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Planet Fitness, Inc. (PLNT) Q1 2024 Earnings Call Transcript

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Q1: 2024-05-09 Earnings Summary

Play Call



Press Release



10-Q

EPS of \$0.53 **beats by \$0.03** | Revenue of \$248.02M (11.61% Y/Y) **misses by \$549.42K**Planet Fitness, Inc. (NYSE:[PLNT](#)) Q1 2024 Earnings Conference Call May 9, 2024 8:00 AM ET

Company Participants

Stacey Caravella - Vice President-Investor Relations

Craig Benson - Interim Chief Executive Officer

Thomas Fitzgerald - Chief Financial Officer

Conference Call Participants

Simeon Siegel - BMO Capital Markets
Christopher O'Cull - Stifel
John Heinbockel - Guggenheim Partners
Megan Alexander - Morgan Stanley
Rahul Krotthapalli - JPMorgan
Sharon Zackfia - William Blair
Joseph Altobello - Raymond James
Maksim Rakhlenko - TD Cowen
Korinne Wolfmeyer - Piper Sandler

Operator

Thank you for standing by. My name is Krista, and I will be your conference operator today. At this time, I would like to welcome everyone to the Planet Fitness First Quarter 2024 Earnings Conference Call. [Operator Instructions] I will now turn the conference over to Stacey Caravella, Vice President of Investor Relations. Stacey, you may begin your conference.

Stacey Caravella

Thank you, operator, and good morning, everyone. Speaking on today's call will be interim Planet Fitness Chief Executive Officer, Craig Benson; and Chief Financial Officer, Tom Fitzgerald.

Both will be available for questions during the Q&A session following the prepared remarks. Today's call is being webcast live and recorded for replay. Before I turn the call over to Craig, I'd like to remind everyone that the language on forward-looking statements included in our earnings release also applies to our comments made during this call. Our release can be found on our investor website along with any reconciliation of non-GAAP financial measures mentioned on the call with their corresponding GAAP measures.

Now I will turn the call over to Craig.

Craig Benson

Thank you, Stacey, and thank you, everyone, for joining us for the Planet Fitness Q1 earnings call. We ended the first quarter of 2024 with approximately 19.6 million members; same-store sales growth of 6.2%, primarily driven by new member growth; and nearly 18% adjusted EBITDA growth. Our system opened 25 new units and ended the quarter 2,599 Planet Fitness locations globally.

Today, I'm going to address three topics: first, the headwinds that we faced in the first quarter that impacted our results; second, our decision to raise the Classic Card price; and third, the exciting announcement about our new CEO, Colleen Keating, who joins us on June 10.

The increase of approximately 900,000 net new members in the first quarter was below our expectations for what has historically been our highest net growth quarter pre-pandemic. The year began with national media headlines about the rising cases of COVID as well as RSV and other respiratory infections that may have made people hesitant to go to public places, including gyms, especially in the first half of January.

In typical January, fitness or gyms are among the top search Internet items. This year, while they are still among the top search items, both flu and savings-related items were even higher. Additionally, an industry source noted that many brands in the fitness industry experienced a similar soft beginning of the year. We also had double-digit decreases in our website traffic.

While we continue to see more than 80% of our joins come via online channels during the quarter, we had fewer people visiting our website to potentially join Planet Fitness. Usage, which historically correlates with join trends, was the same on a quarterly basis year-over-year. However, it was down significantly in the first couple of weeks of January during the peak of our join season. We also believe that a contributing factor to our lower net joins in Q1 versus last year was the effectiveness of our advertising campaign.

We believe that this was due in part to the messaging not resonating as broadly as we anticipated as well as our strategic decision to not include price pointed offers as part of our nationally funded portion of the advertising. We made this decision because we are conducting pricing tests in several markets to inform our pricing strategy going forward. In a study that we commissioned to assess our first quarter campaign, consideration of Planet Fitness is trending upwards and is the highest it's been in years.

However, the lack of a price point in our national funded January sale adds may have created less urgency for consumers to get off the couch and join. To a far lesser degree, the first quarter softness also derived from a reaction to an incident regarding on nondiscrimination policy. The isolated incident took place on March 11 in an Alaska gym. Media mentions relating to the incident peaked in the middle of March, which we believe contributes some of the softness we saw in joins for the balance of the month as well as some increase in cancels.

This policy has been in place for more than a decade and is not dissimilar from other industry peers, including longtime brands such as the YMCA. As a result of these headwinds we faced in Q1, we are updating our 2024 guidance targets to which Tom will cover.

Now to our pricing tests. Last fall, we started testing two price points for the Classic Card, a \$15 and a \$12.99 in about 100 stores each, both reverted back to \$10 during the national sale periods and the advertising in those markets communicated a call to action with an explicit saving in monthly dues to join before the sale expires.

We added an additional test in December to include the New York DMA where we kept the price at \$14.99 regardless of a national sale. We continue to run these tests through the April sale. We use disciplined data-driven approach to determine the best balance between the higher dues while minimizing loss of membership. Based on our learnings, we decided to change the price of the Classic Card to \$15. It drove the most significant increase to average unit volumes with the least impact to the rate of joins. The increase will be effective this summer only for new members.

We continue to test different promotional strategies, as I believe a good portion of our focus on innovation includes exploring pricing and amenities. To that end, we'll be starting Black Card price tests around the time the system migrates to the new Classic Card price. Tom will address more specifics on the role of the Classic Card price increase.

Finally, we announced in April that Colleen Keating will be joining us as CEO next month. Our appointment follows a thorough extensive search process conducted by the Board and we could not be more thrilled to welcome her to Planet Fitness. She brings over three decades of experience across hospitality and real estate as well as expertise in operations, franchise and brand management and leading consumer-facing organizations.

She is excited to join an industry leader that had significant runway for even further growth, both domestically and internationally, and she's eager to get started. I will work closely with Colleen and the management team to ensure a seamless transition. Now for a quick update on our CFO search. The search is well underway. We have interviewed and are considering a number of promising candidates. Colleen will become involved with the process once she officially starts us in June.

Finally, last week, I had the opportunity to address our franchisee community at their annual conference in New Orleans. We had great conversations around new initiatives, including building clubs for smaller markets, which we kicked off a few months ago. We also discussed how we're ahead of schedule to reduce new unit and remodel build costs by at least 10% before the end of the year. Other aspects of the new growth model were part of the discussions which led to a real sense of excitement about a greater return on their investment and our long-term store growth opportunity.

I am grateful to have had the opportunity to serve as interim CEO, especially during a period in which we put in place a number of initiatives that we believe will support the company's long-term growth trajectory. I also look forward to returning to my role as a Board member and a franchisee with an even greater appreciation that I have gained for the Planet Fitness brand, our members, our franchisees, our leadership team and our shareholders.

Now I'll turn it over to Tom.

Thomas Fitzgerald

Thanks, Craig. Before I get to our first quarter results, I'd like to cover our upcoming Classic Card price increase as well as our plans to explore refinancing a portion of our debt this year. As we said previously, we've been working on a number of initiatives to further improve our already strong store economics and new store returns. Our new franchisee growth model that we unveiled in Q3 of last year is primarily focused on reducing the capital requirements for opening and operating a Planet Fitness franchise location.

For the past several months, we have had three different groups of stores testing three different prices for our Classic Card membership. Based on those test results, we have decided to increase the price from \$10 to \$15 to further enhance the average unit volumes for our stores. Our Classic Card membership has been priced at \$10 since 1998, which based on inflation would be about \$20 in today's dollars.

As Craig noted, the price increase will go into effect this summer, only new members who joined after it goes into effect will pay \$15 for a monthly membership fee. Current Classic Card members will continue to pay \$10 for the duration of their membership. It will take some time for the benefit of the price change to expand our store level margins as the price increase will only be on new Classic Card memberships. Additionally, more than 60% of our members join as Black Card member.

Now to our debt. We have a tranche of debt of approximately \$600 million that comes due in September of 2025, which we anticipate refinancing in the middle of this year, subject to overall market conditions. Based on forecasted interest rates, we believe our overall weighted average interest rate for all of our debt would still be below 5% when we refinance that tranche.

Now to our first quarter results and our revised 2024 outlook. All of my comments regarding our quarter performance will be comparing Q1 2024 to Q1 of last year, unless otherwise noted. We opened 25 new stores compared to 36. We delivered system-wide same-store sales growth of 6.2% in the first quarter. Franchisee same-store sales growth increased 6.3% and corporate same-store sales increased 6.2%. Approximately 70% of our Q1 comp increase was driven by net member growth with the balance being rate growth.

Black Card penetration was 62.1%, an increase of 10 basis points. For the first quarter, total revenue was \$248.0 million compared to \$222.2 million. The increase was driven by revenue growth across the franchise and corporate-owned segments. The 12.2% increase in franchise segment revenue was primarily due to increases in royalties, new stores and ad fund revenue.

For the first quarter, the average royalty rate was 6.6%, up from 6.5%. The 15.6% increase in revenue in the corporate-owned store segment was primarily driven by the same-store sales growth as well as new and acquired stores. Equipment segment revenue decreased 8.6%. The decrease was primarily driven by lower revenue from equipment sales to new and existing franchisee-owned stores, which was driven by fewer new store placements as well as the shift to more strength equipment versus cardio.

As we noted last quarter, the shift in the equipment mix brings down overall sales on a per store basis. We completed 14 new store placements this quarter compared to 18 last year. For the quarter, replacement equipment accounted for 59% of total equipment revenue compared to 58%. Our cost of revenue, which primarily relates to the cost of equipment sales to franchisee-owned stores, amounted to \$19.0 million compared to \$19.4 million. Store operation expenses, which relate to our corporate-owned store segment, increased to \$74.4 million from \$66.0 million due primarily to new stores opened or acquired. SG&A for the quarter was \$29.2 million compared to \$27.8 million.

Adjusted SG&A was \$27.3 million. This includes a \$1.6 million adjustment for severance-related expenses incurred in connection with the reduction in force that we mentioned on our last earnings call as well as a \$0.3 million adjustment for CEO transition-related expenses. National advertising fund expense was \$19.8 million compared to \$17.0 million. Net income was \$35.0 million. Adjusted net income was \$47.3 million and adjusted net income per diluted share was \$0.53 per share. Adjusted EBITDA was \$106.3 million, and adjusted EBITDA margin was 42.9% compared to \$90.2 million with adjusted EBITDA margin of 40.6%.

By segment, franchise adjusted EBITDA was \$76.1 million, and adjusted EBITDA margin was 73.2%. Corporate store adjusted EBITDA was \$42.4 million, and adjusted EBITDA margin was 34.6%. Equipment adjusted EBITDA was \$4.8 million, and adjusted EBITDA margin was 22.2%. Now turning to the balance sheet, as of March 31, 2024, we had total cash, cash equivalents and marketable securities of \$486.4 million compared to \$447.9 million on December 31, 2023, which included \$46.2 million and \$46.3 million of restricted cash, respectively, in each period.

In Q1 2024, we used \$20.0 million to repurchase slightly more than 300,000 shares. Total long-term debt, excluding deferred financing costs, was approximately \$2.0 billion as of March 31, 2024, consisting of our four tranches of fixed-rate securitized debt that carries a blended interest rate of approximately 4.0%.

Finally, moving on to our updated 2024 outlook, which we provided in our press release this morning, we're providing wider ranges for the targets that we are updating given the current choppy environment in which we're operating. We continue to expect between 140 and 150 new stores, which includes both franchise and corporate locations. We also continue to expect between 120 and 130 equipment placements in new franchise stores.

For the full year, we continue to expect that reequipped sales will make up approximately high 60% of total equipment segment revenue. We also continue to expect that this year will look more similar to 2023 in terms of the quarterly cadence for those sales as it was a more typical year versus the prior three that were impacted by COVID.

As I noted earlier, the shift to more strength equipment versus cardio will bring down overall sales on a per-store basis. During Q1, we continued to refine the mix that will result in slightly lower sales per store. We are maintaining our equipment segment profit dollars, so therefore, margin rate will increase. We now expect system-wide same-store sales growth to be between 3% and 5%. Previously, we expected between 5% to 6% growth.

This reduction is driven by the factors that Craig noted earlier. All of the following targets are updated to reflect the changes I just mentioned and represent growth over fiscal 2023 results. We now expect full year revenue to grow in the 4% to 6% range. Full year adjusted EBITDA will grow in the 7% to 9% range. Adjusted net income to increase in the 6% to 8% range, and adjusted earnings per diluted share to grow in the 7% to 9% range.

We continue to expect shares outstanding to be approximately \$88 million, which is inclusive of the repurchase of one million shares over the course of the year, the amount we shared back at our Investor Day in November of 2022. And we continue to expect our net interest expense to be approximately \$70 million, which assumes we refinanced the tranche I mentioned earlier at 6.5%. We will update any applicable guidance targets, if necessary, pending the completion of the anticipated refinancing transaction later this year.

Lastly, we continue to expect CapEx to be up approximately 25% and D&A to be up between 11% to 12%. Now despite a challenging start to the year, we believe that the changes we have made as part of our new franchisee growth model, along with the upcoming price increase, improve our store economics and enhance our differentiated brand and market-leading position. We continue to be a highly attractive franchise system that generates strong and stable free cash flow for long-term sustainable growth and increased shareholder value.

I'll now turn the call back to the operator to open it up for Q&A.

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Simeon Siegel with BMO. Please go ahead.

Simeon Siegel

Thanks. Hey, everyone, good morning. Hope you're all doing well. I was hoping you guys could elaborate a little bit on the lower guidance, particularly just in light of it looked like a pretty solid quarter for member growth in top line ex Equipment. So is there anything you've been seeing since the start of the quarter to raise that concern, any uptick in churn or anything like that?

I guess I'm just trying to understand your characterization of the disappointment in the quarter. I guess that member growth was slightly below the last two years, but it still seemed pretty solid, the comps were encouraging and you had the new members. So I just -- I guess I would have thought this was a pretty good quarter, excluding Equipment miss. So any color you could give there?

And then, Tom, does the number -- does the guidance include any of the lift or assumptions from the price hike to \$15?

Thomas Fitzgerald

So in terms of the quarter, we did have decent member growth, \$900,000. It wasn't where we expected it to be. And some of the things we mentioned on the call, we knew when we had our earnings call in February, and we provided our outlook.

I think what we didn't know is sort of what happened in March. The first part of March was pretty good. Joins and cancels were pretty good. And then once social media sort of blew up over our policy issue, we definitely saw a change in the results in the back half of March. Joins and cancels were fairly significantly affected.

Now the good news is, and we're not going to provide a lot of color on Q2, but at a high level, just to provide some perspective, the good news is we've seen the joins rebound, but cancels have remained elevated. So that's really principally what we have seen and therefore, factored into this latest revision in our outlook.

There were some things in Q1 early on that we talked about in January. Our business is definitely probably way more sensitive to what happens in those first couple of weeks of January than most other ones. So we talked about that. But then things definitely were getting better across the back half of January through February and the first half of March, as I described.

So the good news is that the joins have bounced back. And while we're never totally pleased with what we're seeing, it's better for sure. It's the cancels that have remained elevated. And the second question, yes, the price increase won't have a huge impact. As you know, our business, it only is affecting new members. And with it coming in the back half of the year, it's not going to have a huge impact, but it is factored in.

Craig Benson

Simeon, just let me add. One of the benefits that Planet has for its members is your price for life, and we've never made a big deal about that. But as part of this price change, we're going to highlight it much more. And so we ought to get the benefit of a subscription-based business that doesn't change pricing on people in the middle of their usage of those services or what have you. So we're going to start to really trigger that as well.

Simeon Siegel

That's what I was going to ask. I was going to ask, in the test if you saw any of sort mitigant where people want to keep their original grand product price in there?

Thomas Fitzgerald

Yes. We're not going to get into all the sort of -- all the different metrics, Simeon, that we saw in the test. But definitely, as you know, we read it for a long time, read all of the tests for a long time and feel really good about seeing those same results when we roll it out because of how thoroughly it was tested.

Operator

Your next question comes from the line of Chris O'Cull with Stifel. Please go ahead. Chris O'Cull from Stifel, your line is open.

Christopher O'Cull

Thanks. Sorry about that. I was on mute. Craig, the company has had issues with marketing campaigns or media buying during the lower important New Year's Eve membership season in the past few years. I'm just wondering what's the company doing to ensure a higher probability of success going forward?

Craig Benson

Well, as you know, Chris, we are really aggressively chasing a brand identity strategy that we've not had in the past, which will help us with marketing because we will have, as we talked about just a minute ago, price for life as an example. We've never talked about that. And then some of the other benefits we offer our membership whether it's perks or opportunities to use different clubs with the Black Card and that kind of thing, bring a friend. We don't talk about that stuff, and we don't put in the context of our brand identity.

So we have had issues in the past with different people we work with. That's been pretty much fixed. We're down to two agencies now for the entire LAP system. We used to be as high as 16. For one year, we went to one, and now it seems to have settled out. So I think we're doing better on that front. I think the real challenge is hitting the market with a real branding effort to talk about the benefits of Planet Fitness beyond just price and offering that to our membership for two reasons. One is to get them to join, but the other is to get them to stay. And so if we could kill both of those birds with one stone, that would be great.

Christopher O'Cull

You guys called out a lot of different factors affecting joins during this quarter, everything from the weather to the situations with the bathroom incident. I mean I'm just curious how confident are you that the pricing test did not have effect on the joins and the new membership trends in the markets that you were testing the higher prices?

Thomas Fitzgerald

Chris, it's Tom. And so it's a good question. And just to clarify, we did not cite weather as a subscription business, thankfully, it's never typically a big impact for us. Some of the other things and as you know, it's never one thing. It's usually a combination of things. So we tried to highlight what we thought were the larger things that would impact it.

To your question about the price test, we feel very good because the results that we saw through the decision that we took as a team here to change the price, those results were sort of consistent with what we had seen in the prior month. So, essentially, what we saw was not an isolated or geographic impact, it was more broad, more comprehensive.

So the result of that was that we feel good about the fact that the results moved the way we expected and saw in the previous months in the test. So no concern with this particular incident, which we hope is behind us, affecting the veracity of the test results.

Craig Benson

And Chris, the other thing is, as you probably know, but I want to make mention of it. We always have a control group to match up against the test group and the control group is very similar to the test group in the types of clubs, location, that kind of stuff. So we have controls built in to be able to see anomalies between pricing changes and other things, including things like weather, which Tom said we didn't measure, but there may be periods of time where it gets a little busier than others because people can get out or they can't. And so we do a pretty thorough job of controlling the data from the test and with another group that's not involved in the test.

Operator

Your next question comes from the line of John Heinbockel with Guggenheim Partners. Please go ahead.

John Heinbockel

Hey, guys, I wanted to start with -- I think, Tom, you said I don't want to paraphrase, but something about the -- having that social media stuff not behind you, but having seen the worst. So I guess it's not -- your assumption is it's not getting worse.

I guess, built into the guidance is that it will not improve. Correct me if I'm wrong, right? Your assumption is that it will kind of stay the same. And then how do you address that, right? How do you address that issue without drawing more attention to it? And it seems like very difficult to do that.

Thomas Fitzgerald

Yes, John, just to make sure I'm clear, what I was talking about what's really the social media mentions on that. Hopefully, it's kind of died down. It was certainly not broad scale, but it definitely had an impact. And what I would say is and why we talked about providing the wider ranges, it is an election year.

There are things that swirl around and it's certainly been a choppy first few months than we expected coming into the year. So I think it's with that in mind that we provided the wider range to ensure that some of what we're seeing is factored into our outlook. And to the degree that, that ramps up or down a little bit is why we broadened the range. In terms of how we're thinking about the rest of your question, I'll pass it to Craig.

Craig Benson

Yes, so I think we've done a good job of navigating through this whole incident, including involving federal authorities in some of the work that needed to be done. And so I don't want to give -- take my hats off to all of our franchisees and the employees here for navigate through this difficult period of time and hopefully getting to a better side.

John Heinbockel

Okay. And then maybe the other question with regard to pricing, right? So \$15 has a decision been made on, you'll still run promotions. Do you run them at 10, do you run them at 15, 15 becomes the new 10, right, I guess, with no money down.

And then you also referenced Black Card right? So I don't think you want to promote that. So that's really a study on like you had in the past, whether you take that up \$1 or \$2? Or are you thinking about something different?

Craig Benson

Yes. We're going to test a couple of different versions of the Black Card with pricing. We're also going to try and rejigger some of the amenity portions of it, if possible. So there may be a few different iterations here of being able to test Black Card. We do put Black Card on sales from time to time. So it's not that we only put the White Card on sale. With regards to that, we're still working through, as you know, we're a promotional brand I don't like to get away from some of the promotions we've done in the past because it's been 100% promotional based.

But there's more levers to pull as far as promotion goes, whether it's three months or other things that we could put into the mix that we haven't thought of doing in the past. And I think you'll see more variety of that. And just how it rolls out and what we do is undefined at this point in time. We know we want the system to shift up to \$15 and use that price as the price going forward is possible.

Thomas Fitzgerald

Yes. And John, I would say undefined, it's really for competitive reasons, we don't want to signal what we're going to be doing promotionally and when we're going to do it. So -- but again, we feel good about it. And as Craig has pushed, we want to continue to test and learn our way into finding things that are accretive.

And as you know, we take the Black Card price up every couple of years. The last one was May of '22. So there's certainly, we think, room to test different options here as we move the Classic Card.

Operator

Our next question comes from the line of Megan Alexander with Morgan Stanley. Please go ahead.

Megan Alexander

Hi. Good morning. Thanks very much. I wanted to come back to just the comments on member growth. I guess you did talk about a consumer looking for savings. We've heard from a lot of companies. There's been a lot of bad messages about the consumer, particularly the low-end consumer. So I guess, how do you reconcile what we're hearing a bit in the broader market just about the consumer environment with maybe what you've seen from a membership perspective, understanding you've had some noise?

And then how do you think about raising price into the summer months when the summer past member typically joins that high school member typically joins at the White Card and there was an article yesterday in the journal about how Gen Z seems to have more credit card debt than generations before. So just trying to understand whether there's anything there from just a low-end consumer perspective that might be perhaps pressuring things and how you're thinking about it as we head into the high school summer past period?

Thomas Fitzgerald

Megan, it's Tom. I'll start that. So I think broadly, we all see the same things. I think the consumer is definitely squeezed with multiple years of heightened inflation, higher interest rates, if you got a mortgage -- I read recently, mortgage payments are up about one third from when rates were a little -- were lower. When we look at our results from a joins and cancels standpoint across several different income brackets, household income brackets, there's very little deviation.

So it's not like we're losing the low end or gaining the high end. It's -- you could throw a very small blanket across all those numbers. When you index them, they're really quite tight. So we think it's probably a bit broader in that sense. The high school summer pass, we love that program. We're doing it again. It exposes our brand to so many people for free. That's really the benefit. And the fact that we get a few hundred thousand teams to then subsequently join we think is great.

But I think repeatedly, now this will be our third straight year, fourth in total, of running high school summer pass. This is a great thing for our brand and to help kids, if they're not already doing it, to start living a healthier life. So we think the pricing change that we're talking about here, again, we haven't talked specifically about the timing and how that affects high school summer pass. But we think whether that affects this year's group or next year's group it's still a heck of a value for \$15.

And to Craig's point, probably not emphasizing in our 30-second spots, the pricing messages can sometimes drown out all the other benefits or crowd out all the other benefits that we're trying to convey. So by better balancing that message, we think the value will increase, which should drive more demand, but it's not just about price, it's about the rest that we offer.

Craig Benson

And I'd just add two things, Megan. I don't think we've gotten credit price summer pass in the ways we should. This year, we're going to give three free months to every member if we get three million like we had last year. That's \$90 million worth of value that we're putting into the marketplace to allow teams to feel better physically and mentally.

And so it's important to highlight, I think, for the world that Planet Fitness is putting its money where its mouth is by inviting young people who've been through a difficult period of time, both in their school lives and outside lives to use exercise as a way to help them deal with mental or physical challenges they may have.

And I think the other thing that's important rolling out price, as Tom mentioned the last time we did it was May 2022, and the reason we like to do it in the slower summer months is because any price change takes a while to burn in. And so we use the slower months as a burn-in period of time for new pricing. It generally allows us to get through that change period and come back out the other side before we get into the busier time of the year for us.

Megan Alexander

Got it. That's helpful. And then maybe on the unit open just as a follow-up. Can you talk a little bit about how the 25 in the quarter came in perhaps relative to your expectations? You maintained the year. I think maybe puts and takes rates are a little bit higher. Maybe you can give us an update on the real estate availability and how that looks and just your overall confidence level in that placement outlook?

And do the -- do you expect the pricing, perhaps isn't going to have an impact on your top line or bottom line results this year. But is that something that should start to impact the development outlook for franchisees this year? Or is that more of a '25 story as well?

Craig Benson

I think franchisees take into consideration all the different things we've done as to their outlook. I mentioned in my opening remarks, I just came back from the conference in New Orleans. We couldn't talk about price changes there. And so they weren't privy to that. But clearly, that was one of the things that was top of mind for them. And so we spent a lot of time talking about the new growth model and some of the progress we've made on cost cutting and that kind of stuff.

And in fact, smaller clubs in markets that can sustain a 20,000 square foot box. CBRE came out with a statistic, I think fairly recently, they said the amount of available space is going to be half of what's able to be taken down this year. So it continues to be challenging for us. Clearly, there's been some retailers that are running through difficult times. And we're trying to be all over that as ways to sort of mitigate some of those challenges.

But I think all in all, I was very pleased, again, based on the comments I made in the opening script with the tone and tenor of New Orleans conference, pretty much everybody was there. And I got a lot of time to spend with the different franchisees both one-on-one and in a group setting. So I feel very good about this company and where it is right now. I still think we have work to do for sure, but there's really great opportunities.

Operator

Your next question comes from the line of Rahul Krotthapalli with JPMorgan. Please go ahead.

Rahul Krotthapalli

Good morning, guys. Thanks for taking the question. This is on franchise leverage in the system. Certainly, the pricing decision should alleviate a lot of concern here. And interest rates narrative have continue to be key, but it's something not under your control. How has the sentiment been in the convention specific to the leverage concerns. And Craig or Tom, is your sense that franchise consolidation here given the transactions we are seeing out there will help some of these large franchises to compete better for the targeted real estate opportunities? And I have a follow-up on marketing.

Craig Benson

Sure. We are so fortunate that we have now under 100 franchisees. And the reason I say that is because, as you know, I'm part of the Dunkin' Group, too, and we have 2,000. So you can get to a conference in New Orleans and really get some face time with all these different actions. So we have really sophisticated operators in the system. Clearly, by now, we expected interest rates to at least be headed in the opposite direction of where they have been added in the last couple of years.

That is not happening. But most of our operators are sophisticated, have sufficient capital and not huge amounts of leverage. So they're able to sustain their business without a lot of problems. And so again, I feel really good about where we are with price changes as far as taking costs out of clubs and looking at different things that we've done with the new growth model to help them through the difficult times of inflation, which this company has never really had to deal with having been founded in 1992.

I'm old enough to remember inflation in my 16% home mortgage back in the day. And this company has not had to face that. But I think we've hit square on with now pricing changes and changes CapEx and build-outs and remodels and reequips so that we are really working as a partner with our franchisees to keep this ball rolling.

Rahul Krotthapalli

On the marketing mix, would you take this opportunity based on your prior comments on the call to revisit the national versus local mix? And also do you think approaching with the clean slate focusing on the price point promotions and whatnot would make a lot of sense at this time?

Craig Benson

Yes. So Rahul, I think marketing needs to be addressed in the way that you talked about as well as other ways in the messaging we're putting out. So I think it's a whole different look at things. I, in the first time that I met with the franchisees in October, they had a separate conference, talked about rejiggering the which is national advertising fund and local advertising fund. We didn't get into any specifics, but they clearly understand that over time, we're probably going to have to relook at the way we do it and reallocate resources so that we can have a branding campaign nationally that's consistent, concise and more cost effective. And so there's a lot that needs to be done. And I do think over time, we will start to shift.

Thomas Fitzgerald

And Rahul, I think Colleen coming in as our new CEO with both franchise multiunit hospitality and marketing experience will help shepherd that journey.

Operator

Your next question comes from the line of Sharon Zackfia from William Blair. Please go ahead.

Sharon Zackfia

Hi. Good morning. I kind of want to make sure everyone understands the arc of membership. There's a lot of moving parts this year. I guess you talked about obviously what happened with the social media noise in March. And it sounds like rebounding joins subsequently, but elevated attrition. Are you looking at the second quarter having attrition outpaced joins? Or are we going to see a sequential kind of down quarter in membership?

Thomas Fitzgerald

Sharon, this is Tom. I appreciate the question. As you know, we don't guide on membership. And I think what I would say is all the things that we expect to happen in membership, and again, it's a forecast, right, we don't we don't know, are factored into our same-store sales, which is the primary driver there. As you know, member growth is still typically 70-ish percent of our same-store sales growth.

So while it's still positive, it's definitely called down and also with a wider range because it is a little bit more difficult to predict, and we certainly have seen a fairly consistent trend in cancellations year-on-year. We had a number of quarters with year-on-year improvements in attrition.

More recently, I think in Q4, it was more flat. And in Q1, in the early part, it was kind of a similar trend and then it definitely elevated in the back half of March through more recent days. So that's factored into how we adjusted our outlook for same-store sales and the cascading effects or ripple effects on all the other metrics.

Sharon Zackfia

And then I just want to talk about kind of timing of the Classic Card increase. I mean I think in the press release and on this call, you talked about consumers looking for more value. It does seem like an odd time to take a 50% price increase on the Classic Card. I understand why the franchisees would want it.

But I'm also curious, competitively, where you ran these tests, and there are going to be regions where you're not the lowest priced anymore. So how do you think about that? And how do you think about the messaging associated with that price increase?

Craig Benson

Sharon, I'm not sure that what competition may or may not do. There's also a school of thought that if we move other people move it's sort of been waiting for us to do something. We haven't touched the Classic Card since 1998. \$10 is Tom said in his opening remarks, I think it's worth about \$21, \$10 worth around \$21 now. And we've seen in every industry, people moving price. So it is not going to come as a shock to anybody that we are moving a price that's been in effect for a long, long time, 25 years. And so we, again, tested it pretty rigorously in multiple markets with good control groups and again saw positive results.

We think that this is the right time to do it. We also think it's the right time to look at different options on the Black Card, which may or may not change. But we have to be aggressive in testing and innovating amenities and end pricing. And so we're going to do that. OpEx and CapEx are two ingredients for running a successful club. And some of these price changes do change some of the OpEx calculations that are going on, whether it's changes in pay scales and/or its changes in rent or its changes in depreciation schedules, they all have changed and so we need to recognize that.

Thomas Fitzgerald

And Sharon, maybe just to add a couple of things to Craig's comments. As you know, about 60% of the people who joined join as Black Card members. So that is an important point for those who aren't familiar. I know you are.

And I'd say the second point back to what Craig said, we're a promotional brand. We're trying to get people off the couch, 40-ish percent of our new members have never belonged to any gym in their life. So I think it's just a question of the messaging and the types of promotions, but we're not saying back in the day, we're not doing a JCPenney of walking away from all the promotions and going to full price. That's too abrupt. I think it's just a matter of changing the elements, but still not taking our foot off the promotional accelerator.

Operator

Your next question comes from the line of Joe Altobello from Raymond James. Please go ahead.

Joseph Altobello

Thanks. Hey guys. Good morning. The first question on the price change. I understand you couldn't share the \$15 level with franchisees ahead of time, but I'm sure you've gotten plenty of feedback during the test. So what does that look like? And has it been uniform or does it vary by market since \$15 in one geography is a lot different than \$15 in another, for example?

Craig Benson

Yes. But the interesting part is that we looked to test across different demographics, markets. And again, with control groups matched up pretty well. And we were able to say that the price change to this \$15 level would work across the board.

And so we did take all that into consideration. Again, we spent a long time on this test. You recall, Joe, that we started the first set of tests last August and they progressed through the fall and all the way to almost April.

And so we do have a lot of test data by markets. It just -- it seems like the right time to do what we did and the right messaging. And again, the feedback from New Orleans, again, we can't tell them, but a lot of talk about needing some relief on the pricing front.

Joseph Altobello

Okay. Very helpful. And maybe a second question on the advertising campaign. You mentioned it wasn't as effective as you would have hoped. Was the big issue, the inability to highlight a uniform price, which, I guess, now changes going forward?

Craig Benson

Well, it's a factor. It's not the factor. And so the last portion of the advertising in that first quarter is 5x-ish more than the national advertising. So it's a big thing. And the local advertising did have a pricing element that national did not.

So -- but again, I go back to the fact that we have to be more than just about price. Tom's point about promotion is we'll always be a promotional brand, totally get it. But we need to be also talking about all the other benefits we bring to the market. And I think that creates stickiness. And having a brand allows us to be more targeted towards reinforcing a message that we found to be successful versus not having a successful brand where you're taking potshots at what might work and what might not.

And so -- and it's always anchored around promotion. So I think Colleen is going to come in and do a great job with this because, as Tom mentioned earlier, she has in her past has juggled 10 brands simultaneously, and you can't step on one for the benefit of the other and you have to clearly create market space for each one of them with a differentiated message. She knows way more about this than I do by a long shot. So I'm looking forward to coming in.

Operator

Your next question comes from the line of Max Rakhlenko from TD Cowen. Please go ahead.

Maksim Rakhlenko

Great. Thanks a lot, guys. First, can you remind us how many members gyms open with these days? And what does the member waterfall look like over the first few years? And then you previously noted that the 5-point growth plan would contribute about 500 basis points to IRRs. So curious, what about this? How does this price increase compare? And then when you combine the two, does it get franchisees' IRRs potentially quite close to back in line with pre-pandemic levels?

Thomas Fitzgerald

All right, Max. You win the award. Let me -- so the first one is on the ramp. So I think in terms of how stores open. So we measure it through presale periods day one and then subsequently. And I think the good news is we continue to see through Q4 and the early part of Q1 here, very similar ramps that we saw pre-COVID, not quite back to where they were, but definitely much closer than we've seen in the prior years. Certainly, in aggregate, the trends that we're talking about that are affecting our outlook will affect some of that ramp a little bit. But hopefully, again, that's temporal in nature.

I would say the moves that we made in the new growth model to get it somewhere between a 5% and 10% cost reduction in the cost to build, we're ahead of schedule, as Craig mentioned in his prepared remarks there. And the team is continuing to look at ways to find more savings that do not affect the members' experience. So I feel really good about the progress the team has made on that. The -- and combine that with the changes we made in the CapEx obligations, both extending the franchise agreement from 10 to 12 years, adjusting the strength in cardio mix and all the rest that you know moving reequipped cycles out on average a year.

We believe we'll definitely get us back to sort of closing more than half of the gap that we've had in our IRRs recently versus pre-COVID. This pricing test, we believe -- it takes a while for the members to feather in at \$15. As we model it based on the results we saw over the many months of testing, we believe that after a year or so, when the membership has more mix than at \$15 that there's probably a low to mid-single-digit improvement in AUV, which will certainly help improve the IRR.

It may not get -- depending on the circumstance, it may not get it back all the way to pre-COVID, but further helps chip away at the remaining gap that we talked about. So we're the pre-COVID unlevered IRR would might be in the low 30s, more recently and be in the low 20s, the changes in the new growth model get it to the mid-plus-20% range. So this would just be even more accretive may not get back to the low 30s, but we're continuing to find ways to reduce the cost, which should continue to close that gap as well.

Maksim Rakhlenko

Got it. That's helpful. And then this one should be a little more qualitative. But can you speak to the competitive environment. Some of your HVLP peers have been seen pretty significant growth in the opening. It seems like they might have had a bit of a better first quarter. A lot of those boxes are almost twice the square footage of your gyms. So just curious how you're thinking about the competitive set and whether that may have driven part of the weakness here in 1Q?

And then just bigger picture. The competition today is certainly stronger than previously. It's better financed, so definitely going to be something to watch going forward. So curious how you're thinking about where the biggest opportunities are for you guys to step up your own execution because this might become a bigger risk going forward?

Thomas Fitzgerald

Yes, Max, it's a good question. And I think you're right. Certainly, in pockets, both geographically and competitively, brands, there are pockets that are stronger than others. Crunch definitely took down quite a bit of space in 2023 and some of that is where they have franchisees that are PE backed and a bit more aggressive kind of like some of our folks. There are some other bigger boxes like EOS and Vasa that offer a much bigger box and a whole lot more inside of it, whether it's a pool or classes or the theater, cycling rooms that some of them have.

I'd say what they all don't do is provide a non-intimidating environment. We still think that's the thing that sets us apart from the rest. Some use the words. But if you go in there it's kind of loud because people are banging weights and granting and doing all kinds of things that if you've never been in a gym is going to intimidate you. So we still think that's an important part of what we do that others don't do and really can't do based on the number they attract.

So I think back to what Craig was saying about the brand, the positioning, the projection and the messaging, that's got to come through probably stronger. And to many people, that's way more important than whether we're \$10 or \$15 based on some of the research we've done. Because if you've never been, we used to say people get to the parking lot and they're afraid to go in the front door because they're not sure what's on the other side. So we -- to the extent that we can ease that anxiety, we don't think our competitors will. Will there be more -- so I think they're still going after the 20%, we're still going after the 80%.

Operator

And your next question comes from the line of Korinne Wolfmeyer from Piper Sandler. Please go ahead.

Korinne Wolfmeyer

Hey, good morning, guys. Thanks for the question. I'd like to touch a little bit on, first, the international expansion. I know we've been focused more on the U.S. today, but if you could provide an update on efforts internationally in the Spain efforts, that would be great?

Craig Benson

Yes. So we are aggressively going after the Spanish market as we speak. And as you know, made our own investment in Spain to help speed that up. We would like to get a partner to come in and help us, but we're learning a lot by being a part of this whole process. And we're learning where we can be successful and tweaks and so on and so forth, we need to make in order to make the club more suitable for the marketplace in the Spanish marketplace.

And then from there, that will allow us to look at other European potentials to be able to leverage what we've done in Spain and the investment that we've made. So we're pretty pleased with how it's going and look forward to some short-term learning and benefits to the betterment of the entire system.

Thomas Fitzgerald

Yes. And it's -- we're looking -- we're targeting our first store to open Q3, hopefully, the early part of Q3. And to Craig's point, we'll learn a lot and will affect the subsequent openings, but we've been reviewing a lot of sites. We have some in the pipeline in various stages of negotiations. So we feel good about the progress there.

Korinne Wolfmeyer

Great. And then now with a new CEO hiring, I know she is still yet to start, but is there any update on progress with the CFO search? I know you had wanted to get the CEO before the CFO, but any update you can provide on the CFO search? And what kind of criteria the team is looking for?

Craig Benson

Yes. The team started already interviewing. We look forward to coming in and helping. We've identified some internal candidates as well as external candidates. And we've already started interviewing. So it is moving. Colleen will be and is hopefully slated to June 10 once she starts, start with that process as well.

Thomas Fitzgerald

Yes, maybe just one more. I think we're probably in the third inning or so. And hopefully, we're by the time Colleen arrives She's got a short list of candidates to interview and make a selection from. We feel good about the progress we've made, and that will still give some time for transition based on that timing.

Operator

And that concludes our Q&A session for today. I would like to turn the call back over to Craig Benson for closing remarks.

Craig Benson

We very much appreciate your time and patience with us today. Again, this company is, I think, well positioned based on the changes that have been made and changing leadership that's forthcoming. So I want to thank you again and look forward to talking to you soon.

Operator

This concludes today's conference call. Enjoy the rest of your day. You may now disconnect.

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