EZCORP, Inc., Q3 2023 Earnings Call, Aug 03, 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

Conference Call Participants

* Andrew D. Chasanoff

  Oppenheimer & Co. Inc., Research Division - Associate

* Brian Christopher McNamara

  Canaccord Genuity Corp., Research Division - Analyst

Presentation

Operator [1]

Good morning, ladies and gentlemen, and welcome to the EZCORP Third Quarter Fiscal 2023 Earnings Call. [Operator Instructions] As a reminder, this call may be recorded. I would now like to turn the conference over to Jeff Elliott, Investor Relations with Three Part Advisors. Please go ahead, Jeff.

Jeff Elliott [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, 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.

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. I'd now 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]

Thank you, Tim, and good morning, everyone. Our team's persistent pursuit of operational excellence in executing our current 3-year plan as again yielded strong financial results for our stakeholders. Pawn loans outstanding hit a new all-time record of $223.8 million, up 10% for the quarter and 7% on a same-store basis. Merchandise sales were up 12% for the quarter, 7% on a same-store basis. Total Q3 revenue hit a record $249.5 million, driven by higher PSC and sales volumes across all of our regions. Merchandise sales gross margins remained within our targeted range of 36% with strong inventory turns at 2.8x. Aged GM inventory was 1.6% of total GM inventory for the quarter, showing an improvement of 60 basis points over Q2.

Beginning on Slide 3. We are a global leader in pawn broking and pre-owned and recycled retail. We operate 1,212 stores in the U.S. and Latin America, having added another 13 stores this quarter. The macroeconomic environment continues to be a challenge for our customer base as consumers seek cash to satisfy their short-term needs as well as value for money secondhand products, which also represent a more environmentally responsible way to shop. We strive to provide the best, most convenient experience for our consumers through continuous innovation, while positively impacting the environment and the communities in which we serve.

Moving on to Slide 4. Our engaged team drives our success, so we are committed to investing in recruitment, retention and incentivization to ensure our team members are engaged. We promote financial inclusion for underserved communities with our buy, sell and pawn offering, providing customers instant cash for any item of value. We provide outstanding customer service and attractive and well-positioned store footprint, differentiated digital platform, proprietary POS system and an innovative loyalty program for our customers.

We have a very strong and liquid balance sheet, enabling us to fund significant growth in our earning assets, the build-out of new de novo stores, opportunistic acquisitions from what continues to be a robust pipeline and our share repurchase program. Slide 5 shows our progression on our 3-year strategic goals. We believe that we've got the most passionate, productive tenured and committed team in the industry, and we continue to find ways to engage, motivate and retain them.

The results of our efforts are evident in the annual company-wide engagement survey that serves as a scorecard of how our culture is transforming with a record participation of over 90% of our 7,400 team members this year, we scored 84 points, a 3-point jump from last year and 9 points above the global benchmarks, including being 10 points above the retail industry and 9 points above the financial services industry. The implementation of the Workday ERP across HR and finance this quarter will further improve systems and processes, driving greater efficiencies for our team members and the organization as a whole.

Our points-based loyalty program has been extremely well received and has grown to 3.3 million customers, up 14% sequentially. We strive to increase engagement with personalized marketing campaigns and communications to deliver better customer experience and drive business growth.

Turning to our key financial themes for Q3 on Slide 6. The most significant driver of revenue and earnings PLO, hit an all-time high of $223.8 million, up 10%, with an associated 14% increase in PSC. Merchandise sales were up 12%, resulting in total revenue for the quarter of $249.5 million, up 16%, which was a record for Q3. Adjusted EBITDA was $27 million for the quarter, up 8%. Inventory turnover remained strong with aged inventory increasing slightly year-over-year but improved sequentially by 60 basis points. Cash on the balance sheet came down slightly on a sequential basis, primarily due to increases in PLO and inventory.

On Slide 7, EBITDA margin was 12% for the last 12 months ending June 2023 versus 13% in the last 12 months ending June 2022. As discussed last quarter, the EBITDA margin, as expected, has recently decreased due to the inflationary impact on our expenses. On Slide 8, we talk about strengthening the core operations, investing in people and technology in order to drive earnings. In LatAm, we launched a new intranet that provides enhanced access to information and communications that is driving increased efficiencies. Last quarter, we said that we were focused on better execution in LatAm and bringing down aged inventory to get closer to U.S. levels, and we are pleased with our progress on that front.

We've also launched a reimagined U.S. philanthropic strategy to align better with our pillars of people, pawn and passion. Investing in both our people and technology, we've engaged Workday to provide an enterprise cloud application for our team members with an enhanced toolkit to help build a modern employee experience. We continue to upgrade pricing, pawn and e-commerce capabilities to drive faster transaction times and deliver better customer experience.

On Slide 9, innovation and growth is our third strategic pillar. Our EZ+ Loyalty Program has over 3.3 million customers enrolled versus over $2.9 million last quarter, showing a sequential increase of 14%. We launched personalized marketing campaigns to notify members of their points and reward status to encourage further engagement. In the U.S., we collected $14.6 million in online payments versus $12.7 million last quarter, showing a 15% increase. Online extensions in the U.S. grew 4% sequentially and now comprised 29% of total extension, giving our store staff significantly more time to serve customers in stores.

Improving the customer experience and growing the customer base remains key to our strategy. We increased global transacting customers, U.S. visits to pawn websites, grew daily visits to buy online pick up in store test websites, U.S. online extensions and U.S. online layaway. We opened 12 de novo stores in Latin

America with 5 in Mexico and 7 in Guatemala. In the Las Vegas area, we opened 1 luxury de novo Max Pawn store.

Slide 10 outlines our ESG highlights for the fiscal third quarter. We are a neighborhood recycled and a compelling component of the local circular economy and have resold over 1.4 million pre-owned items in the quarter, including toxic consumer electronics, such as computers, TVs and phones, as well as tools, musical instruments, household goods and jewelry. 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 have introduced our fifth affinity group, HOLA, the Hispanic organization for leadership advocacy in the U.S. We have revamped the mission of the EZCORP Foundation in the U.S. and have launched local giving strategies aimed at improving the quality of life in the communities where we live and operate through supporting financial literacy, food security and financial stability. I would now like to turn the call over to Tim Jugmans, our Chief Financial Officer, to provide more details on our financial results. Tim?

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

Thanks, Lachie. Slide 11 details our consolidated financial results for the third quarter. PLO ended the period at $223.8 million, up 10% on a year-over-year basis, 7% on a same-store basis, which is the highest in EZCORP history. PSC revenue was up 14% over last year, with growth driven by both increased same-store PLO growth and acquisitions. Merchandise sales was up 12% to $143.8 million, our highest third quarter sales results. Merchandise sales gross profit was up 7% due to increased sales offset by a 200-basis point margin decrease. Inventory turnover is strong at 2.8x. Aged GM inventory was 1.6%, which is a 60-basis point improvement over the second quarter.

We have been successful working on improvements in U.S. and LatAm to drive this aged GM lower. It was another solid quarter with consolidated EBITDA of $27 million, up 8%. Turning to our U.S. Pawn operations on Slide 12. PLO rose 12%, driving PSC up 16% year-over-year, primarily driven by higher average PLO growth. On the retail side of the business, merchandise sales were up 9%, with merchandise sales gross profit up 3% with an expected 200 basis point drop in sales margin. Store expenses increased by 14%, primarily due to labor in line with store activity, higher store count and to a lesser extent, expenses related to our loyalty program. U.S. Pawn EBITDA for the quarter was $34.8 million, up 8% on the prior year due to higher PSC partially offset by increased expenses.

Slide 13 focuses on our Latin American Pawn operations. Segment PLO grew 1% for the quarter, but down 2% on a same-store basis, primarily due to increased pay downs during the quarter. Last year, there was a change in Mexican law, which increased the profit share to be paid by companies to employees by May 30, which led to this paydown. PSC was up 10% due to higher average PLO and PLO yield.

Merchandise sales were up 21%, 15% on a same-store basis. Merchandise sales gross profit was up 23% due to increased sales and margins up 100 basis points. Store expenses were up 14% and 9% on a same-store basis, mainly due to rent increases linked to inflation and higher store count. Inventory turnover remained strong at 3.4x with aged GM at 2.4%, showing an 80-basis point improvement over Q2 due to improving execution in Latin America. For the third quarter, Latin American Pawn EBITDA improved by 10% to $8.6 million, primarily due to higher gross profit, partially offset by increased expenses.

Looking forward, on a consolidated basis, we should see PLO levels continue to hit record numbers as we build to the end of the financial year. This also means that PSC will also grow year-over-year as well as sequentially. As communicated in prior quarters, we will likely continue to see gross margin remain at the lower end of our targeted range of 35% to 38% as we remain focused on strong inventory times and limited aged general merchandise. Also, as we've seen this quarter, store expenses have increased and will do so on a sequential basis and inflationary pressures continue to affect the business. We also expect G&A expenses to increase sequentially for the same reason. Our focus on growing PLO, selling what we own and investing in technology to gain efficiencies and enhance customer service continues to drive our improving financial results. 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 yet another outstanding quarter. We are consistently delivering strong operating and financial results for our stakeholders. Our balance sheet is robust. We grew PLO to the highest level in our history and opened 13 exciting new stores this quarter. We continue to invest in our team and technology while buying back shares. We are committed to improving the experience of our employees and our customers in an environmentally responsible way. Our 3-year plan and the people who have executed it have produced a very significant financial and operating turnaround for our company, and we are very much looking forward to producing even better results for our shareholders over the next 3 years and beyond. And with that, we will open the call for questions. Operator?

Question And Answer

Operator [1]

[Operator Instructions] Our first question is from Brian McNamara from Canaccord Genuity.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [2]

Congrats on the strong results. A couple for me. First off, I guess, in July, the Google Search trends for pawn shop nearly apparently reached a record high. I'm curious what you're seeing in your stores? I mean, presumably, if you're searching for pawn shop near me, you're not a pawn shop regular per se. So are you guys seeing new customers? And any color on kind of what would be driving your customers into your stores, whether it be financial difficulty, inflation you like would be really helpful.

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

Thanks, Brian. Look, the website activity that we saw as we've had put in the announcement, even up until July has been very, very strong. We've invested in this digital piece now for the last couple of years, and we're really seeing very, very strong trends of customers trying to find us online. In the stores themselves, this macroeconomic environment continues to be tough on our customers. So we're absolutely seeing growth in customers, both in the stores and online. So look, I think all of the trends that we've spoken about in recent quarters continue, and as you can see from our quarterly results here, the numbers are doing some significant momentum.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [4]

And then as you think about PLO, obviously, you've guided to continuing to reach kind of record and highs. I think your PLO, the inventory rate was at 1.5x kind of at the high end of your 1.2x to 1.5x kind of targeted range. Should we expect that target range to move higher? Or we're kind of at max out there? Any color on kind of where you see PLO shaping out and obviously, as we go into your next fiscal year.

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

Tim, do you want to deal with that one?

Jeff Elliott [6]

Yes. So we say that we want to continue to -- there's going to be continued growth in the PLO balance. The demand is still strong. We're talking about hitting record PLO numbers at the end of Q4 as well. And we expect demand unless something strange happens in the economy, we expect it to continue to grow.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [7]

And on the -- and what about on the answer to the question on the ratio inventory, the PLO.

Jeff Elliott [8]

On the ratio, yes, we do expect it to stay. It will move around a little bit depending on the seasonality, but we do expect it to stay in that -- around that 1.3x to 1.5x range. As there's definitely different selling quarters like the Q1 and Q2 are definitely going to show that we're going to sell a lot more inventory in those quarters than in Q3 and Q4.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [9]

And then like there's clearly seasonality in your business. Is that kind of gone out the window this year as you continue to kind of sequentially improve that impressive number. Is the expectation that you kind of settle into more seasonality next year for PLO?

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

I mean the big thing that happened this year was the PLO, the lack of paydown in tax season. And I think you read all lending companies all saw the same thing. It wasn't just us. So look, that is a big swing factor in seasonality. I would expect it's going to get a little closer to normal, but various commentators are saying different things about what they're going to see for next tax season. But that's the big one. But I think generally, this is a seasonal business, and we'll probably rotate back into that rather than continuing with unusual year.

Operator [11]

Our next question comes from Brian Nagel from Oppenheimer.

Andrew D. Chasanoff, Oppenheimer & Co. Inc., Research Division - Associate [12]

This is Andrew Chasanoff on for Brian Nagel. So I just wanted to start with merchandising margin. Can you discuss a little bit further? I know you said in the prepared remarks, but can you discuss a little bit further the puts and takes in the quarter that drove the margin closer to the lower end of the 35% to 38% range. And then just, again, just a little bit of a follow-up. Do you expect these pressures to remain at these Q2 levels over the next several quarters? And the other external factors that we should be considering that might push margins below that 35% boundary?

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

I think Tim will answer the specifics on the puts and calls, but I think it's important for everyone to note here that we run a business that starts at the loan counter but flushing of inventory is critical to what we do. And margin falls out of that. And I think the macroeconomic environment continues to be difficult. So I think we're just wanting to make sure that we are flushing inventory as quickly as we can. And that naturally puts -- can put pressure on margin. So look, I think we're pretty happy with turns, and that is very helpful in driving further loan balance increases. But Tim, why don't you answer the piece on any puts and takes in margin this quarter.

Jeff Elliott [14]

So the -- I think it's important to look at the margin on also a sequential basis here. We've continued to see the margin come down year-over-year every single quarter. The negotiation at the counter has definitely increased as we have had more inventory in the store. And so the customer has more choice, and the customer also has less money than they used to. So a combination of those factors are putting a little bit more pressure on the margin. You also see that on a sequential basis, age, general merchandise is also coming down. So that is a key factor of ensuring whether or not our inventory is healthy and making sure that we continue to have a healthy inventory balance, it does effect -- it does put some pressure on margin.

On your question on can it -- is it what would make it go below that range? I think the big things that would do that is if the economy got significantly worse and put significant pressure on our customers, I think that then we would want to ensure that there's even better pricing in our stores to really encourage consumers to purchase our goods, which will put a little bit of pressure but overall, what we are trying to do here is we have the flex to make the money on either the PSC or the gross sales gross margin. And we led those depending on where our customer is to ensure that we're maximizing our gross profit line at all times. So that is the aim. And the fact that we have very short-term loans allows us to make changes very quickly as the economy changes.

Operator [15]

[Operator Instructions] Our next question comes from Brian McNamara from Canaccord.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [16]

Sorry for hogging all the questions today, guys. But I'm curious, your view on the share price. I know you guys are -- you're frustrated with it, and your results are shining through. I'm just curious, if you could give the market some kind of indication of your view of kind of how undervalued the stock is right here as results come through and it seems like not being rewarded in the share price.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [17]

Yes. Sure, Brian. Look, I think you're right, it is frustrating, given we all earn a very significant part of our compensation in stock. And not only do we want to drive shareholder value for all of you, but for ourselves as well. So we are very much focused on what drives that price higher. And I think the number one thing that the team can do is to drive financial results and I think we're kind of 3 years -- almost 3 years into our strategic plan, and we're doing that every single quarter. So my personal view is it's very -- it's highly undervalued. It's worth much, much more than where it's trading at today.

So I think hopefully, people are going to make a good amount of return by getting involved now. But I think what management can do here is to drive growth, drive scale and do that in a fundamentally conservative fiscal way where we are very liquid so that we can grow our PLO. We can make acquisitions. The pipeline remains really strong for that.

We've got some debt coming due in the next couple of years, not a whole heap or anything, but we're going to be liquid to be able to do that in cash if we would like to. So I think we are doing all the right things. We are earning the market trust. We are proving up our acquisition strategy. And I think if we just keep doing that, my personal view is that the stock will be much, much higher in the next -- meaning long term.

Brian Christopher McNamara, Canaccord Genuity Corp., Research Division - Analyst [18]

Great. And then maybe one for Tim on the inflationary impact on your expense base. Like when do you expect that to kind of tail off? Is that in the next couple of quarters? Is that another kind of fiscal '24 event? How should we think about expenses kind of moving forward given the inflationary catch-up you guys have experienced this fiscal year?

Jeff Elliott [19]

We -- so there's still going to be some going through into '24. We don't expect the rise that we have seen in this year to be as much, but we do see some coming through. We still got -- especially in Latin America, we've got changes in labor laws, increasing those costs. You have -- we have rental agreements, especially in Latin America that are linked to inflation. So you do -- we will see some, just not as great, and we're really focusing on ensuring that we continue to drive even greater revenue growth to ensure that we can continue to grow the bottom line.

Operator [20]

We have no further questions at this time. So with that, I will hand back to Lachlan Given for final remarks.

Lachlan P. Given, EZCORP, Inc. - CEO, Director & Chief Strategy, M&A and Funding Officer [21]

Thank you, everyone, for joining the call. We really appreciate your time. I look forward to talking to many of you today and tomorrow. And thank you to the EZCORP team for another outstanding quarter. Thanks, guys.

Operator [22]

This concludes today's call. Thank you for your participation. You may now disconnect your lines.