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Mister Car Wash, Inc. (MCW) Q2 2024 Earnings Call Transcript

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Q2: 2024-07-31 Earnings Summary

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Press Release

10-Q

EPS of \$0.11 **beats by \$0.02** | Revenue of \$255.04M (7.66% Y/Y) **misses by \$256.91K**Mister Car Wash, Inc. (NYSE:[MCW](#)) Q2 2024 Earnings Call July 31, 2024 4:30 PM ET

Company Participants

John Lai - Chairman and Chief Executive Officer

Jed Gold - Chief Financial Officer

Conference Call Participants

Justin Kleber - Baird
Henry Carr - UBS
Chris O'Cull - Stifel
Christian Carlino - JPMorgan
David Bellinger - Mizuho
John Heinbockel - Guggenheim
Simeon Gutman - Morgan Stanley
Phillip Blee - William Blair
Peter Keith - Piper Sandler
Robby Ohmes - Bank of America
Tristan Thomas-Martin - BMO Capital Markets

Operator

Good afternoon and welcome to Mister Car Wash's Earnings Call to discuss the Financial Results for the Second Quarter ending June 30, 2024. [Operator Instructions] Please note that this call is being recorded and a reproduction of this call in whole or in part is not permitted without written authorization from the company.

Speaking from management on today's call are John Lai, Chairman and Chief Executive Officer and Jed Gold, Chief Financial Officer. After John and Jed have made their formal remarks, we will open the call for questions.

During this conference call, references to non-GAAP financial measures will be made. A complete reconciliation of these measures to the most comparable GAAP measures have been included in the company's earnings press release issued earlier today and posted to the Investor Relations section of the company's website at mistercarwash.com. As a reminder, comments made on today's call may include forward-looking statements, which are subject to significant risks and uncertainties that could cause the company's actual results to differ materially from the management's current expectations.

Please be advised that the statements made today are current only as of this call and are based on the company's present understanding of the market and industry conditions. While the company may choose to update these statements in the future, they are under no obligation to do so unless required by applicable law or regulations. Please review the forward-looking statements disclaimer contained in the company's latest annual 10-K and 10-Q reports. As such, factors may be updated from time to time and other filings with the Securities and Exchange Commission.

I will now turn the call over to Mr. John Lai. Please go ahead, sir.

John Lai

Good afternoon, and thank you for joining our second quarter earnings call. I'd like to start with a quick update on Houston and the impact of Hurricane Beryl. As many of you are aware, the storm damaged a lot of power lines, and it took the city several weeks to get things back up and running. We initially had to close 42 of our stores and then began to reopen as power was restored. I am happy to report that today all stores are open and processing cars.

Now allow me to update everyone on Q2, which is a strong quarter by many measures. Sales increased 8% to \$255 million. Comp store sales increased 2.4%. Adjusted EBITDA increased 20% to \$89 million. Adjusted EBITDA margin increased 360 bps to nearly 35%. Titanium member adoption was 20% of our member base and our UWC member base increased 3% year-over-year. The only headwind right now remains to be retail traffic, which has been soft.

In Q2, we opened 9 new stores, ending the quarter with 491 locations. When we hit the 500 store milestone, which is right around the corner, we plan on raising our glass and having a shot of tequila and celebrating doing what no one thought was possible. When it comes to our Titanium introduction, we couldn't be happier with how our members have responded. Today, we sit at 20% membership penetration or over 400,000 members who are enjoying the mirror-like finish and 360 degrees of protection.

Building upon our long tradition of developing new and innovative products, Titanium has truly accentuated the carwash experience while extending our competitive advantage with our proprietary in-house solution. From the very early stages of our launch, we moved deliberately but remain nimble, staying closely attuned to how our members were responding. Our philosophy around generating trial has always been to respect our customers and allow them to make an educated and informed decision. We know our customers are savvy and they know quality and value when they see it.

Over the last several quarters, I know many of you wanted more specifics around the timing of our roll in, roll out and what our promotional schedule look like. Like any new product launch, we stayed flexible and adapted to how customers responded and made a few tweaks along the way. Our focus was on generating trial in a smart way, not being overly aggressive with discounts, and making sure we drove a stable and enduring member base. Today, most of our Titanium members are paying full price. As a result, we are seeing a nice lift in revenue per member. However, we still see an opportunity in select markets to continue to grow our Titanium and Platinum memberships and will approach those units on a more site-specific basis. Bottom line, we're happy with 20% but we know there's room for improvement in certain regions.

With respect to retail traffic, it's our number one priority from a marketing perspective and the team under Matt Marakovitz, our new VP of Marketing, is laser focused on broadening our reach and driving customer acquisition, beginning with leveraging our database of over 2.1 million members and identifying look-a-like characteristics that can be used for more targeted e-mails, paid social and SmartSearch. It's still little news for us, but our goal is to turn the retail trend around without giving away the farm.

As we scale our company for the long-term, we will continue to make investments in people, technologies and our stores, all while maintaining tight control over expenses. On the people front, our ability to continue to develop future leaders will be the primary determining factor on how fast we can scale our company, which is why we continue to make material investments in our high-potential future leaders with our Mister Learn program, trainer infrastructure and comp and benefits program.

One of the things that makes Mister Car Wash special is that we're always encouraging our general managers to think big, be creative, take initiative and become even more entrepreneurial. Our goal is to cultivate a deep pipeline of talent and set them up with the ability to make independent and autonomous decisions in an agile and somewhat decentralized way. Today, we have over 300 managers at different points in our leadership funnel, working their way through our immersive and very intense Mister University LOOP program. It goes without saying that our success depends on their success which is why we spend so much time investing in their future.

It wouldn't be a Mister earnings call without providing an update on our culture and the speedcore of the team. We just wrapped up our employee engagement survey, which allowed us to quantify how they're feeling about working at Mister and, more importantly, areas where we can improve. Overall, 85% of our team members stated that they recommend Mister as a great place to work. From an opportunity for improvement standpoint, better communications and recognizing those who are contributing at a high level bubble to the top. We believe feedback is a gift, and are committed to continuing to strengthen our culture, which is what makes Mister Unique.

In late June, we announced that Mayra Chimienti will be stepping down as our COO and staying on for now as a special adviser. I'd like to take this opportunity to express my deep gratitude for the instrumental role she played in helping shape this company, particularly during the early years when we were laying the groundwork for where we are today.

Keeping with our tradition of promoting from within, I'm proud to announce the recent promotion of Tim Vaughn to SVP of Operations. Tim has been with Mister for 13 years, 26 in the industry and is one of our best developers of talent. Alongside Tim, I'm thrilled to announce the promotion of Luke Kittley to VP of Operations. Luke is a 12-year veteran of Mister, who will help Tim alongside our directors of operations and regional managers lead our best-in-class operations team.

I've said it many times in the past, but it's worth repeating. We are an operations-driven company. And today, our operations team has never been stronger. As I watch the Olympics unfold in Paris, the grit and determination of the best athletes in the world, remind me of our own team members and their championship drive to help make Mister the best company in the industry.

Before I turn it over to Jed, I'd like to give a big shout out to the entire team who put up a really strong quarter and are having to do it during one of the hottest summers on record.

I'll now turn the call over to Jed to give a deeper dive into our financials.

Jed Gold

Thank you, John, and good afternoon, everybody. We had a strong second quarter, and we're pleased with the underlying trends in our business. Let me touch on a few highlights before we run through the numbers. Our revenue and adjusted EBITDA reached record levels for any quarter in the company's history.

Our subscription business remained resilient, and we didn't see any material changes in our core churn levels from previous quarters. Our new Titanium membership offerings continues to ramp ahead of our expectations. The vast majority of our Titanium wash club members are now paying the regular monthly rate and we are seeing a healthy increase in subscription revenue per member. We know that trial drives adoption when it comes to our unlimited wash club and Titanium offerings, and we will continue to strategically offer trial pricing to club and Titanium members when and where it makes sense.

Similar to prior periods, we continue to see downward pressure on retail transactions. Our greenfield pipeline remains solid, but we have experienced some delays that have pushed the timing of a few stores to later in the year or early next year. Our priority is to build our subscription membership base at our new locations during the first year and our 2023 and 2024 greenfield locations are growing membership in line with our overall expectations. We continue to see paybacks of about 3 years.

Finally, we have done a lot of work around expense management and our strong adjusted EBITDA margin in the second quarter is a testament to the ownership mentality of our team. However, some of the margin growth in the quarter was also from the timing of certain investments that were originally budgeted for earlier in the year.

Now let me run through the second quarter numbers. Net revenues increased 8% and comparable store sales increased 2.4% compared to last year. UWC sales represented 72% of total wash sales, and we added 15,000 net new UWC members in the quarter. On a year-over-year basis, the number of UWC members increased by 61,000 members or 3%. At the end of the quarter, the membership split between Base, Platinum and Titanium was approximately 42%, 38% and 20%, respectively, while the average Express revenue per member was \$28.14 versus \$25.87 in the second quarter last year.

Adjusted net income and adjusted net income per diluted share, which adds back stock-based compensation and certain non-core operating expenses were \$37 million and \$0.11, respectively, in the quarter.

Adjusted EBITDA increased 20% to \$89 million and adjusted EBITDA margin increased 360 basis points to nearly 35%. Total costs and expenses were \$200 million in the quarter and included \$7 million of stock-based compensation and related taxes and \$3 million of losses related to the disposition of assets.

Excluding these items, total operating expenses as a percentage of revenue decreased 260 basis points to 74.6%. The main cost drivers were labor and chemicals decreased 160 basis points to 27.4%. Other store operating expense inclusive of depreciation and amortization increased 90 basis points to 39%. G&A expense decreased 190 basis points to 8.2%.

Commenting on each of these a little further, the decrease in labor and chemicals was driven primarily by greater labor and scale efficiencies, partially offset by increased labor rates. The increase in other store operating expenses was primarily from an increase in rent expense related to our store growth and sale leasebacks.

We ended the second quarter with 31 more car wash leases compared to the same time last year, and cash rent expense increased 14% to \$27 million. The decrease in G&A expense was primarily driven by our focus on managing expenses, optimizing our G&A structure and the deferred timing of some planned investments around marketing, systems and new hires. In the second quarter, interest expense increased to \$20 million from \$18 million last year, primarily due to higher interest rates and slightly higher net debt.

Moving on to some balance sheet and cash flow highlights. At the end of the quarter, cash and cash equivalents were \$4 million and outstanding long-term debt was \$919 million. Our balance sheet remains healthy, and we continue to self-fund our growth and expansion. In the second quarter, we completed 3 sale-leaseback transactions involving three car wash locations for an aggregate consideration of \$14 million.

Let me conclude with a few comments on guidance. We are reiterating our previously provided guidance ranges for the fiscal year ending December 31, 2024, which are included in the table at the back of today's earnings release. Within the context of those ranges, we wanted to provide some directional commentary on the major components.

On the revenue side, we currently expect full year revenue to be at the low end of the guidance range of \$988 million to just over \$1 billion. There are a few key drivers here. First, we've shifted the timing of new store openings to later in the year. Second, we closed 42 stores in Houston in the month of July related to Hurricane Beryl. On the comparable store sales side, we currently expect comp growth to be around the midpoint of the guidance range of 0.5% to 2.5%. The puts and takes here are stronger than forecasted Titanium performance and revenue per member, offset by lower than forecasted retail transactions and the impact of Hurricane Beryl.

On the adjusted EBITDA side, we expect adjusted EBITDA to be at the high end of the guidance range of \$291.5 million to \$308 million. The puts and takes here are we have done a good job of managing expenses and optimizing our G&A structure. We also built our budgets around some additional investments, which have not yet materialized and are now planned for second half of the year. I think it's also worth noting our field merit increases went into effect July of 2024 and will be reflected in the second half of 2024. These were included in our original guidance and will impact the comparability with Q2.

Let me wrap up by recognizing our hardworking team members who are braving the heat and executing the business every day. Also, I appreciate the team for thinking like owners and helping manage expenses. We feel very good about our performance in the second quarter and the way we are navigating an evolving industry landscape.

That concludes our prepared remarks. And we will now open the call for your questions.

Question-and-Answer Session

Operator

[Operator Instructions] The first question today comes from Justin Kleber with Baird. Please go ahead.

Justin Kleber

Hey, good afternoon John and Jed. Thanks for taking the questions. First one for me, just on the comments around the downward pressure on retail transactions, that's continued. I guess when I run the math it looks like the retail declines moderated fairly significantly on a year-over-year basis relative to 1Q. So, just curious if my math is right? And if so, can you speak to what at least appears like an improving trend line? Was it weather, are you starting to see any success with some of the tactics around retail customer acquisition? Just any color there would be helpful?

Jed Gold

Yes, Justin, it's Jed. Good afternoon and listen, you're right. When you look at the retail sales, they did moderate compared to Q1. Retail sales were down low double digits in the second quarter, which was slightly better than what we actually expected. The difference here is the composition of the sales decline. It was a little bit different than what we had expected. Retail transactions were lower than we expected. Retail average ticket was higher than what we expected. So similar to the lift in revenue per member, we're seeing a nice lift in average ticket for retail due to Titanium. We've updated this. We've taken this into account in our – the color and context that we provided as of to what to expect in the second half of the year.

Justin Kleber

Okay. Thanks for that, Jed. And then a question on member growth, members per store are running down across the first half of this year. I imagine part of that is just a function of new builds diluting that average figure. So I was curious if you could just comment on how UWC member accounts are trending in your more mature locations? Are they stable? Are they increasing? Are they declining? Just any color on that would be helpful? Thanks so much, guys.

John Lai

Yes, hey, Justin, this is John. Thanks for the question. So yes, as we've shared previously, we have over the last year, prioritized focusing on taking our existing members and upgrading them to our premium programs, Platinum and Titanium specifically. The offset there is as we pivoted to focusing on upgrading existing members that acted as kind of downward pressure on new member growth. The reality is, though, that the top of the funnel for us is retail traffic. So with pressure on the retail side, that's leading to less of that for our team. And so right now, the net member growth has been modest and we expect that trend to continue probably into the back half.

Justin Kleber

Got it. Alright. Thanks guys. Appreciate it.

Operator

The next question comes from Michael Lasser with UBS. Please go ahead.

Henry Carr

Hi, this is Henry Carr on for Michael Lasser. Thanks so much for taking our questions. I wanted to ask, can you speak a little bit about the penetration cadence for Titanium 360 during the quarter? I think we ended 1Q at 20%. We were expecting to moderate a little bit. And how has that sort of gone into July?

Jed Gold

Yes. So as we think about Titanium penetration, first of all, I think it goes without saying we are very happy with the progression of Titanium sitting at 20% Titanium mix, which is consistent with where we sat at the end of Q1. The difference here is at the end of Q1, that 20% member mix there were still a large number of those members on promotion. And when we look at the 20% titanium mix at the end of Q2, it was – they were vastly off promotion. And as a result, that's what's helping drive this nice lift in revenue per member of \$2.27 that we saw during the quarter. We still see an opportunity in select stores in markets, as John talked about in his prepared remarks, to continue to drive titanium platinum memberships. We're going to approach these units and markets on a more site-specific basis. But bottom line, we're happy with 20%, and we know that there is some room for improvement in certain regions with a little bit more time.

Henry Carr

Thank you. And just as a follow-up, I understand a little bit better for 4Q into 3Q, how is that – rolling off the promotions, I think the penetration for T-360 increased from 6% to 15% in 4Q from 3Q. So is that going to basically benefit the comp a little bit more in 4Q versus 3Q?

Jed Gold

Yes, Henry, the way that we've modeled it out is for Q3 and Q4 that revenue per member is relatively consistent with what we saw in Q2. Obviously, we're going to engage the teams to help drive that further and beat it.

Henry Carr

Thanks so much.

Operator

The next question comes from Chris O'Cull with Stifel. Please go ahead.

Chris O'Cull

Thanks. Good afternoon, guys. Jed, I know you recently said the average retail ticket was around \$14. Did that figure include the impact you're seeing on Titanium or has it climbed more from there?

Jed Gold

Yes, Chris. So retail, when you look at average retail ticket or average retail ticket, it's during Q2, it was sitting at \$14.88, it was up about 5.2% from where we were a year ago.

Chris O'Cull

Okay. And then based on our math, it looks like you had fewer new UWC members joined in the first quarter than last year and that's typically your highest seasonal quarter for additions. Then this quarter, it seems like you followed a fairly normal progression downward off that lower first quarter level. First, when do you become concerned that you simply don't have enough new retail customers coming in the door to keep UWC membership growth positive? And then second, can you help us understand where your conversion rates are today compared to where they maybe ran historically?

John Lai

Okay. Hey, Chris, great question. So let me start by saying we believe that the TAM for subscription is underpenetrated in general and that there is upside growth potential for subscription car washes in general. As we've previously stated, for us, the pressure that we're feeling on the retail is leading to some softness in net member growth.

So the chicken and the egg for us is prioritizing retail traffic growth, customer acquisition of new retail customers coming into our funnel. And then when we get them into the stores, the team has done an amazing job of converting them into membership and our membership conversion rates are at an all-time high. So we're executing really, really well once we get them in the store, the goal is to get them in the store.

So your question of when do we get concerned? Well, we're always concerned, right? our nature is to fret about everything. And I think it's important to put into context that when you look at our current average membership on a per store basis, we're in the top decile giving us our portfolio and given just the scale of our business. So with close to 5,000 members per store, there's a lot of operators out there that would love to have that kind of average. And we're doing it in a way where we're not pushing aggressive pricing. So we have shared openly that the value of that membership and revenue per member is really, really important to us. So we could spike membership, but we want to do it in a profitable way and do it in a way where we're not doing it in a way that dilutes our RPM.

So the plus \$2 per car that Jed shared, we see upside in that. But our focus has been on the premiumization of our membership plans. And really it begs the question, should we get more aggressive with our base offering at \$19.99. We're seeing some operators moving downstream and choosing to offer more aggressive pricing. We think that, that actually devalues your product and ultimately, it has a negative impact on your brand and what your brand stands for. And we would like to see ourselves as the premier operator in the space, and that doesn't need to resort to overly aggressive discount tactics.

Jed Gold

And then, Chris, the second part of your question around conversion rates, conversion rates have held consistent with where we've been in recent quarters hovering at about that 9% to 11% level, as has core churn remained consistent. So this – you're correct, about 60% to 70% of our membership sign-ups are typically in the first half, and as part of our forecast update and the color that we provided on the outlook for the balance of the year reflects those trends.

John Lai

Chris, have we shared our Tommy Boy reference with you?

Chris O'Cull

I don't think so.

John Lai

Do you know when he's selling the brake pads and he's met with resistance and he says – I don't know if you've seen Tommy Boy. But for those who have seen that movie, it's really funny. But what we have is a very easy to get into the program and as a result, easy to cancel setup because we didn't want to be that company that forces you to jump through hoops to cancel your subscription. That said, we've identified, the marketing team identified over 800,000 lapsed members that we can reach out to and we're starting to design some tailored messages and offers that can win them back into the program. So there's a huge opportunity to take existing former members and bring them back into the fold. And so that's right in front of us. And sorry if my Tommy Boy reference didn't land, but it works for me.

Chris O'Cull

When do you think you'll be able to activate some of those marketing tactics? Would that be a third quarter or a fourth quarter event?

John Lai

Yes. They're being activated as we speak.

Chris O'Cull

Okay, great. Thanks.

Operator

The next question comes from Christian Carlino with JPMorgan. Please go ahead.

Christian Carlino

Hi, good evening. Thanks for taking my question. Can you speak to the cadence of comps over the quarter and how things are trending quarter-to-date? And just given revenue per member or customer likely improved over the quarter as the promotions rolled off, was there any meaningful difference in the cadence of business or transactions, whether due to weather or some of the macro events going on?

Jed Gold

Yes. So when you look at comps over the quarter, comp trends, they're fairly – when you look at it on the month, they were fairly consistent throughout the quarter, although April was – it did slightly outperform the other months in the quarter. The other thing to keep in mind as we move into July and August these were strong years. So we're facing a more challenging comparison during those months. We did see a moderation in comps during July, but there was some noise from Hurricane Beryl that was impacting the comp. And then as far as anything specific that jumps out on transactions, it's relatively consistent. RPM was relatively consistent during the quarter. Therefore, trends were as well.

Christian Carlino

Got it. That's helpful. And just going back to your prior commentary about not needing to see retail trends improve to hit above the midpoint of the guide? How should we think about that now that we're halfway through the year? And I guess, could you quantify the expense benefit that you expect to ship into the back half for some of the marketing and store openings?

Jed Gold

Yes. So the retail trends we built into Q3 and Q4, consistent with what we saw in Q2. So we expect those same trends on a year-over-year basis to be relatively consistent in the second half of the year. And then as far as the marketing, the expense load. There's really – I mean, there's a few different things that add up here and are impacting the timing of the spend. The first and most pronounced is really marketing. The new Head of Marketing has come in, and he's taking a very consumer insights approach and doing a lot of customer profiling. So we can be just that much more efficient when we do deploy these marketing dollars. That work is underway, and then the plan will be to have some more targeted consumer media in the second half of the year. There's also a little bit of timing with some IT systems and then also just the timing around some new hires. From a margin perspective, we do expect margins to moderate during the second half of the year to approximately the adjusted EBITDA margin in the low 30%.

Christian Carlino

Alright. That's helpful.

Operator

The next question comes from David Bellinger with Mizuho. Please go ahead.

David Bellinger

Hey, guys. Thanks for the question. The first one on the Titanium promos and the roll off. Just exiting Q1, I think there was something like 15% of stores still on promotions into early May based on some of the recent checks and some of the recent offerings we've seen out there, it looks like July and August might be reverting to some of these free trade ups for titanium. Can you just help us with the thinking there? I know you mentioned a more site-specific approach. But any more detail on what locations those could be? And is this in any way like a step back from your initial cadence of rolling these promos off?

John Lai

No, so to be super clear, we had been pushing trial offers during the introduction over the last year. As we now stop and pause and reset and reevaluate where we sit at 20% on average, that means we have a number of stores in regions that are below 20% and the number of stores in regions that are above 20%. So our opportunity to continue to push and to continue to drive premium member adoption is right in front of us. The way we're going about it, though, is to do it where it doesn't take any revenue off the table. And so if we offer a trial upgrade for the existing price of your current membership, it is not dilutive in any way, shape or form. So those are done, again, on a store-specific and sometimes region-specific basis, but I just want to underscore that it's not going to do anything to shrink our revenues, which is really important to us.

David Bellinger

Understood. Okay. And then just a follow-up on the additional membership breakdown you gave, I appreciate that. Maybe a longer-term question is how should we think about the overall mix and where that could land? Is this more of a barbell approach where that middle package might be the lowest penetration over the next 3 to 5 years? How do we think about the split across the three pieces of membership?

John Lai

Yes. There was a really smart analyst out there that made a very bold statement about operators at 50% of their top-tier package, and I was sitting there going, where did he get that data point? I'm having fun with you, David, when I say that. That was in your last report because that felt very aggressive. By the way, can I ask you, where did you get that data point because I've never heard that before in my life.

David Bellinger

I'll just tell you, just speaking with some of these operators that might be in some regions like Florida, where some of these newest members coming in tend to trade up to that highest premium package. It was a few conversations like that, that some of those numbers shook out 50% or even higher.

John Lai

Yes. Listen, I spent a lot of time at these trade shows and different conferences and oftentimes, the mash pit of the bar, where sometimes people can be loose with their words but also somewhat boastful about what they're doing. Jed Gold when he states the number, he's held to the highest standard, and he can't frivolously or whimsically throw out something that is not accurate that he can't stand behind. So the numbers that we report are true and spot on. Bottom line, short answer to your question is right now, 60% of our 2.1 million members are in our Platinum and/or Titanium plan. So roughly 40% Platinum, 20% Titanium. We feel really, really good about that, then the other 40% are in the base. Is there an opportunity to continue shifting that member base to the right, for sure, hard for us to predict, right? So not knowing that we're one year into this thing, how high the tree line can go. But we do know that we have data points inside of our existing portfolio that have materially exceeded our current targets. And that's given us hope and promise that the possibility of further growth is in front of us, but I'm a little reticent. I don't want to be that guy at the bar who after two drinks that throws out a number. And so we're going to stay reserved and not over sharing.

Jed Gold

David, just a little bit more context, I think that's important. The goal here is not to drive penetration as high as we – what you'll see oftentimes when you talk to some of these competitors is \$5, \$3 memberships. So really, really low RPM but it helps drive that member mix. So it's really a bit of a balancing act. We want to maintain that high RPM that we enjoy. We believe it's best-in-class in the industry and then driving the penetration levels higher. And over time, we expect the 20% to increase, but we're not prepared to say over what time frame and how high it's going to go.

David Bellinger

Thanks, guys. I won't give you my specific sources, but we'll keep the conversation going.

John Lai

Okay, you got it, David.

Operator

[Operator Instructions] The next question comes from John Heinbockel with Guggenheim. Please go ahead.

John Heinbockel

Hey, John, question, is there any correlation between retail traffic and your density and/or market share? Is there any correlation with that? And then when you think about marketing, right? What's your thought in terms of how you want to – where you want to spend that money, right? Do you want to spend in building brand awareness, traditional media, digital? It may vary by market. And then what should – because you guys spend under 1% sales marketing, what's the right number? Is double that? Is it more than double that? What's your thought on that?

John Lai

Yes, John, thanks for the three-part question. Let me start with the first part of your question, which was, is there a correlation between the density of our portfolio on an MSA or DMA standpoint, really looking at it through a market share lens, and then retail traffic. The short answer is no. We haven't seen a correlation there. We do know, though, that in markets where we do have an elevated share, we have elevated AUVs, which supports our thesis that the value prop increases when you have more optionality, and it's just a much stronger program when you're on the ground pitching somebody about the value of your membership and that you can get your car cleaned in any 20 of the stores throughout the Tucson Metro area, versus an operator that may have two or three stores. And so that has held true. But with respect to correlation to retail, that's a little bit fuzzier for us.

To your question on marketing and what our strategy there, so we do see an opportunity to do a better job of building our brand and brand awareness, but we really want to take that and lead it to generating trial. And so specifically things that we're doing through paid social, some targeted e-mails, some digital ad spend. Right now, we're testing various offers through various channels. But our goal is, to your last question, is to increase our ad spend as our return on ad spend improves. And I think there is definitely a correlation between the bigger our network of stores gets, the more efficient our ad spend can be and the more effective we become. As we learn more and become better at our targeted advertising, we will get more efficiencies out of our ad spend, which will then support us taking the 1% today, and perhaps taking it to 2% tomorrow. When tomorrow is, we're not going to overspend too quickly until we have the data to support the efficiency and the effectiveness of our promotional spend.

John Heinbockel

Great. And then maybe just for Jed. Sort of getting back to, right, you think about low 30s or close to 30% in the back half of the year. If Fed spend normalizes, when you think about labor and chemicals was a new good right? It almost seems unsustainable. Does that normalize back to kind of a flattish level year-over-year? Is that the normalization? Or is it really – you didn't quantify the spend in G&A. Is it really that rising much more significantly? Which one of the two would it be?

Jed Gold

Listen, I think let me answer it a slightly different way, John. I think the – first of all, we've worked hard to build this owner-operator mentality within the culture, and the team has done a phenomenal job of finding ways to be more efficient, individuals owning their budgets, looking for what's the return on the incremental dollars that are being spent. And we've got a culture where we can challenge each other, frankly, and make sure that those returns are there.

Very, very pleased with what we've seen on a chemical cost per car as we've leveraged the scale of the business and are purchasing and are buying and helping drive some efficiencies on that chemical cost per car. We've also seen some labor efficiencies on our interior clean, which isn't at the core part of the business, but it represents 13% of our stores and about 30% of our employees. And so how can we be more efficient as we staff those interior clean locations? Freight costs is another one where we've seen some leveraging of the scale, and then some miscellaneous G&A items. So pleased with what we've seen and how those specific items that I just mentioned are going to stick in the second half of the year. What's more timing related is, as I talked about earlier, the marketing IT systems, some of the new hires within G&A. We expect a little bit more of a step-up in the second half from where we were in the – compared to the first half.

John Heinbockel

Thank you.

Operator

The next question comes from Simeon Gutman with Morgan Stanley. Please go ahead.

Simeon Gutman

Good afternoon, everyone. My first question, it's on the top line. The – I guess good progress on the comp. If you take the puts and the takes from the quarter, Titanium being paid for maybe weather, I don't know if hot helps or hurts, and then hurricane. John, would you say that – is your confidence changing at all with regard to the revenue generation of the chain? And then if I can just sneak, as part of it, did you say that most or all of those people getting Titanium or users are paying for it now and it's been rolled across to the entire chain? Or there's still a little bit of penetration and paying customers that could still roll on?

John Lai

So the 20% – well, actually, the 40% of our Platinum members are currently being billed at \$32.99. 20% of our Titanium members are being billed at \$39.99. The promotional offers that we were speaking to were for members that are not in that program and trying to trade them up into that next tier program. So we are enjoying the full lift. And with respect to – I guess you're asking me my mood and sentiment. Well, listen, we've shared with you guys – we've ask for you guys to be patient, as we've been patient, wanting to focus on getting people into the program while our finger was firmly on the promotional button, and then we lifted it. And now we've delivered in a way, with a north of \$2 – this is blended, Simeon, \$2 average revenue per member across 2.1 million members, and we have momentum in that number, right? And so Jed is reticent and somewhat reluctant to want to stick his neck out and say, hey, there is more that we can generate. But with momentum, there's going to be some upside and to what degree, hard for us to determine.

Jed Gold

And Simeon, just a little bit more color. I think what you are seeing, you are asking about the disconnect between the comp and the total revenue generation. I think one point worth noting and had commented on it in the prepared remarks is with the timing of the new builds shifting to later in the year, it does create a little bit of a headwind to the revenue – total revenue from what we had expected earlier in the year.

Simeon Gutman

Okay. And then just as a follow-up to something John mentioned earlier, contemplating something about the base rate, at some point in the future, good or bad, we don't – not good or bad, but whether or not it goes up, I think it probably doesn't go down. Is that a next 12-month to 24-month decision and you see how the rest of Titanium goes, or that's a 3-year strategic decision that you will contemplate?

John Lai

Yes. Well, I know you cover Costco and their cadence is minimum once every 5 years. And so we are – I think we are not worse than Costco. We are – so for us, it's been 20 years at \$19.99. I think you are speaking specifically to that program. And for us, having a, we will call it, our value offering is, we think is good for those more value-conscious customers. Is there an opportunity for us to take some price, perhaps. Are we being overly conservative, maybe. But the bottom line is when we feel it's appropriate, we will choose to take price. But really, it's a judgment call. And right now, we don't think we need to. It certainly will be highly accretive the day that we do it, but right now, we are not going to.

Simeon Gutman

Perfect. Thanks guys. Good luck.

John Lai

Thank you.

Jed Gold

Thanks Simeon.

Operator

The next question comes from Phillip Blee with William Blair. Please go ahead.

Phillip Blee

Hi guys. Thanks for taking my question. Alright. You have spoken a bit about expectations for retail traffic to continue to remain soft in the second half of the year. But I mean what do you expect you need to see for an inflection back to growth? Is it something improving in the macro or maybe a change in the level of the competitive intrusion in the market? Any color there?

John Lai

Yes. So, I think we are all hopeful that this is cyclic in that the state of the U.S. consumer, particularly the lower end cohort, is going to improve over time. But trying to time when that happens, there is a whole lot of people that are a lot smarter than us trying to predict when that happens. So, until then, we know that we have got a product with universal appeal. Everyone loves a car wash. And when we see things come back to whatever the new normal is, we know that our lower end quartile is the one that bounces back the quickest. They come in, in droves. They love – in fact, in some cases, they place more value on their vehicle than the top quartile, which is a little bit interesting. So, that's our kind of non-answer on macro. I think the other positive trend is that as we have stated in some of the previous calls, the 2023 was kind of the high watermark for new units coming into the category, and we are seeing a pretty marked reduction in new units this year. And from all sources, we are expecting that to continue in its decel into 2025. And so there will be less competitive intrusion as a result, which is going to put less pressure on our stores. And quite frankly, if you are going to choose to put up a car wash, do you really want to put it up next to a Mister. And so – and I am not being cocky when I say that. It's just there is other operators that you could choose to and go toe-to-toe with. I would not want to go up against us.

Phillip Blee

Great. That makes sense. And then I believe you previously mentioned certain markets for Titanium mix is trending well above the average, maybe exceeding 30%, some cases. Do those markets typically have an over – or a higher overall premium membership mix as well? And then do you look at these markets as something that could be reasonable for a national average at some point? Thank you.

John Lai

Jed, do you want to answer that one?

Jed Gold

Yes. So, Phillip, the short answer is we do see a higher premium mix in those markets that have a higher Titanium mix. I mean there is always a number of factors that go into this when you start looking market-to-market, the surrounding income demographics of the store base. I think it – seeing some of these markets that are at that 30%-plus level, it does. It instills that sense of confidence that there is opportunity, particularly at some of those markets that are at the lower end, that are still below 20%, and that there is a path to bring them up. And over time, we expect – and we saw this over the last 5 years prior to when we had Titanium, there is just a natural premiumization that takes place. It's not at the same rate that we have seen over the last year on the heels of the Titanium product launch, but there has always been this natural shift into more premium products.

John Lai

Yes. Jed, can I also add, too, when you have a brand-new store with a relatively blank slate, it's so much easier as you are articulating the full suite of programs to get folks in versus having this installed base where you are then trying to trade them into a new program. And so there is a lot of operators out there that, particularly with relatively young portfolios, that are enjoying that benefit. We are having to take this very, very large installed base and shift some of their behaviors and purchasing choices. But we do know that in our greenfield locations, we are seeing really, really amazing premium numbers. And again, that's kind of our north star for what the opportunity is.

Operator

[Operator Instructions] The next question comes from Peter Keith with Piper Sandler. Please go ahead.

Peter Keith

Good afternoon guys. On the comp outlook for the rest of the year, could we think about a quantification of what Hurricane Beryl has done to Q3? Maybe just to help level set our expectations. And then following on that, has there been any change to your Q4 outlook?

Jed Gold

Yes, Peter, so Hurricane Beryl, when we look at it on the month, it was about 40 basis points to 80 basis points of impact to July. I believe that could be a 20 basis points to 30 basis impact to comp stores on the quarter, so a little bit of impact. There was 42 stores in Houston. They were closed, on average, the average came out to about 2.9 days for the time that those were closed. We believe that we have adequately reflected that trend as we think about second half comps and our color around the forecast rolling up to the middle of the guidance – the midpoint of the guidance range that we have provided.

Peter Keith

Okay. Great. And I thought the commentary around the reactivation opportunity is interesting. And I guess is this something that you guys were not doing in the past? It sounds like it's starting now. And so I guess how are you reaching out to some of these expired customers? What's the, I guess the technique, is it mailers, e-mails, give us some color on that, please?

John Lai

Yes. So, it was naturally occurring before where we knew that there was – inside that 800,000 number, there is what we define as a seasonal member that will come in and out, and I choose the Minnesota market as an example, where in the summertime, it's not uncommon for folks to go up to their lake cabin and cancel their membership during the summer period, but then when school is back in session, they come back and reactivate. And so we see that happen in that, not just in Minnesota, in a lot of markets where there will be a temporary pause, they will go on vacation or what have you. But we haven't done anything in a more, I think strategic and targeted way up until now. And this is where the beauty of Matt comes in. Matt said, hey, there is this embedded base that's just sitting right in front of us, let's go reach them. And the way to reach them is, we think the most effective way right now is e-mail. And so we have got some campaigns that are going out as we speak. And we hope to have some more data to share on subsequent calls.

Peter Keith

Okay. Sounds good. Thanks so much.

John Lai

Thank you.

Operator

The next question comes from Robby Ohmes with Bank of America. Please go ahead.

Robby Ohmes

Hey. Thanks for taking my question. Really just a follow-up on some of the ones that have gone before, for the greenfield stores that you have done, and maybe you don't have enough data yet, but where the penetration is really strong with Titanium for a greenfield store, do you have any data on how those stores mature? What the maturation curve looks like versus historical new locations?

Jed Gold

Robby, just to clarify, are you talking about maturation of Titanium or just maturation of the total members?

Robby Ohmes

Maturation of members and in sales of that store, so is there a – does it change the maturation or waterfalls of the store versus stores when you weren't doing the high penetration of Titanium when you opened a new store?

Jed Gold

Yes, it's still early. We don't have enough data points to say definitively whether it impacts how those members ramp compared to prior to having Titanium in our new builds.

Robby Ohmes

And then just one other follow-up, I just wanted to clarify the – are you seeing it's been very promotional and you think it's staying promotional, or is it getting – you think the weaker competitors are getting less promotional, just overall, what's the thought, competitively?

John Lai

Yes, it's kind of a mixed bag. I think those that are executing really well that have really good customer experience and a strong value prop are not having to lean too heavily on aggressive promotions, but those that may not have those things that I just mentioned will need to resort to price as their primary driver, which is why, again, we have been somewhat conservative in our approach to not being overly promotional, because we know at the end of the day, that when we look at the factor analysis of why people choose Mister Car Wash, price is not the primary driver, it's quality, it's speed, is the efficiencies of our stores and then the customer service that they get when they come visit us is second to none. And that's really become our calling card. So, that said, there is a segment of the motoring public that will be motivated by a potential attractive offer. And because our margin profile is healthy, we have some room to lean in on certain offers. But again, we want to be very targeted and measure it, not just spray and pray.

Robby Ohmes

Got it. Thanks so much.

Operator

The next question comes from Tristan Thomas-Martin with BMO Capital Markets. Please go ahead.

Tristan Thomas-Martin

Hey. Good afternoon. Just one question for me, what are you seeing in terms of M&A multiples in the space?

John Lai

Yes, it's been very quiet on the M&A front. I think the appetite for doing deals right now in this kind of environment, given just the cost of capital and then the – quite frankly, the debt loads specific to many of the PE-backed platforms, they are just over-levered right now and can't get access to capital. I think the REIT markets are also kind of wising up, saying, hey, we need to be really smart with some of the businesses that we are underwriting, because at the end of the day, even if the coverage ratios are there, if it starts getting thin, working for the landlord, that's not a single-purpose facility, there are some risks associated with that. So, due to those reasons, I think right now, most operators are looking inward and saying, how do we execute across all the core fundamentals, and to do that, you need to reinvest. And this is kind of a capital allocation question, how do you take some finite resources, you need – you can't sweat the assets,. you got to reinvest back into the business. But as importantly, you got to invest in human capital. And so when we are seeing businesses that are running super lean crews and they are opening and closing with one guy, that's blasphemy for us, right. We would never do that because it's highly unsafe. And – but more importantly, we want to make sure – we don't want to be that company where you pull in on a lot, and there is nobody there to service you. So, we err on the side of running a little heavier, if you will. But we are okay with that because for us, it's all about the customer experience. So, at the end of the day – I am drifting here a little bit, I want to get back to your question on multiples. For the deals that are trading, I think the hard thing for anybody that's on the buy side right now is to pull the trigger on a deal north of where Mister is trading because you really got to think, again, particularly if you are a sponsor-backed platform, what is my exit on this thing, and where does this thing end right now, Mister is one marker, is trading at X, and I am buying it Y. If that Y is materially over where we are trading, if I am on that investment committee, I am stressed out.

Tristan Thomas-Martin

Thank you.

Operator

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

John Lai

Well, thanks everyone for joining today's call. We have a lot of momentum going into the back half, and I couldn't be more proud of our team and all the hard work everyone has put in to get us here. Our emphasis on our people and their happiness and engagement really starts with developing a culture where we work hard, care about doing a good job and have fun along the way. We are very optimistic about our future, and particularly the impact that our marketing and technology investments will have in the years ahead. Look forward to catching up with everyone on the next call, and hope everyone stays cool out there. Talk soon.

Operator

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

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