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Q1 2023 TH International Limited Earnings Call

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CORPORATE PARTICIPANTS

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Yongchen Lu *TH International Limited - Chief Executive Officer, Director*
Albert Li *TH International Limited - Chief Financial Officer*

PRESENTATION

Operator

Ladies and gentlemen, welcome to TH International Limited first quarter 2023 earnings presentation. My name is Ting Zhou, Head of Investor Relations. TH International Limited announced its first quarter 2023 financial results earlier today, a press release as well as a company presentation which contains operational and financial highlights are now available on the company's IR website at ir.timschina.com.

Today, you'll hear from Mr. Yongchen Lu, our CEO and Director, and Mr. Albert Li, our CFO. You can also find a webcast of this presentation on our IR website.

Before we get started, I'd like to remind you that our earnings presentation and investor materials contain forward-looking statements which are subject to future events and uncertainties. Statements that are not historical facts, including but not limited to statements about the company's beliefs and expectations are forward-looking statements.

Forward-looking statements involve inherent risks and uncertainties, and our actual result may differ materially from these forward-looking statements. All forward-looking statements should be considered in conjunction with the cultural statements in our earnings release and risk factors included in our filing with the SEC. This presentation also includes certain non-GAAP financial measures, which we believe can be helpful in evaluating our performance. However, those measures should not be considered substitutes for the comparable GAAP measures. The accompanying reconciliation information related to those non-GAAP and GAAP measures can be found in our earnings press release issued earlier today.

With that said, I would now like to turn it over to Mr. Yongchen Lu, our CEO and Director. Please go ahead.

Yongchen Lu *TH International Limited - Chief Executive Officer, Director*

Thank you, Ting. My name is Yongchen Lu, CEO and Director of Tims China. In the first quarter of 2023, we are pleased to have set a new record for quarterly revenues while achieving positive adjusted store revenue. Despite the difficult circumstances brought by the high number of COVID-19 infection cases across the country in general, our team's diligence, continuous innovation, and creative marketing contribute to our strong recovery with customer demand returning after Chinese New Year, as evidenced by 17.1% and 19.4% same-store sales growth for company-owned and operated stores in February and March, respectively.

Our store network continues to grow briskly. We have accelerated the development of our franchisee stores through the rapid expansion of our most compact store format, Tims Express, largely propelled by our partnership with Sinopec Easy Joy, the largest convenience store network in China with over 27,800 locations, enabling us to be on track to surpass 1,000 system-wide stores by year end.

We have identified a strong pipeline of attractive store locations where we build the store format to suit the location size and custom traffic. This enables us to achieve attractive payback periods and efficiently enter into new cities. We aim to enter into at least 40 new cities in 2023 through a balanced mix of company-owned and franchisee stores.

To highlight some of the new cities we have entered thus far, on opening days for our first stores in Wenzhou, Zhongshan, and Zhenjiang, enjoying RMB50,000, RMB84,000, and RMB56,000 in sales, respectively, while scoring 6.5 million, 8.3 million, and 4.5 million media impressions, respectively. Our innovative store format, Tims Express, has enabled us to enter into meaningful partnerships with reputable companies like Sinopec Easy Joy, Century 21st Real Estate Agency, and Lin Ka, which have notably contributed to our network expansion.

We continue to invest significant resources to increase the frequency of our new product launches. We currently aim to introduce a new beverage or food product at least every two to three weeks. This gives our guests new and fresh options, attracts new customers, while keeps our loyal customers coming back. One such product that we launched during the first quarter of 2023, the avocado fresh coconut cold brew coffee (Spoken in Foreign Language) combines real fresh fruit with Tims unique cold brew, building the foundation for Tims cold brew signature product series, and resulting in peak sales of 50 units per day per store during the first quarter of 2023.

Meanwhile, we broaden our plant-based milk coffee offerings, including almond cafe latte (Spoken in Foreign Language) almond flat white, oat milk flat white, double-double oat milk latte (Spoken in Foreign Language) by leveraging co-branding campaigns with Tesla to highlight a trendy and healthy lifestyle.

The plant-based milk series achieved peak sales of 77 units per day per store in the first quarter of 2023. To better fulfill consumer needs and to further develop Team's advantages on fresh prepared foods, we continue to innovate healthy products such as sea salt sesame bagel, and black sesame bagel to better meet local tastes, we launch new products like cheese fried sticks, and for lunch cuisine, we rolled out new items like roasted beef bagel sandwich, black truffle flavored chicken bagel sandwich, Sichuan tender egg bagel sandwich, et cetera.

In terms of baked goods, we continue to improve our croissant and waffle series that includes the introduction of our pork floss mochi sauce and new matcha waffle series, which has not only increased customer awareness but also fostered our preferences for our new products and strengthened our positioning as a locally relevant innovator in the market.

During the first quarter of 2023, we continue to execute our differentiated coffee plus growth strategy by offering creative and customized beverage and food combos at compelling prices.

This continued initiative has been highly successful, which has resulted in the percentage of orders with food increased from 41% in the first quarter of 2022 to 44.2% in the first quarter of 2023. We have also observed that our customers order combos more frequently while stay longer in our shops, thus building a closer connection to our brands and allowing them the time to buy multiple products during their visit.

With more customers buying beverages and food together, we expect the average transaction size to increase, improving efficiency and margins.

We would like to sincerely thank our loyalty club members, which numbered at 12.4 million as of March 31, 2023, representing 79.3% increase year over year.

Their unwavering support has been a constant source of inspiration, encouraging us to continue to deliver high quality products and services. The digital realm continues to be a crucial part of our business. In the first quarter of 2023, we continue to see revenues from e-commerce sales grow from RMB9.5 million in the first quarter of 2022 to RMB 12.1 million in the first quarter of 2023. We believe technology will remain a core element to building our business and driving opportunity excellence. This quarter, we increase our technological and digital investments in our store supply chain. During the first quarter of 2023, we enhanced our value interface, enabling our guests to see the best available product price in real time on discount or promotional activities applicable to them, if any which have greatly enhanced our customer experience and increased our transaction success rate.

In January 2023, we established a strategic collaboration with data (ph) to utilize data analytics to optimize our new store size selection process and improve operations in existing stores. We have upgraded our digital labor management system and digital goods management system and implemented more RFID technology, which will allow real time sales and inventory forecasting and monitoring the company-owned and operated stores.

As a result, company management can make timely decisions on staffing and inventory to save costs and maintain food quality. We have also deployed AI technologies, including ChatGPT, to improve customer service, help management access information, and assist store designers generate graphics.

In addition to our initiative in technology and e-commerce, we continue to drive growth through our new retail channels like co-branded coffee products and at-home coffee products, such as Tims & Oatly ready-to-drink coffee, packaged liquid coffee, and liquid freeze-dried coffee products.

Lastly, after the Popeyes acquisition in March, we are on track to open our first flagship Popeyes restaurant in Shanghai in the third quarter of 2023 with brand new menu and store designs.

We look forward to introducing Popeyes passion for flavorful, authentic food to our 12.4 million loyalty club members, and we expect to leverage Tims infrastructure and operating expertise to grow the Popeyes business rapidly and efficiently. We believe both brands will benefit from greater economies of scale, stronger financial model, and create synergies in both supply chain and new restaurant development, among other areas.

At this time, I would like to turn it over to our CFO, Mr. Albert Li, to discuss our first-quarter 2023 financial performance in more details. Albert?

Albert Li TH International Limited - Chief Financial Officer

Thank you, Yongchen.

During the first quarter of 2023, total revenue grew by 49.8% year-over-year to RMB336.5 million. The growth was primarily driven by an increase in the number of system-wide stores from 424 as of March 31, 2022 to 648 as of March 31, 2023, and an 8% same-store sales growth for company-owned and operated stores in the first quarter of 2023.

Overall, takeout count was 72.9% higher year-over-year, driven by the rise in both dine-in and delivery and take-away orders. Overall, monthly average transacting customers were 2.3 million in the first quarter of 2023, representing an increase of 73.2% from 1.3 million in the first quarter of 2022. We continue to strengthen our digital capabilities to meet the growing demand from delivery and take-away services. Digital orders, as a percentage of total orders, increased from 75.4% in the first quarter of 2022 to 79.1% in the first quarter of 2023.

Our first quarter 2023 delivery and take-away orders, including those from Meituan, Ele.me, and our own WeChat mini program, increased by 74.2% from the first quarter of 2022. Concurrently, with the end of zero COVID control measures by the PRC government authorities in December 2022, our stores have gradually resumed normal operations and we have attracted more dine-in customers who have enjoyed our welcoming environment.

As a result, the number of dine-in customers increased by 125.8% from March 2022 to March 2023. I am proud to announce that our adjusted store EBITDA margin improved by 13.8 percentage points year-over-year to 1.9% in the first quarter of 2023.

Let me walk you through how we did it.

Our food and packaging costs as a percentage of revenues from company-owned and operated stores increased by 2.9% points from 33.0% in the first quarter of 2022 to 35.9% in the first quarter of 2023, as we offered higher sales discounts and increased promotional activities for our customers.

We expect further cost improvements on the back of our strong bargaining power with suppliers and RBI's initiative to deploy a Tim Horton coffee bean grocery in Malaysia in June 2023. Our rental and property management fee as a percentage of revenues from company-owned and operated stores decreased by 4.7 percentage points from 27.7% in the first quarter of 2022 to 23.0% in the first quarter of 2023. We took advantage of lower rent levels during COVID to secure more favorable lease terms and build a strong pipeline for the future.

Payroll and employee benefits as a percentage of revenues from company-owned and operated stores decreased by 10.5 percentage

points from 34.0% in the first quarter of 2022 to 23.5% in the first quarter of 2023. This reduction was primarily due to optimize the staffing using our digital labor management system and hiring more part-time employees. Delivery costs as a percentage of revenues from company-owned and operated stores from company-owned and operated stores increased by 0.3 percentage points from 7.0% in the first quarter of 2022 to 7.3% in the first quarter of 2023 primarily due to increased home delivery orders.

Other operating expenses as a percentage of revenues from company-owned and operated stores decreased by 6.0 percentage points from 14.1% in the first quarter of 2022 to 8.1% in the first quarter of 2023 primarily due to our continuous efforts to refine our cost controls and drive operating leverage through revenue growth and store network expansion.

Marketing expenses as a percentage of total revenues decreased by 0.2 percentage points from 5.6% in the first quarter of 2022 to 5.4% in the first quarter of 2023.

Our adjusted general and administrative expenses as a percentage of our total revenue decreased by 2.5 percentage points from 22.5% in the first quarter of 2022 to 20.0% in the first quarter of 2023. We expect our operating leverage to continue improving and our general and administrative expenses as a percentage of total revenues to decline over time.

Franchise and royalty expenses as a percentage of total revenues remained flat at 3.5% in the first quarters of 2022 and 2023. On liquidity as of March 31, 2023, our total cash and cash equivalents and short-term investments were RMB 613.6 million compared to RMB 611.5 million as of December 31, 2022. The change was primarily attributable to proceeds from bank borrowings, proceeds from our equity support agreement investors offset by the cash disbursements as a result of the rapid expansion of our business and the store network nationwide.

Looking forward, our top near-term financial priorities are to continue to deliver robust revenue growth to improve profitability at both the store and corporate level and to achieve operating cash flow breakeven by leveraging Tims China's brand influence and positive consumer perception with growing customer recognition and loyalty, continuous innovation, ever expanding store network and disciplined execution.

We expect to further optimize our cost structure, improve operational efficiency and achieve greater economies of scale. We would like to express our heartfelt gratitude to our shareholders and investors for their continued support of Tims China. Your confidence in our company and our team has been instrumental to our success and we are committed to delivering longtime value to our shareholders.

We look forward to updating you on our progress in the coming quarters and continuing to build a bright and successful future for Tims China.

Ting Zhou TH International Limited - Head of Investor Relations

Thank you Yongchen and Albert. That concludes our earnings presentation for today.

We thank you for your participation and look forward to providing you with regular business updates again next quarter.

QUESTIONS AND ANSWERS

Operator

There is no Q&A.

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