S&P Global
Market Intelligence

EZCORP, Inc. NasdaqGS:EZPW

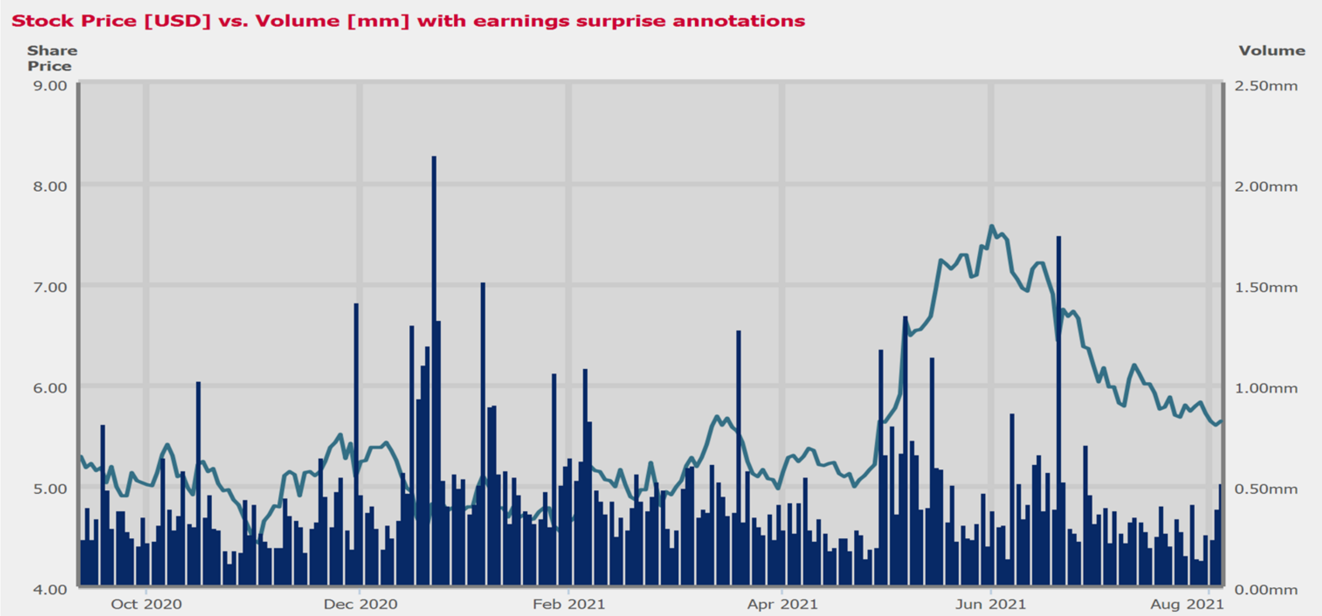
FQ3 2021 Earnings Call Transcripts

Thursday, August 05, 2021 12:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2021-			-FQ4 2021-	-FY 2021-	-FY 2022-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(0.02)	(0.03)	NM	(0.01)	0.26	0.62
Revenue (mm)	169.95	174.03	▲2.40	172.06	705.09	806.46

Currency: USD
Consensus as of Jul-12-2021 5:07 AM GMT



	- EPS NORMALIZED -		
	CONSENSUS	ACTUAL	SURPRISE
FQ4 2020	(0.08)	0.07	NM
FQ1 2021	(0.04)	0.13	NM
FQ2 2021	(0.07)	0.17	NM
FQ3 2021	(0.02)	(0.03)	NM

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Call Participants

EXECUTIVES

Jason A. Kulas
President, CEO & Director

Michael Keim
Director of Financial Planning and Analysis/Pricing

Timothy K. Jugmans
Chief Financial Officer

ANALYSTS

Gregory R. Pendy
Sidoti & Company, LLC

John Hecht
Jefferies LLC, Research Division

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to the EZCORP Third Quarter Fiscal 2021 Earnings Call. [Operator Instructions] As a reminder, today's call is being recorded.

I'd now like to turn the conference over to Mr. Michael Keim, Investor Relations. Please go ahead, Michael.

Michael Keim
Director of Financial Planning and Analysis/Pricing

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 or implied by these forward-looking statements 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.

Now I'd like to turn the call over to EZCORP's Chief Executive Officer, Mr. Jason Kulas. Jason?

Jason A. Kulas
President, CEO & Director

Thanks, Michael, and good morning, everyone. We thought it would be appropriate to start this morning's call by stating our EZCORP purpose. We exist to serve our customers' short-term cash needs, helping them to live and enjoy their lives. We are driven by a diverse team with a passion for pawn who are motivated to be their best because our customers' families, stakeholders in the communities environment in which we live, deserve it.

We talk a lot internally about the importance of having one message. One message that ties to our strategy and communicates our purpose, both internally and externally. And one message that resonates with team members, customers, investors and all of our constituents.

The third quarter marked another period of meaningful progress against the key strategic initiatives that we have laid out to position our core pawn business for durable growth coming out of the pandemic. PLO, the key driver to our revenue and earnings power is up 25% on a sequential basis and 35% compared to a year ago. At north of $150 million, PLO at the end of June reached the highest quarter ending balance since the beginning of the pandemic. The growth began in mid-April and continued through the quarter, and we saw further growth in July.

Looking ahead, the higher starting point for PLO bodes well for growth in pawn service charges revenue in the coming quarters, given the natural lag that exists in the business between pawn originations and related fees.

Merchandise sales volumes are below peak pandemic levels from last year due to the positive impact of stimulus payments on sales last year. However, our merchandise sales gross profit was essentially flat versus the year ago quarter, reflecting sharply improved inventory management metrics, including continued strength in inventory turnover rates, declining aged inventory levels and expanding gross private margins.

We remain on track to realize meaningful cost savings this fiscal year and are focused on optimizing operating cost ratios as expense levels rebuild in conjunction with accelerating transaction volumes at the store level.

Furthermore, we are increasingly leveraging our strong liquid balance sheet. Beyond funding accelerating pawn demand, we completed the acquisition of 128 stores in Mexico, our largest acquisition to date in terms of store count and acquired 11 stores in the Houston, Texas market and opened 4 de novo stores in Latin America during the quarter. We now operate 1,143 stores, with 55% of those locations across Latin America.

We also recently finalized our decision to close our Peru operations in Latin America, consisting of 11 stores, reflecting our ongoing efforts to focus the business on areas where we can drive profitable growth. While there is still much work to be done, we remain confident in the differentiated platform we have built and are encouraged by the progress we've made in further strengthening our core pawn business, particularly through the pandemic.

We remain focused on meeting our customers' needs for cash and affordable preowned and recycled merchandise across the U.S. and Latin America, and our ongoing strategic initiatives will enhance the pace and trajectory of our growth going forward.

As shown in our prior quarter presentations, Slide 4 is a graphical representation of our strategic road map. And Tim and I will go into greater detail on some of our more recent milestones over the next few slides. At a high level, all of the underlying components or pieces of the puzzle work together to enhance relationships with our team members and customers, deliver sustainable growth and strong financial performance and drive long-term shareholder value. You may have noticed in our social media posts that we are highlighting our role in the circular economy and the natural resources that can be saved when you buy an item in a pawn shop instead of buying it new. This component of our business, which is core to who we are, is something we will continue to highlight, along with the rest of our customer value proposition and our financial metrics.

Turning to Slide 5. Key financial themes for the quarter included modestly negative EPS, consistent with the prior year quarter. On an adjusted basis, we reported a loss of $0.03 per share compared to a loss of $0.02 for the third quarter of fiscal 2020, as improved profit before taxes was offset by higher income taxes.

Net revenue was up 1% year-over-year, driven by higher on service charges and strong sales margins making up for lower sales. While adjusted EBITDA totaled $12 million for the quarter, up 126% from $5.3 million due to higher PSC. PLO ended the quarter at $153 million, up 35% on a year-over-year basis and within 17% of fiscal 2019, with further growth in July, despite the transitory step-up in liquidity for customers as a result of the pull forward and expansion of Child Tax Credit payments.

Turning to the retail side of the business. While sales volumes were down from prior year levels that were temporarily propped up by stimulus payments and high inventories, merchandise sales gross profit was essentially flat on a year-over-year basis. For the quarter, merchandise sales margins reached 44%, reflecting continued inventory management efforts. Inventory turnover continues to trend higher and aged general merchandise ratios are now negligible compared to double-digit rates just 12 months ago.

On expenses, we remain on track to realize more than $14 million of expense reductions for fiscal 2021, mostly related to lower G&A spend, and we remain focused on optimizing store operating cost ratios as transaction activity rebuilds.

And finally, our balance sheet remains a key differentiating factor. As mentioned earlier, we closed 2 acquisitions during the quarter, and we continue to fund accelerating PLO growth in de novo store openings. And with over $280 million of cash on hand at quarter end and no near-term debt maturities, we still maintain ample liquidity and flexibility to further enhance growth.

Slide 6 focuses on our ongoing cost optimization and productivity efforts. G&A costs declined by 10% for the fiscal third quarter compared to the prior year quarter, resulting a 19% savings on a year-to-date basis. Store expenses decreased by 3% for the quarter on a year-over-year basis and 7% when looking at year-to-date costs. On a sequential basis, store operating costs were down $1.8 million or 2%. So we do anticipate related expenses to trend higher, starting in our fiscal fourth quarter as transactional demand continues to rebound.

Next on Slide 7. Team member highlights for the quarter, included introducing benchmarking surveys, launching talent and succession plans, enhancing recruitment campaigns and a continued focus on improving inclusion initiatives. And under technology and process efficiency, we walk through specific IT modernization initiatives recently implemented to enhance operations and productivity.

Turning to Slide 8. Innovation is a key driver of our sustainable growth initiatives and our efforts to do more for customers. Online extensions through our Lana digital pawn channel accounted for 9% of total extension payments, with more than 130,000 payments made online in the quarter. In addition, over 5,000 layaway payments were processed online last quarter, and we are in the early stages of bringing online payment capabilities to Mexico.

We also remain focused on our customer service, retention and acquisition initiatives, including launching a loyalty program in the next several quarters and adding searchable online inventories and select stores. And finally, we grew our store footprint by 13% for the quarter, driven by 2 acquisitions and the opening of 4 new locations, as previously mentioned.

With that, I'd like to turn the call over to Tim Jugmans, our Chief Financial Officer. Tim?

Timothy K. Jugmans
Chief Financial Officer

Thanks, Jason. For the third quarter of fiscal 2021, we reported a diluted loss per share of $0.05 on a GAAP basis compared to a diluted loss of $0.10 for the fiscal year's third quarter -- for the prior fiscal year third quarter. On an adjusted basis, we reported a diluted loss per share of $0.03 for the quarter compared to a diluted loss of $0.02 per share for prior year quarter.

Consistent with the 2 quarters of fiscal 2021, adjustments for the third quarter were mostly limited to our standard practice of adding back noncash interest expense related to our convertible debt and constant currency impacts.

Starting with our consolidated financial results on Slide 9. PLO ended the period at $153 million, up 35% on a year-over-year basis and only down 17% compared to the pre-pandemic level in 2019. Following suit, PSC revenue was up 12% versus the year ago quarter, with much of the growth driven by higher average PLO.

Merchandise sales were down 23% from their peak pandemic levels a year ago. That said, merchandise sales gross profit was essentially flat, with lower sales volumes, about offset by higher margins. Merchandise sales gross profit expanded by 967 basis points from the prior year quarter, primarily driven by reduced aged inventory levels and higher sales velocity. Inventory turnover improved to 3x, and the aged general merchandise inventory ratio continued to decline from 11% of total GM inventory a year ago to just 1% at the end of the third quarter of fiscal 2021. Steady sales gross profit and lower inventory levels contributed to a stronger return on earning asset ratio for the quarter at 193% versus 150% for the third quarter of the prior fiscal year.

Finally, consolidated EBITDA of $12 million more than doubled from $5.3 million in the third quarter of fiscal 2020 as a result of higher PSC revenues and our ongoing focus on expense controls.

Turning to our U.S. Pawn operations on Slide 10. Segment PLO rose 35% on a year-over-year basis, mostly driven by our focused pawn operating model and the absence of government stimulus payments. Importantly, U.S. PLO levels continue to trend closer to pre-COVID levels, with quarter end PLO only down 21% compared to the same point in 2019. For the third quarter, PSC was up 7% year-over-year, driven by higher average PLO.

On the retail side of the business, merchandise sales were down 27% to the third quarter of fiscal 2020 when volumes were inflated by stimulus payments. More favorably, merchandise sales gross profit was down a lesser 8% year-over-year as lower sales levels were offset by higher margins. The gross sales margin expanded by 970 basis points versus the prior year quarter.

Lastly, a function of more effective inventory management. Aged general merchandise inventory continues to decline and accounted for just 1% of total general merchandise inventory in the U.S. at quarter end versus 5% of the total a year ago.

Turning to the bottom line. U.S. pawn EBITDA was down 5% compared to the prior year quarter, with a lower net revenue, partially offset by lower expenses. Store expenses were down 5% year-over-year, mostly related to lower labor costs.

Slide 11 focuses on our Latin American Pawn operations. Segment PLO grew 36% compared to the year ago level, reflecting stronger same-store growth as well as the recent acquisition of Cash Apoyo Efectivo in Mexico. As a result, PSC was up 30% on high average PLO for the quarter, combined with a more favorable PLO yield related to an improved redemption rate.

Merchandise sales were up 2% versus the prior year quarter, while merchandise sales gross profit was up 67%, reflecting higher margins, accelerating inventory turnover and tricking aged general merchandise inventory. More specifically, aged GM inventory represent less than 1% of total GM inventory at quarter end, a sharp decline from 18% a year ago.

EBITDA improved from just above breakeven for the year ago quarter to $4.8 million on higher PSC and merchandise sales gross profit, partially offset by increased expenses. Store expenses were up 16% year-over-year, with much of the increase a function of stores being opened for the entire quarter compared to last year's COVID impact.

Finally, I wanted to provide some perspective on the fourth quarter of fiscal 2021. As mentioned earlier, PLO levels have continued to increase since mid-April, reflecting more favorable pawn demand trends, accelerating transaction volumes and a focused team. In July, we have continued to see PLO rise, and it is now only down 15% from 2019 levels. However, the lag in PSC will continue as PLO rises.

The recently enacted Child Tax Credits in the U.S. and more challenging macroeconomic backdrops and increased COVID cases across Latin America likely represent near-term headwinds for the pawn lending activity, though we expect the impact related to these tax credits to be transitory in nature.

Also, we would expect bottom line growth to be somewhat tempered in the near-term in light of rising store operating costs due to additional stores as well as accelerating transaction activity and normalizing merchandise margins with lower inventory levels.

While the resumption of standard sales discounting practice will impact profitability, we will anticipate gross profit margin to remain at the high end of the historical range.

Putting it all together, we do expect adjusted net income and EPS for the fourth quarter as be consistent with the third quarter levels and ahead of a meaningful step-up in earnings power in fiscal 2022, all else equal.

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

Jason A. Kulas
President, CEO & Director

Thank you, Tim. In summary, we are pleased with the progress we've made down the path of generating long-term sustainable growth, with third quarter results across core operating metrics, reinforcing that progress. Our accomplishments thus far can be directly attributable to the ongoing dedication and execution of all of our team members. Their enthusiasm and passion for customer service serves as the backbone for our success. So I'd like to take this opportunity to thank all of them again for their hard work and contributions.

We expect that the steps we have taken over the past year plus will continue to translate into stronger financial performance. As we have said in recent quarters, our ongoing inventory management and expense optimization efforts should continue to drive better results as pawn transaction activity and the related growth in PLO and PSC continues to increase. We look forward to continuing to discuss our progress in future quarters.

And with that, we'll open up the call for questions. Operator?

Question and Answer

Operator

[Operator Instructions] We'll take our first question from John Hecht with Jefferies.

John Hecht
Jefferies LLC, Research Division

You guys did comment on the transitory nature [indiscernible] but I'm wondering generally speaking, is there kind of a linear recovery in the PLO at this point? Or is it going to be very [indiscernible] just trying to get a sense of the near-term model?

Jason A. Kulas
President, CEO & Director

Yes, absolutely. Thanks, John. So we do believe it's transitory. And the example we'll give is one of the things we talked about last quarter is the balance that we've been seeing is faster. So when a new round of stimulus comes through, the recovery in pawn demand comes back quicker in each incremental time. And we saw that with the first kind of round of checks that came through on the pull forward and expansion of the Child Tax Credits, where we saw a little bit of a pullback and then a pretty quick bounce. With more of that coming, we expect to see some headwinds there. Obviously, with -- we're watching the delta variant closely and the impact that will have on our stores going forward. But we expect all of that to be temporary or transitory, however you want to say it. And we do expect that, that growth is going to continue to be fairly linear.

If you look at the growth that we saw throughout the quarter, we talked about hitting the low point in mid-April and then really starting to build from there. That growth continued through the latter part of April, through May, through June. And now, as Tim said, it's continued in July as well. So we're pretty happy to see what's going on there. The lag in PSC, we know how that story ends. We know that the pawn service charges follow the growth in PLO. But we do expect that to be short of a little bit of a stop here and there, fairly linear going forward.

John Hecht
Jefferies LLC, Research Division

Okay. And then margins, yes, you talked about them sustaining at higher than -- toward the high end of long-term ranges, and they've been very high. Do you -- has there been a change in kind of your customer behavior where you think that high level will be sustained? Or as your balances normalize back to pre-COVID levels, do you think that -- or excuse me, margins will go back toward pre-COVID levels as well?

Jason A. Kulas
President, CEO & Director

We think they will, but it's important that you acknowledge that we -- that we're clear that we feel like we're going to end up at the high end of that historical range. Because the way that we operate the business at the store level, the way that we are focused on 0 to 90 day sales velocity, turning inventory, maintaining our inventory without letting it roll into age, those kinds of things, that's going to help us sustain higher margins going forward.

The margins that we see right now aren't reflective of where we think we'll end up, but we'll still end up in a place that relative to where we've been historically and kind of the industry has been historically is a really, really positive place because of the operating metrics that we have in place now.

John Hecht
Jefferies LLC, Research Division

Okay. And then you guys have been pretty active acquiring. Maybe can you just give us some comments on the acquisition pipeline as it stands today and the geographical disposition of that?

Jason A. Kulas
President, CEO & Director

Yes. It's -- obviously, one of the core pieces of our strategy is innovation and growth and to be able to see that we've had some success after all the hard work for a long period of time by our M&A team and closing some acquisitions, we're really pleased to see that progress. I would say the pipeline is strong as it's ever been. The thing with these M&A transactions is that they have their own timing, and they take on a life of their own, and you never know exactly when they're going to hit. So they're difficult to project, but we would hope to continue to be able to have some success there.

Right now, we just announced the acquisition of 128 stores in Mexico and 11 in the U.S., and we want to make sure we integrate those successfully, and we're focused on that as well. But over time, we'll continue to make sure that, that M&A pipeline stays strong and our team is very focused on continuing to make sure we're on top of it.

Operator

[Operator Instructions] We'll go next to Greg Pendy with Sidoti.

Gregory R. Pendy
Sidoti & Company, LLC

Just real quick, just trying to understand the 4Q guidance and a lot of the moving parts with the Child Tax Care -- Credit. So just trying to understand that. Are -- what are you trying to say? And I know we're looking out a little bit, but a little bit of near-term pain, but maybe in that March quarter tax refund season, you might see a little bit less seasonality in the PLO decline that I think happens during tax refund, but maybe offset by lower merchandise sales. Is that fair?

Jason A. Kulas
President, CEO & Director

That's definitely a fair statement. We would definitely see as the Child Tax Credits come early, they -- obviously, they're not going to come during that tax season. So we think that's why there's a little bit of a transitionary nature there. And that would be a fair statement to say.

Gregory R. Pendy
Sidoti & Company, LLC

Okay. Great. And then just trying to -- one of the biggest question seems to be on this, the high cash position. And I know that as pawn loans pick up, you want to maintain liquidity. But just trying to understand, I mean, this company, I believe, in fiscal 2019, supported a PLO book of around $200 million with maybe about $150 million in cash. Your cash levels double that. And I know you've done some acquisitions, but how are you thinking about stock buybacks at this level? I mean, even maybe a moderate amount, just given the cash position?

Jason A. Kulas
President, CEO & Director

We're very committed to making sure that every incremental dollar we put to work is put to work in a way to maximize shareholder value. And also, part of that is making sure that we maintain a strong balance sheet. At the Board level, we had discussions regarding when we would again sort of address those kinds of questions. And we continue to talk about the fact that we'll really engage in those discussions once we feel like we've cleared the impacts of the pandemic. We're very bullish about what 2022 looks like for the business. We've set a really strong foundation. Now we're seeing the PLO growth come through, and we really feel like the business is set up for a strong year ahead of us. But we need to get there before we take up those discussions. We've seen that we have some acquisition opportunities. We've seen that we need some of that liquidity to rebuild the pawn book. At the same time, our business produces a lot of free cash flow, particularly when it gets to the levels of performance that we expect going forward. So those will be interesting discussions to have at that time. We're just not quite there yet.

Gregory R. Pendy
Sidoti & Company, LLC

Okay. And then just one final one. If I'm not mistaken, I think you were testing out some counters at the store. Is that in the stores right now? Any insights into that, if I'm correct, that you're putting some counters in the stores to monitor traffic?

Jason A. Kulas
President, CEO & Director

Yes. Yes. We've completely rolled out the traffic counters in the U.S. and in the process of doing that across Latin America. And we're already seeing that we're able to monitor data and start to collect data. That's going to be very helpful for us. And the most helpful comparisons will be the year-over-year comparisons. But incrementally, sequentially, we'll be able to see that some of these efforts that we talk about on the digital side of the business where we're doing certain social media marketing campaigns and those kinds of things to be able to measure what traffic was before and after those and not have to guess, will be a real advantage for us, we think, and we're excited about what that's bringing to the business. It's still early days for us, but we're excited about it.

Operator

All right. It looks like we have no further questions at this time. So let me turn it back over to our speakers for any additional or closing remarks.

Jason A. Kulas
President, CEO & Director

Thank you, and thanks, everyone, for your interest and time this morning. We look forward to continuing to talk about our progress in future quarters. Hope everyone has a great day.

Operator
That does conclude today's call. We thank everyone for their participation. You may now disconnect.