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Potbelly Corporation (PBPB) Q2 2024 Earnings Call Transcript

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Press Release

10-Q

EPS of \$0.08 **beats by \$0.02** | Revenue of \$119.70M (-5.47% Y/Y) **beats by \$65.00K**

Potbelly Corporation (NASDAQ:[PBPB](#)) Q2 2024 Earnings Conference Call August 8, 2024 5:00 PM ET

Company Participants

Adiya Dixon - Chief Legal Officer, Chief Compliance Officer and Secretary

Robert Wright - President & CEO

Steven Cirulis - CFO & Chief Strategy Officer

Conference Call Participants

Todd Brooks - The Benchmark Company

Matt Curtis - William Blair

Jeremy Hamblin - Craig-Hallum

Operator

Good afternoon, everyone, and welcome to Potbelly Corporation's Second Quarter 2024 Earnings Conference Call. Today's call is being recorded. [Operator Instructions]

On today's call, we have Bob Wright, President and Chief Executive Officer; Steve Cirulis, Senior Vice President and Chief Financial Officer; and Adiya Dixon, Senior Vice President, Chief Legal Officer and Secretary of Potbelly Corporation. At this time, I'll turn the call over to Adiya Dixon. Please go ahead.

Adiya Dixon

Good afternoon, everyone, and welcome to our second quarter 2024 earnings call. By now, everyone should have access to our earnings release and accompanying investor presentation. If not, they can be found in the Investors tab on our website.

Before we begin our formal remarks, I need to remind everyone that certain comments made on this call will contain forward-looking statements regarding future events or the future financial performance of the company. Any such statements, including our outlook for 2024 or any other future periods, should be considered forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are not guarantees of future performance, nor should they be relied upon as representing management's views as of any subsequent date.

Forward-looking statements involve significant risks and uncertainties, and events or results could differ materially from those presented due to a number of risks and uncertainties. Additional detailed information concerning these risks regarding our business and the factors that could cause actual results to differ materially from the forward-looking statements and other information that will be given today can be found under the Risk Factors heading in our filings with the Securities and Exchange Commission, which are available at sec.gov.

During the call, there will also be a discussion of some items that do not conform to U.S. Generally Accepted Accounting Principles, or GAAP. Reconciliations of these non-GAAP measures to their most directly comparable GAAP measures are included in the appendix to the press release and investor presentation issued this afternoon, both of which are available in the Investors tab on our website.

And now, I'll turn the call over to Potbelly's President and CEO, Bob Wright.

Robert Wright

Thank you, Adiya. Good afternoon, and thank you for joining our call today. I'm proud of the hard work and dedication of our over 5,000 team members. The entire Potbelly team is committed to our mission to delight customers with great food and good vibes on our journey to be the most loved sandwich brand in every neighborhood.

Despite the challenging macro environment, we maintained focus on executing our winning strategy, emphasizing what we control to continue growing Potbelly. Our customers, our associates and our franchisees are the people that matter most to our success. We have an incredibly strong brand and a company that understands the power of growth regardless of the environment.

During the second quarter, we grew same-store sales 0.4% as we continue to face a changing consumer dynamic, similar to what you've heard from many others in the industry. While our growth was less than envisioned, we continue to take traffic share from the broader fast casual industry and grew our top line despite macro pressures. Second, we expanded shop margins again, representing the 13th consecutive quarter of year-over-year margin expansion. Finally, we added 4 new shops in the quarter to go along with our franchise commitments to open 22 additional shops.

Early Q3 sales patterns suggest the consumer is still pressured and is managing their restaurant spend carefully primarily by trimming visits in favor of grocery. As I look ahead, however, I've never been more confident in the future of our brand. Our confidence is rooted in our outstanding people and our strategic and executional focus, particularly in 3 main areas. Number one, our customers love Potbelly food and service as well as our ongoing efforts to help them with value. Number two, our digital channels, including our Perks loyalty program, continue to prove that we can drive growth through these channels. And number three, the increasing momentum of our franchising and new shop development efforts.

I'll expand on these factors, beginning with our food, service and value supported by effective marketing. Delighting our customers is always the foundation for sales growth, and I'm very pleased with our strong shop operations and the continued progress of our marketing initiatives that together fuel our traffic-driven sales growth strategy. We see the results in our overall customer satisfaction scores as well as continued improvement in customer ratings of our food, speed, accuracy and friendliness.

Of course, the best thing we market is our amazing food, and our culinary innovation efforts continue to deliver a pipeline of exciting menu items that demonstrate our commitment to quality, craveability and relevance. During the second quarter, we reintroduced the Chicken Cordon Bleu sandwich by adding it to the underground menu, rolled out successful LTOs to celebrate summer with the Jalapeno Popper Chicken Sandwich and American Apple Pie Shake. Our most loyal customers continue to tell us that our focus on food is one of the reasons they keep coming back.

To maintain the excitement among our guests, we kicked off third quarter with the introduction of the Blueberry Muffin Cookie and the Farmhouse Chicken Sandwich. As we move through the remainder of the year, you should expect to see additional limited time only offers, including our hot oven-toasted sandwiches, our fresh baked daily cookies and hand-dipped shakes.

Importantly, as we discussed last quarter, and has become readily apparent across the restaurant industry in recent months, today's consumers more than ever are looking for value when they choose to eat out. The first element of our 5-pillar strategy has always been great food at a good value, and we're constantly working to further amplify our value options. It's important that our customers know we understand their situation and that we're working to help in every way we can.

During the second quarter, we tested Everyday Value Combo meal deals to help provide our more price-conscious infrequent customers with the opportunity to continue to frequent our shops. The testing revealed a clear winner. The \$7.99 skinny combo not only responds to our customers' cravings for Potbelly, but also we've given our less frequent price-conscious guests a great reason to keep us in their eating rotation while simultaneously protecting our margins. Starting in late July, we expanded the \$7.99 Everyday Value Combo, which includes a turkey, ham or chicken skinny sandwich with chips and a drink across nearly all of the system.

Customers have already told us how much they appreciate our efforts to help them with everyday value. In fact, we saw a 7-point lift in value scores and a 5-point lift in return intent among those that ordered the \$7.99 combo. Not only that, the \$7.99 combo has shown to drive both incremental sales and profitability as it continues to build usage. We're proud to have added this new option to our menu in addition to the everyday value already available with our meal deal and our Pick-your-Pair options to further support our customers during these challenging economic times. In addition to our everyday value efforts, we continue to see significant success with digital promotions, including Perks Only promotional activity to drive value, brand affinity and frequency.

So, turning to the Potbelly digital experience. For the quarter, our digital business represented approximately 40% of our total shop sales, an increase of approximately 200 basis points versus last year. As we've mentioned, in recent quarters, we continue to see a shift within our digital mix to Potbelly-owned channels. In fact, during the second quarter, expansion of Potbelly-owned channels represented the entire 200 basis points of year-over-year improvement in our digital mix. As customers progress through our digital funnel, ultimately becoming Perks members, we see increased frequency almost immediately. Over the past 3 years, we've been improving and enhancing our digital capabilities and expect digital and Perks to remain a driver of the business going forward.

Recall in January, we further strengthened our digital platform with the launch of our enhanced Potbelly Perks loyalty program. Our new program is performing exactly as expected, with customers redeeming coins for a balance of the 12 menu items available and in alignment with their purchase patterns. Perks continues to be a key piece of our strategy in driving our growth and celebrates what our customers love the most about Potbelly, great food. While we continue to provide our customers with options on how they can consume our food, be it on-premise, off-premise, digital or in person, we believe the ongoing transition of more of our business to Perks will only further benefit us in the long term, driving closer connections to each and every customer.

I've mentioned how pleased we are with our digital growth, recognizing that we believe we can continue to leverage what we control. Perks member acquisition continues to grow quarter-over-quarter and year-over-year. Importantly as well, once our customers join our Perks program, we see year-over-year growth in transactions and engagement from every consumer segment. Put simply, our customized communication to our various Perks customer cohorts is driving them to evermore loyal and frequent relationships with the brand.

Finally, in addition to the broad-based everyday value efforts I've already mentioned, our digital channels are an incredibly effective and efficient way to deliver value enhancements to our most loyal customers, not only through the intrinsic value of their accumulated coins, but through spot promotions that can activate their engagement and drive sales. Despite Potbelly digital experience already being a consistent and significant area of growth for us, we are not standing still. When customers utilize our digital platforms, it not only ensures a better experience, but it also allows us to more effectively communicate with and market to them. We maintain an extensive road map of digital enhancements aimed at continually improving our Potbelly digital experience to best suit customers' needs, expectations and reduce friction while driving Potbelly brand awareness, customer engagement and business results.

Now let me update you on our franchise growth acceleration initiative. During the second quarter, we continued to make significant progress across all phases of our unit growth funnel. Less than 3 years ago, I shared a vision of Potbelly growing to a 2,000-unit brand in the U.S. primarily through franchising. We're well on our way. We already have 663 open and committed shops as of the end of Q2. So far this year, we've opened a total of 9 shops with further acceleration expected, which I will touch on in a minute. Franchise recruitment and lead generation continues to build, especially with our in-market and in-person recruiting efforts. Importantly, we're moving those franchise candidates to franchisees through deal signings as well.

We're pleased to increase our total year-to-date shop commitments to 54, an increase of 22 relative to last quarter. Our second quarter commitments include a deal that will bring Potbelly to the state of Georgia for the first time with an agreement in the Atlanta market. These new agreements reflect the continued strength of our franchising efforts across the Southeastern U.S. over the last 2 years. And as I said, we now have 663 open and committed shops across 33 total franchise groups. And I'm proud to say that our franchisees are meeting their development commitments, which strengthens our expectations of continued growth through the remainder of 2024 and 2025.

Lastly, with our ongoing acceleration of shop openings, I mentioned we opened an additional 4 shops during Q2 for a total of 7 openings year-to-date through the second quarter. We're also proud to announce that we've opened 2 additional units already in the third quarter. With our current development pipeline, we expect to double Q2 openings in Q3 for a total of 8 new shops with further acceleration in Q4. We currently expect to open a total of at least 30 new shops in 2024, and we already have visibility to the 2025 opening pipeline with more to come.

While it's still early, we're very pleased with our performance of our new 2024 shops. I'm proud to say that on average, these shops are not only outperforming their sales forecast, but their average weekly sales surpasses the system average. We're not simply opening shops. We're opening successful shops. The success of these shops is a sign that our market planning and real estate systems are working. Of course, we expect this unit level success will further accelerate growth as we sign even more commitments to the pipeline, further increasing our confidence in our ability to reach our 2,000 unit potential.

With that, I'll now turn the call over to Steve to detail our financial performance for the second quarter.

Steven Cirulis

Thank you, Bob. Good afternoon, everyone. Revenues in the second quarter were \$119.7 million, with company revenue of \$115.5 million, lower year-over-year driven by the short-term impact of last year's refranchising. Contrast that with our franchise revenue of \$4.2 million, up 117% relative to the second quarter last year, driven by a 53% increase in franchise units. As a reminder, we are deemphasizing the sale of our company shops through refranchising given our strong pipeline of deals in new markets.

Average weekly sales were approximately \$26,110, and system-wide sales were approximately \$142.3 million. Same store sales were up 40 basis points in the quarter. This on top of positive same store sales of 12.9% in Q2 last year. As Bob mentioned, we continued to take traffic share from both the broader restaurant industry as well as the fast casual segment during the quarter.

Turning to expenses. Food, beverage and packaging costs were 27.1% of shop sales, a 90 basis point improvement versus the prior year period. This was driven by a combination of commodity deflation and a modest pricing action in the quarter.

Labor expenses were 28% of sales, a 240 basis point improvement versus the prior year period. This improvement is attributed to the ongoing optimization of our hours-based labor guide and improvement in overtime management and hours of operation adjustments.

Occupancy was 10.9% of sales, a 40 basis point increase versus the prior year period. This was predominantly due to an increase in variable rent charges as many shops with those types of lease arrangements, like airports, continue to outperform prior year.

Other operating expenses were 18.4% of sales, a 160 basis point increase versus the prior year period. This was predominantly due to increased brand fund expense and utility rate increases.

Overall, shop-level margins in the second quarter were 15.7%, an increase of 130 basis points year-over-year.

General and administrative expenses were 8.3% of system-wide sales, largely in line with the year ago period.

Second quarter adjusted EBITDA was \$8.5 million or 7.1% of total revenue. The year-over-year increase driven by the 130 basis point improvement in shop-level margins and continued strong performance of our franchise shops and ongoing disciplined management of G&A.

We reported net income of \$34.7 million for the quarter, driven by a \$31.3 million benefit from the release of most of the company's tax valuation allowance during the period. The change in the valuation allowance is the result of our recent profitability and our expectation for continued sustainable profits moving forward. The release of the valuation allowance allows us to record \$31.3 million of deferred tax assets on our balance sheet, which will be used to satisfy a substantial portion of our future cash taxes, freeing up additional capital to reinvest in our business.

Adjusted net income was \$2.5 million, a \$0.5 million increase versus the prior year period.

As we announced on our last earnings call, our Board authorized a \$20 million share repurchase program, driven by their confidence in the sustainability of our cash flows as a franchise business model. During the second quarter, we purchased approximately 86,000 shares of our common stock for a total of approximately \$700,000. We are excited to be able to use this additional lever at our disposal to help drive long-term shareholder value.

Incorporating our year-to-date results with the category outlook for the remainder of the year, we expect our Q3 performance to land in the following ranges: same store sales growth of negative 3.5% to negative 1.5%; adjusted EBITDA of between \$6.5 million and \$8 million. For the full year 2024, we have updated our same store sales guidance to negative 1.5% to positive 0.5%, and our adjusted EBITDA to between \$27 million to \$30 million. As a reminder, the impact of refranchising on our adjusted EBITDA growth rate is most pronounced in the first 3 quarters of 2024 as 25 of our 34 refranchised sales to date occurred in the second half of 2023. In addition, as Bob previously mentioned, we anticipate opening at least 30 new shops for 2024.

With that, I'll turn the call back over to Bob.

Robert Wright

Thank you, Steve. I'm excited for what the future holds for Potbelly. The second quarter represented yet another step in our transition to a franchise-led growth story as we grew comparable restaurant sales, expanded restaurant margins for the 13th consecutive quarter and continue to grow our open and committed shop count. As we move forward, I'm confident that our customers' love of our food, the continued strength of our digital channels and the success of our recent shop openings will allow us to capitalize on the immense opportunity ahead of us. We're proud of what we've accomplished thus far, and I can assure you, we're only getting started.

In closing, I'd like to thank all our Potbelly team members from our frontline associates to our support center employees, and of course, our franchisees and their teams for their hard work and commitment to making Potbelly the most loved sandwich brand in every neighborhood. With that, we're happy to answer any questions. Operator, please open the line for questions.

Question-and-Answer Session

Operator

[Operator Instructions]. And we'll take our first question from Mark Smith with Lake Street Capital.

Unidentified Analyst

This is Alex [indiscernible] on the line for Mark Smith today. First one for me is largely around the consumer. Last quarter, you mentioned that frequent visitors were visiting less. Just kind of curious, did that persist this quarter? Or did you kind of retain more of that from the Everyday Value Combo meals that you rolled out this quarter?

Robert Wright

Yes. Thanks, Alex. Good to talk to you. I think what we saw is a little bit of a continuation from our discussion in Q1. It is those less frequent consumers, and they're less digital, they're less loyal. So because of that digital disconnection, it's harder for us to get to them. And that's why we shared last quarter that we intended to test some everyday value options. Something that you can make sure is present all the time. Things you can market and merchandise in the shops for those infrequent customers that are coming in. And as we told you in the prepared remarks, by the end of the quarter, we had discovered which of the ones that we tested was driving the business the most for us, the \$7.99 skinny combo. You get one of those turkey, ham or chicken sandwiches, chips and a drink. And I think what customers are looking for is they're looking for a meal that's in the sweet spot of what they can afford to continue to go out to lunch and not start making decisions to trade to the refrigerator to grocery. But they don't want to compromise on getting a whole lunch. And so the fact that this is a full combo makes a lot of sense.

Look, we still grew sales in the quarter, up 0.4%. And the full impact of the \$7.99 combo was not really fulfilled in Q1. But the other piece of it, as I mentioned, on the frequent side, our more digital customers, we continued to drive growth on that side of the business. We're very pleased with our ability to stay connected with those customers, offer them not only just the intrinsic value of the Perks loyalty program, the coins and that new program we put into place in Q1, but then some spot promotions that help them with that, too. Those most loyal customers or more frequent customers also, they're the ones that really like the LTO innovations and the food innovation that we bring because they're familiar with the brand and they like to explore our menu a little bit. So that's helped them, too.

But yes, look, it's that customer. And they're not just -- I want to be clear that our insight doesn't suggest they're pulling back visits from Potbelly. What we're seeing is that they're pulling back visits period, at lunch and a little bit at dinner, too, because they're just trying to manage their overall restaurant spend, and they're doing it with shaving transactions. And our goal with \$7.99, which we're pleased with, was to give you a very good option to trim that visit from somebody else and not put ourselves in a position where we're overly promoting the brand and creating some profitability challenges. So I'm really pleased with what we've discovered with that combo meal.

Unidentified Analyst

Got it. Yes, that makes sense. That's a lot of help. And then just the last one for me. And you guys kind of introduced it last quarter, but the new prototype, 1,800 square foot store size, you opened one in Arkansas this quarter, I think. Just kind of curious, what's the puts and takes, maybe the learnings from this? And then if you have in mind an ideal mix of these to the traditional store size, kind of like a 1 in 10 or 1 in 5, anything there?

Robert Wright

Yes, look, the prototype is the template for all new builds going forward. Now the reason we only had one last quarter is because the shops that were in the pipeline had already been through design, engineering and permitting, and you don't want to waste time to go re-permit those. And to be clear, the 1,800 square foot is a targeted square footage. We know that the brand can deliver everything we're looking to deliver at 1,800 square feet. Honestly, we've got some franchise locations later this year that are 1,600 square feet. So we can go smaller. In some cases, franchising may go a little bit bigger. That one in Arkansas, we're very, very happy with. It's just like the others that I spoke about on average, but very happy with the sales there, and I'm really happy with the way the prototype look came together.

What it does aesthetically is that -- and as we build more and more and more, you're going to see this become the standard, but it really preserves what's so special about Potbelly's atmosphere, but it does it in a more efficient way. Fewer seats matches our digital business mix today and actually accentuates a few things that we think are so important to the brand. The stove, the drinks, not only the grab-and-go drinks, but our drink station, the varied seating. We've held many of the custom items that make Potbelly so special, those things that we produce uniquely for each shop when it opens. So a lot of that has been preserved, but it's more efficient. And I think I was clear last quarter, but just to remind you, that square footage, if the average unit in our legacy system is 2,300 feet, for a franchisee that's targeting lease spaces that are 1,800 feet, that's 500 square feet can be tens of thousands of dollars a year in occupancy costs that just go away. And that is an occupancy advantage that just keeps on giving to those franchisees when they open.

Operator

We'll move next to Todd Brooks with The Benchmark Company.

Todd Brooks

A few quick questions to lead off and then a couple bigger picture ones. Steve, is there a way that you can decompose the 0.4% same store sales of us kind of traffic versus price versus mix?

Steven Cirulis

Yes, sure. Let me start with price. That's always the easiest thing to begin with. We had about 4.3% of gross price for the quarter. About 1 -- sorry, about 2.5% of that was carryover, and then we had 1.9% that we introduced with a pricing action in Phase 2, and then we had one at the end of the quarter in P7 to get us to the 1.9%. We saw about half of that come to us in check. So 4.3% in check -- or sorry, in gross price. About a little over 2% in average check for us.

Which leaves you with traffic, obviously, and there was -- traffic was down for us a bit. And what we always like to look at as we compared ourselves to fast casual is are we doing better even in a tougher environment. And yes, for another quarter, we did better on traffic than did fast casual. There's a little bit of mix shift down there, too. We saw some things that we've already called out in prior calls with some customers moving to different sizes on our menu down from the Bigs. Of course, our \$7.99 combo that features a skinny plays a part in some of that mix shift as well as some of the discounting that we did in the quarter. So we're proud of the fact that even in this environment, we were able to put forth a same store sales gain when a lot of folks are struggling out there.

Todd Brooks

Absolutely. No, absolutely. Do you want to take the opportunity -- and we can frame it a couple ways. One, do you want to talk about the quarter-to-date commentary that kind of frames up the same-store sales guidance that you provided for Q3? Or do we want to attack it maybe another way, talking about you're delivering more value, but I mean Subway's rolled out I think a \$3 meat tube now for people, so competitive value as well. And as you've settled on the \$7.99 for the combo, we feel good about that value, but just wondering about competitive pricing actions and potential impact on the business.

Robert Wright

Todd, I think those are great companion questions. Let's -- Steve can tackle the guidance piece of it because I think that's important how we're starting the quarter. And then I can pick up on the competitive piece because there's a lot going on in the competitive space for sure.

Steven Cirulis

Sure. Look, Q3 has started out a little softer than we would have wanted, and there's a few factors at play. I think the beginning of the quarter had a slightly different dynamic as it relates to the 4th of July for us. So 4th of July was on a Thursday this year, which meant that the weekend that everybody usually travels really was in P7 for us this year when it was more in P6 last year. So that had a dynamic relation to the comp. And Hurricane Beryl affected us a bit. We have 20-some odd Houston shops. And for the period, it was 75 to 80 basis points drag on the comp. So those were headwinds that we started out with right away. Also, we're still building that \$7.99 combo deal. As Bob mentioned, it's performing well and it continues to build. So that's something that we're looking forward to seeing.

So the consumer environment is something that's not lost on us. And so what's reflected in the guidance is not a change -- a material change in that behavior. But we've got a situation where we feel like we're highly competitive with our value. We're highly competitive with our LTOs that are coming out. And of course, that Perks program is really going to help us move through the quarter. And if you look at our full year guidance, you'll see that we've got a positive same store sale at the high end of that range. So that just gives you a sense for the kind of confidence we have in the way that the business is going to move and improve as we hit Q4 and the latter part of the year.

Undaunted by what's happening out there because we feel like we've got the right kinds of tactics. Not just to kind of make sure that we're competitive here and building the business back to positive same store sales, but also ultimately, we get judged on profitability. And so that EBITDA number that we've guided to for the year is also something we're confident in. Even with softer sales, you can see we have the ability to kind of manage margins really well, not just at the company -- or not the shop level, but also at the company level as we control some expenses along the way. So look, it's not going to be an easy back half of the year. But I think we've got a strong management team and a great plan to get after it, not just within the environment that we're in right now, but to continue to build against the long-term growth plans that we've set out.

Robert Wright

Yes, Todd, if I can build on that. I think that there's a couple of things in the guidance, too, that we have not factored in a significant shift in consumer behavior. And there's a lot to be read that there are some reasons to believe maybe that is the case later in the year. That -- we're not counting on that. And we don't like to build into our guidance things that we haven't tested. And that \$7.99, as much as we like it, we've already screened 20 more everyday value ideas that could be companion ideas. We get a lot of credit from our customers for Pick-your-Pair. \$7.99 fits nicely into that type of everyday value because it builds on the menu. It makes sense to our customers who may already order skinny sandwiches or see that chips and a drink that they can make a meal deal out of.

And then when it comes to what's going on competitively, something that we know from all of our experience on this team, there are things you can do that are far more aggressive. But the risk to the profitability, and also as we become more and more of a franchise organization, the risk to franchisee adoption really goes up as you get more aggressive. Especially if you just on its face discount a core menu item to a different price. And we see a lot of that out there. The transactional breakeven on those types of deals tend to be very high. And if you don't have millions of dollars to spend -- and I mean maybe tens of millions to spend on television to try to get that traffic to break through that breakeven, it can be a very bad idea for the P&L, and it may not get you the sales you need even to get back to even.

So we've been very careful with that. I mentioned in our remarks that \$7.99 works really well for our customers. It works well for us, too. And I think that's why you're not seeing us do some of the super aggressive ideas that some others are. But I also mentioned, these things -- people seem to really recognize when you're doing something that helps them out. To get a 7-point bump in value and a 5-point bump in intent to return off of a single price pointed combo like we've gotten is not something I've seen very often in my career. And it didn't take us cutting the price in half to get there. It just really broke through that starting place where someone says, this is something I'll come back for on the day or maybe the day before my payday instead of the day after I got paid.

Todd Brooks

Yes. No, that's great to hear the lift you got. And then one final one, and I'll jump back in queue. We've got another quarter of history behind us with the new Perks reward tier structure. Are you finding -- and I know we had good redemptions at lower tiers, surprisingly good at that 200 and 300 coin level early out of the gate. What I'm wondering is as you're seeing those customers redeem at that level, are you getting updated the point to them continuing to redeem to that level? That that's enough for them from a value standpoint, and they're happy to get a free cookie after 300 coins. And they're happy, and they'll keep visiting and keep -- actually, are you seeing evidence of the frequency benefit at the lower reward tiers? I guess that's a more succinct way to ask it.

Robert Wright

We really are. And it's very interesting how different customers are using the new program to their advantage. Some of our most frequent customers are the ones that only get cookies. They almost kind of have this position that I'm coming all the time anyway, but I -- this is like a free dessert when I come back. And others are saving up for their sandwich. It is still entree. It still skews more entrees than it does desserts and sides, which is what we expected. The mix on the redemption is almost exactly what we expected it to be. But when you go a layer deeper and you look at the individual consumer behaviors, you can see that they're dialing it in to fit their personal preferences for their visit patterns.

I mentioned in the remarks, too, we continue to see growth in member acquisition, and we continue to see growth in the penetration of those Perks transactions. But something new that I shared this quarter is we have divided those Perks customers up into frequency cohorts. And as you might expect, people first enter the program. They're not nearly as frequent as when they've been in the mature relationship with us for maybe a year or longer, whatever the number is. I'm using that as an example, not a specific marker of time. But across those cohorts, all of them have increased transactions and frequency. So we're bringing people into the Perks program at rates and growing year-over-year and quarter-over-quarter. And once we get them into the program, we're advancing their frequency regardless of the level that they may be at when they enter. So we're just really pleased. The last thing I'd say is the frequency overall for Perks is consistently delivering what we have seen in past quarters. So even as it's growing, we're getting the frequency on average that we want out of those groups.

Operator

We'll move next to Matt Curtis with William Blair.

Matt Curtis

Just on the third quarter comp guidance, I mean, which obviously includes the slowdown you saw in July. Maybe I could just ask you -- or approach it in a different way. I mean, could you walk through what's happening with traffic and ticket as you move from the second quarter to the third quarter? I mean, is most of the slowdown related to letting some price roll off the menu, or is it more driven by the stepdown in traffic?

Steven Cirulis

Yes. Thanks, Matt. It's honestly it's a combination of both. We have -- if you look at in Q3, our carryover dropped from 2.5 in Q2 to 1.4 in Q3. So that's part of it, for sure. But there is softness that we see in traffic as well. So I would -- I think what we're able to do, though, is think about what we want to do with price. We've always discussed pricing as a way to outrun inflation in terms of its increases. And we've seen some really, I think, beneficial commodity numbers and some labor inflation lower than we thought. So we have another price increase planned for Q3, but honestly, we're contemplating whether or not we need it at all as we want to continue to kind of support the business and meet the customer where they are. So it's not one of those things where we've seen traffic fall off to the extent that pricing isn't helping us a bit. So it's a combination of the two.

Matt Curtis

Okay. So assuming you do go ahead and take that price increase in the third quarter, can we expect your price benefit in the third quarter to remain at that 4-point something level? I think you said 4.3 in the second quarter. Or would it fall into the 3-point something range?

Steven Cirulis

It'd be in that low 4 range.

Matt Curtis

Low 4 range. Okay. So shifting over to something else. With the unit development guidance for this year being lowered, could you tell us what you're seeing in the franchise pipeline and how you'd expect the ramp to be in franchise development in 2025? I mean, what I'm getting at basically is do you see right now the potential to move back into double digit franchised unit growth territory next year?

Robert Wright

Yes. I'll be brief because I want to be clear. Yes, absolutely. What we're seeing, we had talked about the 30 shops that we could see in the 2024 pipeline. I was really clear in the last quarter that you never know how some of these things move, depending on an issue with the water line or whatever may happen. And then there were 10 more that we saw that were potential. Those 10 didn't go away, and there are others beyond those. But we -- I know we've stated our long-term growth algorithm would be low-double digit CAGR unit growth rate. We do not expect to wait beyond 2025 to get to that number. I think what we can see in our pipeline, we're looking at 10% growth or better next year. And this is just building momentum. That's the other reason I tried to be clear with what we're seeing in Q3. If we open 4 in Q2, we can double that number in Q3. You don't have to double it, but you nearly double it again in Q4, and that's that picking up of momentum. And the reason we believe in those things is because we can see every layer of the systems that we're providing the support for the franchisees to get there. So, yes. Look, the long-term growth of the brand is still something that has us all super excited about the future, and unit growth development is not an exception.

Matt Curtis

Okay. Great. Thanks for clarifying that. And last one for me, I guess. On the combo meals, I mean it's good to hear you're getting some traction with the value combos. But what's the other value ideas you've screened? I think, Bob, you mentioned you screened 20 more, if I heard that right. Does that imply --

Robert Wright

That's right.

Matt Curtis

Does that imply that you may expand your value offerings in the second half of the year?

Robert Wright

That's exactly what I'm implying, Matt. Thanks for clarifying. What I wanted to make clear when we were answering the previous question is that we did not bake any success in any of those expanded value offerings into our guidance, because until they've been tested, we're just not comfortable betting on that. So we do have things that we're working on that we believe can set us up to beat our own trajectory this year, but we've really got to get to work and get those things done. I'm actually pretty excited about some of the things that were in that screening. And we screened them, of course, with customers, and the customers were very excited about some of the things that are in there. So yes, you should expect to see us do some more and do some of it rather quickly, to be honest with you.

Operator

We'll move next to Jeremy Hamblin with Craig-Hallum.

Jeremy Hamblin

Congrats on the nice execution in a tough environment. Want to just come back to same store sales. Sorry, I missed the beginning part of the call. But in terms of just fleshing out, can you remind us how your compares are in Q3, whether or not July 2023 I think might be your toughest comparison, monthly lap of the quarter, but just how we can think about that. And in terms of kind of thinking about from here, your expectations for kind of comp levels to reaccelerate, or what you're looking for in terms of getting to your guidance.

Steven Cirulis

Yes, sure. I think, look, last year was a good year for us in terms of comp, but it started to normalize in the back half of the year. So you're right. We see kind of Q3 as our peak in last year. And so what will be helpful for us is certainly that relaxation a bit. But the way that we start to think about comps, and we mentioned that in our prepared remarks is on a 2-year basis. So if we look at even quarter 2, I think we mentioned in the prepared remarks we're at the end of 12.9% on a 2-year basis, which relative to I think some of the other things that are going on in the market, it's a pretty strong performance.

I think one of the other things that is important to note, if we look at sort of Q3 on a 2-year basis, if we're kind of in our guidance range, we're still doing over 3% same store sales comp. And then similarly, into Q4, it's positive outright if you kind of look at the full year, but on a 2-year basis, you're still north of 3% as well. So look, the environment's different this year than it was last year, of course. And as Bob discussed, we've got a lot of firepower that we're deploying against the back half of the year. And the comps that we've put into the guidance, just to remind everyone, reflect not a material change in the consumer environment. And we don't have all the things that we discussed completely tested. So there's a lot of potential here in the back half of the year for the comp, which is why if you look at the range, we still got -- we've got our sights set on a positive comp for the full year.

Jeremy Hamblin

Got it. But July is the toughest monthly lap of Q3?

Steven Cirulis

I believe that's right, yes.

Jeremy Hamblin

Okay. And then just moving on in terms of thinking about the unit openings. You've got 9 shop openings year-to-date, of which I think 7 franchised to company. Can you help us think about the progression of that here in Q3 in terms of expectations and then into Q4?

Robert Wright

Yes. Thanks. And you've got that right. We have shared before that we would keep a company development somewhere along the way if it made strategic sense or if it were a special site of some kind. I think you saw we made news with the opening in the Pentagon. That would have been a very difficult opening to do through franchising, and we were so excited to get started with the military. I was actually at that grand opening. Shop's performing very, very well. But going forward, we opened 4 in the quarter. We opened 3 in Q1. We're anticipating 8 in Q3, and the remainder will be in Q4. So it's kind of a steady pattern of acceleration. And we expect all the other ones that we can see in the pipeline in 2025. Obviously, we just keep getting farther and farther ahead of our own pipeline.

The other qualitative commentary I offered was our franchisees are on track with their development schedules. That's a major sign of optimism for us in the ability to continue to be on track. And just as importantly, the shops that we're opening are averaging better than anticipated. So that's really important to us. Franchisees offer us their own forecast of what they expect to do. And we're seeing our new openings beat their forecast and beat the system average. So our ability to open new shops that are on time and performing as well as we'd like them to perform and we expect them to perform just bodes really well for the future.

Jeremy Hamblin

Great. Last one for me. On your progress on labor, really nice execution there. In terms of thinking about sustainability of that here as you progress, and I think you still have probably some other initiatives that you're working on in that particular category of expense. Just any additional color you might be able to share in thinking about that on a go-forward basis.

Steven Cirulis

Sorry, you were breaking up on that question for me. I don't know if, Bob, he was for you as well. If you could repeat it.

Robert Wright

Yes, a little bit. I heard part of it related to labor. Go ahead, Jeremy.

Jeremy Hamblin

Yes. Sorry. So I was saying great execution in Q2 on labor. I know you have probably some additional initiatives that you're still working on. But wanted to just get a sense for sustainability of that. You noted that the labor costs were a little bit lower than you expected, but where -- kind of where you go from here and the ability to sustain that.

Steven Cirulis

Yes, sure.

Robert Wright

If Steve can hear it -- okay. Sorry, go ahead, Steve.

Steven Cirulis

No, thank you for that. Sorry, it was a little choppy on my end. But listen, we're proud of the way that we were able to manage labor in Q2. And a lot of these things are ongoing efforts. We had a 240 basis points improvement in labor versus last year. A lot of that driven by efficiency work from our ops team and our COO. Our hours-based labor guide, we continue to find new ways to wring efficiencies out of that. We also optimize some of the overtime spend that we saw. We also added some new effect from trimming and optimizing some of our hours of operation where we were having inefficiencies in our labor. That was well over half of the benefit that we saw in the quarter. We had some -- because we had lower sales, obviously we had less of a bonus accrual there as well. So those things will continue to pay dividends into Q3, but we'll also even get better at them. I think we've had several quarters in a row where we said, hey, hours-based labor guy. We continue to get efficiency out of that. So we expect to do that as well.

And we've -- when we brought on Pat Walsh as our Chief Human Resources Officer last year, he has created a lot of programs at the field level to help us optimize things like training and efficiencies and hiring and things that also give us just a benefit overall on the labor side. So those are additional things that are going to play into our favor throughout the year. So it is not a one-time benefit, we don't expect, on expanding and working harder to continue to get labor optimization.

Robert Wright

I'd love to -- Jeremy, thank you. The only thing I would add to that, because as an operator at heart, where I grew up is you want to keep watching the customer experience. When you're managing labor, the third rail, of course, is to start to take it out of the experience itself. And that's why we added in our prepared remarks to speed, taste, friendliness, overall satisfaction -- overall satisfaction, both with digital and with in-shop orders all improving. And so that's really the best combination. We're able to be more efficient. And there's always a systems layer gets kind of boring. Start looking at wage management and keeping turnover down and all those things that give us that stability. But yes, I think -- but for a little bit of that bonus tailwind, we'd love to start writing those checks again. That still gives us a lot of leverage with the brand now.

Operator

Thanks. Ladies and gentlemen, we have reached the end of today's question-and-answer session. I would like to turn the call back over to Mr. Bob Wright for closing remarks.

Robert Wright

Thank you, operator, and thank you all again for your time this evening. We look forward to talking to you again soon. I hope you all have a great night.

Operator

This does conclude today's program. Thank you for your participation. You may disconnect at any time and have a wonderful evening.

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