iPic Entertainment Inc.

First Quarter 2018 Earnings Conference Call Transcript

May 15, 2018

CORPORATE PARTICIPANTS

Hamid Hashemi, *Founder & Chief Executive Officer and Chairman of the Board of Directors*

Paul Westra, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Jim Goss, *Barrington Research*

PRESENTATION

Operator:

Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome to the iPic Entertainment Quarterly conference call. At this time all participants have been placed in a listen-only mode and the lines will be open for your questions following the presentation. Please note that this conference is being recorded today, May 15, 2018.

On the call today we have Hamid Hashemi, Founder and Chief Executive Officer of iPic Entertainment and Paul Westra, Chief Financial Officer. And now I would like to turn the call over to Paul Westra to begin.

Paul Westra:

Thank you operator and good afternoon everyone. By now you should have access to our earnings press release which can be found on our investor relations website at investors.ipictheaters.com in the News Release section.

Before we begin, I need to remind everyone that part of our discussion today will include forward-looking statements. These forward-looking statements are not guarantees of future performance, and therefore undue reliance should not be placed upon them.

These statements are also subject to numerous risks and uncertainties that could cause actual results to differ materially from what we expect. We refer all of you to our Annual Report on Form 10-K which was filed with the SEC on May 1, 2018 for a more detailed discussion of the risks that could impact our future operating results and financial condition.

During today's call, we will also discuss non-GAAP measures which we believe can be useful in evaluating our performance. The presentation of this additional information should not be considered in isolation or as a substitute for results prepared in accordance with GAAP. Reconciliations to comparable GAAP measures are available in today's earnings release which is available on our website.

With that, I would like to turn the call over to Hamid Hashemi, Founder and Chief Executive Officer.

Hamid Hashemi:

Thank you, Paul. Good afternoon, everyone, and thank you all for joining the call today. We appreciate your interest in iPic Entertainment, where we are working hard every day to deliver a world-class hospitality experience that is innovative, unique, and cannot be easily replicated at home or elsewhere. I'd like to start with an update on our growth plans and then Paul will review our first quarter results and reiterate our 2018 guidance. I will then conclude with a few additional comments before turning the call over for Q&A.

As you know, we believe that we are still in the very early stage of our growth story; and, in order to take advantage of the significant opportunity ahead, are focused on 4 Key Strategic Initiatives:

- One – Improving existing location profitability;
- Two – Opening new high-returning iPic locations domestically;
- Three – Pursuing international growth opportunities; and
- Four – Expanding our digital growth options.

We believe that executing on these strategic initiatives will meaningfully improve our top and bottom-line results over time and create long-term value for our stockholders.

In terms of improving the profitability of our existing locations, our primary tactic for 2018 will be executing our remodeling program. As we've said before, we currently have two types of seats in our theaters:

- Premium seats that do not recline and where guests go to our iPic Express counter themselves to order their food and drinks;
- And luxurious Premium-Plus seats that fully recline, come with full table service throughout the show, as well as come with a pillow, blanket, and unlimited popcorn.

When given the option between the two seats, our guests overwhelmingly choose Premium-Plus seating by a 4:1 ratio even with the typical seat charge of over $8.

We are now planning for up to five remodels this year, which is up from our original guidance of up to three remodel locations. To-date, we have completed the remodeling of our Scottsdale, Arizona and Pasadena, California locations in April to full Premium-Plus seating and we expect to complete similar remodels at up to three more locations by year-end, including Fairview, Texas; Austin, Texas; and Redmond, Washington.

With two remodels already completed, we now currently have only five remaining locations with Generation I auditorium configurations where about 2/3rds of their seats are Premium and only about 1/3rd are Premium-Plus. With up to three additional remodels completed by year-end, we will then likely have only 2 remaining locations with Generation I auditorium configurations that are expected to be targeted remodels in 2019.

Our Second Key Strategic Initiative is to open new iPic locations domestically. Today, we operate 115 screens at 15 locations in 9 states. As previously announced, with the signing of our Atlanta, GA lease earlier this year, we now have six signed leases in addition to a robust pipeline of another 15 sites where we are in various stages of lease negotiations that put us on target to open up to four locations annually beginning in 2019.

We think there is tremendous whitespace opportunity to expand in both existing and new U.S. markets, and we have invested in our infrastructure through new hires at our corporate office to enable us to continue growing with discipline. Our ultimate long-term goal is reaching 200 locations and some 1,600 screens across the United States. In 2019-through-2021, the majority of our dozen planned openings are targeted to help achieve critical local-market scale in our core markets in Florida, Texas, California and the Tri-State area.

Our Third Key Strategic Initiative is to pursue international growth opportunities. Over the last year, I have made several trips to Saudi Arabia to meet with Saudi government officials as well as developers to discuss the new theater regulations and licensing process. As a result of these in-person meetings and related conversations, we remain confident in the likelihood that iPic will receive a license to operate cinemas in the Kingdom of Saudi Arabia; and, once we obtain proper licensing, we would then expect to be able to potentially open our first iPic theater in Saudi Arabia by year-end. We could not be more excited about the opportunity that lies ahead for us in Saudi Arabia as we expect iPic to become an integral part of the country's Saudi Vision 2030 plan to transform the overall economy towards more recreation and tourism spending.

Lastly, our Fourth Key Strategic Initiative is to increase our digital growth options, with the goal of growing revenues associated with customer memberships and corporate sponsorships at a faster pace than our four-wall revenues. Earlier this year we created four classes of membership to help achieve this goal.

Our first level of Silver Membership has no cost and allows guests to purchase tickets online and enables us to market one-on-one with these guests. Our next three levels of Membership, called Gold, Platinum, and Elite - entail a $29/year cost and enables guests to, among other things, access tickets ahead of the general public and to start earning points and one-of-a-kind benefits that are more generous as spending levels increase.

A key part of our plan to grow membership revenues is by greatly expanding the value offering to paid members by providing them with more one-of-a-kind deals and free offerings from our branded partners.

Over time, we expect to materially expand both the quantity and quality of special offers and giveaways to our members. By doing so, the financial value of their annual membership fee will continue to grow far above the current $29 per year membership fee.

Moving on to our efforts to grow our sponsorship revenues; our primary focus in 2018 will be on our iPic Life content – which is a 20 minute filmed segment that plays on the theater screen before the previews start – and where we showcase some of our partner brands and products as well as our latest menu dishes. The show is a cross between Entertainment Tonight and the Food Network, and it is where our current sponsorship partners include luxury brands like Louis Vuitton, Lexus, and Burberry, as well as Google, M&Ms and many more.

Both in 2018 and beyond, we think that there a meaningful opportunity to grow this revenue stream. This is because there are many co-branding partners that are attracted to our large and growing membership base, which has very favorable demographics – including 60% female and average household income of about $120,000.

So, as you can see, we are in the very early stages of our growth story and are laser focused on executing on our four strategic pillars in order to capitalize on the significant opportunity ahead. We are committed to expanding our presence both domestically and internationally and leveraging our membership network and brand strength through revenue-driving sponsorships and partnerships.

With that, I'd like to now turn the call over to Paul to provide more details on our financial results.

Paul Westra:

Thanks, Hamid.

Our first quarter performance was in-line with our expectations and we are on track to achieve our full year outlook. Here are financial highlights for the three month period, which ended on March 31st, 2018.

Total revenue for the first quarter increased +4.7% to $37.3 million, primarily driven by the addition of one new location in May of 2017 in Dobbs Ferry, NY. Additionally, our Other Revenue line, while small, increased +72% in the first quarter driven by higher membership revenue that, as Hamid mentioned, is part of our plan to grow digital-related revenues at a faster rate than base revenue.

Comparable-Store sales for the first quarter decreased 5.1%, compared to a box-office industry decline of 2.0%. Our underperformance versus the industry was primarily due to 2.5% of lost capacity as a result of screen closures during our two remodels that were completed in April as well as from other weather-related impacts to our Northeast locations. Additionally, we continued to experience below-industry performance from our five remaining Generation 1 auditorium locations; but, importantly, our Generation II and III locations again out-performed the industry on a comparable-store basis in the first quarter of 2018 by over 200 basis points.

Store-level EBITDA, a non-GAAP measure, decreased $600,000 to $3.3 million in the first quarter, with the decline due to the deleveraging associated with our negative comparable-store sales, higher labor and other operating expenses, which was partially offset by lower cost of goods sold.

Digging into each of the cost line items a bit deeper:

- On Total Cost of Goods Sold, we experienced a year-over-year decline of -100 basis points to 31.5% driven by lower costs for theater-related revenue driven by an increasing revenue mix of non-traditional revenue and positive film-slate changes. This decline was partially offset by food-and-beverage costs increasing +10 basis points year over year to 27.4% as a percent of applicable revenue as menu-price increases and greater efficiency was slightly more than offset by input cost inflation. For the full year, we expect to achieve leverage on the overall COGS line.
- On the Labor line, we saw a +140 basis point increase year-over-year to 28.4% largely due to deleverage from negative comparable store sales. However, for the full year of 2018, we expect our labor cost percentage to improve versus 2017, driven by the combination of predicted positive same-store-sales for the remainder of the year and from the beneficial impact of our new labor scheduling module that we rolled-out in March.
- Our Occupancy Costs for 1Q18 were 12.5% vs. 12.3% last year, with the +20 basis point of increase driven by the deleverage from negative comparable store sales, partially offset by lower occupancy costs at our newer locations. For the full year of 2018, we expect our occupancy costs to be roughly comparable to 2017 as a percentage of revenue.
- On the Other Operating Expense line, excluding the impact of non-recurring items which were $652,000 during the first quarter of 2018 compared to $726,000 last year, Other Operating Expenses increased by +160 basis points in the first quarter of this year primarily due to investments in temporary stages for our live show initiative and to a lesser extent, from fixed operating cost deleverage that was incurred during screen closures for the two remodels. During the first quarter of 2018, given positive guest response, we accelerated the number of live shows to 81 events - compared to 30 events during the fourth quarter of 2017. We now plan to add a permanent stage to our Fulton Market location this summer, and will be targeting additional locations for potential permanent stages throughout the year; and, going forward, all new iPic locations will have a permanent live stage. For the full year of 2018, we expect other operating costs to be roughly comparable to 2017 as a percentage of revenue.

Moving now further down the income statement, Total Adjusted EBITDA, another non-GAAP measure, decreased to a loss of ($1.2) million versus an Adjusted EBITDA profit of $41K in the first quarter of 2017. Note, we expensed $8.6mm of stock-based compensation during the quarter that was mostly related to the IPO and therefore non-recurring.

Going forward, we continue to believe that we have the key strategic initiatives in place to drive meaningful top and bottom line year-over-year improvement as we look to leverage our unique and disruptive offering in pursuit of becoming America's premier entertainment destination – which, we believe will lead to per-store sales and profit growth in 2018 and beyond.

And today we are reiterating our full-year 2018 financial guidance, where:

- We expect total revenue growth of +3% to +7%.
- Comparable-store sales growth in the range of 0% to plus +5%.
- Store-level EBITDA of $17.0 million to $18.0 million.
- An Adjusted EBITDA loss of between $1.5 million and $0.5 million.
- And net capital expenditures of between $20mm and $25mm, including the remodel of up to five Generation I iPic locations.

Let me remind you of some important metrics that underpin our 2018 guidance and support our strategic initiatives.

With respect to our Strategic Pillar One: Growing Per-Store Profits: We are in the process of completing up to three additional remodels that will convert the vast majority of seating into our latest generation Premium-Plus Pod seating. Currently, our remaining Generation One theaters average Premium-Plus seating of only 35%; And compared to Premium seats….. our Premium-Plus seats have four-times higher utilization rates; garner approximately +60% higher average ticket prices; and generate approximately +80% more in food-and-beverage sales per guest.

We expect our second half 2018 results to see some modest net benefit from these remodels but expect the full impact of these remodels to be primarily realized in our 2019 results. In fact, for modeling purposes, assuming we complete five remodels by year-end, we would then expect our remodels to reduce our screen capacity in 2Q18 by 100 basis points, 3Q18 by 500 basis points and 4Q18 by 100 basis points -- all other things being equal.

With respect to Strategic Pillar Two: Growing our US presence: As we've said previously, we now have six signed leases and over 15 additional sites in various stages of negotiations that give us confidence that we will be able to achieve our domestic unit-growth goals of up to four new units per year in 2019 and beyond.

With respect to Strategic Pillar Three: Growing our international opportunity: we have always believed that the iPic concept has global growth potential. In Saudi Arabia, we continue to make significant progress towards opening our first location, including: First, in securing our license to operate in the country; Second, in finalizing our JV Organization with our partner BAS Global Group; Third, in securing predominately local funding for our 10-year growth plan; and, finally, in securing several leases to potentially opening our first Saudi Arabia location by year-end. We plan to provide investor updates throughout the year as we achieve each of these milestones; and we continue to believe that there is a significant growth opportunity for iPic within the Premium retail market of Saudi Arabia with the potential for 25 to 30 iPic locations within the next ten years.

Finally, with respect to our Fourth Strategic Pillar: Expanding our Digital Growth Options: In 1Q18, 47% of our total revenue came from members, which is the highest percentage of member sales that we are aware of within the foodservice and/or theater industries. We believe there is the potential for significant network effect opportunities as we continue to grow in scale both locally, domestically, and internationally – as more units increase the number of iPic members, it would likely lead to more sponsorship interest from brand partners. That, in turn, would then increase the value of being an iPic member driving an increasing membership rate.

With that, I'd now like to turn the call back over to Hamid for closing remarks.

Hamid Hashemi:

Thank you, Paul. We are in the very beginning stage of our growth journey as we execute on the strategic initiatives that we've laid out to successfully grow the iPic brand across the US and internationally. We've pioneered the dining and movie experience and will continue to lead the industry in innovation. I want to sincerely thank all of our team members for their commitment and dedication to iPic. It is because of the hard work and hospitality of our people, that we have such a strong brand with a loyal and growing membership base.

We could not be more excited about the opportunities that lie ahead and we are working hard every day with the goal of delivering long-term profitable growth and increased value to our stockholders over time. We greatly appreciate you taking the time today to follow our story and we looking forward to updating you on our future calls.

With that, operator, please open the lines for questions.

Operator:
At this time we will be conducting a question and answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star key. One moment, please, while we poll for questions.

Our first question comes from the line of Mr. Jim Goss with Barrington Research. Please proceed with your question.

Jim Goss:
All right, thanks. I've got a couple of them to start. One is that you have pretty ambitious growth plans, this four units per year, beyond the renovations you're planning. I'm wondering if you could discuss your financing strategy for the growth. That means the strategy and any limiting elements you think that might get in the way of completing that four unit per year objective.

Paul Westra:

Thanks, Jim. It's Paul Westra here. We have a couple of funding opportunities in front of us. Obviously as we try to grow in Saudi Arabia and overseas, we think that is moving along quickly, is our first goal. Then as the second goal, I think we will then go to a domestic secondary raise to achieve funding.

Hamid Hashemi:

We currently have an existing credit facility with Retirement Systems of Alabama, with a remaining balance of approximately $70 million, which we'll be using to build our domestic plans.

Jim Goss:

Okay, and you itemized it, I think Paul just itemized the four stages of events that needed to take place to get to the opening in Saudi Arabia, including receiving the operating license. I'm wondering, is that a lot to do to get through all those and still have an opening before year-end, and if not, does BAS Global have other partners? I'm wondering, are some of these things going simultaneously, such that some construction is taking place or there are facilities that can be repositioned for your purposes? Just in terms of lead lag of that sort of thing.

Hamid Hashemi:

Sure. To your point, all of these activities—there's three things that needs to happen. One, the first step is getting the license. We've already applied for the license; we're in queue. I was there last week and I had dialogue with the officials. There are no issues as far as we're aware of with our license, it's a matter of processing. Given that this is a new industry for them and all these regulations that they've created and application forms that we filled out—frankly, everything is submitted, and this is all new to them as well.

They're going through the process; I am confident we'll get our license in the market. Our JV agreement with BAS Global, we're on a third or fourth draft of it at this point. I'm confident that will get signed.

Finally, in terms of locations, we've had a number of meetings with various developers. There's a number of sites that are active, one in particular that's an existing space, that's the one that we feel confident we can open before end of the year. That site, we're already doing plans and we've done some design work. All these—we hope that everything will come together with the licensing over the next 30 to 60 days and we'll be able to open our first site before the end of the year. That's the plan right now.

Jim Goss:

Okay. One last one. Branded partners, you mentioned you have—I know you've highlighted a deal with Evian Water, which seems straightforward enough. I'm wondering what other sort of branded partner options you might have? You mentioned Lexus and things like that; I don't see you giving away cars exactly. What sort of other types of things more like the Evian Water are you expecting to materialize?

Hamid Hashemi:

I mean, we have an agreement going back and forth right now with one of the car manufacturers that offers substantial incentive to our members. It's not signed but I can tell you that's what's been going back and forth. There are benefits to—they're two consumer goods companies that are really well known brands that we've negotiated and begun finalizing—we're on the final stages of negotiating our agreements, where they will, in addition to their exposure and the revenue that they bring to us through our, I think, live show, they will provide benefits to our members that are not available at their stores or on their website unless you're an iPic member. It's a greater benefit than any offering that they're done before, and it's only for the members.

Those are the kinds of things that we're working on. Obviously, we'll announce those as soon as they're signed, but there's a number of similar type offerings that are being negotiated at the moment.

Jim Goss:
All right. Thanks very much.

Paul Westra:
Thanks, Jim.

Operator:
As a reminder, if you would like to ask a question, please press star, one on your telephone keypad. One moment, please, while we poll for questions.

Hamid Hashemi:
Well, Hector, there doesn't seem to be any other questions. At this point, we look forward to updating you about our progress at our next call. With that, again, we thank you for your time. I'll turn it over to Hector.

Operator:
Thank you. This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.