

Advanced Auto Parts Inc.

Long | April 25th, 2025

Advance Auto Parts (AAP) is a structurally essential aftermarket distributor undergoing a strategic transition from legacy inefficiency to operational precision. With a sweeping restructuring plan, targeted asset reallocation, and exposure to durable maintenance demand, AAP is positioned for long-term margin recovery and a fundamental re-rating. While markets remain fixated on store closures, management turnover, and execution friction, we believe they overlook three core drivers: restructuring-linked operating leverage, embedded rural market defensibility via Carquest, and non-discretionary tailwinds from aging vehicle fleets and constrained new car affordability. With rationalized distribution, SKU standardization, and an underappreciated footprint advantage in ex-urban America, AAP represents a high-conviction turnaround embedded with latent pricing and earnings power.

AAP's restructuring is both comprehensive and deliberate: warehouse consolidation (from 46 to 14), closure of 700 underperforming stores, and investment in "Uber-like" last-mile delivery and SKU optimization are designed to mirror the supply chain architecture of best-in-class peers like O'Reilly (ORLY) and AutoZone (AZO). Management is shedding inefficient volume in favor of unit economics, seeking to restore gross margin and reestablish earnings credibility. While short-term noise remains, we believe normalized SG&A and inventory efficiencies will enable EBITDA margin convergence with peers over the next 24–36 months.

Simultaneously, Carquest represents a deeply underappreciated asset: its presence in rural and tertiary markets provides high-frequency demand from pro repair shops and DIFM customers underserved by national chains. Independent franchisees foster community loyalty and customer stickiness, while physical locations can be tactically repositioned as micro-distribution nodes for same-day or 24-hour part fulfillment. The Worldpac divestiture removes international complexity and allows reinvestment in these defensible, high-turn geographies.

From a macro lens, tailwinds are compounding: vehicle age in the U.S. now exceeds 12.5 years, new car affordability is structurally impaired due to interest rates and elevated sticker prices, and tariffs further incentivize long-term ownership. This extends the maintenance cycle and benefits distributors with wide SKU availability and proximity coverage. AAP's exposure to aging car populations and pro-channel intensity positions it as a direct beneficiary of these durable themes.

Industrials Coverage

Price Target: \$57.00
Upside Potential: +79%
52 Week High: \$76.31
52 Week Low: \$30.31
YTD: -48.3%

Complementing the fundamental view is a signal from **Shelke Global Research's VANTAGE Model**, our proprietary multi-factor framework engineered to isolate dislocations between market narrative and intrinsic enterprise value. AAP has recently triggered internal alerts — indicating statistically significant divergence in sentiment vs. fundamentals — placing the name in a high-probability inflection zone. While inputs remain confidential, VANTAGE synthesizes behavioral, technical, and structural indicators to identify moments where risk is mispriced. This alignment reinforces our conviction that the current equity discount fails to reflect AAP's medium-term earnings trajectory or strategic repositioning.

Commentary on Valuation:

At ~\$32, AAP trades well below intrinsic value implied by normalized mid-cycle margins and peer comparable. Assuming \$6.50 in NTM EPS and applying a 9x EV/EBITDA (in-line with AZO/ORLY historical troughs), we arrive at a \$57 PT — supported by supply chain rationalization, SG&A optimization, and operating leverage as store productivity improves. We believe the current multiple reflects transient distress rather than forward earnings power.

Catalyst on Valuation:

Q2/Q3 Earnings Commentary on Execution and Margin Path

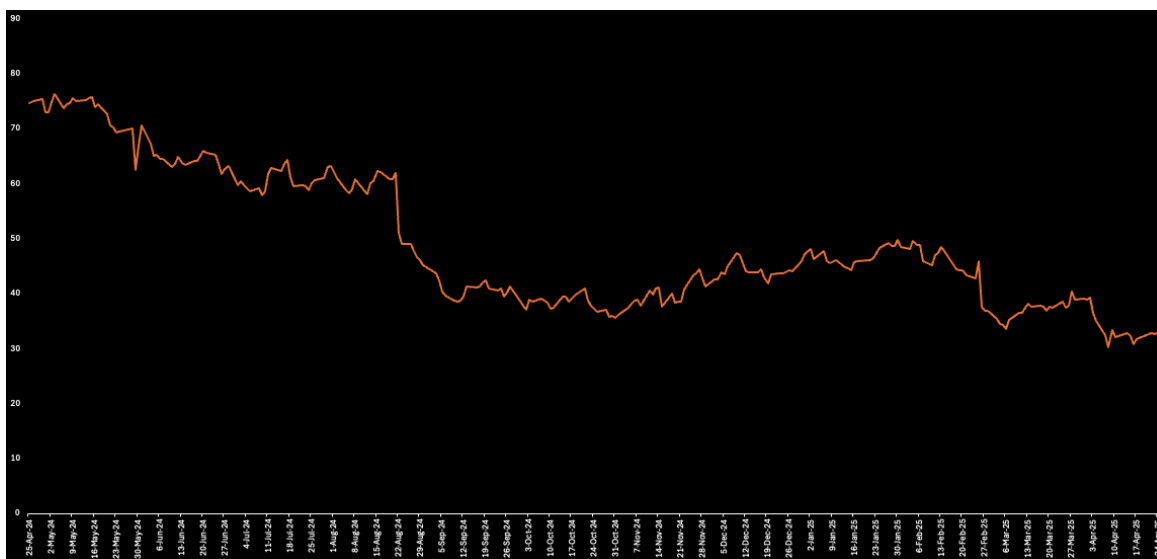
Management clarity on cost capture from DC consolidation and SG&A run-rate normalization could de-risk the restructuring narrative. Early signs of EBITDA margin recovery — even incremental — would validate the turnaround trajectory and support multiple expansion.

Expansion of Pro Customer Penetration and DIFM Metrics

AAP's growing DIFM segment and high-frequency pro customer base offer a resilient revenue stream. A step-up in share of wallet, attach rate per order, or improved fulfillment metrics (via Carquest micro-hubs) would signal long-term defensibility.

Behavioral Confirmation of Non-Discretionary Auto Spend

High-frequency economic data continues to show elasticity in vehicle maintenance spend relative to macro conditions. Further strength in parts categories like alternators, batteries, and brake systems — paired with stable Miles Driven metrics — would affirm the resilience of AAP's end markets.



While the opportunity in Advance Auto Parts (AAP) presents asymmetric upside, we acknowledge several key risks that warrant monitoring. We believe these risks are adequately mitigated and reflected in current market pricing, but they remain essential to the long-term thesis:

- **Execution Risk from Restructuring**

The \$960M+ restructuring plan is expansive and complex, involving consolidation of distribution centers, store closures, and SKU harmonization. Execution missteps — including cost overruns, disruption to store operations, or organizational misalignment — could delay margin recovery and damage investor confidence.

► *Why it's chosen:* This is the most immediate and material risk given the ongoing transition and capital intensity of the plan.

► *Mitigant:* AAP is following a proven playbook used by AutoZone and O'Reilly. Investor expectations are already low, and early signs of simplification (DC reduction from 46 to 14) provide a roadmap toward long-term efficiency.

- **Brand Erosion or Customer Churn Post-Closures**

The closure of ~700 stores could lead to short-term revenue attrition or reputational damage if legacy customers feel underserved.

► *Why it's chosen:* Store closures inherently reduce physical presence and can weaken brand perception in local markets.

► *Mitigant:* The Carquest franchise model, particularly in rural and ex-urban markets, preserves brand trust and localized loyalty. Independently operated locations tend to maintain community connections and reduce churn risk.

- **Supply Chain and Geopolitical Volatility**

As a distributor reliant on a global network of suppliers, AAP remains exposed to disruptions from trade tensions, tariffs, and freight volatility.

► *Why it's chosen:* Auto parts rely on global manufacturing footprints; sourcing risk is material amid geopolitical instability.

► *Mitigant:* SKU unification, regional distribution hubs, and third-party logistics investments increase sourcing flexibility and reduce overdependence on any single node in the supply chain.

Bottom Line

Advance Auto Parts represents a textbook asymmetry: limited further downside priced in, with high-return optionality on turnaround execution and structural demand tailwinds. If management can deliver even partial margin normalization and working capital improvement, we see a credible path to both earnings growth and multiple re-rating. The current setup — a combination of pessimistic sentiment, visible self-help levers, and secular tailwinds — fits our VANTAGE Model's high-conviction dislocation framework.

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