TRANSCRIPT

TH International Limited (THCH) Q2 2024 Earnings Call

August 29, 2024

Company Participants:

Yongchen Lu – CEO & Director

Albert Li – CFO

Gemma Bakx - Investor Relations

Operator:

Ladies and gentlemen, welcome to Tims China's Second Quarter 2024 Earnings Conference Call. All participants will be in listen-only mode during management's prepared remarks, and there will be a question-and-answer session to follow. Today's conference is being recorded.

At this time, I would like to turn the call over to Gemma Bakx, who heads Tims China's Investor Relations efforts, for prepared remarks and introductions. Please go ahead, Gemma.

Gemma Bakx, Investor Relations of TH International Limited:

Good morning and good evening, everyone, and thank you for joining us on today's call. My name is Gemma Bakx, head of Investor Relations. TH International Limited announced its second quarter 2024 financial results earlier today. The press release as well as an accompanying presentation which contains operational and financial highlights, are now available on the Company's IR website at ir.timschina.com.

Today, you will hear from Yongchen Lu, our CEO & Director, and Albert Li, our CFO. After the Company's prepared remarks, the management team will conduct a question-and-answer session. You can find the webcast of today's earnings call 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 results may differ materially from these forward-looking statements. All forward-looking statements should be considered in conjunction with the cautionary statements in our earnings release and risk factors included in our filings 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 Yongchen Lu, our CEO & Director. Please go ahead, Yongchen.

Yongchen Lu, CEO & Director of TH International Limited:
Thank you, Gemma. Good morning and good evening, everyone. I'm Yongchen Lu, CEO and Director of Tims China. The second quarter of 2024 represents a significant milestone for our company, as we achieved adjusted corporate EBITDA profitability for the first time in our corporate history. This result was driven by an intense focus on our core strengths of delivering guests great value for money products and a differentiated fresh food offering, coupled with continuous improvements in operational efficiency. This important milestone comes as we deliver our highest ever adjusted store EBITDA margin of 10.3%.

Our focus on sustainable profitable growth has included greater emphasis on building our franchise network, collaborating closely with our sub-franchisees to deliver them compelling unit economics while providing our guests with a consistent experience and driving our bottom-line profit. Despite a 6.6% reduction in revenue from company-owned stores due to our strategic decision to prune underperforming stores since the fourth quarter of 2023， we have sustained to achieve a 1.6% growth in system sales. Our efforts are paying off not just in our improving profitability but in the strength of our sub-franchisees pipeline, which stands at over 3,600 applications at the end of June.

As of June 30, 2024, our registered loyalty club members reached 21.4 million, reflecting a remarkable 45.4% year-over-year growth. The average number of members per store has now surpassed 23,000, serving as a strong catalyst for our growth and clearly demonstrating our customers' enthusiastic support for Tims China's loyalty programs. The ongoing support from our customers inspires our team to continue delivering the best value-for-quality products.

During the second quarter, we launched several impactful marketing campaigns, including collaborations with the Suzhou Museum and the Minglan ("知否知否") IP, which collectively garnered a combined total exposure of over 45 million across WeChat and the Little Red Book social platform.

Continuous product innovation is central to our strategic vision. In Q2 2024, we introduced 25 new beverages and 9 new food products, which contributed approximately 14% of our top-line sales. Standout offerings such as the floral latte ("栀子花绿茶拿铁"), buffalo milk latte ("水牛乳拿铁"), and the low-fat, real juice fruit Americano series ("甜橙美式"、"香梨美式") have resonated strongly with consumers.

We are committed to delivering healthy food options for our guests. With our customers' preference for healthy products in mind, we have also advanced our distinctive Coffee Plus strategy, launching new bagel products like the strawberry yogurt smile bagel ("微笑贝果 * 草莓酸奶") and fig yogurt smile bagel ("微笑贝果 * 无花果酸奶"). The total number of bagels sold increased from 4.8 million in Q2 2023 to 6.0 million in Q2 2024, with the percentage of orders that included food rising to 51.9%.

To further enhance our strengths and leadership in differentiated food products offerings and healthy food options, we completed made-to-order renovations for nearly 300 stores to date. With very limited capital expenditures investment, we have witnessed strong incremental food revenue growth already. We are on track to roll out our renovations model to more stores by end of the year to demonstrate to our customers that at Tims China our food is freshly prepared on site.

Additionally, we secured up to USD50 million in financing in Q2 2024 from our founding shareholders, Cartesian Capital Group and RBI, which underscores the commitment of our founding shareholders to our dynamic business. This year is a pivotal one for us, and fortifying our balance sheet is an important step forward towards ensuring our long-term success in a highly competitive market. This transaction enables us to drive growth in and intensify our focus on our core Tim Hortons brand.

Strengthening our core brand remains a key element of our strategy, and in order to provide an even sharper focus on developing the Tims brand, we agreed with RBI to transfer the Popeyes China business to them at the end of the second quarter. This transaction allowed us to streamline our operations and focus on our core business areas, while providing us with USD15 million in capital, which will be instrumental in driving further business expansion and optimizing our balance sheet.

At this time, I would like to turn it over to our CFO, Albert Li, to discuss our second quarter 2024 financial performance in more detail. Albert?

Albert Li, CFO of TH International Limited:
Thank you, Yongchen. In the second quarter of 2024, we achieved positive adjusted corporate EBITDA for the first time. We reached this significant improvement in our financial performance by optimizing our store unit economics, cutting costs at headquarters and closing underperforming stores.

We remain committed to delivering cost-effective, high-quality products to our growing customer base. Our overall monthly average transacting customers reached 3.1 million in Q2 2024, a 12.1% increase from 2.8 million in the same quarter of 2023. Additionally, digital orders as a percentage of total orders rose from 80.6% in Q2 2023 to 86.5% in Q2 2024. We continue to enhance our digital capabilities to meet the growing demand for delivery and takeaway services.

During the second quarter of 2024, we made more significant strides in enhancing our operational efficiency:

Through refinements in our supply chain management and economies of scale, we reduced food and packaging costs (as a percentage of revenues from company-owned and operated stores) by 3.1 percentage points year-over-year.

We continued to streamline our operations by pruning underperforming stores and optimizing unit economics. These actions led to a year-over-year reduction in rental expenses, labor costs, and other store operating expenses (as a percentage of revenues from company-owned and operated stores) by 1.5 percentage points, 3.0 percentage points, and 1.3 percentage points, respectively.

Benefiting from our cost optimization measures and increased brand recognition, our marketing expenses as a percentage of total revenues decreased by 2.6 percentage points year-over-year.

Additionally, we streamlined our headquarter costs, resulting in a significant reduction in adjusted general and administrative expenses as a percentage of total revenues by 3.4 percentage points year-over-year.

Turning to liquidity, as of June 30, 2024, the Company's total cash and cash equivalents, time deposits, and amount due from related parties in relation to the financing from RBI were RMB253.2 million (USD34.8 million), compared to RMB219.5 million as of December 31, 2023. The change was primarily attributable to the financing from our founding shareholders, partially offset by cash disbursements on the back of the expansion of our business and store network nationwide and the repayment of bank borrowings.

Looking ahead, our focus remains on executing our strategy to drive profitable, and capital-efficient growth. We will continue to strengthen our brand and expand our great value for money, freshly prepared food offering. We will also work closely with our sub-franchisees to drive traffic and enhance our supply chain efficiency, improving their store economics and, in turn, driving our bottom-line profitability.

Now I will turn the call over to Gemma for today's Q&A session. Gemma?

Question & Answer Session:

Gemma Bakx:

Thank you very much, Albert. We have a question here that came in via the webcast: Congratulations on achieving your first-ever adjusted corporate EBITDA profitability, that is a significant milestone. Can you elaborate on how Tims can maintain and achieve continuous profitability going forward?

Yongchen Lu:

I will take this one. We successfully reached adjusted corporate EBITDA profitability for the first time - amidst macroeconomic challenges and intense competition in the Chinese coffee market. This inspires us to provide more exceptional value-for-money products for our guests

Moving forward, we are steadfast in prioritizing profitable growth as our core strategy. Firstly, we will be bolstering our revenue through our unique Coffee Plus Fresh Prepared Food strategy, complemented by targeted precision marketing initiatives that resonate with our customer base very well. Secondly, we have achieved significant benefits from improving operational efficiency, reducing basically all cost elements year over year. This confirms to us that a relentless focus on optimizing unit economics is crucial for securing our long-term profitable growth and success.

Given the significant brand recognition we have cultivated, partnering with our franchisees makes us well positioned to drive our profitable growth capital-efficiently.

Back to you.

Operator:

Our next question comes from Steve Silver, from Argus Research. Steve, your line is open now.

Steve Silver, Argus Research:

Thank you, operator. My question is that in the past Q4 has been the most active quarter for new store openings. Is there any visibility into the number of stores growth for this Q4?

Yongchen Lu:

Thank you for the question, Steve. Yes, we are expecting more store openings in Q3 and especially in Q4 as usual. We have done very well for individual franchising in the first half of the year, and by the end of June. We opened 20 already. We have good momentum in individual franchising and so we are expecting to open many more in the second half of the year.
Thank you.

Operator:
Thank you. As a reminder, if you'd like to ask a question via phone, please press *11 to ask your question. Alternatively, you can submit your question via the webcast.

Gemma Bakx:
I will ask the next question that came in via the webcast: Does your Q2 adjusted store EBITA margin of 10.3% have room to growth further in the coming months – typically the busiest of the year as Steve just mentioned?

Yongchen Lu:
Yes, we always keep a sharp eye at streamlining our operations, optimizing our supply chain and cutting costs where appropriate. We are happy with the store margin level that we have achieved in Q2 and will always seek further improvement where we can find it.

Gemma Bakx:
The next question that came in is how does Tims analyze and interpret the competitive landscape within China's coffee market as it stands today – in the context of competitors exhibiting signs of growth weakness?

Yongchen Lu:
I will take that one. In the second quarter of 2024, the Chinese coffee market continued to face challenges, with notable players like Luckin and Starbucks China experiencing a decline in same-store sales by 20% and 14% respectively - as disclosed in their last quarter earnings.
We believe our distinctive Coffee Plus Fresh Prepared Food strategy sets us apart and does well amongst the intense competition – as we have done. Even as China navigates the trend of trading

down, there continues to be a strong and enduring pursuit of convenient and healthy food options among consumers. Our great value for money “Coffee Plus Bagels” combination is well positioned to cater to this trend.

To accelerate this strategy, we have completed made-to-order renovations in nearly 300 stores to date, which have shown sales growth already, and are on track to further roll out this renovations model to most of our stores by the end of the year. With very limited capital expenditures investment, we anticipate that this strategic enhancement will significantly drive incremental growth in our food revenues.

Back to you, thank you.

Gemma Bakx:

Thank you very much. I will follow up with the next question: with regards to the ongoing price war, are you seeing any signs of it cooling off or losing steam?

Yongchen Lu:

We have possibly been as bewildered as the next person about how long some of our competitors have been going at it. Some can last longer, some cannot go on forever. That said, we had not expected it to last this long.

Gemma Bakx:

As a follow up: in that ongoing price war, where does Tims position itself? Where do you see Tims in this?

Yongchen Lu;

While it obviously has an effect on us we do not really proactively participate in the pricing war. We are not in the premium category; we are good value for money. Rather than lowering our coffee prices, we have been attractively promoting our attractive combos, in line with our “Coffee Plus” strategy. We will continue to offer coffee and freshly prepared food at attractive prices and differentiate ourselves. And we’re launching value lines both in coffee and food to adapt to the market right now.

Thank you.

Operator:

Thank you. We now have a question from the audio line. We have a follow up question from Steve Silver, from Argus Research.

Steve Silver:

Thank you for taking this follow up. With the recent capital infusions and the achievement now of corporate EBITDA positivity, what do you see as the primary needs for use of capital moving forward, given that the sub-franchise model is capital light by nature?

Albert Li:

As Yongchen mentioned and to further our leadership and execute our strategy, we will be making investments, such as to implement the made-to-order renovations, which will enable our customers to see the ingredients we use and our fresh food prepared process, to be better visualized to them. We believe this will offer expanded revenue opportunities for us. With these renovations we can ensure that our food can come in a standard menu amongst all store formats. We also believe that the returns in our 'MTO' stores will be very good. Secondly, we also plan to increase spending on marketing efforts to expand in new addressable markets from multiple channels. So we will definitely invest in marketing. Also, we will invest in R&D to develop more value-for-money products – more value line products for our customers. Lastly, I want to mention, in the context of efficient use of capital, we do have plans to open more company owned and operated stores. First on the back of reusage of certain coffee machines, kitchen equipment and furniture from those closed underperforming stores, the additional CAPEX will be quite limited. So to address your question, that is how we plan to use capital from here.

Thank you.

Steve Silver:

Thank you for the additional color, I appreciate it.

Operator:

Thank you. We have no further questions from the audio lines.

Gemma Bakx:

I have one more question here if I may: do you expect the store to go up this year, or will you focus on pruning more underperforming stores and on store renovations? The second part of the question is – now that you have demonstrated success in expanding your capital-efficient sub-franchise model, do you foresee further changes in store concepts for Tims?

Yongchen Lu:

Yes, we do expect the store count to go up in the second half, and definitely in Q4. As I mentioned earlier, our individual franchises are ramping up quickly. The first half of the year we focused more on pruning underperforming stores. Now we have achieved positive corporate EBITDA, we will pick up with individual franchises in the second half.

Back to you, thank you.

Operator:

Thank you to all participants for your questions today. There are no further questions. I will hand over to Gemma for any closing remarks.

Gemma Bakx:

Thank you all very much. I have no further questions here either. Thank you all for sharing our good news with us today and we look forward to speaking with you very soon. Thank you very much.

Yongchen Lu, Albert Li:

Thank you very much.

Operator:

This concludes today's conference call. Thank you again participating, you may now disconnect.