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Transcription

Mister Spex Q2/H1 2023 Results Presentation

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PRESENTATION

00:01 Irina Zhurba

Good morning, everyone, and welcome to our Q2 2023 results call. The presentation, as usual, will last around 30 minutes. Then we'll allow another 10–15 minutes for the Q&A. As usual, you can find the presentation online on the Investor Relations website under reports and presentations. The speakers today with me are Dirk Graber, founder and co-CEO, and Dr. Mirko Caspar, the co-CEO of Mister Spex. That said, let me hand over to Dirk to begin today's call. Thank you.

00:28 Dirk Graber

Hello from my side as well. Thank you for participating. And let's quickly jump to the executive summary of today and our agenda. So, Q2, we continued to outperform the market and showed a very solid trading result. Consumer sentiment is slightly improved in Q2 versus the last two quarters. And we continued also to execute on our Lean 4 Leverage program, and we will give you further insights in the next couple of minutes. We also made good further progress in fulfilling our brand promise, which is to deliver the perfect frame for every face and perfect lens for every eye. Mirko is going to elaborate on that, how we progressed over the last months on this topic as well. And then I will lead you through the financials in the second part of the presentation, going into our good revenue development of +10% in Q2, a total of 8% in H1, and the return to EBITDA profitability for the first half-year, which is an improvement of EUR 4.7 million versus the first half of last year. And this is also supported by a very strong improvement of our operational cash flow. So, having said that, heading over to Mirko for the strategic update on Mister Spex.

02:10 Mirko Caspar

Thanks, Dirk. Good morning, everyone. As Dirk said before, we are seizing opportunities. We are increasing our market share while we are improving profitability. And on the other hand, we continue to develop our brand strength through delivering on our promise of the perfect match for every face with ease, style, and expertise. So let me give you the overview.

On the left-hand side, you see the consumer sentiment development. And while we do see an improvement in sentiment quarter over quarter, the absolute level is, of course, still very low. Regardless, we are – and you see that on the right-hand side – outperforming the market and taking market share. And we continue to do so in the months where the market is growing, and we do so in the months like three, four, five, six, where the market has been slightly shrinking. Now the market here is Prescription and sunglasses in Germany, as a reference measured by the GfK.

A significant driver of the market share gain has been our store performance. So let's look at that in detail. We have seen on the left-hand side a significant improvement of the average sales per store. And you see on the right-hand side a

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step-up in store profitability, and we are returning to solid EBITDA per store on average. Now the EBITDA on the right-hand side that you see is the four-wall EBITDA; it includes rent, but it excludes the central overhead costs. But you see, starting from March, we have been consistently going back to strong EBITDA on average per store. And if you remember, the drivers that we introduced in our Lean 4 Leverage program for the stores were mainly the price optimization, which holds true for all channels, online and offline. A second bigger measure was that we started selective campaigns to create local demand in areas where we still see low traffic numbers. Still, we do some discounts but are being very targeted and selective in those campaigns. And on the bottom line on the lower part of the P&L, you see a tighter grip on costs and a higher flexibility of the workforce. So we did actually reduce the average staff per store, but the even bigger lever was the significant increase in flexibility, so we could put the workforce where we actually need it.

Those improvements that I mentioned with regards to the stores, as you recall, they are under the joint umbrella of our Lean 4 Leverage program. And the first pillar is the concentration on the core. That is, A) we focus significantly on the DACH region of our business, and B) we focus on the existing stores. The like-for-like growth has been 6%. And I already touched on the improvements of the profitability of our stores in the store network. The second pillar is basically to earn more money with every product sold. And you see again, also in the second quarter, a strong improvement in gross margin. And we'll double-click and zoom in on that in a second, but I already highlight one driver of that, and that's the introduction of the price for the formerly free lens of 1.5 single vision. And on the third pillar, the Lean efforts to increase our operational leverage. The first thing is we're rolling out the Lean philosophy in a large-scale training program. Over 20% of employees have been trained by now, and they're using process analysis, value chain analysis, team boards, shopfloor boards, etc., to continuously improve the efficiency of what they're doing. On the other hand, we closely looked again at our headquarter functions, and actively made FTE adjustments to support our continuous focus on profitability and cash.

Let's double-click on the optimization for the margins. What you see is 189 bps improvement quarter year over year for the second quarter and, again, a significant improvement in margin—and mind you, while we are growing and taking market share. And in the first driver that I already mentioned, in the middle of April, we introduced the price of EUR 19.95 to the 1.5 lens, which was formerly free, which added significantly to the base point improvement of the margin. The second is we continue to reduce discount rates. You see that in the middle of the slide. And also a significant driver in Q2 was the margin-accretive product mix. You see that we were growing significantly in sun at the expense of contact lens, which is the lowest-margin category, and that was deliberate.

Before I hand over to Dirk, I want to highlight a few initiatives that continue to build our brand strength. Why is that so important? We have again reduced the share of marketing spend while increasing the margin and taking market share. And that's quite tricky in that magic marketing triangle. And one thing that supports that is the power of our brand, which allows us to outperform in all three of those categories. And what we do to improve our brand positioning and work continuously on our brand strength? So the first one is the perfect frame for every face, with ease. We rolled out our bespoke frames technology and the collection for the perfect fit and comfort. It is based on our own face-capturing technology and fit algorithm. We've rolled it out to 23 stores, and we continue to do so. Also, the same fit algorithm is in our app. We launched it in the iOS store for new customers so they can measure their face, and we can recommend the fitting frame from our large assortment. And that increases the conversion rate of new customers and reduces the return rate for those new customers. If we look at the style, we added six new brands to already outstanding assortment Maui

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Jim, with incredible lens technology. And in addition, we launched seven collabs. And just one highlight: Mrs. Bella from Mister Spex net collection sold out in 1.5 hours. And what you also see is we continue to deliver on expertise, and that was one of the biggest focuses of our 15 years anniversary campaign. What we did is featured our own employees and highlighted the 15 years of optical expertise that we deliver. So as you see, we continue to deliver every quarter on our brand promise, and that's why we are so confident about our strategy. Now over to Dirk with more numbers.

09:50 Dirk Graber

Okay, thank you, Mirko. So, let's quickly look at the highlights of the financial update. I mentioned a few of them. So we accelerated our growth rate in Q2 to 10%, bringing H1 to a total of 8%. So we are fully on track on our full-year plan on the revenue side. In terms of profitability, we also went back to a profitable adjusted EBITDA in H1 with EUR 0.7 million, which was a significant improvement versus the first half of last year by EUR 4.7 million. Also, here we are on track. Second quarter, we see a very strong cash flow development of EUR 13 million. I will comment on that in more detail in a few minutes. And we ended the quarter with EUR 124 million in cash and cash equivalents, which is a very solid basis for us.

So now let's look into the details a little bit more. This year in Q2 but also in H1, the revenue split is slightly different than last year. Why? Because we focused on the higher margin categories. You see that the growth in prescription glasses accelerated versus last year to 8% in Q2, and for sunglasses by 22% in Q2. For the first half, prescription is up 13% and sun is up 18%. Please remember always that in our sunglass revenues, also prescription sunglasses are included. So, within the season, we typically see a marginal trade-off between prescription and sunglass growth, but balancing this out typically on a per year basis. Contact lenses – we told you already in earlier calls – we took the deliberate decision to really focus on margin-accretive revenues. And so, therefore, we optimized margin management for contact lenses, which led to slightly reduced revenues, so Q2 -6% and H1 -8%. There's also a certain FX impact, which I will explain to you on the next slide, in particular in the Nordic countries included in that -6% and -8% for contact lenses. Overall, we continued to really show strong mid-double-digit numbers for our boutique segment and also a healthy growth on our own brands. In total, we added three stores in the second quarter; currently running 74 in total.

So now let's look into the segments Germany and International. Part of our Lean 4 Leverage program is to focus on the core business and really tweak our total business for profitability and getting to a positive cash flow. And so, the focus on Germany is part of that. And we have a strong brand awareness here. And also the investments in our retail store network, and so on, are quite advanced in that market. So, therefore, we showed a very strong 14% growth in Q2. That is supported by the 6% like-for-like growth of the retail stores in the second quarter. First half, basically, double digit like-for-like growth on our retail network. International, we see a slight contraction by -2%. Constant currency is +2%. So we see some headwinds on Nordic currency development in the second quarter. And overall, basically, we continue with our very strict margin management also in the international markets, focusing on bottom line.

So now let's look at the financial performance based on where is the improvement of EBITDA coming from. So, in the second quarter, we continued to improve our gross margin by roughly 190 basis points. So, first half year, it's 290 basis points improvement. The HR costs are slightly increasing in percent of sales. Why? Because we significantly added

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retail personnel for our 14 new stores. But on the other hand – Mirko explained it – we also been very cost-sensitive on our overhead. Marketing expense in the second quarter contributed by roughly 30 basis points to the EBITDA improvement, and a significant contribution came in the second quarter from the other operating expenses. So EBITDA improved by 270 basis points and the adjusted EBITDA by 250 for the second quarter. In the first half, it's a total improvement of 230 basis points. On the marketing, just a comment, here, we are on a good path to continue our optimization levers. But we had also a very successful 15-year anniversary campaign that started in Q2, which focused on our optician expertise and helped to drive our sales in the German market as well.

So, now, if we dive a little bit deeper, what you see is the gross margin improvement, which is the biggest lever on EBITDA improvement in the first half. It's really driven by price adjustments, and the reduction and simplification of discounts. We continue that path, and we see that we are having a strong brand equity and that our consumers are basically accepting that. And will continue to grow and increase our absolute profit. Personal expenses, I just explained. We streamlined headquarter functions, but on the other hand, have an additional 14 stores. Operational expenses, here next to the higher AOVs, which drive significantly these operational improvements, we also see the first positive impacts from productivity improvements through the lean management approach that we started to implement in the internal organization. But the first impacts we see in operations. Marketing, I mentioned, continued reduction optimization, which really helps to drive the improvement in the effectiveness of marketing. And we also have lower one-off expenses and adjustments, leading to this 230 basis points in improvements of adjusted EBITDA in the first half of 2023.

Now, if we look at cashflow, which shows a very strong development in the first half of 2023, we ended Q1 with EUR 113 million in the bank. Now, we added from Operations EUR 18 million. We invested EUR 4 million, which party is store expenses; the other one is capitalized IT investments and negative EUR -3 million on the financing, which is mainly through these payments that we had. So we're ending the quarter and the half-year by EUR 124 million. So next to, obviously, the good trading results and the EBITDA improvement, the operating cash flow improved significantly through working capital management. There are some seasonal effects on this because of sunglasses, but overall, we are very satisfied with that development.

So let's look at the second half. What do we expect and what you can expect from us? So, I think Mirko mentioned it: consumer sentiment is not easy, right? And also, if you look at the latest GfK numbers or the comments on the German economy, which is our core market, it's not so promising. We see that. I would say there are some headwinds on trading or potential trading because of that consumer sentiment, but overall, we are committed to what we initiated, our Lean 4 Leverage program. So, on gross profit, we continue to reduce and simplify discounts. That will also be true in the second half. We continue to grow in the highest margin category, which is prescription glasses, and also increase the share of prescription in our total revenue mix. What are the headwinds on gross profit? It is, over the summer we've seen significant promotional activities also from competitors. And while the second quarter showed really good weather patterns, and you've seen our sunglass growth for Q2, I would say the weather, at least for our core markets, in Q3 showed mixed results, with headwinds impacting also the revenue there.

Personal expenses, we continue to streamline our headquarter functions – Mirko mentioned it. So there will be some benefits from that in the second half. But we also continue to add new stores. We're planning to open up to three new stores in the second half, ending the year with eight or nine. And also, we see continued labor cost deflation and overall

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cost deflation in our core business. On the operating side, I mentioned we started to implement the lean management philosophy. First impacts are shown in operations, but also customer service. And we roll that out to headquarter function as well, and we continue to focus on our marketing effectiveness. But on the downside, headwinds would be any kind of operational key leverage in case the market sentiment is further deteriorating.

All right. So let's look at the guidance. That stays unchanged. So, we are committed to our mid- to high-single-digit revenue growth for 2023 on top line, and a low-single-digit percentage adjusted EBITA margin for the full year. Q3, I just mentioned. So, we see mixed weather patterns, especially impacting, obviously, sunglasses. We see the GfK consumer climate lowering in the last month or two. And we also see that the world is in flux. So, there are a lot of things happening. And therefore, we stay cautious on the overall management but are fully committed to the guidance, as I said. So, looking ahead, we will present our Q3 numbers on November 9th, and then also attend a number of conferences in the second half of the year, followed by a company-sponsored roadshow this afternoon. So, having said that, I would like to thank you for your listening and participation. And then we're going to open Q&A.

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Q&A

22:54 Operator

Thank you. If you do have a question for our speakers, please press *11 on your telephone keypad to enter the Q&A queue. Once your name has been announced, you can ask a question. If you do find that your question has already been answered, and it is your turn to speak, you can press *11 again to cancel your question. Please stand by it whilst we compile the Q&A queue.

Once again, if you would like to ask your question, please press *11 on your telephone keypad. Our first question comes from the line of Graham Renwick from Berenberg. Your line is open. Please ask your question.

24:01 Graham Renwick (Berenberg)

Hello, good morning. Thanks for taking my questions. I have a few. Firstly on Q3, you've mentioned a bit of softness due to the weather. Are you able to give us a bit of color on what sort of growth you are seeing so far over the summer? Should we still be expecting sales to grow in Q3 but just at a more moderate pace versus what we've seen in Q2?

Second question is on cash. You've obviously had a very strong cash performance in Q2. I know there's a few technical factors within that, but where are you expecting cash to land at the end of the year? What are your expectations for cash burn this year?

Third, just on the AOV, up 10%, how much did price increases contribute to that solely versus price mix? And on the price mix topic, where is the mix of progressive lenses now in the business and how has that been developing? And then just finally, your store opening plans for the second half and what your current pipeline is for next year. Thank you.

25:08 Dirk Graber

Thank you, Graham. So I take the first two, and then on AOV I will hand over to Mirko, and also for the store expanding. So, on growth, we expect single-digit growth also in Q3. I would say maybe a little bit more moderate than in Q2, but so far we are on track for that. On the cash balance, I mentioned, I think we're satisfied with the current progress. But there are also some seasonal working capital impacts on that. So we remain with our cash flow guidance for the full year,

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which we gave, to end the year with EUR 105 to 110 million. So that's the current expectation that we have. And then over to Mirko on the AOV development.

26:07 Mirko Caspar

We see, due to the fact that we have FX effects negatively affecting the AOV of contact lenses, actually, a lot of the average AOV development is price increases for prescription. And that's a healthy, stable development that we can bank on for the second half of the year. The development of multifocal, I think, and the progressive lens share, what you see is that the share improved online roughly 10%, and offline roughly 10%, as an order share. So, that shows you that our continued effort on optical expertise is driving those positive share developments, not only through more stores that we opened. But in both channels, we see an increase in the share of multifocal that also contributes to the AOV, obviously. But again, there, you see that the price increase for single vision and multifocal, we drive that in both categories, so to say.

27:31 Dirk Graber

So, on the scope expansion, in the second half, it will be likely quite backloaded. So, to the end of the year, we've signed a number of contracts. So we've secured the locations already, which I mentioned. And for 2024, we currently expect a similar pace as this year, but we haven't finalized the plans for next year yet. So we are always screening the market for attractive opportunities, and we have a running pipeline there.

28:23 Operator

Thank you very much. Our next question comes from the line of Cedric Rossi from Bryan Garnier. Your line is open. Please ask your question.

28:34 Cedric Rossi (Bryan Garnier)

Yes, good morning, everyone. So I have two questions. The first one is regarding the consumer sentiment, so a follow-up on Graham's question. Do you feel that, even if we stay at low levels, that the consumer patterns and the traffic is

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becoming more predictable, also helping you to probably increase your marketing effectiveness? That's my first question.

The second one is regarding the boutique format. So it continues to outperform the other price points. I recall that over the past quarters you are not planning any additional store openings with regard to this format. But looking at the performance and probably also maybe a discussion that you have with other brands, do you feel that probably you could maybe reconsider this scenario and open a new boutique format in the near future?

And my third question is regarding consolidation. So we have been seeing many M&A deals over the past quarters in the eyewear industry. So the market consolidation is probably also helped by smaller chains and brands being under pressure. Is M&A still on the table with regard to Mister Spex?

29:54 Mirko Caspar

Hi, Cedric. Let me let me take the first two questions. On consumer sentiment, well, I think it is predictable in the sense that it'll stay relatively low in our core territories for quite a while. However, just to shed a bit of light on it, we saw boutique sales grow roughly mid-double-digit. So really strong boutique growth, again. That is relatively independent of the average consumer sentiment in the market. We see a strong demand for the fashionable and luxurious eyewear. And so that's relatively predictable. Also, our targeted campaigns for the fashion-oriented private label and value buyers are also over-proportionally successful. So we see an overproportionate growth in those two segments – the targeted fashion for private label and the boutique. And we do feel that, with those two targeting efforts, we expect a further improvement in marketing spend, or at least to keep the spend deficiencies that we've seen in the first half of the year.

On the boutique store format, actually, we are really satisfied with the success of the boutique store format, even though it's only one store. What we have done is that we selectively increased boutique assortment, and also tweaked a bit of the boutique environment in the existing stores. So that is one aspect of the boutique format that we wanted to do. And actually, the rollout of the custom-made frames in all of our stores, as the next step, is one sign that we back our boutique and premium strategy in all stores. And now to the question that you really ask: will there be new boutique formats? There is no concrete plan, but I definitely do not rule it out, since it is actually quite successful. And over to Dirk, maybe, on the consolidation in the industry.

32:20 Dirk Graber

So, Cedric, I share your view. We have also seen a lot of the same movements in the market. I think our first priority is always to improve our core business and to also grow organically. Nevertheless, yes, they are, every once in a while, attractive opportunities in the market, which we, if reasonable and if value-accretive, look at. And so, therefore, we continue to do so. And in case there is an opportunity for us to strengthen our position in another European market, existing or new, we would consider that also in the future. I think the further we progress with Lean 4 Leverage, and

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especially, if it gets to where we aim for on the organic path, the easier it is to then also think of adding potential add-ons, if they are accretive in value.

33:37 Operator

Thank you. The next question comes from the line of Alexander Thiel from Jefferies. Your line is open. Please ask your question.

33:47 Alexander Thiel (Jefferies)

Hi, good morning. Most of my questions have already been answered. Just a quick follow-up on the Q3 seasonality. Is it fair to assume that Q3 is still going to be stronger than Q4 in absolute revenue terms? And then looking at your EBITDA line, the D&A increased significantly year over year. If you could touch on the impairments that you saw on that side, and from a margin progression perspective, is it also fair to assume that Q2 is now the peak of the year, with the 3.4%? Because you're seeing higher promotional activity. So how should we basically think about the competitive situation on the market when it comes to pricing for the rest of the year? Thank you.

34:34 Dirk Graber

Sure. So maybe I start with the margin improvement, Alex. So, what we see is, we started to improve our focus on pricing and gross margin in Q3 last year. So we do expect, also because of product mix with prescription increasing in share again in the second half of the year, to see margin improvements on a year-over-year basis, but maybe not as high as in the first half. But we do expect, basically to improve. There's always an assortment mix effect, as we said, but overall, we do expect, basically to see further gross margin improvements on a year-over-year basis in Q3.

On the D&A, we had some technical effects. Because if your equity value is higher than your market cap, there are some triggering events in IFRS, where you have to have impairment tests. And we've done that also again in the H1 report. And you have to do this on a CGU level, so cash generating units, which at Mister Spex are individual stores. And if an individual store is slightly below the expectation, you need then, basically, to adjust. That means also, if market cap would go up and store performance picks up, that effect would reverse. But there was an impairment test done for

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roughly EUR 2.7 million, fully on the retail network, where a low number of stores were impacted. And we have then to write up the investments into the store and to write up used assets. And that we've done according to the IFRS rules.

36:59 Mirko Caspar

And maybe just adding quickly, I wasn't 100% sure, Alexander, if you were referring to the absolute strength of Q3 versus Q4, or the margin, or the growth. So, on absolute levels, Q3 is stronger than Q4 because we have a significant share of sun still. In terms of growth, it's very hard to tell. It's just we have a normal growth path as we guided the market. But on an absolute level, Q3 is stronger than Q4 due to seasonality.

37:42 Alexander Thiel

Okay, that's very clear. Maybe a follow-up. On the Fielmann call, there was again a pretty heavy discussion on the employee market situation for opticians. Could you give us some insight into how you're basically progressing with sourcing new opticians and store employees for your new stores that you're planning to roll out? What's the situation on the employee market, basically?

38:09 Dirk Graber

So, I think we continue with our existing strategy, and that is the following. We need to be an attractive employer brand for opticians to join Mister Spex. And I think, with our approach to leadership, to culture, I think we demonstrated definitely to – especially – younger, dynamic opticians that we are basically strong. So that's the first one in hiring. Also, when we enter new cities, obviously, we need to hire people, but we also try to transfer often existing employees to new city stores. Because then we have, I would say, a mix of new and existing Spexies, as we call them, who know the process already and can run the store more efficiently if you compare to just a new team. Secondly, we also invest in apprenticeship. So, this year, we had an intake of more than 14 new optician apprentices across our five training centers. Cologne is the latest training center that we opened. And now we run five of them across Germany in different cities. And this is always a three-year program where they finish as a certified optician. Additionally, we also updated our program to basically have an education for most opticians which are required to run a retail store. So at least we have one. And here we have an attractive program for existing opticians that want to become a master optician to work either part-time at Mister Spex and do their education, or to take a leave and do this as a block, and then take over also a leadership position within one of our retail stores. So overall, we see that in the market. So it's not that we don't see it.

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But I think we have good programs and measurements in place to not struggle, to continue to grow, and to further develop and also educate and train our existing retail staff.

40:45 Alexander Thiel

Okay, that's very clear. Last from my side would be on your international markets. Which country is currently ripe, from a brand-building perspective, that you can go from the pure online site also to an offline store site? Which countries are currently, based on your estimate, your next store openings?

41:11 Dirk Graber

We do focus on DACH right now with the store expansion. As you know, we already have stores in Sweden on top, but for now, that's our focus within our strategy. Within Lean 4 Leverage, it's focused on the core, and that holds true for the omnichannel strategy for now.

41:39 Alexander Thiel

Okay, thank you.

41:44 Operator

Thank you. The next question comes from the line of Albrecht von Witzleben. Your line is open. Please ask your question.

41:56 Albrecht von Witzleben

What is your present market share in Germany?

42:07 Mirko Caspar

If you only look at revenue, depending on which source you use, the German market is typically estimated to EUR 500 to 600 billion in sales, across all categories, across all panels. So, within that market, our market share is roughly, purely on revenue, 3%. But that's a ballpark number. Obviously, within the individual categories, it's very different. And also on units it's a different game. So I think, if we look at the numbers, we see that in sunglasses, within optical retail, we are

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even the market leader. In contact lenses, I think the estimates are slightly low double digits in terms of revenue. And if you look at prescription glasses in terms of the units, we are at a high-single-digit market share. But since we have a higher single-vision share because of the average age of our customers being high-30s, and therefore the price being significantly lower for single-vision and for varifocals, the revenue share is lower in prescription in terms of revenue.

43:40 Operator

Thank you. We have no further questions at this time.

43:59 Irina Zhurba

Okay, thank you so much. I think then we're done for today. Thank you for participating in our call. As usual, if you have any questions, please reach out to me. I'll be very happy to answer. Alternatively, very happy to see you during one of our roadshows in the coming month. Thank you so much and have a great rest of the day.

44:18 Dirk Graber

Thank you so much. Thank you.