired	(7,106,000)
Fair value of liabilities assumed	\$ 362,000

In connection with the accounting for income tax benefits related to the exercise of stock options, the Company decreased current liabilities and increased paid-in capital by \$2,106,000.

In connection with the acquisition of a store property, the Company increased fixed assets by \$700,000 and decreased other current assets and other non-current assets by \$161,000 and \$539,000, respectively.

**SIX MONTHS ENDED SEPTEMBER 26, 2009:**

In connection with the fiscal 2010 acquisitions, liabilities were assumed as follows:



## Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

Fair value of assets acquired	\$ 6,818,000
Goodwill acquired	5,543,000
Cash paid, net of cash acquired	(9,307,000)

Fair value of liabilities assumed \$ 3,054,000

In connection with recording the value of the Company's interest rate swap contracts, other comprehensive income and other current liabilities increased by \$181,000 and \$717,000, respectively, and other long-term liabilities and long-term deferred tax assets decreased by \$1,009,000 and \$111,000, respectively.

In connection with the recording of capital leases, the Company increased both fixed assets and long-term debt by \$2,695,000.

In connection with the accounting for income tax benefits related to the exercise of stock options, the Company decreased current liabilities and increased paid-in capital by \$1,596,000.

**Table of Contents**

MONRO MUFFLER BRAKE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENT

**Note 7 Cash Dividend**

In April 2010, the Company's Board of Directors declared its intention to pay a regular quarterly cash dividend during fiscal 2011 of \$.09 per common share or common share equivalent to be paid beginning with the first quarter of fiscal 2011. However, the declaration of and any determination as to the payment of future dividends will be at the discretion of the Board of Directors and will depend on the Company's financial condition, results of operations, capital requirements, compliance with charter and contractual restrictions, and such other factors as the Board of Directors deems relevant.

**Note 8 Subsequent Event**

In October 2010, the Company signed a definitive asset purchase agreement to acquire three retail tire stores located in Virginia for approximately \$3.2 million. These stores produced approximately \$5 million in sales annually based on un-audited pre-acquisition historical information. The transaction is expected to close on October 31, 2010. These stores will operate under the Mr. Tire brand name. The acquisition will be financed through the Company's existing bank facility.

**Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**Results of Operations**

The statements contained in this Form 10-Q that are not historical facts, including (without limitation) statements made in the Management's Discussion and Analysis of Financial Condition and Results of Operations, may contain statements of future expectations and other forward-looking statements made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results to differ materially from those expressed. These factors include, but are not necessarily limited to, product demand, dependence on and competition within the primary markets in which the Company's stores are located, the need for and costs associated with store renovations and other capital expenditures, the effect of economic conditions, the impact of competitive services and pricing, product development, parts supply restraints or difficulties, industry regulation, risks relating to leverage and debt service (including sensitivity to fluctuations in interest rates), continued availability of capital resources and financing, risks relating to integration of acquired businesses, the availability of vendor rebates and other factors set forth or incorporated elsewhere herein and in the Company's other Securities and Exchange Commission filings. The Company does not undertake to update any forward-looking statement that may be made from time to time by or on behalf of the Company.

The following table sets forth income statement data of Monro Muffler Brake, Inc. (Monro or the Company) expressed as a percentage of sales for the fiscal periods indicated:

	Quarter Ended Fiscal September		Six Months Ended Fiscal September	
	2010	2009	2010	2009
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales, including distribution and occupancy costs	59.1	56.9	58.7	56.5
Gross profit	40.9	43.1	41.3	43.5
Operating, selling, general and administrative expenses	26.6	30.1	26.9	30.3
Intangible amortization	.2	.1	.2	.1
Loss on disposal of assets	.1		.1	
Total operating expenses	26.9	30.2	27.2	30.5
Operating income	14.0	12.8	14.1	13.0
Interest expense - net	.7	1.1	.8	1.3
Other income - net		(.1)		
Income before provision for income taxes	13.3	11.8	13.4	11.8
Provision for income taxes	5.1	4.5	5.1	4.5
Net income	8.2%	7.3%	8.3%	7.3%

*Second Quarter and Six Months Ended September 25, 2010 Compared To Second Quarter and Six Months Ended September 26, 2009*

## Edgar Filing: MONRO MUFFLER BRAKE INC - Form 10-Q

Sales were \$162.1 million for the quarter ended September 25, 2010 as compared with \$136.6 million in the quarter ended September 26, 2009. The sales increase of \$25.5 million or 18.6%, was partially due to a comparable store sales increase of 6.4%. Additionally, there was an increase of \$18.0 million related to new stores, of which \$16.8 million came from the fiscal year 2010 and

**Table of Contents**

2011 acquisitions. Partially offsetting this was a decrease in sales from closed stores amounting to \$1.0 million. There were 91 selling days in the quarter ended September 25, 2010 and in the quarter ended September 26, 2009.

Sales were \$320.3 million for the six months ended September 25, 2010 as compared with \$264.7 million in the six months ended September 26, 2009. The sales increase of \$55.7 million or 21.0%, was partially due to a comparable store sales increase of 5.8%. Additionally, there was an increase of \$42.5 million related to new stores, of which \$40.3 million came from the fiscal year 2010 and 2011 acquisitions. Partially offsetting this sales increase was a decrease in sales from closed stores amounting to \$2.1 million.

The Company has slightly modified its methodology for calculating the number of selling days in each month and quarter. Previously, in computing its comparable store sales percentage increases (adjusted for days), the Company did not include Sundays or open holidays in the number of selling days, but included all sales in each comparable period. This was because only a small number of stores were open Sundays, and some were not open holidays. Also, these days were generally much shorter selling days. Now that over 50% of the Company's stores are open Sundays, almost all stores are open holidays, and the selling days are longer, the Company concluded that counting Sundays and open holidays as selling days is now appropriate. Accordingly, selling days now include each day other than Easter, Thanksgiving and Christmas. This change was made beginning in fiscal year 2011 (April 2010) and retroactively applied to prior months and quarters. There is no impact on reported actual comparable store sales increases for any prior periods. Nor will the change impact calculated comparable store sales increases in future periods. However, this change may result in a change in the calculated comparable store sales percent increase in certain prior periods when adjusted for days.

For the fiscal year 2010 fiscal quarters and full year, the results were as follows:

	<b>Reported Comparable Store Sales Increase</b>	<b>Originally Reported Comparable Store Sales Increase, Adjusted For Days</b>	<b>Restated Comparable Store Sales Increase, Adjusted For Days</b>
Q1 FY10	6.2%	6.2%	7.4% (1)
Q2 FY10	7.4%	7.4%	7.4%
Q3 FY10	7.2%	7.2%	7.2%
Q4 FY10	8.0%	8.0%	6.8% (2)
Full year FY10	7.2%	7.2%	7.2%

- (1) This adjustment for days relates to the fact that the Easter holiday fell in April 2009, reducing the number of selling days as compared to the prior year quarter.
- (2) This adjustment for days relates to the fact that the Company was open for business for the first time on New Year's Day on January 1, 2010, increasing the number of selling days as compared to the prior year quarter.

At September 25, 2010, the Company had 783 company-operated stores and three franchised locations compared with 739 stores at September 26, 2009. During the quarter ended September 25, 2010, the Company closed two stores.

Management believes that the improvement in comparable store sales resulted from several factors, including an increase in sales across all product categories. It is management's belief that strong in-store sales execution, highly effective advertising campaigns and price increases in several product categories also contributed to the sales improvement. Comparable store traffic as well as average ticket increased over the prior year second quarter. Soft economic conditions and the related decrease in consumer spending and tightening of credit, resulting in declining automobile sales (as compared to historical levels), helped to contribute to the improved sales. Management believes that consumers are keeping their cars longer and repairing them instead of trading them in for new cars. Additionally, while consumers can and often defer repairs when the economy is weak, most repairs can only be deferred for a period of time. When customers do come in to have their vehicles repaired, it is management's belief that they spend more on average because the problem with their vehicle has worsened due to additional wear.

Management also believes that the recent closings of dealerships by Chrysler and General Motors are driving more business to the Company's stores as consumers look for alternative, proven, economical and more geographically convenient locations to service their automobiles.

Gross profit for the quarter ended September 25, 2010 was \$66.4 million or 40.9% of sales as compared with \$58.9 million or 43.1% of sales for the quarter ended September 26, 2009. The decrease in gross profit for the quarter ended September 25, 2010, as a



## Table of Contents

percentage of sales, is due to several factors.

Total material costs, including outside purchases, increased as a percentage of sales as compared to the prior year. The fiscal year 2010 and fiscal year 2011 acquisitions, all but one of which were tire stores, have resulted in a more pronounced shift in mix to the lower margin tire category, causing margin pressure. Over 80% of the gross margin deterioration was attributable to these acquired tire stores. Tire and oil cost increases also contributed to the decline in margin. Partially offsetting these factors were selling price increases across the chain.

There was also a decrease in labor costs as a percent of sales due primarily to a continued shift in mix to tire sales and improved labor productivity, helping to improve gross profit. Additionally, distribution and occupancy costs decreased as a percentage of sales from the prior year as the Company, with improved sales, was able to better leverage these largely fixed costs.

Gross profit for the six months ended September 25, 2010 was \$132.4 million, or 41.3% of sales, compared with \$115.3 million or 43.5% of sales for the six months ended September 26, 2009.

The Company expects the decline in gross margin versus the prior year quarters to be most pronounced in its first and second quarters of fiscal year 2011, since it did not own the Tire Warehouse stores, whose mix is almost 100% tires, until its third fiscal quarter last year. Management expects gross margin for the third and fourth quarters to begin to flatten out as compared to the same quarters of fiscal 2010, and operating profit to be approximately 100 basis points better.

Operating expenses for the quarter ended September 25, 2010 were \$43.7 million or 26.9% of sales as compared with \$41.3 million or 30.2% of sales for the quarter ended September 26, 2009. Within operating expenses, selling, general and administrative ( SG&A ) expenses for the quarter ended September 25, 2010 increased by \$2.0 million to \$43.1 million from the quarter ended September 26, 2009, and decreased as a percentage of sales from 30.1% to 26.6%. The increase in dollars is directly attributed to the acquired stores' operating expenses. The decrease in percentage of sales is due to improved sales which have allowed the Company to leverage largely fixed costs, as well as a continued focus on cost control.

For the six months ended September 25, 2010, operating expenses increased by \$6.3 million to \$87.0 million from the comparable period of the prior year and were 27.2% of sales compared to 30.5%.

SG&A expenses for the six months ended September 25, 2010 increased \$5.9 million to \$86.2 million from the comparable period of the prior year and were 26.9% of sales as compared to 30.3%.

Operating income for the quarter ended September 25, 2010 of approximately \$22.7 million increased by 29.5% as compared to operating income of approximately \$17.5 million for the quarter ended September 26, 2009, and increased as a percentage of sales from 12.8% to 14.0%.

Operating income for the six months ended September 25, 2010 of approximately \$45.3 million increased by 31.4% as compared to operating income of approximately \$34.5 million for the six months ended September 26, 2009, and increased as a percentage of sales from 13.0% for the six months ended September 26, 2009 to 14.1% for the six months ended September 25, 2010.

Net interest expense for the quarter ended September 25, 2010 decreased by approximately \$.2 million as compared to the same period in the prior year, and decreased from 1.1% to .7% as a percentage of sales for the same periods. The weighted average debt outstanding for the quarter ended September 25, 2010 decreased by approximately \$14 million as compared to the quarter ended September 26, 2009, primarily related to repayments made on the Company's Revolving Credit Facility agreement. The weighted average interest rate was relatively flat as compared to the prior year.

Net interest expense for the six months ended September 25, 2010 decreased by approximately \$.7 million as compared to the same period in the prior year, and decreased .5% as a percentage of sales for the same periods. Weighted average debt decreased by approximately \$7 million and the weighted average interest rate declined by approximately 90 basis points as compared to the same period of the prior year.

The effective tax rate for the quarter ended September 25, 2010 and September 26, 2009 was 38.2% and 38.1%, respectively, of pre-tax income.

The effective tax rate for the six months ended September 25, 2010 and September 26, 2009 was 38.0% and 37.9%, respectively, of pre-tax income.





## **Table of Contents**

Net income for the quarter ended September 25, 2010 of \$13.3 million increased 33.2% from net income for the quarter ended September 26, 2009. Earnings per share on a diluted basis for the quarter ended September 25, 2010 increased 28.6%.

For the six months ended September 25, 2010, net income of \$26.5 million increased 36.7% and diluted earnings per share increased 32.6%.

### **Capital Resources and Liquidity**

#### *Capital Resources*

The Company's primary capital requirements in fiscal year 2011 are the upgrading of facilities and systems and the funding of its store expansion program, including acquisitions of existing store chains. For the six months ended September 25, 2010, the Company's primary capital requirements were divided between the funding of capital expenditures related to existing and greenfield stores totaling \$6.6 million, and the funding of acquisitions totaling \$7.1 million. Funds were provided primarily by cash flow from operations and bank financing.

The Company paid dividends of \$3.7 million during the six months ended September 25, 2010. In April 2010, the Company's Board of Directors declared its intention to pay a regular quarterly cash dividend of \$.09 per common share or common share equivalent beginning with the first quarter of fiscal year 2011.

Management believes that the Company has sufficient resources available (including cash and equivalents, net cash flow from operations and bank financing) to expand its business as currently planned for the next several years.

#### *Liquidity*

In July 2005, the Company entered into a five-year, \$125 million Revolving Credit Facility agreement with five banks. A sixth bank was added in June 2008. Interest only is payable monthly throughout the Credit Facility's term. The facility included a provision allowing the Company to expand the amount of the overall facility to \$160 million. Amendments in January 2007 and June 2008 were made to these amounts which increased the overall facility to \$200 million and extended the expiration to January 2012. Currently, the committed sum is \$163.3 million and the accordion feature is \$36.7 million. Approximately \$46.8 million was outstanding at September 25, 2010, including \$16.8 million of outstanding letters of credit.

The Company has financed certain store properties and equipment with capital leases, which amount to \$45.1 million and are due in installments through 2039.

The terms of the Credit Facility permit the payment of cash dividends not to exceed 25% of the preceding year's net income, and allow stock buybacks subject to the Company being able to meet its existing financial covenants. The Agreement requires the maintenance of specified interest and rent coverage ratios and amounts of net worth. At September 25, 2010, the Company is in compliance with the applicable debt covenants, and does not foresee a risk of being out of compliance for the foreseeable future. These agreements permit mortgages and specific lease financing arrangements with other parties with certain limitations.

The Company enters into interest rate hedge agreements, which involve the exchange of fixed and floating rate interest payments periodically over the life of the agreement without the exchange of the underlying principal amounts. The differential to be paid or received is accrued as interest rates change and is recognized over the life of the agreements as an offsetting adjustment to interest expense. The Company entered into three \$10 million interest rate swap agreements in July 2008 which expired in July 2010.

The purpose of these agreements was to limit the interest rate exposure in the Company's floating rate debt. Fixed rates under these agreements ranged from 3.27% to 3.29%.

### **Recent Accounting Pronouncements**

There have been no developments to recently issued accounting standards, including the expected dates of adoption and estimated effects on the Company's consolidated financial statements, from those disclosed in the Company's 2010 Annual Report on Form 10-K.



**Table of Contents**

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company is exposed to market risk from potential changes in interest rates. At September 25, 2010 and March 27, 2010, approximately 2% and 58%, respectively, of the Company's long-term debt, excluding capital leases, was at fixed interest rates and therefore, the fair value is affected by changes in market interest rates. The Company's cash flow exposure on floating rate debt, which is not supported by interest rate swap agreements, would result in interest expense fluctuating approximately \$.3 million based upon the Company's debt position at quarter ended September 25, 2010 and \$.2 million for fiscal year ended March 27, 2010, given a 1% change in LIBOR.

The Company regularly evaluates these risks and had entered into three interest rate swap agreements, which expired in July 2010, with an aggregate notional amount of \$30.0 million. These agreements limited the interest rate exposure on the Company's floating rate debt, related specifically to the Revolving Credit Facility, via the exchange of fixed and floating rate interest payments periodically over the life of the agreements without the exchange of the underlying principal amount. The fixed rates paid by the Company under these agreements ranged from 3.27% to 3.29%.

The Company believes the amount of risk and the use of derivative financial instruments described above are not material to the Company's financial condition or results of operations.

Item 4. Controls and Procedures

*Disclosure controls and procedures*

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in reports that the Company files or submits pursuant to the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's (SEC) rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

In conjunction with the close of each fiscal quarter and under the supervision of the Chief Executive Officer and Chief Financial Officer, the Company conducts an update, a review and an evaluation of the effectiveness of the Company's disclosure controls and procedures. It is the conclusion of the Company's Chief Executive Officer and Chief Financial Officer, based upon an evaluation completed as of the end of the most recent fiscal quarter reported on herein, that the Company's disclosure controls and procedures were effective.

*Changes in internal controls*

There were no changes in the Company's internal control over financial reporting during the quarter ended September 25, 2010 that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents**

MONRO MUFFLER BRAKE, INC.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Company is not a party or subject to any legal proceedings other than certain claims and lawsuits that arise in the normal course of its business. The Company does not believe that such claims or lawsuits, individually or in the aggregate, will have a material adverse effect on its financial condition or results of operations.

Item 1A. Risk Factors

There have been no changes to the risk factors described in the Company's previously filed Annual Report on Form 10-K for the fiscal year ended March 27, 2010.

Item 4. Removed and Reserved

Item 6. Exhibits

a. Exhibits

- 31.1 Certification of Robert G. Gross pursuant to Section 302 of the Sarbanes Oxley Act of 2002
- 31.2 Certification of Catherine D. Amico pursuant to Section 302 of the Sarbanes Oxley Act of 2002
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002

**Table of Contents**

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MONRO MUFFLER BRAKE, INC.

DATE: October 29, 2010

By /s/ Robert G. Gross  
Robert G. Gross  
Chief Executive Officer and Chairman of the Board

DATE: October 29, 2010

By /s/ Catherine D Amico  
Catherine D Amico  
Executive Vice President-Finance, Treasurer and Chief Financial Officer

**Table of Contents**

**EXHIBIT INDEX**

Exhibit No.	Description	Page No.
31.1	Certification of Robert G. Gross pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	20
31.2	Certification of Catherine D Amico pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	21
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	22