FINAL TRANSCRIPT

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PRESENTATION

Operator

Welcome to the Advance Auto Parts first-quarter 2011 conference call. Before we begin, Joshua Moore, Director of Finance and Investor Relations, will make a brief statement concerning forward-looking statements that will be made on this call.

Joshua Moore - *Advance Auto Parts, Inc. - Director of Finance and IR*

Good morning, and thank you for joining us on today's call.

I'd like to remind you that our comments today contain forward-looking statements we intend to be covered by, and we claim the protection under, the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Forward-looking statements address future events, developments or results and typically use words such as believe, anticipate, expect, intend, will, plan, forecast, outlook or estimate, and are subject to risks, uncertainties and assumptions that may cause our results to differ materially, including competitive pressures, demand for the Company's products, the economy in general, consumer debt levels, dependence on foreign suppliers, the weather, business interruptions and other factors disclosed in the Company's 10-K for the fiscal year ended January 1, 2011, on file with the Securities and Exchange Commission.

The Company intends these forward-looking statements to speak only as of the time of this conference call and does not undertake to update or revise them as more information becomes available.

The reconciliation of any non-GAAP financial measures mentioned on the call with the corresponding GAAP measures are described in our earnings release and our SEC filings, which can be found on our website at advanceautoparts.com.

For planning purposes, our second-quarter earnings release is scheduled for Wednesday, August 10, 2011, after market close, and our quarterly conference call is scheduled for the morning of Thursday, August 11, 2011. To be notified of the dates of future earnings reports, you can sign up through the Investor Relations section of our website.

Finally, a replay of this call will be available on our website for one year.

Now let me turn the call over to Darren Jackson, our Chief Executive Officer. Darren?

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Thanks, Joshua. Good morning, everyone. Welcome to our first-quarter conference call.

First, I'd like to thank our 52,000 team members for their hard work and dedication to serving our customers.

We entered this year with considerable momentum and expect that 2011 would be a continuation of a very strong 2010. Our Service Is Our Best Part plan was very ambitious, including the launch of our national advertising campaign, the Company-wide rollout of our new district and commercial leadership model, and the restart of our wave efforts.

We made these decisions and begin implementing them in the fourth quarter of last year, anticipating that our momentum and exceptional industry dynamics would position us for a strong first quarter and fiscal 2011.

Our momentum and overall performance proved to be different than we expected. We highlighted that during our Q4 conference call in mid-February, the change in momentum and the volatility principally driven by weather.

We shared with you that we expected our Q1 comparable sales growth to be flat to up low single digits. Our comparable-store sales were 1.4% for the first quarter of 2011. While they were in the range, quite frankly, we expect better topline and bottom-line outcomes.

That being said, our first quarter demonstrated the great resolve of our team as we achieved record customer satisfaction and team member engagement scores for the quarter. This bodes well for the future.

However, our first quarter also highlighted the short-term bumps of accelerating the pace and the breadth of change in pursuit of the long-term goals to differentiate ourselves and ultimately win with the customer.

The fundamentals of our business continue to be strong, and we benefit from the structural advantages of our industry. Advantages include the average age of vehicles, constrained new car sales and a fragmented commercial market.

We continue to see opportunity for us to become a more differentiated, fully integrated service model focusing both on DIY and commercial customers. To that end, our first quarter reinforced to us that our goals and objectives are the right ones to lead in service and to provide our customers with Superior Availability.

Simply said, we are committed to providing our team the tools necessary to increase productivity and engagement, which will allow them to serve our customers better than anyone else.

We will continue our efforts to provide the products and services necessary to help our customers succeed. However, our slow start to the year has caused us to step back and examine our current business environment, which has been quite volatile. For sure, our prior-year sales comparisons are challenging. The weather has not cooperated, and the sharp rise in fuel prices will cause challenges to both the consumer and business.

We have adapted our plans to this change changing context. However, our strategic and financial commitments have remained the same for 2011. These commitments include delivering our earnings outlook for the year of $4.60 to $4.80 per share and improving our customer satisfaction and our team member engagement. Our path to those outcomes will flex, though.

Through the balance of the year, we will be making appropriate adjustments to the pace of change, initiatives and cost structure aimed at making us more efficient while delivering our service promise. Ultimately, we will continue on the path to greater service levels and profitability over the foreseeable future. Mike will discuss these changes later in the call.

Our Service Leadership and Superior Availability strategies will continue to guide and prioritize our focus for the balance of 2011 and beyond. The principal initiatives driving our margin improvements, sales growth and service-level improvements will sound familiar. We will continue to invest and focus on commercial, resulting in double-digit comp sales, which is our Q2 trend right now.

We will elevate our service and foundational excellence as a top priority to improve our in-store service and execution, resulting in higher customer satisfaction and productivity. We will continue to increase our availability and expand our product offerings and profitability.

We will continue to communicate Service Is Our Best Part promise, but at a more targeted and more cost-effective medium to reignite our DIY growth.

And finally, we will ensure the appropriate pacing of initiatives that minimizes disruptions to our field and our customers.

Before I close, I want to provide a real-life example of a leader in our Company who embodies Service Is Our Best Part. Her store was one of our early commercial wave stores, which two years ago received more parts pros, trucks, inventory and support from our national salesforce.

Two years later, General Manager Natasha Carter and her team score in the top deciles for customer satisfaction and team member engagement. Natasha was provided with the resources we believe necessary for us to win, and Natasha is leveraging those resources to their fullest. She is serving her customers better than anyone else, inspiring her team, and helping them succeed and grow our business profitably and with integrity. Thanks, Natasha, for bringing Service Is Our Best Part to life and for delighting our customers with dependable and fast service every job, every day.

In closing, I speak for Advance in saying we are never satisfied when we miss our expectations. However, we are confident in our team and our business. We remain focused on delivering our goals, including our full-year earnings outlook.

Now I'd like to turn the call over to Jim Wade, our President, to discuss our Service Leadership strategy.

Jim Wade - *Advance Auto Parts, Inc. - President*

Thank you, Darren, and good morning. As always, I wanted to start by thanking our team as we accelerated our journey to Service Leadership in the first quarter.

During a quarter where business was not where we wanted it to be, our customer satisfaction measures increased again over last year in both our DIY and commercial business, which we believe is a very positive sign as we look to the future.

We also take full ownership of the results we achieved in the first quarter, and I know I speak for our entire team when I say we are fully committed to achieving the expectations Mike has outlined for the remainder of the year.

I will review with you our primary focus areas during the first quarter and how we are approaching the remainder of the year to drive our sales and our profit.

Our total comp-store sales grew by 1.4% in the first quarter compared to 7.7% during the same quarter last year. This was lower than our expectations in both DIY and commercial, although commercial continued to comp strongly relative to the market and was just shy of double digits.

Commercial represented 36.6% of our total sales in the first quarter. All of our operating areas were under our internal expectations as a result of both impacts of unseasonable weather in certain geographic regions such as the Northeast and Mid-Atlantic and the impact of the pace and breadth of change.

In the first quarter, we accelerated our commitment to carry out our Service Is Our Best Part promise through Service Leadership. The core of this focuses on several key areas that will better enable every Advance team member to serve our customers with dependable and fast service consistently in every store, every day. We believe that to provide a great customer experience, we must achieve a new standard of operational and service excellence, and that has to be brought to life for the customer by our store teams.

We've made good progress on each of these key focuses in the first quarter. We increased the number of district leaders, which reduced the number of stores they lead in order to allow them to spend more time in their stores coaching and developing their teams. The changes in districts and the related realignment of our salesforce created some disruptions as the district leaders and salesforce transitioned to different stores and customers.

During the last few weeks, we've been focusing the team so they can be in our stores full time as we head into the busiest season of our year.

Our work to achieve a greater level of consistent foundational excellence in every store has been rolled out across the Company. With greater clarity on the team member behaviors that are most important to our customers and the ability of each General Manager to measure their progress, we believe our customers will see our service levels and our consistency continue to rise.

As we've discussed for the last few quarters, we continue to build on our customer-driven staffing model to ensure we have the right people at the right time to align with customer traffic. These tools provide our team greater visibility to where our greatest opportunities for staffing, quantity and quality improvements exist. It's also enabled us to create more flexibility in opening and closing hours and in staffing core positions based on sales volume.

For the last couple years, we've significantly advanced our tools for accelerating training and development in both parts knowledge and selling skills to better enable our team to find solutions for their customers. This year, we've added more advanced courses based on skill levels of individual team members to further deepen those skills.

As in most businesses, a relatively small number of commercial customers make up a significant part of our sales volume. We continue to be focused on building stronger relationships with our highest-potential commercial customers through the partnership of our store teams and salesforce to visit and support those customers.

Commercial garages always rate timely delivery as the most important attribute they expect from their parts supplier. We can now measure our delivery times in order actually to our commercial customers to ensure we are meeting and exceeding their expectations.

Lastly, we are working to leverage to its fullest potential the record availability of parts that Kevin will describe, along with all the tools his team is providing so that we can find the part and get it to the customer fast.

We believe these priorities focus on the fundamentals of what our DIY and commercial customers expect from us.

Our core part of our Service Is Our Best Part promise is to continue to raise service levels to our customers while making our store model more efficient. Our team is excited about the opportunities we are identifying to leverage our expenses and our investments and look forward to delivering on both parts of our promise.

In regard to new store openings, during the first quarter we opened 37 stores, including nine Autopart International stores. As of the end of our first quarter, our total store count was 3600, including 203 Autopart International stores.

In closing, thanks again to our team as we take the steps to have another successful year by inspiring our teams and serving our customers through our Service Is Our Best Part promise.

Now I'd like to turn the call over to Kevin Freeland, our Chief Operating Officer, to discuss our Superior Availability strategy.

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Thanks, Jim, and good morning. I'd also like to thank the team for their hard work in the first quarter.

I will take a moment to highlight a few of our accomplishments during the quarter, as well as update you on our initiatives to support our Superior Availability strategy.

During the first quarter, our gross profit rate increased 73 basis points versus the first quarter of 2010 and has increased 298 basis points in the past three years. The first-quarter improvement was driven by increases in both front-room and back-room categories resulting from the rollout of our custom mix and price optimization strategies, the strengthening of our category management capabilities, and the impact of our rapidly growing global sourcing capabilities. We saw strong increase in shipments versus Q1 of 2010.

Through the balance of the year, our gross margins will be much more constrained, driven by fuel prices, supply chain investments, high commodity inflation, and an economic landscape that continues to put pressure on our customers, which ultimately limits our ability to fully pass through the product cost increases.

We completed nearly 400 inventory upgrades during the quarter, including upgrades of 60 new hub stores. As a frame of reference, we operated approximately 85 delivery hub stores three years ago versus nearly 240 today. This pace of investment substantially improves our competitive position on same-day part availability.

Combined with the significant increase in overall inventory, we ended the quarter with the highest inventory per store and set Company records for in-stocks, parts coverage and the customer perception of availability.

Our adjusted accounts payable inventory ratio increased to 74.3% at the end of first quarter from 68.9% at the end of first quarter 2010. The increase in our AP ratio continues to be driven by more favorable payment terms, supply chain financing and the timing of inventory purchases. Our owned inventory was essentially flat despite a 21% increase in total inventory from Q1 2010.

Supply chain leverage stalled in the quarter, primarily driven by the heavy inventory buildup, DC inefficiencies as we approach maximum DC capacity, higher fuel costs and supply chain investments. Both the inventory buildup and overcapacity will abate in the quarters ahead, but the fuel costs are anticipated to remain above last-year comparisons, and the costs associated with our supply chain investments will increase throughout the year.

It is expected that supply chain costs will remain a headwind to gross profit for the balance of the year.

We continue to be pleased with our e-commerce platform. We saw significant increase above Q1 last year on our DIY site. That's on top of a very successful performance last year. All metrics continue to improve, including our product assortment, number of site visits and our close rate, driven by site enhancements.

Our commercial site, launched last quarter, continues to grow rapidly as well. Sales increased substantially from one quarter to the next, setting new weekly highs throughout the quarter.

After a year of careful research, we launched our Service Is Our Best Part ad campaign in the quarter, with a unified message to both DIY and commercial consumer groups in multiple languages and across all marketing channels, including TV, radio, direct marketing and in-store signage. We will update you on this effort in the quarters ahead.

I am pleased with the strategic progress our team has made as we continue to focus on providing Superior Availability.

Now let me turn the call over to our Chief Financial Officer, Mike Norona, to review our financial results.

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Thanks, Kevin, and good morning, everyone.

I'd like to start by thanking all of our talented and dedicated team members for their contributions to evolving our service model during our first quarter of 2011.

I plan to cover the following topics with you this morning -- one, provide some financial highlights from our 2011 first quarter; two, put our first-quarter results into context with both our expectations and key financial dimensions that we are using to measure our performance; and three, share with you the actions we are taking to deliver our annual financial outlook for 2011.

Our revenue increased 3.7%, driven by 138 net new stores over the past 12 months and a comparable store sales increase of 1.4% during the first quarter.

This was on top of a 7.7% comp sales increase last year, representing a 9.1% two-year comp-store sales increase. While we've continued to see strong performance in commercial, which was just shy of achieving double-digit comp-store sales growth, our first-quarter comp sales were below our expectations. I will provide further insights on the actions we are taking later in my remarks.

As Kevin mentioned, our gross profit rate increased 73 basis points versus 2010 and continues to be driven by improved merchandising and pricing capabilities and improved parts availability, partially offset by higher supply chain costs. The 73-basis-point increase was on top of a 93-basis-point gross profit rate improvement during the first quarter of 2010.

We continued to expand our margins while maintaining a strong competitive pricing position, as well as mitigating the impacts of the mix pressure of the strong growth of our commercial business, which has a lower gross profit rate.

Our commercial mix represented 36.6% of our 2011 sales versus 33.4% in 2010. While we exceeded our internal expectations for gross profit rate improvement, our gross profit rate will be constrained for the balance of the year, as Kevin previously shared.

Our SG&A rate of 40.7% increased 88 basis points versus the first quarter of 2010, primarily due to increased advertising spend, store labor and fixed cost deleverage due to the modest comparable-store sales increase, partially offset by lower incentive compensation compared to last year.

All-in, our operating income grew 2.1%, and our OI rate decreased 15 basis points to 9.8%, primarily driven by our sales shortfall. However, our diluted earnings per share increased 13.4% to $1.35 versus $1.19 last year. This increase was primarily driven by our share repurchase activity over the past year.

Free cash flow through the first quarter was $152.9 million versus $262.9 million last year. This decrease in free cash flow was driven by the change in owned inventory this year versus first quarter 2010 and higher capital expenditures.

Our accounts payable to inventory ratio increased to 74.3% as of the first quarter of 2011 from 68.9% over the same period last year as part of our continued efforts to reduce our net owned inventory.

During our first quarter, we repurchased 4.2 million shares of our stock for $270 million at an average price of $63.72 per share.

Our earnings release for the fourth quarter of fiscal 2010 reported 1.9 million of these shares that had been repurchased between January 2, 2011, and the earnings release on February 9, 2011. Through the end of our first quarter, we had approximately $352 million remaining on our existing share buyback authorization. These repurchases reflect our view of our valuation and our internal confidence in our Company's ability to grow profitably and to create long-term shareholder value.

During the first quarter, we made progress with our customer satisfaction and team member engagement scores, which we view as leading indicators of future performance. That said, our first-quarter operating and financial performance fell below our expectations.

With our strong 2010 fourth quarter, where we accelerated market share growth and customer satisfaction scores, and with our sequential and accelerating financial and operating performance over the past three years, we expected to build on that momentum in the first quarter.

We did share with you on our fourth-quarter earnings call that we had gotten off to a slower start. While our comp sales increase came in the range we shared with you on our fourth-quarter conference call, they were below our internal expectations we set at the beginning of the year.

We know some external factors outside our control had some impact, such as weather in our markets, gas prices and slower industry growth than last year. We also know things directly in our control played a role in our underperformance. These include minimizing the short-term impacts of structural changes needed to deliver on our service promise, better pacing of our initiatives, better leveraging and delivering the benefits from our previous strategic investments, and execution.

We are confident in our team's ability to execute on these improvements based on our progress over the last three years.

Looking forward, we continue to believe growth, profit and value are the right holistic financial measures. However, our first-quarter results require us to focus in each of these areas to adjust to ensure we maximize the performance of each measure.

Turning to growth, we are pleased with our commercial growth, but our 5% share in a highly fragmented commercial market demands continued urgency to ensure we continue to make this a primary focus, as it is a key driver of continuing to grow our sales per store. We also are closely monitoring the industry growth to ensure we adjust our variable costs in light of our more volatile business environment.

Turning to profit, we have previously shared that we see a pathway to 12% operating margins over the next two to three years. With a large portion of our investments made, and key capabilities built, we are placing a large emphasis on getting to 12% operating margins.

We expect to get there through modest gross profit expansion in areas such as global sourcing, availability and supply chain efficiencies. However, the largest contributor to us improving our operating margins will come from our cost structure.

We started this work last year and shared on our last earnings call that we expected SG&A dollar growth per store to decelerate in 2011 from 2010. We shared that we expected SG&A per store to grow in the range of 2% to 4% in 2011 from 6.7% in 2010. With our performance in our first quarter, we are adjusting our FY '11 SG&A per store growth to be flat to 2%.

To be clear, our work to reduce our cost structure will not take us off course of delivering on our service promise to serve our customers better than anyone else, growing our market share and delivering the expected outcomes we have shared from our Service Leadership and Superior Availability strategies. Instead, it will require a better balance to the pace of change, initiatives and cost reductions that enable our service promise and make us more efficient.

Our cost structure work will be multiyear work in the areas of labor productivity, operational efficiencies, reducing variability in store performance, and reductions in cost driven by a slower pace of investments and a more competitive support structure. These actions will position us to enable growth and improve our profit model.

Turning to shareholder value, we continue to maintain our disciplined approach to capital, as reflected in our return on invested capital, which is now at 18% or 210 basis points over the first quarter last year and represents a 340-basis-point improvement on a two-year basis. We are also pleased with our 74.3% AP ratio and continue to see opportunities to improve our AP ratio to reduce our owned inventory.

We also are focusing on ensuring we are benefiting from our increased inventory per store to meet our customer availability needs and to maximize our cash flow. We are now expecting our comp sales increase to grow in the low single digits for the year. Darren, Jim and Kevin outlined several efforts underway which are designed to focus our Company, reinvigorate our topline performance and continue our strategic progress on delivering our service promise.

We also have adjusted our cost structure and pace of strategic initiatives to position us to leverage SG&A at lower comp levels.

With the adjustments we have made, we still expect to deliver on our previously communicated annual EPS outlook of $4.60 to $4.80.

In closing, while our first quarter was challenging, we are confident in delivering on our annual outlook with the adjustments we are making. We are focused and committed to building an integrated service model to deliver our service promise of Service Is Our Best Part through our Service Leadership and Superior Availability strategies.

Our improved customer satisfaction scores from our first quarter reinforce we are on the right path. We also are committed to making the necessary adjustments to our operating model that are fiscally prudent and that will improve our profit model.

Our talented team members will continue to propel us forward and ultimately allow us to reach our full potential.

Operator, we are now ready for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Gary Balter, Credit Suisse.

Gary Balter - *Credit Suisse - Analyst*

First of all, Darren and team, I just want to congratulate you on doing such a good job on the expense pullbacks that you talked about on the call and keeping it in line to deliver the bottom-line earnings. It's very impressive in this environment.

The question that Kevin touched on and Mike touched on is, could you go into gross margin a little bit more? Like, you talked about how it's going to be subdued to the supply chain. Does "subdued" mean decline, or does it just mean lower growth rate?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, so maybe I will start, and then we can get Kevin to give some color on how it relates to our strategy.

So in terms of our gross profit rate, it's been a great story, as you know, for the last few years. And actually, we overperformed in Q1. And if I link that back, we've been [beginning it to] our availability, our supply chain efficiencies, our merchandising and pricing capabilities.

As we now head into a more volatile environment -- and Kevin will go deeper into it -- but inflation, price competitiveness, supply-chain investments that we've made in our business, we see from here on through the balance of the year our gross profit rate is going to be constrained. And if I link that back to our outlook, if you remember, we said at the beginning of the year that we expect to see modest improvement in our gross profit rate.

We overperformed in Q1, and we still anticipate that for the year we are going to see that modest improvement in our gross profit rate, which would just mean that for the balance of the year, our gross profit rate is going to be constrained in those areas I just outlined.

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Yes, Gary, this is Kevin. To build on Mike's point, we are seeing pretty material commodity inflation, predominantly in oil and steel. So while we've certainly seen price inflation in the past and over the life of the products, our industry is not highly price sensitive, and generally become reflected in retail prices. That's true over the long term, but I think in the short term, we would expect in this economic environment there may be somewhat of a delay in our ability to pass those price increases on to the retail price.

In terms of the supply chain expenses, we were hit from a fuel perspective, just like anyone else that has a material hauling component to their business. And those will actually increase as we go into the back half of the year, as we are making incremental investments into the supply chain.

And then we have an impact that we will be facing throughout the course of the year. Our inventory levels were up materially in the quarter and will moderate their way back down by the end of the year, and that will have somewhat of a headwind as well.

That all said, global sourcing, which is growing dramatically at this point, will continue to grow throughout the course of the year. And our price optimization that we successfully did on the DIY side is deploying as we speak on the commercial side.

So, to Mike's point, I think the numbers that we put up in the last three years are not sustainable through the course of the balance of the year, but we still see a margin increase for 2011.

Gary Balter - *Credit Suisse - Analyst*

Thank you. Just one follow-up. As you look at the comps, and especially on the DIY side, and if you looked at it, how much do you think is weather impacted versus the price of gas? Because gas looks like it's going to be coming back down over the next few months.

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Yes, Gary, this is Darren. What we can see regionally, as we look across the nation, is that our regions look to be hit by 200 basis points for sure in the quarter. If we had all of our stores in Texas, we would have felt better, but we don't. And sometimes regionality helps us; sometimes it hurts us. It worked against us in the quarter, and I know for many on the call that are up there in New York and Boston, you lived through it. It's just a little more challenging.

We could also see in the quarter as we got deeper in the quarter -- and as you'll recall, we have four periods in our quarter -- April was tougher. And that was partly because of gas prices. If we look at it on a two-year basis, though, our two-year trends were okay. So we faced some of our more challenging comparisons in the quarter as we got to the end of the quarter, and we faced more challenging gas prices.

I think the way we thought about it is that this gas thing is just too hard to predict. So we've made an assumption. It is coming down; it has come down a little bit in the last few weeks. But our forecasts going forward are a little more conservative because of that inability to predict some of that gas price.

So we're assuming it's going to be a little higher and adjusting our costs accordingly. And if it turns out to be gas goes lower, it's a win in the supply chain. It should be a win in terms of reigniting DIY sales. And I would rather be on the side of pleasantly surprising on that than having to keep adjusting down.

Operator

Scot Ciccarelli, RBC Capital Markets.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

Darren, you mentioned that April was tougher. Can you help us just with the cadence of the quarter a little bit more? You know, obviously, the quarter started off tough. Can you just kind of give a size of maybe the impact in April? Because, obviously, April was pretty tough for a lot of people on the weather front, and we kind of know your geography, so we understand why you would get hit maybe more than some others.

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Yes. Well, the way I would think about it, Scot, is like a camel's back, is that, as we said earlier that January was really tough. We liked the middle part of the quarter, and the back end of the quarter, to be really frank, is -- our last period was probably our best period last year. We had a terrific finish to the quarter last year. And this year, it was just more challenging.

So that's why I said, I think you have to back up and look at it on a two-year basis. And on a two-year basis, you know what? The back end of the quarter was okay in terms of trend for us, for sure. But in light of record temperatures last year, really strong growth last year, and higher gas prices this year, I think it was just a convergence of events that the back end of the quarter was more challenging.

So the good news is, our comparisons get a little lighter as we go into the second quarter, and, now, that being said, doesn't change the fact that gas is up year over year $0.80-plus in many of our markets.

So, like I said, we're going to have to manage that volatility for sure, make sure that our expenses reflect that, and stay focused. And the good news is our commercial business, as I said in my remarks, had bounced back to double-digit growth again. So we are pleased about that. The DIY thing we're going to have to monitor as we monitor gas prices.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

I guess my question, Darren, is -- okay, so April was a little bit tougher. We know we've seen some results from some competitors, only through March; I understand that. But the delta is pretty sizable. So when I look at that and I hear your comments about gross margin, I'm wondering if you think you might have pushed your price optimization plan maybe a bit too aggressively.

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Kevin?

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Yes, Scot, this is Kevin. We actually have a process where we monitor our prices vis-a-vis our primary competitors. And it is literally down to the individual item and the individual location, so it is highly precise.

And where we were in our price competitiveness this year versus last year, we manage ourselves in a very tight range of proximity to our key competitors and essentially try to shoot for a neutral price position. It's not a prime driver in our industry. And those metrics through the quarter stayed where they have been over the last several years. And so, at least the view that we have of it is -- would suggest that the increases that we've had in margin are from reduction of what we pay for products, not increases in what we charge for products.

Scot Ciccarelli - *RBC Capital Markets - Analyst*

All right. Thanks a lot, guys.

Operator

Greg Melich, ISI.

Greg Melich - *ISI Group - Analyst*

Could you guys go into a little more detail on the inventory increase, the up-21%, and how much of that could be -- sort of break it down into inflation and how much more you are doing global sourcing earlier, getting it on the boat and stuff like that?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes. Thanks, Greg; it's Mike. Maybe I'll start off, and then I will have Kevin link it a little bit to our Superior Availability strategy.

So, first of all, the growth of our inventory has been a concerted effort around growing our parts availability. It's very important in this space, and we've been doing it. And as a link to that is, during the quarter, we opened 60 new hubs. We did 400 upgrades. So, obviously, those require inventory.

Second of all is, if you remember, last year our comparison is probably at the lowest point. So last year, in FY '10 Q1, our inventory grew 3.8% and our sales grew close to 9%. So we were up against a very -- we were up against a lower comparison. And to be honest with you, we had a lot of momentum going into Q1, and we invested ahead -- and we said that we had invested ahead. But to be clear, our inventory has been steadily building. It steadily built last year.

Third is timing. So we are probably at the highest -- just the seasonality of our business, we are at the highest point that we are for the year. We would expect to flex down throughout this year.

And the other thing is, the quality of our inventory -- and Kevin will get a little bit into that -- has never been better. So we feel really good with the quality of our inventory.

And then lastly, and quite frankly, we came a little short on the sales. That magnified the inventory. However, we are pleased with our net owned inventory, which was virtually flat last year. So it didn't cost us a lot.

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Yes, Greg, I would maybe repackage what Mike said into two buckets. There's a temporary element to the 21% increase, and then there's a structural element.

The temporary portion, as Mike mentioned, with your inventory up last year 3.8%, when sales were up nearly 9%, we fell short of inventory. And the customer surveys that we had of availability suggested that we had had an opportunity to pick up even more sales.

So as we went into this year, we planned for -- to ensure that that did not occur. And as everyone has said on the call, sales fell short of expectations. So where we had guessed too low last year, we guessed too high this year.

Those two phenomena account for half of the change in inventory. The other half is we had 157 hubs this time last year. We have 240 this year -- and that's a material increase in inventory per store -- and had 400 upgrades in the quarter, and had material upgrades in the year between those two quarters.

Additionally, sales were up 3.7%. There is an investment that we need to keep up with the rate of sale. Those upgrades and additional hubs and keeping up with the business is about the other half.

So, what we see as we look out to the end of the year is, it's not a 21% year-over-year increase, but something closer to a high-single-digit to low-double-digit increase year over year.

Greg Melich - *ISI Group - Analyst*

Great. And then sort of a bigger-picture question on the SG&A. It's good to see it come -- get it down quickly, given the change in the environment. I'm just curious as to the way you actually execute that. I mean, the organization has been growing a lot the last couple of years. You've had a lot of initiatives. How do you actually get it done in terms of the labor scheduling, whatever projects you have, getting them online? I mean, how quickly can you really change that?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, so, and I think Gary mentioned it -- you know, we are pleased with what we did with SG&A in the quarter. It's our lowest SG&A-per-store growth in the last three years. And when you think about it, this is not a new story for us. I think the first part of our journey, we talked about building capabilities, focusing on growth and returns. And then we said the next part of the journey, which is the journey that we are in now, is to improve our profit model. And our cost structure is an important driver of that.

And you know what? We did a lot of the work last year. We kind of bucketized it into kind of productivity and efficiencies opportunities, variability in store performance, scaling back some of the investments because we've got a lot of them behind us now, and then just getting more competitive with our cost structure for things like occupancy, goods not for resale, and just some discretionary things.

And maybe I will illustrate with an example. So we've been investing ahead in our business for the past three years. So we've invested in parts pros and trucks and commercial programs. And we are getting pretty good now at understanding what the expectation is for our teams to deliver on. And in fact, we've got targets, and we share those targets with our field. And really, we have a lot of confidence in our field's ability to execute on some of those productivity targets, some of those efficiency targets.

So I think we've started the work last year, we feel very confident, and it's also going to be a multiyear journey.

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Maybe to build on that, Greg, is, so just think about three buckets. We would be doing the things you would expect us to do.

I will start with the corporate center here. You know, over the past several years, it has been a heavier investment in places like professional services, whether that's in our IT business or whether that's in our overall parts of the business. And we've just gone in and edited it out.

If you think about our initiatives, as Mike said, as we've looked at the scale of initiatives going forward, it's just clear to us that we better understand that.

In the first quarter, we had many initiatives. We restarted the wave process, new district leaders, all that. It probably cost us a little bit in terms of field rhythm. So we've made a decision to say, let's actually get the most out of those initiatives and edit out some of those things that are certainly things that we believe in long term for the business. But what's most important now is getting the rhythm of the business right. So you can edit costs out there.

Then we've gone into our field organization and looked across the organization. It's very good for -- we have a different set of tools than we did just a year ago to begin to look across hours, rates and the like in our stores, and we've made some edits there.

And so we feel -- I feel, quite frankly, as confident as I've ever felt that we are able to see a flat to 2% SG&A growth.

So, as Mike said, a year ago we wouldn't want to be in a position that we are just -- I will say it this way -- chaotically going in and cutting the expenses of the business. We can go in and more surgically take those costs out, given the work that we did a year ago. And that's in part what's showing up in the first quarter, because first quarter had a lot of those investments. Advertising is the easiest one to see. What you can't see underneath the water line are the edits from the cost structure. And what will become more visible in the upcoming quarters is the fruits of that work.

Greg Melich - *ISI Group - Analyst*

Great, thanks a lot.

Operator

Matt Fassler, Goldman Sachs.

Matt Fassler - *Goldman Sachs - Analyst*

Thanks a lot, and good morning. Just one -- two follow-up questions, actually. First of all, can you talk about the role of incentive compensation in driving SG&A growth last year, and talk about how you anticipate that moderating? And presumably it does as you work through -- as you see the rate of expense growth moderate here in 2011?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Sure. Matt, it's Mike. So, as you saw in our results in Q1, our SG&A deleveraged about 88 basis points. And when you think about that, the majority of that deleverage came from a concerted effort that we shared with you in our brand advertising.

And what was interesting is -- so that's the majority -- what was good is, the other deleverage came in a little bit in payroll because of lower sales -- we weren't able to pull back fast enough -- and some of the fixed cost deleverage. Those two buckets -- the deleverage in labor and the deleverage in our fixed cost structure -- was almost entirely offset by deleverage in our incentive compensation.

So, said differently, in times of heavy growth that we saw last year, incentive compensation is going to be a big driver of SG&A, because -- and we are happy to pay our team members and our leadership team for growth. And in times where we don't grow as much, we are going to leverage, and we actually saw that in our first quarter.

Matt Fassler - *Goldman Sachs - Analyst*

So one would think that something like 2% or 3% of SG&A declines, I guess, year on year, [given] incentive comp offset by some of the other items?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, we don't break it out like that, Matt, but I would tell you the leverage in our incentive comp virtually offset the deleverage we saw in the other buckets, except for the advertising, which was a concerted effort.

Matt Fassler - *Goldman Sachs - Analyst*

And then your thought process for the rest of the year presumably is that the incentive comp rolls off at the same rate, but some of the other expense pressures that led to the deleverage in the first quarter probably abate as well?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, I guess what I would say is, I hope we pay a lot of incentive compensation, because that means we are growing.

Matt Fassler - *Goldman Sachs - Analyst*

Fair enough. My other question is a follow-up I think on Kevin's comment. He talked about the moderation in inventory over the course of the year as being a factor in the expectation of moderating gross margin increases. And I just wanted to get some clarity as to how that works its way through the numbers.

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Yes, Matt. So, essentially, the 21% increase, we had planned an increase year over year, and it was based on an assumption that we had ended last year too low. And we didn't want to walk business, and that we had made and intended to make material increased investments in hubs and inventory upgrades.

As we look out to the tail end of the year, we are obviously not planning to overguess sales, and we did not end last year under stock. We had caught the in-stocks by the end of the year, and were up materially year over year at the close of last year.

So our assumption at this point is, it's relatively easy in our business. Our products don't, per se, go obsolete. It's largely a replacement business. We have new orders that go out each and every week, replenishing the shelves of stores that have had sales throughout the prior week.

And by essentially targeting an assumed softer sales trend for the balance of the year, our assumption is that we will be up modestly year over year and that with each quarter, that 21% will melt its way back down to, as I said, high single digits to low double digits, which is accounting for just the growth in the business, growth in store count, and general improvements in availability that we've been investing in over the last several years.

Matt Fassler - *Goldman Sachs - Analyst*

I totally hear you on how the inventory comes down. I might have misheard, but I thought that you said that one of the factors in the margin expectation related to the rate of inventory growth. If I didn't mishear, I just want to understand how that works.

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

Well, essentially, there's a -- the way that LIFO would work, there's many components that are in there. And to be honest, Mike is the expert in that. But just as a general rule, one of the components in there is that as inventory levels rise, it's a tailwind, and as inventory levels abate, it's a headwind.

Matt Fassler - *Goldman Sachs - Analyst*

Were vendor incentives part of that thought process at all, to the extent that purchasing went your way in Q1? Or is that not part of the equation?

Kevin Freeland - *Advance Auto Parts, Inc. - COO*

The vendor programs are largely based in two areas. They are volume based throughout the course of a year. And then as you hit certain thresholds for large -- any large company in our competitive set, there's also rebates that are available. And those programs have been improving over the years through our category management capability. But generally, directionally, that has been going on for the last several years.

Operator

Tony Cristello, BB&T Capital Markets.

Tony Cristello - *BB&T Capital Markets - Analyst*

I guess one of the questions I want to ask about is, you mentioned a little bit on adding some staffing in terms of district management and general management, and really allowing a less number of stores from a coverage standpoint.

Can you talk about what's going on there, how that looked, how that looks today? And is that then something that you believe will allow for better productivity? Because I feel like cutting the SG&A, I get a little worried that the sales component is going to be negatively impacted at a time where comparisons are even tougher. So, can you just kind of tie that all together for me?

Jim Wade - *Advance Auto Parts, Inc. - President*

Yes, Tony, this is Jim. The way we've looked at that is, over the last two or three years, as we grew store count and we grew as a company, our spans at the district level had gotten larger than they had historically been, and we felt too large for the amount of change that was coming in regard to focusing on raising our service levels and our operational consistency in our stores.

So as we went into the latter part of last year, we made the decision to increase the number of district leaders to lower that span back down to something closer to what I think most businesses that are like us would be used to. And we implemented that at the first of the year.

And as we did that and we put those additional district leaders in place, that caused us to redistrict the remainder of our Company, to fit them in and also cause some change in our salesforce at the same time. So it was a fair amount of change that was going on as that group of new leaders were integrated into the districts.

That's behind us now. Darren mentioned earlier that the last couple of months, we've really focused on, what are we going to do the rest of this year, and how do we enable our district teams and our field teams and our salesforce to focus on driving sales? And I think we are in a good position at this point to do that.

And the way I would think about how does that tie to our productivity opportunities, Mike mentioned earlier, most of what we did in the first quarter to adjust to our sales trend were things that we had had in place and had planned for some time. And we spent quite a bit of time with our field team and our leadership preparing to not only drive service and improve our service level, but also improve our consistency of operation in the store and increase our productivity.

So we don't see those as being separate things that we are doing, but being able to do those consistently and drive our customer experience, which we've seen increase; drive our sales; and drive our productivity at the same time.

So the change in district leaders is a piece of the positioning for us to do those things as we go forward, as opposed to something that was separate or unique.

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, Tony, I just want to build -- share an example, just to tie what Jim says to a comment Darren made around we're being surgical. So, for instance, in Q1, our commercial sales per program increased to $605,000 per store compared to $542,000 per store last year. That's about an 11.5% increase.

That built on a double-digit increase from '10 over '09. So what's happening is, we are using the same resources and getting more productive as people are in their positions longer, as we've added these resources. So, there's an example of how you can do a job of leveraging your SG&A by getting more productive.

Tony Cristello - *BB&T Capital Markets - Analyst*

Okay, that's very helpful. Thank you. And maybe one other question, and perhaps for Darren. You started off, I guess on the fourth-quarter call, and gave the guidance of $4.60 to $4.80. And I'm assuming your internal plans obviously were for better than that, since your first-quarter plans were for better than that.

And I guess what I'm wondering now with what seems to be a little bit tougher sales backdrop and perhaps a bit more gross margin constraint, should we now expect that guidance, while you are still affirming it, is more driven by share repurchase benefit? Or do you think there are other levers that you can still pull outside of what you talked about on the SG&A expense to get there?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Yes, so, Tony, maybe I will start, and Darren, you can build on it.

So let's talk about our outlook. At the beginning of the year, we gave $4.60 to $4.80. We said that sales would be up in the low to mid-single digits. We've adjusted that assumption down now to low single digits, really for a couple of reasons.

One is our performance in the first quarter. It's a little bit choppy as we see ahead, and we've had some tough comparisons, so we've adjusted our sales.

Our margins, we actually haven't changed. We said it would be modestly up. We overperformed in Q1, and we see some -- it will be constrained in the back half of the year. That's kind of why we give an annual outlook.

And then, SG&A per store, we said it would grow at 2% to 4%. Now it's going to grow at 0% to 2%. So that will help; that will offset.

And then the last component will be shares. So I think when we last got together on our Q4 call, since that time, we've bought about 2.3 million shares, which brought us for the quarter to roughly 4.2 million. That added, that incremental sales since Q4 -- I'm sorry, since our Q4 release, adds about $0.10.

So, think about your range of $4.60 to $4.80. $0.10 of that is new shares, so depending on where you were in the range. And the rest of it is, we just moved some of the places that will drive that outlook.

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Yes, I think that's right, Tony. So, what do I say? We are not changing course, but we do have to make a few course corrections. And we've tried to outline that in the call, is that, you know what? I hope we are wrong on the sales going forward, but we thought it appropriate to plan sales more conservatively, for the reasons you mentioned.

And a year ago, as we said, if you think about how we've gone at this business, it's been somewhat, you could say, systematically. We've made terrific gross margin progress and topline progress and even balance sheet progress over the last three years.

We began the process of turning our attention to the SG&A and productivity. And so, what we had to do was just make some different decisions over the balance of the year, and that's what we needed to do.

What I'm actually upbeat about is that, with those decisions, with gas prices if they continue to come down, the focus of our field teams that will all be in their positions as we had begun the second quarter, I think that positions us for some upside in the back half.

So we've made some edits for sure. We've made some course corrections for sure. Mike outlined that $0.10 of our numbers is being helped by stock repurchase. And what you should read into that and our stock repurchase in the first quarter is that our confidence in the future is every bit what it was in the fourth quarter. And you know, in running these businesses, you have to watch the context and make the appropriate adjustments. And we are making the appropriate adjustments without necessarily giving away what we intend to accomplish over the long term.

Tony Cristello - *BB&T Capital Markets - Analyst*

Very helpful. Thank you.

Operator

Dan Wewer, Raymond James.

Dan Wewer - *Raymond James - Analyst*

A question -- so, do-it-yourself market share, I guess a year or so ago we were going through a period where the Company was finding it difficult to maintain share, and then that appears to kind of corrected itself. The results for the quarter just ended suggest that maybe share at best was flat, probably dropped year over year.

You alluded to in your prepared comments some execution issues inside the Company. Could you elaborate on what those were and how that may have impacted your do-it-yourself business?

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Yes, I would frame it this way, Dan -- and Jim alluded to it -- is that when we began this year, one of the decisions we did make is to bring our spans of control down for our district leaders. And then, it was purposeful as we think about delivering on a service promise, one of the things is, our spans did grow.

When we did make those changes, you could say, well, you increased your district leadership team by just under 20%. But what it does is it has a multiplying effect, because you end up almost redistricting the Company, and you change relationships. And that bumped into our commercial relationships as well.

And there's never a perfect time to make these changes, but coming out of the fourth quarter, there was quite a bit of momentum. We started the wave process. We are working with our teams across the nation in what we call our Service Excellence training.

And, you know what? Human beings trying to do the right thing have to rebuild some relationships. And I can't tell you whether it was worth 1 point or 2 points, but what I can tell you going forward as we start the second quarter, our district teams are in place. Our commercial sales teams are in place. And those relationships over the last 30 to 60 days have been building.

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And so we wouldn't change that decision, because for the long term what we look to accomplish is the right thing to do. But there was a little bit of a price I'm certain that we paid in the quarter.

Dan Wewer - *Raymond James - Analyst*

Darren, I know you have a home delivery program, I think in about 600 or 800 stores, that's in place. Do you think that's generating sufficient return for Advance, or is that one of those initiatives that you may have to scale back at this point?

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

I would say this, Dan -- it's one of a handful of initiatives that are just -- I can't stress this enough -- it's just in a test mode. And we've been known to run tests for a year. You know, you see things where you would say, on the one hand, customers give you pretty good marks for it. On the other hand, you have to ask yourself, is it adding to the level of complexity in running a store?

And so, what we've decided is to keep it in test because we are trying to look at both, because it's a marginal return for what you're getting for those home delivery customers. Yes, they like it. The complexity it can cause in the store -- which is already a somewhat complex box for such a 6000 square feet -- I think we will continue to monitor it for the rest of the year or so, and then, like many things, make a decision then.

Dan Wewer - *Raymond James - Analyst*

Okay, great. Thank you.

Operator

Mark Mandel, ThinkEquity.

Mark Mandel - *ThinkEquity - Analyst*

Just a couple of quick follow-ups. In terms of the DIY business, did you see any significant variances by region? For example, out West in the CSK areas, the O'Reilly CSK areas, did you see any underperformance in that territory?

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Jim?

Darren Jackson - *Advance Auto Parts, Inc. - CEO*

Well, our stores in California performed at the same level this year as they did last year. So there is -- what we could see, Mark, is that, as I said in my opening comments, there is a regionality to our business, for sure. And clearly, whether it was our Texas markets, which certainly outperformed our Northeast markets, for the reasons we talked about earlier in the call, were very tough. And they tend to be some of our stronger markets.

And we can look at the data and just know that the volatility in part was principally weather related. One of those markets had its driest period in a long, long time, and one of those had their more challenging weather conditions. So, you can bet we can see some of that in the market.

THOMSON REUTERS

So, regionality certainly played a role in it. And as I said in my earlier comments, we made some changes in the business for the right long-term reasons that created some instability in the short term. But we think that district leadership model is the right model, and, you know what? There will be benefits ahead from having that tighter span of control.

Mark Mandel - *ThinkEquity - Analyst*

And then a quick question for Mike on the interest expense line. It came in certainly higher than I was modeling. And I assume that that's a function of the share repurchases and the inventory build. Mike, what kind of guidance can you give us for the duration of the year on that line item?

Mike Norona - *Advance Auto Parts, Inc. - EVP and CFO*

Actually, it had nothing to do with the inventory build, and we have a little bit more debt than last year.

It's the timing of our cash flow and when we bought those share repurchases. We had $130 million into our revolver, $130 million into our revolver. More debt, that's what caused the difference. And we don't break out interest going forward, but I think you would expect -- what I will say is, our free cash flow outlook that we've given, we are sticking to that. I think we said it will be a minimum of $300 million.

Mark Mandel - *ThinkEquity - Analyst*

Okay, thanks a lot, and good luck.

Operator

Thank you. And that is all the time we have for questions. I will turn the call back to management for any final comments.

Joshua Moore - *Advance Auto Parts, Inc. - Director of Finance and IR*

Thank you, Wendy. And thanks to our audience for participating in our first-quarter earnings conference call. If you have additional questions, please call me, Joshua Moore, at 952-715-5076. Reporters, please contact Shelly Whitaker at 540-561-8452. And that concludes our call. Thank you.

Operator

Thank you. That concludes our call today. You may now disconnect. Thank you for joining us.
