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GEN Restaurant Group, Inc. (GENK) Q1 2024 Earnings Call Transcript

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GEN Restaurant Group, Inc. (NASDAQ:[GENK](#)) Q1 2024 Earnings Call Transcript May 14, 2024 8:00 AM ET

Company Participants

Thomas Croal - CFO

David Kim - Co-CEO

Conference Call Participants

Todd Brooks - Benchmark Company

George Kelly - ROTH Capital Partners

Operator

Good afternoon, and welcome to the GEN Restaurant Group First Quarter 2024 Earnings Conference Call. All participants will be in listen-only mode. [Operator instructions] After today's presentation, there will be an opportunity to ask questions. [Operator instructions] Please note, this event is being recorded.

I would now like to turn the conference over to Tom Croal, the company's Chief Financial Officer. Please go ahead.

Thomas Croal

Thank you, operator, and good afternoon. By now, everyone should have access to our first quarter 2024 earnings release. If not, it can be found at www.genkoreanbbq.com in the Investor Relations section.

Before we begin our formal remarks, I need to remind everyone that our discussions today will include forward-looking statements within the meaning of federal security laws, including, but not limited to, statements regarding how growth plans and potential new store openings as well as those types of statements identified in our quarterly report on Form 10-Q for the period March 31, 2024, and our subsequent reports filed with the SEC.

These forward-looking statements are not guarantees of future performance, and therefore, you should not put undue reliance on them. These statements represent our views only as of the date of this call and are also subject to numerous risks and uncertainties that could cause actual results to differ materially from what we currently expect.

We refer you to our recent SEC filings, including our quarterly report on Form 10-Q for a more detailed discussion of the risks that can impact our future operating results and financial condition. Except as required by law, we undertake no obligation to update or revise these forward-looking statements in light of new information or future events.

During today's call, we will discuss some non-GAAP financial measures, which we believe can be useful in evaluating our performance. The presentation of this additional information should not be considered in isolation or as a substitute for results prepared in accordance with GAAP. Reconciliations of the non-GAAP financial measures to the most directly comparable GAAP financial measures are available in our press release and our SEC filings, which are available in the Investor Relations section of our website.

Now, I'd like to turn it over to our Board Chair and Co-CEO, David Kim.

David Kim

Thank you, Tom, and good afternoon, everyone. In the first quarter, we continued executing on our strategic growth road map to expand GEN's geographic coverage and overall market share. This quarter, we achieved a 16% year-over-year increase in total revenue, largely driven by the opening of two new locations, both of which have been performing at or above our expectations.

Additionally, we bought out our 50% partner in Hawaii and can now consolidate the revenues and results of operations in our financial statements starting in the second half of February. We also completed the build-out of our business development infrastructure, which provides us with a much clearer view into our growth pipeline and gives us the ability to accelerate restaurant openings moving forward.

We experienced an improvement in the second half of the quarter by achieving stronger margins as a result of implementing operational efficiencies, which we have also seen continued into April. As a result, I'm proud to report that our overall financial performance was in line with expectations for the quarter, and we remain on track to achieve our goals for 2024 and excited to see the positive momentum building.

Before I discuss our performance in more detail, I'd like to reiterate who we are, what makes GEN Korean BBQ truly unique and why we believe it sets the stage for sustained successful going forward. GEN Korean BBQ is an all you can eat, full service, cooking yourself at your table, casual dining restaurant concept that offers consumers a variety of best-in-class proteins, including stake, pork, chicken, seafood as well as salad alternatives across both lunch and dinner, all at an affordable all-inclusive price.

GEN is value concept. Unlike other restaurant concepts, GEN Korean BBQ's model allows us to minimize our kitchen space and maximize the number of tables while benefiting from the absence of costly traditional kitchen staff because we don't make anything as all products come premade because of this, less labor is required. Thus, we can keep our prices low and provide the best value to our guests.

This is incredibly important to keep in mind as we continue to navigate an uncertain consumer demand environment where value becomes a key component for today's consumers' decision-making. We've been able to replicate this model over and over again by opening new restaurants with an average unit volume of \$4 million to \$5 million per year, generating \$800 plus per square feet and 18% to 20% restaurant level adjusted EBITDA margin. These attractive unit level economics allows us to generate, on average, a cash-on-cash return of 40% and a payback period of approximately 2 to 2.5 years, which ranks amongst the best in the industry.

With that background, I'd like to address our restaurant development. In the first quarter, we opened two new restaurants in Seattle, Washington and Dallas, Texas. And most recently, in April, we opened a new restaurant in Jacksonville, Florida. With these three locations plus our acquisitions of the remaining ownership of our Hawaii location and five others starting construction that are expected to open by year-end, we have made significant progress towards reaching our goal of at least eight to nine new restaurants in 2024.

We also have an additional 10-plus leases in various stages of negotiations in new markets as well as existing markets that we would expect to open in 2025. As we look at our broader expansion plan, we have strong forward momentum and remain highly confident in our ability to achieve our five year plan that we discussed at the time we went public.

In addition to the 2024 and 2025 restaurant developments I mentioned, we expect to develop 20 to 30 additional new restaurants, totaling between 70 to 80 by the end of 2026. We will have more than double the size of the company since our IPO. With our attractive unit level economics, we believe this positions us well to deliver notable profitable growth and expand shareholders' value over the next three years.

We're doing all this primarily using free cash flow with minimum debt. Recently, we launched our new premium menu at all 40 locations nationwide that features Gourmet Options for an additional charge per guest. The new menu options helped us improve our revenues in the month of March. It is proving to be a valuable addition to our overall consumer experience, and we believe the additional premium menu pricing will begin to increase our average customer check in the coming quarters. Additionally, we have started testing our new premium drinks. We'll provide more data on this program in the coming quarters.

In conclusion, we are confident about our growth prospects moving forward. We're a company that was profitable when we went public, it is still profitable and will be profitable going forward. This makes sense among the best in the industry.

Our culture of growing while maintaining profitability is a core principle and value of our management team. With that, I would like to turn the call over to our CFO, Tom Croal, to discuss our quarter one financial results.

Thomas Croal

Thank you, David. For the first quarter, revenue increased 16% to \$50.8 million compared to \$43.9 million in the first quarter of 2023, driven primarily by new unit openings and the addition of our Hawaii restaurant in February. Same-store sales decreased by 1.8% in the first quarter of 2024, while estimates indicated we would have a 3% drop in the first quarter.

We had a strong month of March, which continued into April and brought us back closer to last year's revenue levels. Cost of goods sold as a percentage of company restaurant sales increased by 80 basis points to 33.4%, primarily due to the initial start-up of the company's new premium menu.

Payroll and benefits as a percentage of company restaurant sales increased by 70 basis points to 31.8% due to increases in minimum wage rates in certain markets, primarily California as well as short-term higher labor costs in newly opened restaurants as the company trains staff and management.

It's worth noting that despite the minimum year-over-year increase, we reduced payroll and benefits by 30 basis points on a sequential basis compared to the fourth quarter of 2023. Occupancy expenses as a percentage of company restaurant sales increased by 60 basis points year-over-year to 8.3% due to the new restaurant openings over the last 12 months.

Other operating expenses as a percentage of company restaurant sales increased 60 basis points year-over-year to 10%. Other operating expenses have been reduced by 112 basis points from the fourth quarter of 2023.

Adjusted restaurant level EBITDA as a percentage of total revenue was 16.4% compared to 19.6% in the first quarter of 2023. The year-over-year decline was due to the previously mentioned cost increases. Going forward, we anticipate our 2024 restaurant-level EBITDA margin to approach 18% range or better as we optimize our operating expenses and labor costs.

It's worth noting we had a strong month of March in this regard, which we believe not only sets us up well for continued improvement in the coming quarters but also continues to put us on a strong long-term trajectory.

G&A during the first quarter was approximately \$3.9 million or 7.7% of revenue, excluding stock-based compensation, which went mostly to employees of the company and not to the founders. The year-over-year increase in G&A is primarily due to the addition of new personnel required for our increasing level of new restaurant development, along with public company costs, which weren't present in the prior year period.

Adjusted EBITDA increased to \$6.4 million, including preopening costs. This compares to \$5.8 million for the first quarter of 2023. Without preopening costs, adjusted EBITDA would be approximately \$7.9 million.

Our net income was \$3.7 million or \$0.11 per diluted share compared to net income of \$4.5 million in the first quarter of 2023. The decline was largely due to increased expenses related to new restaurant development and increased general and administrative expenses associated with being a public company, partially offset by the \$3.4 million gain on purchase related to the buyout of the remaining 50% of our Hawaii restaurant.

Now, turning to liquidity. As of March 31, we had no long-term debt, except for a minor \$5 million in government-funded EIDL loans, which we had when we went public. And we still have \$20 million available in our revolving line of credit, which we have not used.

Additionally, we maintained a strong balance sheet with \$28.1 million in cash and cash equivalents, which declined from \$32 million at December due to two nonrecurring payments. The first payment was \$3 million used to acquire the remaining 50% of our Hawaii location, which included the rights to participate in future GEN Restaurants in the state. And the second payment was repaying in advance to a founding member of \$0.9 million.

Without these onetime payments, our cash balance remains relatively unchanged as we generated strong free cash flow, allowing us to self-fund most of the \$4.1 million of capital expenditures in the quarter. I will say it again, the free cash flow we generated from operations paid for most all of our restaurant development costs in the first quarter.

GEN generates strong free cash flow, and we'll continue to self-fund the majority of restaurant development costs throughout all of 2024. As for the outlook for 2024, we expect total revenues to range between \$200 million and \$205 million and to open eight to nine new restaurants.

This concludes our prepared remarks. We'd like to thank you again for joining us on the call today, and we are now happy to answer any questions that you may have. Operator, please open the line for questions.

Question-and-Answer Session

Operator

We will now begin the question-and-answer session. [Operator Instructions] Our first question today is from Todd Brooks with The Benchmark Company. Please go ahead.

Todd Brooks

Hey, thanks for taking my question and congrats gentlemen on really good sales performance and what was a choppy environment for those all operators in the first quarter.

David Kim

Thank you, Todd.

Todd Brooks

If I could dig in a little bit on the premium. When do we reach the point that we were fully rolled out across the 40 units?

David Kim

I'm having a little bit of a hard time due to the background noise.

Thomas Croal

David, the question was, when did we finish the rollout of the premium main menu.

David Kim

I think we've completed and we couldn't do it all at once because our distributor and our manufacturers couldn't keep up. So, we rolled it out in segments by markets, but I think the completion of the total rollout was towards the end of February.

Todd Brooks

Okay, great. And anything you can share with us, David or Tom, around attach rates? And I think at one point, you were looking at making premium meats available on an a la carte basis, too. I'm just trying to get to the kind of calculation behind how we should think about premium needs as a driver of higher average test going forward.

David Kim

Yes. So, how the premium menu works is, the guest has a choice to either purchase a premium menu for an additional dollar, but if they don't want the all-you-can-eat option, they can select from each item on the menu and just purchase a la carte. You don't have to have an all-you-can-eat experience. Therefore, we have prices on the premium menu per item. So, they can either choose to say, I will take the all-you-can eat or I'll just purchase one or two or three a la carte.

Todd Brooks

Okay, great. So, just two final ones, and I'll hop back in queue. One, if you had to take the early experience in March and apply it to a full quarter, maybe what do you think the average check impact from premium should be in our modeling? And then second, David, you mentioned a test of premium drinks. Any additional color you can give us on that? And at one point, the table turns were so strong that we didn't want to slow down transaction time. So, how do we work premium drinks into the experience without slowing visit times? Thanks.

David Kim

Sure. I can cover the drink side first here. The premium drinks is not the drinks that perhaps one experience is going to a high-end steakhouse. These premium dreams, we're working with Coca-Cola and our other vendors where there are cocktails, Korean cocktails, the premium drinks are not designed to where our guest stays longer.

It is more of a fun drink. So, it is part of our just spending the time while they're cooking the food that they can experience that. So, it will not come in. The drinks won't come with, let's say, Martin Glass where it's fancy. That's not the premium dreams that we're thinking of. It's another way of creating new drink experience that will not hinder the table trend.

The second question, Tom, perhaps you can answer that? I don't think we still have clear numbers in terms of the guest track average because the numbers we're getting still, we still need a lot more training to be done with our staff to suggest or premium needs. It's not consistent when a store will do very well in percentage of sales. One store needs help in that. So it's still very fluid. But one thing is a fact, we're not going to go off this premium menu. This will be a permanent offering going forward for GEN.

Thomas Croal

Todd, I would just add that we'll have more information in the coming quarters. We've really just had a month under our belt, and we're building on our database, but we are seeing an uptick, but we'll report that back in the future as we get more information.

Todd Brooks

Okay, great. Thanks to you both.

Thomas Croal

Thank you.

David Kim

Thank you.

Operator

The next question is from George Kelly with ROTH Capital Partners. Please go ahead.

George Kelly

Hi, everyone. Thanks for taking my questions. Just a quick follow-up on the last question that you guys just responded to. Tom, didn't you say in the prepared remarks though that comps -- did you say it was the line that they approached breakeven? Or could you be more specific, I guess, on what comps were in March and April?

Thomas Croal

Yes. The comps in March and April were better than January and February. So, as the whole industry has been down by much larger percentages, if you remember, in the fourth quarter, we were down 1.7% to the prior year. In the first quarter, we ended up at 1.8%. That was more than that in January and February, and we closed the gap in the month of March, and then we kept that closed gap in the month of April. So, we've been more closer to zero in the last March and April.

George Kelly

Okay. That's helpful. And then a couple of questions on your openings plans for this year. I think it's 5% that you mentioned. I'm curious if you could fill us in on where those are and what the cadence of the openings is throughout the year? And then also, I was a little unclear, David, I think you said something about 20 to 30 by year-end 2026. And I was just not quite sure, is that sort of cumulatively between now and year end 2026? Or was there something about that fiscal year that you were trying to hint at?

David Kim

Okay. So, when we announced that for the year 2024, we will finish 8% to 9%, correct. So, we have opened three right now, and we have five under construction. And if you add the one that we purchased in Hawaii, that should get us up to that 9% number. We announced additional 10 anywhere in lease or lease negotiations. But we wanted to be conservative. We actually have a lot more, but we did not want to press upon but to execute and then tell the Street that we are able to execute.

So, it is actually an additional going all the way to 2026. As the quarters go by, as we close more deals and sign more deals, we'll get a better picture of how 2026 is going to look. At this point, our 2025 basically filled up and there's another doubling of quotes we have that we think we can announce probably next quarter or in following quarter. So, the numbers are very fluid, but more in the larger numbers than what we have disclosed today.

George Kelly

Okay. Thank you. And maybe I'll just ask one more still on openings. You commented that the two or I guess three that you've opened so far this year have performed well versus your targets. I was just curious, like is there something that you would attribute that to, whether it's maybe good locations or good marketing or anything else? And then can you quantify what a good opening is versus your targets? I was just curious if could you give an AUV or any kind of more quantification around it?

David Kim

Okay. Let's try it this way. We have restaurants that opened in average versus in this particular one that we opened, we don't want to disclose due to perhaps maybe competitors out there. But we had one restaurant that we opened probably was our number two in terms of new restaurant openings in terms of sales.

So, our brand is very well known throughout the country. And by the way, this location was a new market. So, we know that our brand crosses very well outside of our core market, which we started in California. So, it just proves that our younger generation customer base are able to communicate our message and our products very well, which travels in terms of how people communicate amongst themselves promoting who we are as GEN.

So, it's the same promotion we do. We still don't have a marketing department. These are all organically grown. And we've been very fortunate and very blessed. But all comes down to how we execute. Execution is everything to what we do. We have a lot that we still need to improve on, but we think that our management team is doing a really good job executing the opening of these restaurants.

It's a lot of pressure opening new restaurants because of sometimes the new markets, we don't have the staffing. We have to spend management to open these. So, there's a lot of moving pieces that get behind the new openings. So, when I said it is like the number two store opening in terms of sales volume with our previous restaurant, it means that -- it means a lot in terms of how well we are doing right now.

George Kelly

Thank you.

Operator

The next question is from CJ Dippolito with Craig Hallum. Please go ahead.

Unidentified Analyst

Hi, guys. It's CJ on for Jeremy. Thanks for taking my questions. Just wanted to see if you guys could comment on any sort of uplift that you might be seeing from the FAST Act being implemented in California. I know a lot of other QSRs had to raise menu prices in response to the wage increases. So, I would think that kind of enhances your value proposition. So, I know you're still early on, but curious if that's resulted in better traffic.

David Kim

In my opinion, not just the increase of labor costs going up, there are headwinds with the public. So, we've always maintained our position that we are a value-driven concept. We might raise a price here and there in location, but we did not raise our price. And when we were perhaps challenged in the past to say how come we're not raising prices enough? And can we sustain this margin with an increase of the labor cost.

Yes, we deal with those issues, but we did not raise our prices. We made better decisions on labor control and we think we can continuously maintain even under the pressure of an increased labor cost by continuously finding ways to be more efficient.

And we don't want to be outpriced in the market when we all know in my humble opinion that the consumers, because of many reasons, including inflation, they are hurt. We hear that with restaurant companies that are shutting down, retail companies like \$0.99 places shutting down. So, we just maintain that we want to continuously provide value, continuously find efficiencies to combat those external pressure that a lot of restaurant companies are getting, especially the labor side.

Unidentified Analyst

Okay. Got it. Thank you. That's helpful. And then now one more, if you don't mind. Sorry, if I missed it at the beginning of the call, but I'm curious to hear about lead times for new openings. I think previously, you said it takes 11 months to a year. Have you seen that come in at all? And have you seen the price of new builds come in at all as you're progressing through the pipeline?

David Kim

It is all over the map, depending on which state, which city. We've seen some improvements, very little improvements with cities, but we've seen improvements with our contractors, with the build-out of the team that we have, we are shrinking the build-out time by at least a half a month, and we're finding more ways to get the cost down.

So, we're not just depending on whether the municipalities will change their behaviors. Some have, but it's a very small amount. So, therefore, we have to put a lot more locations under contract so that we are not tied to and be dependent on the outcome of how the cities will give us our permit. Here is this. Once we get our governmental permits to start construction, we're in full control of when these restaurants can complete their construction and open.

Unidentified Analyst

Okay. Thank you. I'll hop back in the queue. Good luck with the rest of the year guys.

David Kim

Thank you.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to David Kim for any closing remarks. Mr. Kim?

David Kim

Thank you very much for being on this conference. If there is any questions, you're welcome to reach us, and thank you for believing in what we do. Thank you.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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