Transcript of
RCI Hospitality Holdings, Inc.
1Q25 Earnings Call
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Participants

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Greetings, and welcome to RCI Hospitality Holdings First Quarter 2025 Earnings Call. You can find the company's presentation on RCI's website. Go to the Investor Relations section, and all the links will be at the top of the page.

Please turn with me to Slide 2 of our presentation. I'm Mark Moran, CEO of Equity Animal. I'll be the host of our call today. I'm coming to you from Denver, Colorado. Eric Langan, President and CEO of RCI Hospitality, and CFO Bradley Chhay, are in Houston.

Please turn with me to Slide 3. RCI is making this call exclusively on X Spaces. At this time, all participants are in a listen-only mode. A question-and-answer session will follow. This conference call is being recorded.

Please turn with me to Slide 4. I want to remind everybody of our safe harbor statement. You may hear or see forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those currently anticipated. We disclaim any obligation to update information disclosed in this call as a result of developments that occur afterwards.

Please turn with me to Slide 5. I also direct you to the explanation of RICK's non-GAAP financial measures.

Now I'm pleased to introduce Eric Langan, President and CEO of RCI Hospitality. Eric, take it away.

[1] This is a clean verbatim transcription that has been edited to increase readability.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Thanks, Mark. If everyone could please turn to Slide 6. Thank you for joining us today. Let me run through some key takeaways. All comparisons are year-over-year unless otherwise noted.

In our Nightclubs segment, we generated increases in total sales and same-store sales, while GAAP and non-GAAP operating profit was approximately level with the year ago quarter. In our Bombshells segment, total sales declined as expected, with the sale closure of underperforming locations, but GAAP and non-GAAP operating profit and margins both improved. On a consolidated basis, net cash provided by operating activities and free cash flow nearly matched year ago levels, and we continued to make notable progress with our Back to Basics 5-year Capital Allocation Plan.

During the first quarter, we sold or closed four underperforming locations in the Bombshells segment, for a total of five since September of 2024. We also repurchased 66,000 shares for $3.2 million. As of 12/31, we had 8,889,000 shares of common stock outstanding. In January, we acquired the Flight Club, a premier gentleman's club in the Detroit market. Purchase price was $8 million for the club and $3 million for the real estate. We estimate the club to generate about $2 million in annually adjusted EBITDA. We also opened a Bombshells in Denver. As part of the effort to improve Bombshells, we have changed leadership. Rafael Pedraza has been promoted to Director of Operations from Assistant Director.

Now here's Bradley to review our performance in more detail.

Bradley Chhay - Chief Financial Officer, RCI Hospitality Holdings, Inc.

Thank you, Eric. Please turn to Slide 7. All comparisons are year-over-year unless otherwise noted. Fourth quarter sales totaled $71.5 million. That largely reflects the sale and closure of the nonperforming locations in the Bombshells segment, partially offset by increased sales in the Nightclubs segment. Other gains totaled $2.2 million. Net income attributed to RCIHH common shareholders was $9.0 million. EPS was $1.01 GAAP and $0.80 non-GAAP. Net cash provided by operating activities was $13.3 million, free cash flow was $12.1 million, and adjusted EBITDA was $15.7 million.

Please turn to Slide 8. Nightclubs revenues increased $0.7 million or 1.1%. Key factors driving first quarter revenues included a 3.7% increase in same-store sales and the addition of three new or reformatted clubs. This was partially offset by the absence of Baby Dolls Fort Worth. Food, merchandise and other increased 8.6%; alcoholic beverages increased 3%; and service declined 3.7%. Other net gains totaled $0.8 million versus virtually nil in the year ago quarter. The first quarter 2025 amount included $1 million in additional cash proceeds from Baby Dolls Fort Worth insurance. Operating income was $20.9 million compared to $20.4 million. Margin was 33.8% of segment revenues versus 33.4%. Non-GAAP operating income was $20.6 million compared to $21 million, and non-GAAP margin was 33.4% of segment revenues versus 34.3%.

Please turn to Slide 9. Bombshells revenues declined $3.1 million or 24.7% due to the sale or closure of five underperforming locations and a 7.5% decline in same-store sales. This was partially offset by a full quarter of the Stafford, Texas location, which opened in mid-November 2023. Other net gains totaled $1.3 million versus virtually nil in the year ago quarter. The first quarter 2025 amount reflected a gain for the Bombshells that was sold. Operating income increased $1.9 million with a margin of 20.6% of segment revenues versus 0.7%. Non-GAAP operating income increased $0.5 million with a margin of 6.7% of segment revenues versus 1.2%.

During the first quarter, there were no weather-related closures for Nightclubs or Bombshells. To date, however, in the second quarter, we've had 14 days for Nightclubs and seven days for Bombshells.

Please turn to Slide 10. Corporate expenses increased $1.7 million on a GAAP and non-GAAP basis. This was due to the establishment of an insurance reserve.

Please turn to Slide 11. We have some slides upcoming that discuss free cash flow and adjusted EBITDA, which are non-GAAP. In advance of that, we wanted to present the closest GAAP equivalents on this slide, which are operating income, net cash provided by operations, and net income.

Please turn to Slide 12. We ended the first quarter with cash and cash equivalents of $34.7 million. During the quarter, we used $3.2 million to buy back shares. As a percentage of revenues, free cash flow was 17% and adjusted EBITDA was 22%. Free cash flow was slightly lower than the year ago quarter because maintenance capex was almost 30% higher.

Please turn to Slide 13. Debt at December 31 declined $2.7 million from September 30, reflecting scheduled paydowns. The weighted average interest rate was 6.65% compared to 6.61% in the year ago quarter. Total occupancy costs were 8% versus 8.2% a year ago. Debt to trailing 12-month adjusted EBITDA was 3.32x compared to 3.28x in the preceding quarter. This metric will decline as sales grow from locations that have come online more recently and from those anticipated to open. Debt maturities also continue to remain reasonable and manageable.

Now here's Eric.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Thank you, Bradley. Please turn to Slide 14. For those of you new to the company, let me review our capital allocation strategy. Under our plan, we will allocate 40% to club acquisitions and 60% to share buybacks, dividends, and debt repayment. The goal is to grow free cash flow per share by 10% to 15% on an average annual basis.

Please turn to Slide 15. Operationally, this means focusing on our core Nightclubs business. Currently, we are evaluating every club in our portfolio. The goal is to increase same-store sales on a regular basis. Our Nightclubs plan also involves acquisitions. Our goal is to acquire an average of $6 million of adjusted EBITDA a year, focusing on the best clubs, buying base hits with occasional home runs. Our target metrics remain the same: 3 to 5x adjusted EBITDA for the club business and fair market value for the real estate, targeting 100% cash-on-cash returns in three to five years. Purchases would be made with cash on hand, bank financing and seller notes.

For Bombshells, our plan calls for improving the performance of existing locations. Our near-term target is 15% operating margins and a return to same-store sales growth. Our plan also calls for finishing two other locations currently in development in Lubbock and Rowlett, Texas.

For the final part of our plan, we anticipate continuing to implement a program for regular buybacks. We also anticipate small dividend increases annually.

Altogether, we expect to generate more than $250 million in free cash flow over the next 5 years and buy back a significant amount of stock. Given where our shares are trading, and our view of what the business can do, we believe this is a great use of our capital.

Our fiscal '29 targets call for hitting $400 million in revenues, $75 million in free cash flow, and reducing share count to 7.5 million shares. This would result in a doubling of free cash flow from fiscal '24 to approximately $10 a share in '29.

Please turn to Slide 16. With Bombshells Denver now open, we have six remaining developments. Chicas Locas El Paso is finished and reopening is planned for March 1. Interior construction at Bombshells Lubbock is underway, and we are targeting a mid-March opening. We're completing final finish outs at Rick's Cabaret Central City, and we are targeting an April opening. Framing and stucco are underway at Bombshells Rowlett, and we are targeting a May open. I would like to note that both Lubbock and Rowlett construction are being financed through bank loans. We are still awaiting construction permits for Baby Dolls Fort Worth West, and we are awaiting engineering review of our plans for the original Baby Dolls to be rebuilt.

At this point, I'd like to thank our loyal and dedicated teams for all their hard work and effort and for all our shareholders who believe and make our success possible. Now, here's Mark.

Mark Moran - CEO, Equity Animal

Thank you very much, Eric and Bradley. To start things off, we'd like to take questions from RICK's analyst, Scott Buck of H.C. Wainwright. Scott, please take it away.

Q – Scott Buck - H.C. Wainwright & Co, LLC, Research Division

Bradley, I want to ask about the $1.7 million to establish the self-insurance reserve. Is that a non-cash or cash expense? Should we think of that as onetime in nature?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

I can answer that, Scott. I think it's one time. It was a catch-up deal since we decided to self-insure starting in October due to the outrageous cost of insurance. We're in the process of setting up our captive. Once the captive is set up, we will see how that all plays out. But right now we have to follow GAAP rules on accounting for this insurance potential liability. It goes into a reserve account and the balance just sits there. If we get claims or have to pay defense costs, for this time period, it will come out of those reserves.

Q – Scott Buck - H.C. Wainwright & Co, LLC, Research Division

Okay. You guys did not add that back into your adjusted EBITDA number, right? So I think that adjusted EBITDA is a little north of $17 million.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Yes, we did not have that back in. The rules don't allow for that.

Q – Scott Buck - H.C. Wainwright & Co, LLC, Research Division

Okay. I appreciate that. And Eric, the club you acquired in Detroit, can you talk about whether there's any opportunity there to improve the EBITDA margins? I know you said $2 million this year, but I'm curious if that could move a little higher over time?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

It's too early to tell. We've only had it for a few weeks. I don't know if you're familiar with the Detroit weather and how it's been for the last few weeks, but old man winter has given us a very, very cold welcoming into Detroit with extremely cold temperatures and lots of snow. It's really hard to tell. But yes, we believe that we will definitely be able to do much better as we get rolling in that market and get out of this unseasonably cold weather.

Q – Scott Buck - H.C. Wainwright & Co, LLC, Research Division

Great. I appreciate that. On the Bombshells that closed, are there any residual cash outlays that you guys are responsible for on those five locations that you shut down?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Not at this point. We do have a landlord that's suing us, but we believe that our defense will be fine there. The parent company did not guarantee the lease in any form or fashion. They're trying to tie the parent company in, but we don't believe that it’s going to be feasible for them to do it based on Texas contract law.

Also, I want to make sure you understand that the $1.7 million insurance reserve is the excess insurance that we put on corporate. The actual number for reserve is $4.1 million, and it was basically divided by segment based on previous years’ insurance and a prorated share of the excess. The $1.7 million is what we call a makeup for how they do these actuarial tables. It's insane math. I've studied and I get it, but it's extremely complicated. I call it trigonometry.

It was pretty insane as we were trying to go through all this and figure out how to do it because we've never guessed our insurance costs in the past. We've always had it, but this is a guess of in a worst case scenario what would our maximum liability for the quarter be, is how we had to look at this. We had to take all these historic deals and take best quarters and worst quarters over a five-year period, combine it all in together, and it became very complicated. But this is what the people who do these actuarials came up with. So that's how we looked at it

Q – Scott Buck - H.C. Wainwright & Co, LLC, Research Division

I appreciate the clarification there. And then last one for me. If you could just kind of speak broadly to the operating environment, especially on the club side. What are you seeing? What is kind of in-store here for the first part of 2025?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

If you look at the December quarter, we saw our two largest contributors were actually down a little. A lot of our midsize clubs were up. I don't understand that other than that we've really gotten very good at going from quality to quantity of customer, trying to push more people through the door. Some of our VIP spend is back, but obviously we saw service revenues decline 3.7% year-over-year. So it's not where we'd like it, but we were able to make some cost or some pricing changes and make up some of that in food, merchandise and other revenue sources by increasing that to 8.6% and raising overall Nightclubs revenues 3.7%.

I'm very confident that we have the pricing power that we need if we do need to increase prices to keep our margins in line and keep our same-store sales growth as close to 3% as possible, which is our goal as part of our five-year plan, keep that same-store sales growth as steady at 3% as we can, as well as increasing revenues with new acquisitions and monitoring and controlling costs.

If you look right now, we have somewhere between $23 million and $28 million in non-income-producing assets that we're going to start trying to lease or sell or somehow make those assets produce income for us or give us our cash back so that we can take it and put it in other places. That's going to be a big component of the next 9-12 months.

If you go back and look at when we originally adopted the capital allocation strategy in 2015, I think we're in early 2017, where we've divested some properties. We have a couple of clubs that we're looking to sell as part of that $23 million to $28 million in assets as well as plain, raw properties that we bought in the past. We'll keep pushing on that, working on that, and that will play into our factors of getting to our growth rates as we get into 2026.

Mark Moran - CEO, Equity Animal

Next up, we have Orchard Wealth. Please take it away.

Q – Jason Scheurer – Orchard Wealth Management

I see that we have 56 clubs right now. Does Detroit make it 57?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

I believe so, but I don't know if we're counting El Paso in the 56 or not. We might have 58 when El Paso opens on March 1. We have so many clubs. I actually have to go to the accounting office to know exactly how many clubs are open and generated revenue this quarter. So I think those are revenue generating.

Q - Jason Scheurer – Orchard Wealth Management

With El Paso reopening, what are you thinking about sales from these locations? You've got seven locations -- four clubs and three Bombshells that are going to come online, not including Detroit. What are you thinking that total sales would be once all of those are incorporated onto the existing number?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

We've reformatted El Paso. The old El Paso club used to generate about $600,000 in EBITDA. I'm hoping with the new format that we can actually generate more income than that, but I just don't know at this point. We don't have liquor yet, but we're trying to get the liquor license there. Probably very similar numbers to what we're doing before, around $600,000 in EBITDA out of El Paso.

Q - Jason Scheurer – Orchard Wealth Management

Obviously, we don't know anything about Central City because that's brand new.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Yes, that will be brand new. I'm hoping it's $1 million to $2 million EBITDA a year. There's a lot of moving factors when we get it open -- whether we open the whole club, whether we open four days a week or seven days a week. There are a lot of factors at this point until summer. I'll have a really good idea on the August call with that location.

Q - Jason Scheurer – Orchard Wealth Management

And then the Baby Dolls West Fort Worth?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

We're shooting for around the 1st of October to complete that construction and get open on the West Side. Then we're shooting for January on the location where we had the fire. But both of those are still up in the air because we're still in permitting. I know once we get the permits, we can build them in about six months, but we've got to get the permits in place and get everything rolling on both.

Q - Jason Scheurer – Orchard Wealth Management

And then just to go back because obviously, the rebuild because of the fire, how much was that contributing before the fire?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

We had it up to about $4 million in revenues and margins were probably about $1.5 million, about 35% margins on $4 million for that location. The good news is we didn't lose all of that because a lot of that customer base went to the club that we own across the street which we reformatted. I'm going to guess we recouped about 40% of that. So we really only lost about $1 million, not $1.5 million. Say a third of it we recouped, so we're probably up about $0.5 million at the other location. We probably lost about $1 million location.

The big hit for us was the late night change in Dallas that made us reformat XTC Cabaret. That's been the biggest hit. If you look at all the numbers, if we still have XTC, we would be in way, way better condition than we are right now, as far as EBITDA, free cash flow -- everything would be up probably between $2 million to $2.5 million on EBITDA and $1 million plus on free cash flow.

Q - Jason Scheurer – Orchard Wealth Management

So the way it's looking, we've got about 60 locations right now. And with all said and done a year from now, we're looking at seven more. So 67?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Denver plus six. Denver is open now. Denver was not open in this quarter, but it opened in January.

Q - Unknown Analyst

Any news on any buys or things you're still working on?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

We have clubs out there that we're looking at, lots of opportunities. You'll see that we actually adjusted the capital allocation strategy from 50-50 with debt and acquisitions on one side and stock buybacks and dividends on the other. We moved debt to the stock buyback and dividend side and raised that to 60%. That basically works out to about $13 million in stock buybacks, $2.5 million in dividends, $14.8 million in debt reduction or debt payoff. That leaves us with $20 million in cash on the other side of that equation to go to the cash portion of acquisitions.

Q - Jason Scheurer – Orchard Wealth Management

But I'm assuming if something comes along that's better, you'll make an exception.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

We'll always follow strategic rationale should one arise. But for the next five years, any strategic rationale I can see in the foreseeable future will relate directly to allocation of capital per the capital allocation strategy. In other words, we would change percentages here. We'd buy less stock because we have better acquisitions or the stock price gets really, really cheap, or we do fewer acquisitions and much more stock buyback. Those are the only two real factors that we're going to be juggling any kind of money around. I don't have any intentions of building anything new at this point. I'm not even looking. People call me all the time, and I say, "No, we're not building anything." Would you be interested in this? I say, "Is it open? Is it making money? No? I would probably not be interested."

We are very risk off until all of this construction is done, all of our stuff is open, and we've really tightened our capital strategy to the max—all of our expenses, all of our non-income producing assets—basically, we've got all our ducks in a row before we go out and say, "Okay, maybe we can risk building a club over here or buying this club and re-concepting it" or something if we think we have a really good concept that can go into a license that's not producing. But for at least the rest of this fiscal year '25, I think we stick correctly with the plan. We have enough on our plate, we don't need to add anything else. What we need to do now is just batten down all the hatches and make everything perfect.

Q - Jason Scheurer – Orchard Wealth Management

And then on the last point -- the idea being over the course of the year, you got $23 million to $28 million worth of nonperforming assets that you'll be repositioning that could be used for any of these other items we discussed.

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

Absolutely. It will become capital and go into our cash, and then we'll allocate it accordingly.

Mark Moran - CEO, Equity Animal

Fantastic. Thank you so much for that. Next up, we have D&D Realty. Please take it away.

Q – @D_Drealty @D_Drealty

So you just mentioned that you're looking at selling some clubs. How many clubs are you currently looking to divest? You guys have, I guess, now 88 properties that you own. Have you done an analysis on how much your real estate is actually worth? I know your property and equipment, you carried at about $280 million. But what do you think is fair market value for all your real estate?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

A lot of that is equipment and not necessarily real estate. Appraised values have been all over the place. We haven't really had appraisals. I think the last appraisal that we got was in 2021 on a few properties that we put into the new refi. The original refi was done in '17, I think. So we haven't done any new appraisal on those properties. If I had to guess, real estate is probably in the $250 million to $280 million range, real estate without all the equipment and everything else. But it's hard to tell. I just haven't laid it all out.

Q – @D_Drealty

And then how many clubs are you looking to divest?

Eric Langan - President and CEO, RCI Hospitality Holdings, Inc.

There are two clubs that are both in the same area. It's just a market we want to get out of, and we've got a broker who sells adult clubs, who's meeting with people. We're keeping it on the downlow. We're not going to publicly advertise these clubs for sale. We will sell them through a broker who has a lot of contacts with people already in the adult entertainment business who are looking at those two locations with us right now.

Mark Moran - CEO, Equity Animal

Fantastic. Thank you for that question. On behalf of Eric, Bradley and the company as well as our subsidiaries, thank you, and good night. Please visit one of our clubs or restaurants to celebrate Valentine's Day, Saint Patrick's Day, or just to have fun and have a great time. Take care, and have a good one.