EZCORP, Inc., Q1 2023 Earnings Call, Feb 02, 2023 (EditedCopy)

TEXT version of Transcript

Corporate Participants

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  EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer

* Timothy K. Jugmans

  EZCORP, Inc. - Chief Financial Officer

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* Alexander Villalobos-Morsink

  Jefferies LLC, Research Division - Equity Associate

* Brian Christopher McNamara

  Canaccord Genuity Corp., Research Division - Analyst

* Brian William Nagel

  Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst

* John Hecht

  Jefferies LLC, Research Division - MD & Equity Analyst

Presentation

Operator [1]

Good morning, ladies and gentlemen. Welcome to the EZCORP First Quarter Fiscal 2023 Earnings Call. [Operator Instructions] A reminder, this call may be recorded. I'd now like to turn the conference over to Jean Marie Young, Investor Relations with Three Part Advisors. Please go ahead, Jean.

Jean Marie Young [2]

Thank you, and good morning, everyone. During our prepared remarks, we will be referring to slides which are available for viewing or download from our website at investors.ezcorp.com.

Before we begin, I'd like to remind everyone that this conference call, as well as the presentation slides, contain certain forward-looking statements regarding the company's expected operating and financial performance for future periods. These statements are based on the company's current expectations. Actual results for future periods may differ materially from those expressed due to a number of risks or other factors that are discussed in our annual, quarterly and other reports filed with the Securities and Exchange Commission. And as noted in our presentation materials, and unless otherwise identified, results are presented on an adjusted basis to remove the effect of foreign currency fluctuations and other discrete items.

Joining us on the call today are EZCORP's Chief Executive Officer, Lachie Given; and Tim Jugmans, Chief Financial Officer. Now I'd like to turn the call over to Lachie Given. Lachie?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [3]

Thanks, Jean, and good morning, everyone. Our team continues to consistently execute on the 3-year strategic plan put in place at the end of fiscal 2020. We began fiscal 2023 with an excellent first quarter. I want to thank our passionate, engaged and highly productive team members for their continued focus on operational excellence, which continues to drive our very strong financial results. Pawn loans outstanding, the key driver of our business, were $208.6 million at quarter end, an 18% year-over-year increase and our highest ever result for Q1. And merchandise sales were up 14% to $161.9 million, the highest ever quarterly sales result.

Beginning on Slide 3, we are a global leader in pawn broking and pre-owned and recycled retail. We operate 1,186 stores in the U.S. and Latin America, with strategic investments in adjacent businesses, which expand our geographic footprint worldwide. Because our diverse store base, we offer 2 core products to our consumers: We make pawn loans and we sell secondhand goods. The macroeconomic environment continues to be a challenge for our customer base. Inflationary pressures and economic uncertainty drive increased demand for pawn loans. The demand for secondhand goods also increases as consumers increasingly seek value for money and environmentally responsible alternatives. Our goal is to provide the best, most convenient experience for our customers through continuous innovation, while positively impacting the environment and the communities in which we serve.

Moving on to Slide 4. We continue to embrace People, Pawn and Passion as our core operating theme. We know that our engaged team drives our success, so we are committed to investing in recruitment, retention and incentivization. We strive to be the best option for our customers by providing outstanding customer service and attractive and well-positioned store footprint, a differentiated digital platform, a proprietary POS system, and importantly, ample liquidity from our balance sheet to provide pawn loans across all of the regions in which we operate.

Slide 5 sets our progression towards our 3-year strategic goals. I believe we have the most passionate, productive and committed team in the industry and we continue to find new ways to motivate and retain them. In the U.S., we implemented no-cost team member health insurance and in Mexico, we reinstituted the employee savings program. This has been extremely well received by our operating teams. We are also committed to enhancing our customers' experience by growing and improving our points-based loyalty program.

Turning to our key financial themes for Q4 on Slide 6. As mentioned, PLO, the most significant driver of revenue and earnings, was up 18% year-over-year, with an associated 21% increase in PSC. Total revenue for the quarter was $261.6 million, up 18%. EBITDA was $37.9 million for the quarter, up 22%.

PLO on a same-store basis continues to remain strong above pre-COVID fiscal year 2019 levels and same-store sales and merchandise sales gross profit are at record levels. We have seen aged inventory increase in LatAm and are focused on better execution in that region to address this issue. The slight increase in cash on the balance sheet was a result of the net cash proceeds from the convertible debt refinancing, offset by an increase in earning assets, acquisitions of new stores, strategic investments and share repurchases.

On Slide 7, EBITDA margin was 13% for the last 12 months ending December 2022 versus 11% in the last 12 months ending December 2021, with the U.S. driving the growth. Recently, EBITDA margin has flattened due to inflationary pressure affecting the business.

On Slide 8, we talk about strengthening our core, with a primary focus on people and systems. We are focused on recruitment, retention, inclusion and incentivization to ensure that the team remains highly engaged. Improving the bench strength of our field team continues to be a major priority.

In addition, we continue to invest in technology and believe we are leading the industry in this area. All in-house applications have been transitioned from co-location data centers to the cloud. Our technology and digital initiatives are improving our operational efficiency at the store level and the ease of use of our products and services to our customers. We have now deployed store network and system upgrades in 80% of our stores to improve the stability and support digital initiatives.

With Max Pawn, our first venture into the luxury pawn broking business, we enhanced e-commerce capabilities by migrating to a secure, mobile-ready and user-friendly platform and have a full e-commerce offering that we tested in that business.

On Slide 9, innovation and growth is the third pillar of our 3-year strategy and we continue to execute our plan. Our EZ+ Loyalty Program has over 2.4 million customers enrolled versus over 1.9 million last quarter, showing an increase of 26%. We also collected $11.8 million in online payments this quarter, up $6.6 million from the first quarter of fiscal 2022. Adding points earned, balance and account QR to our physical receipts and bonus points, campaigns increased visibility, enrollment and transactions.

We received more than 15,000 Google reviews this quarter, averaging 4.9 stars in the U.S. and Latin America. Website visits for the main brands are up 35% from the previous quarter and we believe we are attracting new customers by making shopping more convenient.

From an inorganic perspective, we acquired 9 stores in the Houston area. We bought the country's leading luxury pawn store in Las Vegas and opened a second store there this week. Both of these acquisitions have started very well from an operating and financial perspective. We also invested an additional $15 million in preferred equity and $15 million in debt into Founders, which purchased additional ownership in SMG. This capital was used by SMG to complete the 100% acquisition of La Familia Pawn, which operates 53 stores in Florida and Puerto Rico, where it is the market leader.

In addition, we opened 2 de novo stores in Latin America. We continue to be disciplined in evaluating acquisition opportunities and the pipeline remains robust. We increased our stake in CCV from 41.6% to 43.7% during the quarter. After receiving a cash dividend from CCV for $1.8 million, our net cash outlay was $300,000.

Slide 10 outlines our ESG highlights for the fiscal first quarter. Our business, by its very nature, makes us a neighborhood recycler and a compelling component of the local circular economy. We are a significant recycler of secondhand goods in hundreds of local neighborhoods. We sold over 1.6 million pre-owned items in the quarter, including toxic consumer electronic items such as computers, TVs, phones, as well as tools, musical instruments, household goods and jewelry, saving them all from landfills. We use sound recycling and e-waste processing in the U.S. We do not use factories, distribution facilities or heavy trucking. Importantly, we provide an essential, simple, regulated and transparent financial resource for those who are underserved by traditional sources.

Diversity and inclusion are a significant focus and we continue to have excellent engagement in both our Black Empowerment and Women's Empowerment Affinity Groups. In addition to the previously mentioned no-cost health insurance for team members in the U.S., we have also implemented Paid Parental Leave and enhanced Voluntary Paid Time Off to support our team members at home and in the communities where they live. I would now like to turn over the call to Tim Jugmans, our CFO, to provide more details on our financial results. Tim?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [4]

Thanks, Lachie. On Slide 11, we laid out the effects of the $230 million, 7-year convertible debt refinancing on the near-term convertible notes, diluted shares outstanding and cash interest expense. We derisked the balance sheet and enhanced our low cash cost capital base so we can continue to grow.

Slide 12 details our consolidated financial results for the first quarter. PLO ended the period at $208.6 million, up 18% on a year-over-year basis, which is the highest first quarter in EZCORP history. PSC revenue was up 21% over last year, with growth driven by both increased same-store PLO growth and acquisitions. Merchandise sales was up 18% to $161.9 million, our highest quarterly sales results ever, but as expected, margins fell back to 36%, which is within our normal range.

Inventory turnover is strong at 2.8x. It was another great quarter with consolidated EBITDA of $37.9 million, up 22%.

Turning to our U.S. Pawn operations on Slide 13. PLO rose 18% to the highest ever in the U.S. PSC was up 23% year-over-year, primarily driven by higher average PLO growth. On the retail side of the business, merchandise sales were up 16%, with merchandise sales gross profit up 2%, with an expected 500 basis points drop in sales margin. Store expenses increased by 13%, primarily due to labor in line with store activity, and to a lesser extent, expenses related to our loyalty program and rent associated with lease renewals. U.S. Pawn EBITDA for the quarter was $42 million, up 13% on the prior year.

Slide 14 focuses on our Latin American Pawn operations. Segment PLO grew 17% for the first quarter, or 15% on a same-store basis, with the resulting PSC up 15%. Merchandise sales were up 22%, 18% on a same-store basis. Merchandise sales gross profit was up 28% due to increased sales and margin is up 200 basis points. Store expenses were up 20% and 18% on a same-store basis, mainly due to increased labor in line with store activity and to a lesser extent, expenses related to our loyalty program and rent associated with lease renewals. Inventory turnover remained strong at 3.3x. However, aged GM is up 2.9%, which has been driven mainly by the recent acquisitions. The team is focused on improving execution to bring this down.

For the first quarter, Latin America Pawn EBITDA improved by $1.2 million. With the successful placement of a $230 million, 7-year convertible note, we have derisked the balance sheet and are in a stronger position to fund continued growth across our business. We repurchased $7 million of shares during the quarter and $1.9 million of shares in January 2023.

We will continue to execute this program in an opportunistic and responsible way, taking into consideration general market conditions, liquidity and capital needs and the availability of attractive alternative investment opportunities.

Looking forward, on a consolidated basis, we should see PLO levels continue to hit records on a seasonal basis. As we have suggested in prior quarters, we are likely to continue to see gross margin remain at the lower end of our range of 35% to 38% as we remain focused on strong inventory turns and limited aged general merchandise. Also, as we have seen this quarter, store expenses have increased and will do so on a sequential basis as inflationary pressures continue to affect the business. We also expect G&A expenses to increase sequentially for the same reason. We are excited to see our business continue to achieve earnings results above what we had pre-COVID, with a superior operating model.

I will now turn it over to Lachie for a few closing comments.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [5]

Thanks, Tim. In closing, I want to thank our EZCORP team for another outstanding quarter. We are consistently delivering strong operating and financial results for our stakeholders and driving additional inorganic growth through de novo store build-outs, disciplined acquisitions and investments. We strengthened our already robust balance sheet during the quarter and returned capital to shareholders. We are committed to improving the experience for our employees and our customers in an environmentally responsible way. We are excited to continue to execute on our 3-year plan in what is a supportive macroeconomic environment for our business and drive enhanced value for all of our shareholders. And with that, we will open the call for questions. Operator?

Question And Answer

Operator [1]

[Operator Instructions] We have our first question comes from Brian Nagel from Oppenheimer.

Brian William Nagel, Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst [2]

Congrats on another nice quarter. So a couple of questions here. First, I guess, this is probably more for Tim, but just on the margin front. I mean you talked about -- in your script about essentially margins kind of normalizing now and then you gave some longer-term parameters. But as we think about the trajectory of margins from here, can you just help us understand better kind of the key puts and takes and some of the timing there of how this should be realized?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [3]

Yes. Thanks, Brian. The margins definitely have, as you've seen, have come down over a period of time back to this normalized range, which we think operates between 35% and 38%. At the moment, as our customer does come under some pressure, there definitely has been -- we've definitely seen some more negotiation at the store level. And so we believe that it will stay at that lower end of the range for the moment as the pressure continues to mount on our customer base.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [4]

Tim, do you want to talk a little about -- that's obviously gross margin, do you want to talk about EBITDA margin? Is that -- were you wanting to talk EBITDA margin, too, Brian? Or you just meant gross margin?

Brian William Nagel, Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst [5]

I was primarily focused on gross margin, but a discussion on EBITDA margin would be helpful as well.

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [6]

On the EBITDA margin, as we talked a little bit about in -- when we produced our annual results, the -- we will have some pressure this year on -- from wage and inflationary pressures on expenses. And we did see a little bit of that come through in this quarter. We're really comping on last year where we really hadn't taken on much of that inflationary pressures, even though lots of other businesses have had and it's a bit delayed for us. So we'll continue to see a little bit. So there will be some pressure on EBITDA margins as we try and keep expenses under control, but continue to grow the top line.

Brian William Nagel, Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst [7]

That's helpful. And then my second question, I guess maybe longer term or more strategic in nature, but just with respect to the loyalty program, can you talk about just the kind of the consumer acceptance of the program and then what you're seeing as far as the benefits of the business as this continues to sort of say, roll out?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [8]

I think from a strategic perspective, it's incredibly pleasing to see that we've got 2.4 million customers that have signed up. It's been very, very rapid growth. I think there are a lot of benefits to the program for both the customer and for us, much better retention, much better engagement, and that should drive in turn better sales and better margins going forward. But we are just really -- we're a year in and we're only just really starting to track that. So I think we've done a wonderful job in the sign-ups. I think now it's all about maximizing the benefit for both our customers and for us. And I think in coming quarters, we'll be able to comment more on the financials. But I think, strategically, it's incredibly pretty pleasing to see the growth there. Tim, would you add anything to that?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [9]

No, that's -- a very similar comment there, Lachie. It's a great addition. The stores love talking about it and the customers are definitely embracing it.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [10]

More to come there, Brian, on that in the coming quarters.

Operator [11]

We have our next question comes from John Hecht from Jefferies.

John Hecht, Jefferies LLC, Research Division - MD & Equity Analyst [12]

Maybe you -- touch on the recent investment in the Caribbean stores, maybe touch on the accounting of that? And then anything else with respect to the acquisition pipeline? You guys have been pretty active, just maybe get an update on the opportunity set there?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [13]

Yes. Thanks, John. So it was a very active quarter, obviously. We bought 9 stores in Houston. That's really our home base, home market, so right down the middle of the fairway. So that started off really well. As we'd already announced, we've commenced our luxury pawn strategy by buying Max Pawn in Vegas and we opened a new store there this week under that brand, so we're all excited about that. And then the investment in Founders is obviously significant. That has then been in turn invested into Simple, which bought La Familia. That is the market leader in Puerto Rico, which is a really exciting market and has 25 stores in Florida.

So that is now becoming a real scale business, all focused on pawn with a very strong management team that we know well. So we're really excited about that opportunity. And on the accounting, we continue to cost account. It's -- we have a preferred equity return there. And then in the future, it is obviously a potential acquisition opportunity. We feel we're well placed there and the way that we're doing it now, we're very comfortable with the super exciting opportunity given the Puerto Rico leadership position that it has.

And then I think going forward elsewhere, it remains a really robust acquisition pipeline. While we're exploring new markets around the world where there's still plenty of opportunity, I think our bias is to the places where we've got strongest existing management, and clearly, that's in the U.S. and Latin America. So look, it remains robust, lots there to do. It was a really great quarter. But as I say to our team, it's not about doing the deals, it's actually about making them work. So we're very focused now on making those acquisitions work for our shareholders. And I think we're really happy with the progress there, but a robust pipeline and you'll continue to see more from us on that front.

John Hecht, Jefferies LLC, Research Division - MD & Equity Analyst [14]

Okay. That's very helpful. And then maybe touch on -- you touched on the consumer and how it's impacting margins as you want to continue to clear inventory and so forth. But maybe -- I mean -- I guess any thoughts on kind of -- are we kind of getting to the point where we've kind of lapped inflation, so things are stabilizing? Maybe talk about kind of bargain shopping and is that pulling more people in the stores? Or just any kind of way to characterize the overall -- I know the results have been healthy, but maybe anything transitioning in the overall retail environment for you guys, both plus or minus?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [15]

Look, it's a good question. I think on the top line, we're continuing to see kind of unprecedented results in both our pawn loans and our sales. So it's clearly -- the quarter was, as you said, very, very strong in terms of growth and core demand for our products. Where that goes from here, it's difficult to predict, but our expectation is that both of our core products will continue to grow. We're comping -- we're now starting to comp against some pretty fantastic numbers from last year. But I think the consumer is definitely -- you can see in our sales results, they're definitely bargain-shopping. We're -- anecdotally, young people who are much more -- who are very environmentally conscious, seem to be coming to our stores to buy secondhand. So look, we are -- we remain excited and bullish about core demand for those 2 products.

I think on the cost side, as Tim said, we are seeing inflationary pressures hit the business. But those are hitting our customers as well. So with higher rates, higher interest rates, higher inflation, we expect to see continued growth in both of those core products.

Operator [16]

We have our next question comes from Brian McNamara from Canaccord Genuity.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [17]

Congrats on the strong results. A few for me. So your aged inventory was up significantly in LatAm, albeit off a low base. I think you cited an impact from recent acquisitions. But you guys have a proprietary POS system that should help with potentially mispricing loans or goods. I guess my question is, do you expect, over time, for your merchandise margins to improve structurally closer to what your larger peer earns?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [18]

Tim, you want to take that?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [19]

Yes. Thanks, Brian. So yes, the recent acquisition, especially in Cash Apoyo Efectivo, is really a lot about training and how to use the system. We did have a little bit of turnover in that acquisition. And so it's taken a little bit longer than expected to get them fully embraced on how to use the system. So we feel confident about that number coming down over time.

From a margin perspective, we do run a little bit different business to our competitor. We do focus a little bit more on the lending side and they focus a little bit more on the retail. But overall, we do expect that we will continue to try and maximize the return from the goods that come in, whether that is trying to get a little bit more out of the PSC or a little bit more out of the margin, it depends on the customer.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [20]

Got it. And then just on store expenses, you had kind of broadly spoke about inflationary pressure. Store expenses per unit were up pretty significantly in Q1. Should we model kind of similar growth rates for the balance of the year? Or how should we kind of think about that, if you could provide a little more color?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [21]

Yes. Obviously, that we're -- comping against Q1 last year, where there was no real effect on inflation yet. If you look back at Q4 last year on a sequential basis, you definitely could see some of that inflation coming through. And so on a sequential basis, we expect to continue to see some lift in expenses, but not -- that's a better way to look at it rather than on a comping basis. The major reasons are we've hired a number of people. We were very short staffed a year ago. So definitely a lot more people in our stores supporting the extra transactions that are going on. And obviously, there's been some wage inflation and some change in laws in Latin America are pushing wages up as well.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [22]

Got it. And just one last one for me on the rewards program. I think you have about 2,000 members per store now, which is an incredible number a year in. How many of those members are actually "active"? I mean if you just look at your online payments per member, it's down quite a bit, but I know that's probably not the way to look at it, but like -- I guess what I'm trying to get at is like what percent of your customers are regulars versus those that come in more episodically? And how should we think about maybe the longer-term opportunity about how high those memberships can go?

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [23]

Tim, do you have that number at hand?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [24]

Those numbers are -- those numbers are -- because of the program has only been in effect for a short period of time, we're still working through on exactly what we're going to be calling active versus inactive. Basically, those are all people that have done a transaction within the last year, which we would call -- which we generally call an active customer.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [25]

Any commentary on like the upper bound of that? I mean I think it's -- the recruitment in and of itself has been tremendous. I'm just curious kind of what you think the upper bound of the long-term potential range could be?

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [26]

Yes, that is obviously -- we -- this has definitely grown much quicker than we expected. So it's definitely beating our expectations at the moment. So the upper bound, we really haven't talked about that at this stage, but pretty excited about how it could drive additional revenue through the business.

Operator [27]

We have our next question comes from Alexander Villalobos from Jefferies.

Alexander Villalobos-Morsink, Jefferies LLC, Research Division - Equity Associate [28]

Hey guys, congrats on the strong quarter. Just wanted to see if you could recap real quick just for modeling purposes, the -- just the guidance points maybe for next quarter and for the full year? Just want to make sure we have those in the model and as accurate as possible.

Timothy K. Jugmans, EZCORP, Inc. - Chief Financial Officer [29]

Thanks. So what we -- just to reiterate a couple of points there. We definitely -- we're likely to continue to see PLO on a sequential basis continue to hit record levels. We definitely see the sales margin remaining at the -- at the low end of our stated range of 35% to 38%. Expenses, we think that will continue -- continue to have pressure on expenses and we're likely to see sequential growth on the expense base.

Operator [30]

We currently have no further questions on the line. I will now hand the floor back to Lachie for closing remarks.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [31]

Thank you, Operator. Thank you, everyone, for joining. And again, on behalf of our leadership team, thanking our entire EZCORP team for another outstanding quarter, driving value for our shareholders. So thanks everyone for joining and we'll talk soon. Thanks.

Operator [32]

Thank you. Ladies and gentlemen, this concludes today's call. Thank you for joining. You may now disconnect your lines.