

O REILLY AUTOMOTIVE INC
Form 10-K
March 03, 2008
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-K

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

For the fiscal year ended December 31, 2007

OR

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

For the transition period from _____ to _____

O'REILLY AUTOMOTIVE, INC.
(Exact name of registrant as specified in its charter)

Missouri
(State or other jurisdiction)

0-21318
Commission file number

44-0618012
(IRS Employer Identification No.)

of incorporation or organization)

233 South Patterson
Springfield, Missouri 65802
(Address of principal executive offices, zip code)

(417) 862-6708
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on which Registered
Common Stock, \$0.01 par value	The Nasdaq Global Select Market

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Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No

Note – Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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 o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained here, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by a check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. Large Accelerated Filer Accelerated Filer o Non-Accelerated Filer o Smaller Reporting Company o

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

At February 28, 2008, an aggregate of 115,390,026 shares of the common stock of the registrant was outstanding. As of that date, the aggregate market value of the voting stock held by non-affiliates of the Company was approximately \$3,243,613,631 based on the last sale price of the common stock reported by The Nasdaq Global Select Market.

At June 30, 2007, an aggregate of 114,836,096 shares of the common stock of the registrant was outstanding. As of that date, the aggregate market value of the voting stock held by non-affiliates of the Company was approximately \$4,197,259,309 based on the last sale price of the common stock reported by The Nasdaq Global Select Market.

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DOCUMENTS INCORPORATED BY REFERENCE

As indicated below, portions of the registrant's documents specified below are incorporated here by reference:

Document	Form 10-K Part
Portions of the Annual Shareholders' Report for the Year Ended December 31, 2007	Parts II and IV
Proxy Statement for 2008 Annual Meeting of Shareholders (to be filed pursuant to Regulation 14A within 120 days of the end of registrant's most recently completed fiscal year)	Part III

Forward Looking Information

We claim the protection of the safe-harbor for forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You can identify these statements by forward-looking words such as “expect,” “believe,” “anticipate,” “should,” “plan,” “intend,” “estimate,” “project” or similar words. In addition, statements contained within this annual report that are not historical facts are forward-looking statements, such as statements discussing among other things, expected growth, store development and expansion strategy, business strategies, future revenues and future performance. These forward-looking statements are based on estimates, projections, beliefs and assumptions and are not guarantees of future events and results. Such statements are subject to risks, uncertainties and assumptions, including, but not limited to, competition, product demand, the market for auto parts, the economy in general, inflation, consumer debt levels, governmental approvals, our ability to hire and retain qualified employees, risks associated with the integration of acquired businesses, weather, terrorist activities, war and the threat of war. Actual results may materially differ from anticipated results described or implied in these forward-looking statements. Please refer to the Risk Factors section of this annual report on Form 10-K for the year ended December 31, 2007, for additional factors that could materially affect our financial performance.

PART I

Item 1. Business

General

O'Reilly Automotive, Inc. is one of the largest specialty retailers of automotive aftermarket parts, tools, supplies, equipment and accessories in the United States, selling our products to both do-it-yourself (DIY) customers and professional installers. At December 31, 2007, we operated 1,830 stores in Alabama, Arkansas, Florida, Georgia, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Minnesota, Mississippi, Missouri, Montana, Nebraska, North Carolina, North Dakota, Ohio, Oklahoma, South Carolina, South Dakota, Tennessee, Texas, Virginia, Wisconsin and Wyoming. Our stores carry an extensive product line consisting of:

- new and remanufactured automotive hard parts, such as alternators, starters, fuel pumps, water pumps, brake shoes and pads, belts, hoses, chassis parts and engine parts;
- maintenance items, such as oil, antifreeze, fluids, filters, wiper blades, lighting, engine additives and appearance products;
- accessories, such as floor mats and seat covers; and
- a complete line of auto body paint and related materials, automotive tools and professional service equipment.

We do not sell tires or perform automotive repairs or installations.

We were founded in 1957 by Charles F. O'Reilly and his son, Charles H. "Chub" O'Reilly, Sr. and initially operated from a single store in Springfield, Missouri. The O'Reilly family has been highly involved in the management of the Company since our inception.

Our goal is to continue to achieve growth in sales and profitability by capitalizing on our competitive advantages and executing our growth strategy.

Our Internet address is www.oreillyauto.com. Interested readers can access the Company's annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, through the Securities and Exchange Commission website at www.sec.gov and searching with our ticker symbol "ORLY". Such reports are generally available on the day they are filed. Upon request, the Company will furnish interested readers a paper copy of such reports free of charge.

See "Risk Factors" beginning on page 11 for a description of certain risks relevant to our business. These risk factors include, among others, risks related to competition in the automotive aftermarket business, our growth strategy, our acquisition strategy, our sensitivity to regional economic and weather conditions, our dependence upon key and other personnel, the volatility of the market price of our common stock and the effect of sales of shares of our common stock eligible for future sale.

Competitive Advantages

Proven Ability to Execute Dual Market Strategy. We have an established track record of effectively serving at a high level both DIY customers and professional installers. We believe our ability to execute a dual market strategy is a competitive advantage, which enables us to:

- target a larger base of consumers of automotive aftermarket parts;
- capitalize on our existing retail and distribution infrastructure;
- profitably operate in both large markets and less densely populated geographic areas that typically attract fewer competitors; and

- enhance service levels offered to our DIY customers by offering a broad selection of stock keeping units (SKUs) and the extensive product knowledge required by professional installers.

We have been committed to a dual market strategy for over 20 years. In 2007, we derived approximately 52% of our sales from our DIY customers and approximately 48% from our professional installer customers. As a result of our historical success of executing our dual market strategy and our 250 full-time sales representatives dedicated solely to calling upon and selling to the professional installer, we believe we will continue to increase our sales to professional installers and will continue to have a competitive advantage over our retail competitors who derive a high concentration of their sales from the DIY market.

Superior Customer Service. We seek to attract new DIY and professional installer customers and to retain existing customers by offering superior customer service, the key elements of which include:

- superior in-store service through highly-motivated, technically proficient store personnel (Professional Parts People) using an advanced point-of-sale system;
- an extensive selection and availability of products;
- attractive stores in convenient locations; and
- competitive pricing, supported by a good, better, best product assortment designed to meet all of our customers quality and value preferences.

Technically Proficient Professional Parts People. Our highly proficient Professional Parts People provide us with a significant competitive advantage, particularly over less specialized retail operators. We require our Professional Parts People to undergo extensive and ongoing training and to be technically knowledgeable, particularly with respect to hard parts, in order to better serve the technically oriented professional installers with whom they interact on a daily basis. Such technical proficiency also enhances the customer service we provide to our DIY customers, who value the expert assistance provided by our Professional Parts People.

Strategic Distribution Systems. We believe that the geographic concentration of our store network in 26 contiguous states and the strategic locations of our 14 distribution centers enable us to optimize product availability and inventory levels throughout our store network. In addition, our inventory management and distribution systems electronically link each of our stores to a distribution center, providing for efficient inventory control and management. Our distribution system provides each of our stores with same day or overnight access to over 100,000 SKUs, many of which are hard to find items not typically stocked by other auto parts retailers. We believe this timely access to a broad range of products is a key competitive advantage in satisfying customer demand and generating repeat business.

Experienced Management Team. Our management team has demonstrated the consistent ability to successfully execute our business plan, including the identification and integration of strategic acquisitions. We have experienced fifteen consecutive years of record revenues, positive comparable store sales results and earnings growth since becoming a public company in April 1993. We have a strong senior management team comprised of 88 professionals who average over 16 years of experience with O'Reilly. In addition, our 127 corporate managers average over 13 years of experience with Team O'Reilly and our 177 district managers average over 10 years of experience.

Growth Strategy

Aggressively Open New Stores. We intend to continue to aggressively open new stores to achieve greater penetration in existing markets and to expand into new, contiguous markets. We plan to open approximately 205 stores in 2008. A majority of the sites for our proposed 2008 store openings have been identified. In selecting sites for new stores, we strategically locate store sites in clusters within geographic areas to achieve management, advertising and distribution economies of scale.

We target both small and large markets for expansion of our store network. While we have faced, and expect to continue to face, aggressive competition in the more densely populated markets, we believe that we have competed effectively, and that we are well positioned to continue to compete effectively, in such markets and achieve our goal of continued sales and profit growth within these markets. We also believe that because of our dual market strategy, we are better able to operate stores in less densely populated areas within our regional markets, which would not otherwise support a national or regional chain store selling primarily to the retail automotive aftermarket. Consequently, we also expect to continue to open new stores in less densely populated market areas.

To date, we have not experienced significant difficulties in locating suitable store sites for construction of new stores or identifying suitable acquisition candidates for conversion to O'Reilly stores. We typically open new stores either by (i) constructing a new store at a site we purchase or lease and stocking the new store with fixtures and inventory, or (ii) acquiring an independently owned auto parts store, typically by the purchase of substantially all of the inventory and other assets (other than realty) of such store. Store sites are strategically located in clusters within geographic areas that complement our distribution system in order to achieve economies of scale in management, advertising and distribution costs. Other key factors we consider in the site selection process include population density and growth patterns, age and per capita income, vehicle traffic counts, the number and type of existing

automotive repair facilities, other competing auto parts stores, and other competitors within a pre-determined radius, and the operational strength of such competitors. When entering new, more densely populated markets, we generally seek to initially open several stores within a short span of time in order to maximize the effect of initial promotional programs and achieve economies of scale.

Profitable same store sales growth is also an important part of our growth strategy. To achieve improved sales and profitability at existing O'Reilly stores, we continually strive to improve the service provided to our customers. We believe that while competitive pricing is essential in the competitive environment of the automotive aftermarket business, it is customer satisfaction (whether of the DIY consumer or professional installer), resulting from superior customer service, which generates increased sales and profitability.

Selectively Pursue Strategic Acquisitions. Although the automotive aftermarket industry is still highly fragmented, we believe the ability of national and regional specialty retail chains, such as ourselves, to operate more efficiently than smaller independent operators or mass merchandisers will result in continued industry consolidation. Thus, we intend to selectively pursue acquisition targets that will strengthen our position as a leading automotive products retailer.

Continually Enhance Store Design and Location. Our current prototype store design features enhancements such as greater square footage, higher ceilings, more convenient interior store layouts, improved in-store signage, brighter lighting, increased parking availability and dedicated counters to serve professional installers, each designed to increase sales and operating efficiencies and enhance customer service. We continually update the location and condition of our store network through systematic renovation and relocation of our existing stores to enhance store performance. We believe that our ability to consistently achieve growth in same store sales is due in part to our commitment to maintaining an attractive store network, which is strategically located to best serve our customers.

Products and Purchasing

Our stores offer DIY and professional installer customers a wide selection of brand name and private label products for domestic and imported automobiles, vans and trucks. We do not sell tires or perform automotive repairs or installations. Our merchandise generally consists of nationally recognized, well-advertised, name brand products such as AC Delco, Moog, Murray, Wagner, Gates Rubber, Federal Mogul, Monroe, Prestone, Quaker State, Pennzoil, Castrol, Valvoline, STP, BWD, Cardone, Wix, Armor All and Turtle Wax. In addition to name brand products, our stores carry a wide variety of high-quality private label products under our O'Reilly Auto Parts®, BestTest®, MicroGard®, PowerTorque®, Miles Ahead®, SuperStart®, BrakeBest®, Ultima®, Master Pro® and Omnispark® proprietary name brands. Because most of our private label products are produced by nationally recognized manufacturers and meet or exceed original equipment manufacturer specifications, we believe that the private label products are generally of equal or, in some cases, better quality than comparable name brand products, a characteristic which is important to our DIY customers. We further believe that our private label products are packaged attractively to promote customer interest and are generally priced below comparable name brand products carried in our stores.

We purchase automotive products in substantial quantities from over 400 vendors, the five largest of which accounted for approximately 30% of our total purchases in 2007. Our largest vendor in 2007 accounted for approximately 11% of our total purchases and the next four largest vendors each accounted for 4-6% of such purchases. We have no long-term contractual purchase commitments with any of our vendors, nor have we experienced difficulty in obtaining satisfactory alternative sources of supply for automotive parts. We believe that alternative supply sources exist at substantially similar costs, for substantially all of the automotive products that we sell. It is our policy to take advantage of payment and seasonal purchasing discounts offered by our vendors and to utilize extended dating terms available from vendors. During 2007, we entered into various programs and arrangements with certain vendors that provided for extended dating and payment terms for inventory purchases. As a whole, we consider our relationships with our vendors to be very good.

Inflation and Seasonality

We have been successful, in many cases, in reducing the effects of merchandise cost increases principally by taking advantage of vendor incentive programs, economies of scale resulting from increased volume of purchases and selective forward buying. As a result, we do not believe our operations have been materially affected by inflation.

To some extent, our business is seasonal primarily as a result of the impact of weather conditions on customer buying patterns. Store sales and profits have historically been higher in the second and third quarters (April through September) than in the first and fourth quarters.

Store Network

Store Locations. As a result of our dual market strategy, we are able to profitably operate in both large, densely populated markets and small, less densely populated areas that would not otherwise support a national or regional chain selling primarily to the retail automotive aftermarket. The following table sets forth the geographic distribution of our stores:

State	December 31, 2006		2007 Net New Stores		December 31, 2007	
	Store Count	% of Total Store Count	Store Count	% of Total Stores Added	Store Count	% of Total Store Count
Texas	434	26.5%	33	17.4%	467	25.5%
Missouri	154	9.4%	15	7.9%	169	9.2%
Tennessee	112	6.8%	5	2.6%	117	6.4%
Georgia	94	5.7%	21	11.1%	115	6.3%
Oklahoma	101	6.2%	2	1.1%	103	5.6%
Alabama	95	5.8%	5	2.6%	100	5.5%
Arkansas	87	5.3%	3	1.6%	90	4.9%
Louisiana	65	4.0%	8	4.2%	73	4.0%
Iowa	65	4.0%	-	-	65	3.6%
Kansas	61	3.7%	2	1.1%	63	3.4%
Mississippi	59	3.6%	4	2.1%	63	3.4%
Illinois	57	3.5%	4	2.1%	61	3.3%
Minnesota	43	2.4%	15	7.9%	58	3.2%
Indiana	35	2.1%	20	10.5%	55	3.0%
Kentucky	42	2.6%	8	4.2%	50	2.7%
North Carolina	30	1.8%	8	4.2%	38	2.1%
South Carolina	24	1.5%	8	4.2%	32	1.7%
Nebraska	26	1.6%	1	0.5%	27	1.5%
Montana	18	1.1%	2	1.1%	20	1.1%
Florida	14	0.9%	6	3.1%	20	1.1%
Ohio	-	-	14	7.4%	14	0.8%
Wisconsin	11	0.7%	-	-	11	0.6%
North Dakota	3	0.2%	4	2.1%	7	0.4%
Wyoming	4	0.2%	1	0.5%	5	0.3%
Virginia	3	0.2%	1	0.5%	4	0.2%
South Dakota	3	0.2%	-	-	3	0.2%
Total	1,640		190		1,830	

Our stores on average carry approximately 21,000 SKUs and average approximately 6,800 total square feet in size. At December 31, 2007, we had a total of approximately 12.4 million square feet in our 1,830 stores. Our stores are served primarily by the nearest distribution center, but they also have access to the broader selection of inventory available at one of our 102 Master Inventory Stores, which on average carry approximately 34,000 SKUs and average approximately 9,100 square feet in size. In addition to serving DIY and professional installer customers in their markets, Master Inventory Stores also provide our other stores within the contiguous area access to a greater selection of

SKUs on a same-day basis.

We believe that our stores are "destination stores" generating their own traffic rather than relying on traffic created by the presence of other stores in the immediate vicinity. Consequently, most of our stores are freestanding buildings situated on or near major traffic thoroughfares, and offer ample parking and easy customer access.

Store Layout. We utilize a computer-assisted "plan-o-grammed" store layout system to provide a uniform and consistent merchandise presentation; however, each store's inventory assortment is customized to meet the specific needs of a particular market area. Merchandise is arranged to provide easy customer access, maximum selling space and to prominently display high-turnover products and accessories to customers. To ensure the best customer experience possible, we have selectively implemented bilingual in-store signage based on the demographics in each store's geographic area. Aisle displays are used to feature high-demand or seasonal merchandise, new items and advertised specials.

Store Automation. To enhance store level operations and customer service, we use IBM I-Series and X-Series computer systems in all of our stores. These systems are linked with the IBM AS/400 computers located in each of our distribution centers. Our point-of-sale terminals provide immediate access to our electronic catalog to graphically display parts and pricing information by make, model and year of vehicle and use bar code scanning technology to price our merchandise. This system speeds transaction times, reduces the customer's checkout time and provides enhanced customer service. Moreover, our store automation systems capture detailed sales information which assists in store management, strategic planning, inventory control and distribution efficiency.

New Store Site Selection. In selecting sites for new stores, we seek to strategically locate store sites in clusters within geographic areas in order to achieve economies of scale in management, advertising and distribution. Other key factors we consider in the site selection process include:

- population density and growth patterns;
- age and per capita income;
- vehicle traffic counts;
- the number and type of existing automotive repair facilities; and
- the number of auto parts stores and other competitors within a pre-determined radius and the operational strength of such competitors.

When entering new, more densely populated markets, we generally seek to initially open several stores within a short span of time in order to maximize the effect of initial promotional programs and achieve economies of scale. After opening this initial cluster of new stores, we seek to begin penetrating the less densely populated surrounding areas. This strategy enables us to achieve additional distribution and advertising efficiencies in each market.

Distribution System

We currently operate 14 distribution centers comprised of approximately 4.7 million square feet (see the "Properties" table in Item 2 of this Form 10-K for a detailed listing of distribution center square footages). Our distribution centers are equipped with highly automated conveyor systems, which expedite the movement of our products to loading areas for shipment to each of our stores on a nightly basis. The distribution centers utilize technology to electronically receive orders from computers located in each of our stores. In addition to the bar code system employed in our stores, each of our stores is connected through secured data transmission technology to our distribution centers and corporate headquarters.

We believe that our distribution system provides industry leading parts availability and store in-stock positions while lowering our inventory carrying costs and controlling inventory. Moreover, we believe that our significant capital investments in expanding the network of distribution centers allows us to efficiently service new stores that are planned to open in contiguous market areas as well as servicing our existing store network. Our distribution center expansion strategy complements our new store opening strategy by supporting newly established clusters of stores located in the regions surrounding each distribution center. As part of our continuing efforts to enhance our distribution network, in 2008 we plan to:

- open a 15th distribution center in Lubbock, Texas that will provide greater capacity for growth in new markets. The Lubbock distribution center will also begin to service existing West Texas stores currently serviced by distribution centers in Houston and Dallas thus providing additional capacity for growth in those markets;
- continue to implement a hands-free/eyes-free voice picking system in additional distribution centers;
- develop further automated paperless picking processes;
- improve proof of delivery systems to further increase the accuracy of product movement to our stores;
- continue to define and implement best practice procedures in all distribution centers; and

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- make proven, ROI based capital enhancements to material handling equipment in distribution centers including conveyor systems, picking modules and lift equipment.

Marketing

Marketing to the DIY Customer. We aggressively promote sales to DIY customers through an integrated marketing program, which includes direct mail, newspaper, television and radio advertising in selected markets, sports sponsorships and in event signage. We believe that our advertising and promotional activities have resulted in significant brand awareness in each of our geographic markets. Newspaper and radio advertisements are generally directed toward seasonal product and price promotions, frequently in connection with specific sale events or promotions.

To promote sales to race enthusiasts, who we believe on an individual basis spend more on automotive products than the general public, we sponsored multiple nationally televised races and over 1,500 grassroots to major motor sports races and car shows in 26 states, including 3 NASCAR Craftsman Truck Series Races, 2 NASCAR Busch Series Races, 6 National Hotrod Racing Association races, as well as the 21st Annual Chili Bowl Midget Nationals. In addition to sponsorships, O'Reilly Auto Parts is the "Official Auto Parts Store" of Texas Motor Speedway, Kansas Speedway, Bristol Motor Speedway, Houston Raceway Park, Texas Motorplex, Memphis Motorsports Park, Heartland Park, Gateway International, Atlanta Dragway, O'Reilly Raceway Park at Indianapolis, Darlington Raceway and Talladega Superspeedway.

Since 2003, we have aggressively sought to market the O'Reilly brand in the National Collegiate Athletic Association. Our first initiative was to partner with Texas Tech University and their former head basketball coach, Bobby Knight. Our success with Coach

Knight let to placement of the O'Reilly logo on courts, goal stanchions, seatbacks and scoring table signs at over 70 colleges and universities across the country. O'Reilly is the title sponsor of numerous college basketball tournaments and events including the CBE Classic, All-College Classic and ESPN's Bracketbusters.

In 2007, we increased programs targeted toward Hispanic customers, expanded brand awareness campaigns into college and professional football and initiated integrated consumer promotions with the goal of increasing retail traffic in our stores. We have found that the more progressive marketing concepts utilized in the DIY portion of our business have also resulted in increased awareness for professional installer customers.

Marketing to the Professional Installer. We have 250 full-time O'Reilly sales representatives strategically located across our primary market areas. Each sales representative is dedicated solely to calling upon, supporting and selling to the professional installer. Targeted marketing materials such as flyers, quick reference guides and catalogs are produced and distributed on a regular basis to professional installers and fleet customers. Our industry leading First Call program includes a dedicated sales force, promotions directed solely to the professional installer, electronic shop management systems and electronic access to our stores. Moreover, each district manager and store manager throughout our store network calls upon existing and potential new professional installer customers on a regular basis. Our First Call marketing strategy, with respect to professional installers, emphasizes our ability to offer:

- dedicated Installer Service Specialists in all of our stores;
- prompt delivery using small trucks or vans operated at all of our stores;
- a separate counter in every store dedicated exclusively to serving professional installers;
- trade credit for qualified professional installers;
- broad selection of professional grade merchandise at competitive prices;
- First Call Online, a dedicated internet based catalog system designed for our professional installers that connects directly to our inventory system;
- training and seminars covering topics of interest to professional installers, such as technical updates, safety and general business management;
- access to inventory of the equipment and repair parts for the equipment needed by professional installers to operate their shop; and
- the Certified Auto Repair Center Program, a program that provides professional installers with the business tools that they need to profitably grow and market their shops.

Marketing to the Independently Owned Parts Store. Along with the operation of the distribution centers and the distribution of automotive products to our stores, Ozark Automotive Distributors, Inc., our wholly owned subsidiary ("Ozark"), also sells automotive products to independently owned parts stores (jobber stores) throughout our trade areas. These jobber stores are generally located in areas not directly serviced by an O'Reilly store. Ozark operates its own separate marketing program to jobber stores.

Approximately 191 jobber stores currently purchase automotive products from Ozark and participate in the Parts City Auto Parts® program, our proprietary jobber service program. As a participant in these programs, a jobber store which meets certain financial and operational standards is permitted to indicate its Parts City Auto Parts® membership through the display of the respective logo, which is owned by Ozark. We provide advertising, promotional assistance, marketing and sales support to Parts City Auto Parts® stores purchasing automotive products from Ozark. In return for a commitment to purchase automotive products from Ozark, we offer assistance to Parts City Auto Parts® jobber stores by making available computer software for business management and inventory control.

Management Structure

Each of our stores is staffed with a store manager and one or more assistant managers, in addition to the parts specialists and support staff required to meet the specific needs of each store. Each of our 177 district managers has general supervisory responsibility for an average of 10 stores.

Each district manager receives comprehensive training on a monthly basis, focusing on management techniques, new product announcements, advanced automotive systems and our policies and procedures. In turn, the information presented at such meetings is covered by the district managers at bi-monthly meetings with their store managers. All assistant managers and managers in training are required to successfully complete a six-month manager-training program, which includes classroom and field training, as a prerequisite to becoming a store manager. This program covers all facets of store operations, as well as principles of successful management. In addition, all new or prospective managers attend a manager development program, at the corporate headquarters in Springfield, MO, which includes 40 hours of classroom training. Upon returning to the stores, managers are given continuous field training throughout their management tenure.

We provide financial incentives to our district managers and all store team members through an incentive compensation program. Under our incentive compensation program, base salary is augmented by incentive compensation based upon the achievement of sales and profitability goals. In addition, each our district and store managers participate in the Company's stock option program. We believe that our incentive compensation program significantly increases the motivation and overall performance of our Professional Parts People and our ability to attract and retain qualified management and other personnel.

Most of our current senior management, district managers and store managers were promoted to their positions from within the Company. Our senior management team averages 16 years of experience with the Company, corporate managers average over 13 years of service and district managers have an average length of service with the Company of over 10 years.

Professional Parts People

We believe our highly trained team of Professional Parts People is essential in providing superior customer service to both DIY and professional installer customers. Each of our Professional Parts People is required to be technically proficient in the workings and application of automotive products due to the significant portion of our business represented by the professional installer. In addition, we have found that the typical DIY customer often seeks assistance from a Professional Parts Person, particularly in connection with the purchase of hard parts. We believe that the ability of our Professional Parts People to provide such assistance to the DIY customer creates a favorable impression during a customer's visit to our store and is a significant factor in generating repeat DIY business.

We screen prospective team members to identify highly motivated individuals either with experience in automotive parts or repairs, or an aptitude for automotive knowledge. Each person who becomes a team member first participates in an intensive two-day orientation program designed to introduce the team member to our culture and his or her job duties before being assigned specific job responsibilities. The successful completion of extensive training is required before a team member is deemed qualified as a parts specialist and thus able to work the parts counter at our stores. All new parts specialists are required to successfully complete a six-month basic automotive systems training course and are then enrolled in a six-month advanced automotive systems course for certification by the National Institute for Automotive Service

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Excellence (“ASE”), which administers national exams for various automotive specialties and requires ASE certified specialists to take recertification exams every five years.

Each of our stores participates in our sales specialist-training program. Under this program, selected team members complete two days of extensive sales call training for business development, after which these team members will spend one day per week calling on existing and new professional installer customers. Additionally, each team member engaged in such sales activities participates in quarterly advanced training programs for sales and business development.

Customer Service

We seek to provide our customers with an efficient and pleasant in-store experience by maintaining attractive stores in convenient locations with a wide selection of automotive products. We believe that the satisfaction of DIY and professional installer customers is substantially dependent upon our ability to provide, in a timely fashion, the specific automotive products requested. Accordingly, each O'Reilly store carries a broad selection of automotive products designed to cover a wide range of vehicle specifications. We continuously refine the inventory levels and assortments carried in our stores, based in large part on the sales movement tracked by our inventory control system, market vehicle registration data and management's assessment of the changes and trends in the marketplace.

Pricing

We believe that a competitive pricing policy is essential to compete successfully. Product pricing is generally established to compete with the pricing policies of competitors in the market area served by each store. Most automotive products that we sell are priced based on a combination of competitive shops and internal gross margin targets and are generally sold at discounts to the manufacturer suggested prices with additional savings offered through volume discounts and special promotional pricing. Consistent with our low price guarantee, each of our stores will match any verifiable price on any in-stock product of the same or comparable quality offered by our competitors.

Competition

We compete in both the DIY and professional installer portions of the automotive aftermarket. We compete primarily with:

- national and regional retail automotive parts chains (such as AutoZone, Inc., Advance Auto Parts, CSK Auto Corp. and the Pep Boys-Manny, Moe and Jack, Inc.)
- independently owned parts stores;
- wholesalers or jobber stores (some of which are associated with national automotive parts distributors or associations such as NAPA and Car Quest);
- automobile dealers; and
- mass merchandisers that carry automotive replacement parts, maintenance items and accessories (such as Wal-Mart Stores, Inc.).

We compete on the basis of customer service, which includes merchandise selection and availability, price, helpfulness of store personnel, store layout and convenient and accessible store locations.

Team Members

As of December 31, 2007, we employed 18,546 full-time team members and 5,030 part-time team members, of whom 18,914 were employed at our stores, 3,372 were employed at our distribution centers and 1,290 were employed at our corporate and regional offices. None of our team members are subject to a collective bargaining agreement. Our 50 years of tradition is to treat all of our team members with honesty and respect and to instill in them our "Live Green" Culture. This focus on professionalism and fairness has created an industry leading team and we consider our relations with our team members to be excellent.

Service Marks and Trademarks

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We have registered the service marks O'Reilly Automotive®, Parts Payoff®, Parts City Auto Parts®, O'Reilly Auto Parts®, BestTest®, MicroGard®, PowerTorque® and Miles Ahead® and the trademarks First Call®, SuperStart®, BrakeBest®, Ultima®, Master Pro® and Omnispark®. We believe that our business is not otherwise dependent upon any patent, trademark, service mark or copyright.

Regulations

Although subject to various laws and governmental regulations relating to our business, including those related to the environment, compliance with any such laws and regulations has not had a material adverse effect on our operations to date. We cannot give any assurance, however, that we will not incur significant expenses in the future in order to comply with any such law or regulation.

Item 1A. Risk Factors

Our future performance is subject to a variety of risks and uncertainties. Although the risks described below are the risks that we believe are material, there also may be risks of which we are currently unaware, or that we currently regard as immaterial based on the information available to us that later may prove to be material. You should be aware that the occurrence of the events described in these risk factors, elsewhere in this Form 10-K and in our other filings with the Securities and Exchange Commission could have a material adverse effect on our business, operating results and financial condition. Actual results, therefore, may materially differ from anticipated results described in these forward-looking statements.

The automotive aftermarket business is highly competitive, and we may have to risk our capital to remain competitive.

Both the DIY and professional installer portions of our business are highly competitive, particularly in the more densely populated areas that we serve. Some of our competitors are larger than we are and have greater financial resources. In addition, some of our competitors are smaller than we are overall but have a greater presence than we do in a particular market. We may have to expend more resources and risk additional capital to remain competitive. For a list of our principal competitors, see the "Competition" section of Item 1 of this Form 10-K.

We cannot assure future growth will be achieved.

We believe that our ability to open additional stores at a high growth rate will be a significant factor in achieving our growth objectives for the future. Our ability to accomplish our growth objectives is dependent, in part, on matters beyond our control, such as weather conditions, zoning and other issues related to new store site development, the availability of qualified management personnel and general business and economic conditions. We cannot be sure that our growth plans for 2008 and beyond will be achieved. Failure to achieve our growth objectives may negatively impact the trading price of our common stock. For a discussion of our growth strategies, see the "Growth and Expansion Strategies" section of Item 1 of this Form 10-K.

Risks associated with acquisitions may not lead to expected growth and could result in increased costs and inefficiencies.

We expect to continue to make acquisitions as an element of our growth strategy. Acquisitions involve certain risks that could cause our actual growth to differ from our expectations. For example:

- we may not be able to continue to identify suitable acquisition candidates or to acquire additional companies at favorable prices or on other favorable terms;
- our management's attention may be distracted;
- we may fail to retain key personnel from acquired businesses;
- we may assume unanticipated legal liabilities and other problems;

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- we may not be able to successfully integrate the operations (accounting and billing functions, for example) of businesses we acquire to realize economic, operational and other benefits; and
- we may fail or be unable to discover liabilities of businesses that we acquire for which we, as a successor owner or operator, may be liable.

We are sensitive to regional economic and weather conditions that could reduce our sales.

All of our stores are located in the Central, Midwest and Southern United States. In particular, approximately 26% of our stores are located in Texas. Therefore, our business is sensitive to the economic and weather conditions of those regions. Unusually inclement weather, such as significant rain, snow, sleet or freezing rain, has historically discouraged our customers from visiting our stores and reduced our sales, particularly to DIY customers.

We depend on certain key personnel to successfully manage and grow our business.

Our success has been largely dependent on the efforts of certain key personnel, including David O'Reilly, Ted Wise and Greg Henslee. Our business and results of operations could be materially adversely affected by the unexpected loss of the services of one or more of these individuals. Additionally, the successful implementation and management of our growth and expansion strategies will depend on our ability to continue to attract and retain qualified personnel. We cannot be sure that we will be able to continue to attract such qualified personnel, which could cause us to be less efficient reducing our sales and profitability. For a further discussion of our management and personnel, see the "Business" section of Item 1 and Item 4a of this Form 10-K and our Proxy Statement on Schedule 14A for the 2008 Annual Meeting of Shareholders, a portion of which is incorporated herein.

The market price of our common stock may be volatile and could expose us to securities class action litigation.

The stock market and the price of our common stock may be subject to wide fluctuations based on general economic and market conditions. The market price for our common stock may also be affected by our ability to meet analysts' expectations. Failure to meet such expectations, even slightly, could have an adverse effect on the market price of our common stock.

In addition, stock market volatility has had a significant effect on the market prices of securities issued by many companies for reasons unrelated to the operating performance of these companies. Downturns in the stock market may cause the price of our common stock to decline. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted against such a company. If similar litigation were instituted against us, it could result in substantial costs and a diversion of our management's attention and resources, which could have an adverse effect on our business.

Sales of shares of our common stock eligible for future sale could adversely affect our share price.

All of the shares of common stock currently held by our affiliates may be sold in reliance upon the exemptive provisions of Rule 144 of the Securities Act of 1933, as amended, subject to certain volume and other conditions imposed by such rule. We cannot predict the effect, if any, which future sales of shares of common stock or the availability of such shares for sale will have on the market price of the common stock prevailing from time to time. We believe sales of substantial amounts of common stock, or the perception that such sales might occur, could adversely affect the prevailing market price of the common stock.

Item 1B. **Unresolved Staff Comments**

Not applicable.

Item 2. Properties .

The following table provides certain information regarding our administrative offices and distribution centers as of December 31, 2007:

Location	Principal Use(s)	Square Footage	Interest
Atlanta, GA	Distribution Center	482,860	Leased (a)
Billings, MT	Distribution Center	109,642	Leased (b)
Dallas, TX	Distribution Center	463,000	Owned
Des Moines, IA	Distribution Center		