Transcript of
RCI Hospitality Holdings, Inc.[1]
Second Quarter 2023 Earnings Conference Call
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Presentation

Mark Moran - Chief Executive Officer, Equity Animal

Greetings and welcome to RCI Hospitality Holdings' Second Quarter Fiscal 2023 Earnings Call. You can find RCI's presentation on the company's website. Click "Company and Investor Information" under the RCI logo. That will take you to the "Company and Investor Information" page. Scroll down and you'll find all the necessary links.

Please turn with me to slide two of our presentation. I'm Mark Moran, CEO of Equity Animal. I will be the host of our call today. I'm here in New York City with Eric Langan, President and CEO of RCI Hospitality, and Bradley Chhay, the Chief Financial Officer.

Please turn with me to slide three. If you aren't doing so already, it's easy to participate in the call on Twitter Spaces. On Twitter, go to @RicksCEO and select the space titled "$RICK RCI Hospitality Holdings Inc 2Q23 Earnings Call."

To ask a question, you'll need to join the Twitter Space with a mobile device. To listen-only, you can join the Twitter Space on a personal computer. RCI is also making this call available for listen-only through traditional landline and webcast. At this time, all participants are in listen-only mode. A question-and-answer session will follow. This conference is being recorded.

Please turn with me to slide four. I want to remind everyone of our safe harbor statement. You may hear or see forward-looking statements that involve risks and uncertainties. Actual results

[1] This is a clean verbatim transcription that has been edited to increase readability.

may differ materially from those currently anticipated. We disclaim any obligation to update information disclosed in this call as a result of developments that occur afterwards.

Now please turn with me to slide five. I also direct you to the explanation of RICK's non-GAAP measurements. Finally, I'd like to invite everyone listening in the New York City area to join Eric, Bradley and me tonight at 7:00 to meet management at Rick's Cabaret, New York, one of RCI's top revenue-generating clubs. Rick's is located at 50 West 33rd between Fifth Avenue and Broadway, a little in from Herald Square. If you haven't RSVPed, ask for me or Eric at the door.

Now, I'm pleased to introduce Eric Langan, President and CEO of RCI Hospitality. Eric, take it away.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Thanks, Mark. Thanks, everyone for joining us today. Please turn to page six for today's news. We moved ahead on a number of fronts in the second quarter. Revenue grew to $71.5 million. That's an increase of 12.3% year-over-year, reflecting both same-store sales and acquisitions. Free cash flow was $14.8 million, up 33%. Adjusted EBITDA was $21.7 million, up 8.8%. We completed our 5-club, Baby Dolls-Chicas Locas acquisition and look forward to optimizing their contributions. On a sequential quarter basis, our Bombshells turnaround program has started to produce results. We also advanced many of our projects involving club acquisitions, new club developments, the Rick's Cabaret Steakhouse and Casino in Colorado, and new Bombshells locations. I'll be back to tell you more and answer questions later. Now here is Bradley to review the financials.

Bradley Chhay - Chief Financial Officer, RCI Hospitality Holdings, Inc.

Thanks, Eric and good afternoon everybody. Looking at some of the other major numbers in the quarter, EPS was $0.83. This reflected some non-recurring items. On a non-GAAP basis, EPS was $1.30, up 9.2% year-over-year. Net cash from operating activities was $16.8 million, up 44.8%. We had 9.3 million weighted average shares outstanding. That's down 2.4% year-over-year due to prior period repurchases. The 200,000 shares issued as part of the Baby Dolls-Chicas Locas acquisition had minor impact. That's because they were issued late in the quarter.

Now, moving on to the income statement. Please turn to page eight to review the nightclubs segment. Revenues totaled $57 million, up 18.4% year-over-year. That was driven by $6.9 million from acquisitions and newly remodeled clubs and 3.7% same-store sales growth. Operating margin was 31.6% and 39.3% non-GAAP. GAAP operating margin included a legal settlement expense and an impairment. Compared to the first quarter of fiscal 2023, revenues increased by 1.3%, driven primarily by acquisitions, while non-GAAP operating margin declined 1.1 percentage points. That reflected the fact that we had two weeks of the Baby Dolls-Chicas Locas acquisition, which did not allow enough time for full optimization.

Please turn to page nine to review the Bombshells segment. I only have three things to say here. Number one, results improved sequentially. Revenues increased 6.6%, driven mainly by the acquisition of Bombshells San Antonio and the Grange Food Hall with its new Bombshells kitchen. Non-GAAP operating margin expanded 1.6 percentage points. All this reflects initial progress from our turnaround program. Number two, while our operating margin target remains 18% to 21%, the segment's performance at 15.4% non-GAAP was right in the middle of many well-known publicly traded restaurant chains that have recently reported their results. And lastly, number three, the segment was profitable, generating $1.8 million GAAP and $2.2 million non-GAAP.

Please turn to page 10 to review our consolidated statement of operations. Note that all comps are as a percentage of revenues. Cost of Goods Sold declined year-over-year reflecting increased service revenues. Salaries and wages were higher year-over-year and quarter-over-quarter. This was due to minimum wage increases starting on January 1 in many states where we have clubs. It also reflects higher labor costs at newly acquired clubs. SG&A was higher year-over-year but declined quarter-over-quarter. Year-over-year reflected newer acquisitions that are not fully optimized, and quarter-over-quarter reflected the absence of year-end audit expenses. Depreciation and amortization were higher year-over-year and quarter-over-quarter. The second quarter of 2023 included a one-time accelerated amortization of Grange food stall leases. Other charges and gains reflected $3.1 million in legal settlement expense and $662,000 of non-cash impairment. Operating margin was lower year-over-year and quarter-over-quarter but on a non-GAAP basis was approximately level with the year ago quarter and expanded one percentage point from the first quarter. Interest expense was higher year-over-year but lower quarter-over-quarter. Second quarter of 2023 included initial cost of new debt for the mid-March Baby Dolls-Chicas Locas acquisition.

Please turn to page 11. We ended the quarter with cash and cash equivalents of $22.8 million. Keep in mind that this was after paying $18.4 million for the cash portion of acquisitions. Free cash flow was 20.6% of revenues and adjusted EBITDA was 30.3%. Both increased sequentially and are in line with our 20% and 30% targets, respectively, as a percentage of revenue.

To wrap up our discussion of the income statement, please turn to page 12 for an update of our geographic focus. In the second quarter of 2023, our regional revenue breakdown was: Texas at 41%; Florida at 25%; New York, Colorado and Illinois were 8%, 7%, and 6% respectively; and the other eight states combined for 13%. This demonstrates our geographic diversification, our exposure to growth states like Texas, Florida, and Colorado, and how we develop our business clusters in key areas.

Turning to our Balance Sheet, please turn to page 14 to review our debt metrics. Net of loan costs, debt was $245.8 million as of March 31. That's an increase of $35 million from December 31. The increase primarily reflected financing for the five club Baby Dolls-Chicas Locas acquisition, partially offset by scheduled paydowns of other debts. Our weighted average interest rate was 6.52%. This compares to 6.14% a year ago and 6.6% five years ago. Excluding balloons, our amortization schedule is now in the $12 million to $15.7 million annual range, which is very manageable with our higher level of cash flow.

Please turn to page 15 to review some of our other debt related metrics. The ratio of debt to adjusted EBITDA for the trailing 12 months was 2.7 as of March 31, below our comfort level of around three. Please note that this reflects our new debt related to the Baby Dolls-Chicas Locas acquisition, but only two weeks of contribution. Occupancy costs were 7.6% of revenues and continued to be well within the 6% to 9% range we've averaged when sales weren't dramatically impacted by COVID.

Now please turn to page 16 to look at our March 31 debt pie chart. Our debt now consists of 54.9% secured by real estate; 30.4% seller financing secured by respective clubs and/or the real estate to which it applies; 6.6% of unsecured debt; 4.1% of debt secured by other assets; and, lastly, 4% that relates to the new bank line of credit that was used in the Baby Dolls-Chicas Locas acquisition that is also secured.

Now, let me turn the call back to Eric.

Eric Langan – President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Thank you, Bradley. For this quarter, we added a third section to our presentation. We call it “Our Take” and are using it to explain our underlying thinking to where we are going. I want to remind everybody of our Safe Harbor statement. You may hear or see forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those currently anticipated. We disclaim any obligation to update information disclosed in this call, as a result of developments that occur afterwards.

Please turn to slide 18. Everything we do is about our capital allocation strategy, which is similar to those outlined in the book, The Outsiders by William Thorndike. First and foremost, the goal of our strategy is to drive shareholder value by increasing free cash flow per share by at least 10%-15% on a compound annual basis. We have been implementing this strategy since the end of fiscal 2015 with three different actions, subject to whether there is strategic rationale to do otherwise. One is mergers and acquisitions, specifically buying the right clubs in the right markets. We like to buy solid cash flowing clubs at three to five times adjusted EBITDA, using seller financing, and acquire the real estate at market value. Another strategy is growing organically, specifically expanding Bombshells to develop critical mass, market awareness, and sell franchises. Our goal in both M&A and organic growth is to generate annual cash-on-cash returns of at least 25% to 33%. The third action is buying back shares when yield on free cash flow per share is more than 10%. As a result of these efforts, we have exceeded our primary goal. Through the end of fiscal 2022, we have increased free cash flow by 22% on a compound annual basis, while reducing shares by 1.5% on a compound annual basis.

Please turn to slide 19. So what is the current break point between whether we should buy shares or invest in buying or opening new locations? Using a possible range of $68 million to $78 million for fiscal 2024 against 9.43 million shares, the 10% yield point for buying back shares comes in at $72 to $83 per share, subject to whether we can make better investments.

Please turn to slide 20. Let's take a look at our most recent club acquisition. We used $15 million in cash, $16 million in stock, and $35.5 million in debt to acquire five Baby Dolls and Chicas Locas clubs and their real estate. We estimate the acquisition will generate $11 million in adjusted EBITDA in the first full year after closing. After that with remodeling and some expansions, we estimate it will generate $14 million to $16 million in adjusted EBITDA. Let’s assume conservatively, we go from $11 million in year one to a midpoint of $13 million in year two and

$15 million in year three. That total of $39 million would represent an average annual cash on cash return of more than 50% on the $15 million that we put down on this acquisition.

If you turn to page 21, let's take a look at our planned Rick's Cabaret Steakhouse & Casino in Central City, Colorado. We bought the building and real estate for only $2.4 million. We anticipate it will take us about $8 million to complete, which would include 200 slot machines. Excluding the casino, similar-sized RCI clubs generate between $8 million and $10 million of revenue. Slot machines at existing Central City casinos average $129 per day. That's another $9.4 million in annual revenue. So the combined estimated revenue of $18.4 million at a 40% average club margin would generate a $7.4 million operating profit. Let's assume conservatively that we only do $3.7 million in year one, and in year two, we build to $7.4 million. That's a total of $11.1 million. That would represent an average annual cash-on-cash return of more than 50% on the $10.4 million invested. Keep in mind, this does not include any table games or sports betting revenue.

Please turn to slide 23. We also believe we have the opportunity to add even more locations. For example, it took 28 years for the company to go from one location to 21 locations. The following seven years, we added 19 more. And in the next five and a half years, we added another six to total 56 clubs, which represent only a small portion of the market we want to consolidate. As our company expands in size, we believe we can continue to potentially accelerate our rate of growth. This is due to a variety of factors, including increased economies of scale, enhanced market penetration, and greater access to resources. With a larger company footprint, we may be better positioned to capitalize on opportunities, take advantage of synergies, and achieve operational efficiencies that can help drive growth. Therefore, we believe, as we continue to grow as a company, we can potentially experience faster rates of growth and achieve greater levels of success.

Turning to slide number 23, we believe we have the cash to do this. Let's take a look at what happened in the second quarter. On December 31, we had $34.1 million. We made an additional $7.1 million in net new cash. We used $18.4 million in cash primarily for the Baby Dolls-Chicas Locas acquisition, ending the quarter with $22.8 million in cash. Now let's look at what could happen in the next fiscal year. Using the range of $68 million to $78 million in free cash flow, less $21.7 million in debt maturities, leaves us with a range of $46 million to $56 million in projected cash available to use for future investments.

Turning to slide 24, we also have shares we can use to finance acquisitions provided we continue to do it carefully, judiciously, and in an accretive manner. To that end, we believe we have demonstrated a strong track record. Since the implementation of our capital allocation strategy, we have acquired more than 2 million shares at an average price of $19.55 per share. We have issued 700,000 shares at an average price of $65.71 to provide $46 million of capital for acquisitions. From our viewpoint, we used shares that we bought at an average of $19.55 and sold them for $65.71 for a 236% cash on cash return.

To sum up, we have a long list of investment opportunities with the potential to generate significantly compelling returns when combined with our strong, disciplined, and proven track record to make it happen.

Please turn to slide 25. We'll be holding our 30th anniversary Gentleman's Club Expo convention, August 20th to the 23rd at the Paris Hotel in Las Vegas. For more information, go to the website listed on the slide.

Thank you to our loyal and dedicated teams for all their hard work and efforts. We can't do it without you. Now here's Mark to start the Q&A.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you, Eric and Bradley. Before we move on, I'd like to congratulate you both on the one year anniversary of the first ever earnings call on Twitter Spaces.

If anyone would like to ask a question, please raise your hand in the Twitter Space. When you finish your question, please mute your microphone to eliminate any background noise. We have a limited number of speaker spaces and after your question, so we may move you back to the audience to free up space.

We'd like to take questions from RICK's equity research analysts and some of its largest shareholders first. To begin, we'll have Scott Buck of HC Wainwright.

Q: Good afternoon and thank you, Mark. Eric, I'm curious, can you give us an update on where you are in terms of licensing for gaming for the Central City, Colorado location?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Typically, it takes 12 months. We filed at the end of November 2022, so we're hoping to hear something soon. Typically, you'll get some type of preliminary deal, which allows us to then set up the casino. I'm hoping we see that in August, September. It could be as late as October.

Gaming in Colorado, it's been a very slow process, not just for us, but for all new licensees. I believe there are seven or eight licenses that are now applied for in the State of Colorado, some are much older due to various reasons on funding of the casino, things like that. I think as a publicly traded company, our funding will be super easy to explain. So, I don't think we're going to have any issues when we reach that point. It's just getting to that point.

I know that there's been some shuffling at higher levels in the Colorado gaming department and so hopefully the new people coming in are going to speed this process up a little bit. We would definitely like to see our license issued by the end of the year. We'd like to do a grand opening as a New Year's Eve party, but I think worst case, we could be looking at as late as March. Until they contact you, there's not really much we can do. Just sit and wait.

Q: Understood and thank you for that. Could you give us an update on what you're seeing in the clubs, given the current environment? I know in the past couple of quarters, there had been some weakness in a few of the blue collar clubs, but you were more than making up for that with the higher-end stuff. So any kind of update there on business would be great.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I think right now it's just inconsistencies. I don't see real trends forming up or down. I think we're just seeing more of the same. A location gets down a little bit, we make some adjustments and it goes up. Then we have another location that's down a little bit, we make some adjustments and it goes up. So it's a constant right now. It's like a shell game, where we're moving parts around, moving pieces around, and overall shooting for a set number each week. We look for the weak spots and the strong spots, and we focus on those.

Overall, though, revenues have been strong, as you've seen in this quarter. We've acquired enough new stuff, I don't think you will see any decline in revenues. The question now is, can we continue to keep the double-digit growth rates? We are looking at other club acquisitions right now that will help that, hopefully, by the time we get into the fourth quarter or definitely through 2024 and we've been priming the pump here. I think you'll see a lot of activity as we move into 2024.

Q: Great. I appreciate that. And then just one last one on the acquisition front. First, congrats on the deal closed earlier this year. What are you seeing in terms of pricing, when you talk to folks, any changes there or people kind of holding that?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

It's always been three to five times. We basically set the market. Other operators that are trying to expand don't have the capital or the cash that we're able to pull into a transaction. They definitely don't have the track record and public track records. So, I think we just stick to the plan right now. It's all about the adjusted EBITDA.

If we see trends, if numbers are trending down then we are going to forecast based on those trend numbers and can make an offer according to that. If numbers are trending up, then we will make an offer according to that. So we watch where everyone is at and what we're seeing in our markets and their market. It's pretty basic math these days for us and nothing is going to really change much.

Q: Super. Well, appreciate the additional time guys. Thank you.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you very much, Scott. Next up, we're going to bring Anthony of Sidoti and Company.

Q: Yes. Good afternoon. Thank you for taking the questions. I just wanted to follow-up about the adjustments that you said you're making in some of the clubs where you've seen some intermittent softness. Can you just expand on that as to what you're doing and then what's the common theme as for as the clubs that you have seen some softness last few quarters?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

What we'll do is increase social media, make sure our staff is working to get people into the clubs. We may run some bottle service specials on slower nights. We may do whatever we need to do to create a better value for the customers and guests that are visiting the location and doing things to put more people through the door, whether that's social media, whether that's onsite promotion.

We had huge crowds out of the Nuggets game the day before. We become more promotional. We've become more proactive on a lot of things. And if our main floor is not full, we try to fill it up, and if VIP is empty, we'll try to run some specials. We may do more shots specials, we may do more social media promotions. Things that put people through the door, that's how we fix it.

Q: Thanks for that color. And then just in terms of the second quarter here, you also cited higher labor costs at the newly acquired clubs. Do you expect to bring those costs down as a percentage of revenue now that you've had a few weeks already under the belt?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Yes, certainly. When we first take stuff over they’re a little heavy. We put some extra labor in there as well. So we've become a little heavy on labor. We move people around. If there's dead-weight, we have to get rid of the dead-weight to get the numbers where they need to be. Typically, it's a three-month to six-month process, like Denver. Denver took a lot longer. I think these locations, because they’re in Texas, will be much faster for us.

Q: Got it. Okay. And then, it was good to see Bombshells margins up sequentially. Do you still expect longer term you can get to your target range of 18% to 22% segment margins for that piece of the business?

Eric Langan – President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Absolutely. We were viewing prices through most of March. We raised most of the prices we needed to raise at the end of the March period. You didn’t see any of those price increases in that quarter. You'll see the effect of price increases in April, May, and June.

We had a couple of really big fights in April and the first week of May. NBA playoffs have been fantastic, some unbelievably close games that are bringing people out. James Harden playing in Philadelphia, there's still a lot of James Harden fans in Houston, so that's bringing people out to Bombshells in Houston to watch games. It hasn't disappointed, it's been a great series. I think next season is going to be even better, which I think will bring more people out and then we get to the playoffs. And I guess we're relying on baseball for a while and then football season will start back up.

Q: Got it. All right. Well thank you, and best of luck.

<u>Mark Moran - Chief Executive Officer, Equity Animal</u>

Thank you so much, Anthony. Next up we have Lynne Collier of Water Tower Research.

Q: Thank you and congratulations on a great quarter. I had a couple of questions around your incredible growth opportunity in Central City. The first question is, is there some reason that Central City cannot be as built out as Black Hawk? In other words, is there some sort of zoning issue that prevents it from being as big as Black Hawk from a gaming perspective, number one? And then number two, what do you envision for Central City, looking out over the next two or three, four years?

<u>Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.</u>

There's no reason Central City can't be built like Black Hawk, other than in the Historic District. But there are other gaming areas, where they can build some larger hotels like the Z Casino. I think it's a 400 and some room hotel with close to 700 gaming devices. That whole area, I think, can be developed at some point in the future. I think the biggest change is Black Hawk had much more business-friendly leadership in the city and grew their town faster.

I think what's changed as well is the gaming laws. They changed in September of 2021, which is now allowing Central City to grow. If you look, I think there are seven or eight licenses applied for in the State of Colorado, all but one is in Central City. So Central City is the next growth area for gaming in Colorado. Central City has so much charm, so much more to offer in terms of entertainment, art, and opera than Black Hawk. I really don't look at that as two competing cities, because the reality of it is they're 0.9 miles away from each other. Does the Strip and Downtown Las Vegas really compete with each other? Or do they each have their customer base? Do they cater to their own clientele?

I think that Central City and Black Hawk will be the same in that regard. They'll share some customers, of course. Sometimes, they'll go to Black Hawk and sometimes they'll go to Central City. But I think the reality is most people on most visits will end up in both towns at one point or another because they're just so close. And as they grow together, as the Gulch is developed and Black Hawk develops up towards Central City, and they develop into each other, they're just going to seem like one giant gaming area, and that's what I see over the next maybe three, five, 10 years in that market up there.

Q: That sounds great. I have one follow up question. You talked about Bombshells and the new initiatives you have that are resonating with the consumer. And you talked about pricing. But what other things are you doing from an initiatives perspective that you are doing with Bombshells?

<u>Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.</u>

The pricing was at the end of the quarter, so none of the results are from pricing. A lot of it is, I always call it, getting back to the basics. Teams get lazy or teams get complacent so we have to remind them to get back on the basics. That's getting back on social media, getting the girls on TikTok, getting the girls on Instagram, getting out there and taking the girls to promotion events, whether it's a basketball game or going to hit all the automotive car lots and bringing all the car dealers and salesmen in. Just getting out there and getting seen and getting our name out there, so that people come into the business.

Then, of course, once they're in the store, providing the best customer service we can provide, making sure that managers are touching tables and that they're making sure the guest experience is the best that it can be, so that not only do we have happy guests, but we get returning guests. That's how you build and that's how you build the margins.

Of course upselling drinks and upselling appetizers and desserts all help with margins. It's just getting everybody doing the things they're supposed to be doing. When your margins slip, it is typically those types of things that just slip by a little bit or people let go a little bit, maybe they didn't go to this game or they didn't go to that game, because they thought they were too busy. We need to make people understand that we're never too busy. We must continue to promote. We must continue to bring people into the business.

Q: Thank you so much. And after going out to Colorado, I am just amazed at what you've accomplished and you really have a true home run and congratulations. That's all from me but I appreciate the time.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you so much, Lynne, for those great questions. Next up, we're going to bring Rob McGuire of Granite Research.

Q: Congratulations on the quarter. I just have a couple of questions here. First off on Bombshells, can you get the Bombshells margins back to 18% if the Arlington on ramp, off ramp has not yet reopened?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I believe we can.

Q: Okay, great. And since the price increases went into effect this quarter, can you just give us an idea of how those have been going?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

It's too early. I don't have the numbers from that period yet.

Q: All right. Can you talk about where cash is today? What is your cash today in general?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I think $22.8 million is what we ended the quarter with, and we haven't disclosed anything after that publicly, but it is increasing.

Q: Very good. And then, if you could just look at the wages, they're a little higher in terms of wages as a percentage of overall revenues, is that something we can expect going forward? Do you think that will correct back towards the mean with the price increases you've been putting in?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I think we will continue to be in that 25% range. I think that's what we try to normally shoot for, give or take a couple of points. I don't really worry about one quarter, simply because you could have a bunch of overtime, you could have a lot of little things that affect one quarter. If we start seeing a trend up on a longer-term basis then we'll have to be much more concerned about it, but right now it's a very, very small amount of money anyway.

Q: Okay, I appreciate that. And then lastly, can you talk a little bit about the softness in nightclubs? Has the trend of the softness really been limited to blue-collar or has it continued to be contained in that segment, as you look at the business for the last six to nine months?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

In the past, yes, it's been pretty much based on blue collar. It's hard to say with April, because this April we had Easter, but last year Easter was in March and so the only weakness was the week of Easter weekend and Good Friday and of course the Monday after Easter was a little weak. I don't know if the softness was just because of that one-week period or if there is softness.

There are no trends. I'm just not seeing any trend in weakness or any trend in strength either way so we'll continue to watch. As long as we're doing our total weekly numbers, we will monitor the best locations, we'll monitor the weakest locations. We'll try to fix the weakest locations and try to make sure that's our focus and that the high locations continue to build and do the big numbers.

Q: Great. Thank you so much for your time.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you so much. Rob. Next up, we have Joe Gomes of Noble Capital Markets.

Q: Congrats on the quarter and thanks for taking my questions. So again, service revenues continue to perform nicely. Just wondering, in your mind, Eric, is that something that you think can just continue or do you think that at some point in time they start to level out?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

They're going to find a top at some point, but I think they're going to continue to be in these ranges. I think at the highest peak of the business, we were doing 42% or 43% service revenues, so we're still below those peaks. But we do have more Bombshells nowadays than we had back then. So I think they're an ongoing trend. We'll keep watching and as certain markets do better with the higher service revenues like New York, we can see service revenues increase, but the reality is they're going to fluctuate.

For example, Miami, this weekend was insane. Formula 1 racing, big UFC fights, and then you had the big boxing event, so there were a lot of things driving traffic. When there's that much traffic on the floor, of course that drives VIP, because customers want the private areas, which drastically increases our service revenue. It really depends, as we move forward, how many events and those types of things that we have in a quarter, you will see higher service revenues. If there are not a bunch of events in the quarter, we could see a little bit lower service revenues.

Overall, I'm much more concerned with monitoring our total revenues, and our total revenue numbers are beating our internal goals for April and through May so far. I'm very, very happy to see those numbers being beaten. I thought they were pretty optimistic numbers to begin with and the fact that we set goals at the clubs and are beating those numbers, I'm excited about it.

We are going to get some major comps. Like I said, April last year had no Easter, so we did have a very strong April last year. I think April was our strongest month of the year last year. And I want to try to figure out why. I know it can't just be Easter, there must have been some major sporting events and some other things in that month as well.

We started out the first week of May with a very, very strong week. F-1 and the NBA games have been fantastic for us. You've got Phoenix, Miami, New York, Denver, all teams that definitely help our revenues right now are in the playoffs. We can't lose in the Miami-New York game because either one of those are great. I think we're leaning towards Denver. We have more clubs in Denver than we do in Phoenix, so I'd love to see Denver advance because I think that will be more revenue for us. We're watching those games close. And with James Harden, a lot of Houston fans for James Harden still, and so I think that if the Sixers continue to advance that will help our business as well. Three of the four series are great for us.

Q: Excellent. Now, I think at the end of the first quarter, you had talked about reopening the Galveston Heartbreakers and the Jaguars in San Antonio. Just wondering how they were performing in the past couple of months?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Both have continued to see improvements. Heartbreakers just had a couple of record weeks, so we're very excited that location is continuing to get better and better for us. The real thing now is to get the Baby Dolls in Fort Worth reopened, which should open by mid-June, I think at the latest. We probably could have opened a week earlier, but we decided we wanted to do things right and so there were some electrical and heating/air conditioning issues. We had to add additional power to the building, which added about four to six weeks to the process, but there's no sense in opening in June or July or August and having huge problems because we can't cool the building.

That's all being worked on right now. Our Lubbock Jaguars location is under construction. They've got the steel up, they're closing the building, the parking lot's poured, so that location will come online soon, as well as the former Pin Ups location that we bought in Fort Worth, Texas. They will start construction, probably in the next 90 days, on that property. We have three more clubs coming up.

Q: Great. And then one more for me, if I may, I know you have that $200 million goal of investment for each year over the next couple of years. I think at the end of the first quarter, we were around $110 million. Are you still confident you'll be able to get that other, let's call it, $90 million invested over the remainder of this fiscal year?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

We're certainly going to try. We've got to find the right deals. We've got a lot of construction going on. We're in the process of four bank loans right now for various construction and property, so hopefully those will all come through. We're getting rates between, I think, 6.8% to 7.25%, so rates are not horrible yet. We're going to try to lock in what we can lock in and get these other construction projects going.

Some of the construction projects we're doing in cash, like the Jaguars in Lubbock, are all cash. At our Stafford location, we've basically paid all cash for the construction there. So we've got multiple properties that we could turn around and cash out of at some point in the next six months if the Fed stops and the rates come back down.

If we start seeing a 6% rate again, I would look for us to do a cash out of probably around $20 million to $25 million. That would give us a nice chunk of cash going forward, which will make it easier to hit that $200 million mark. Right now, I'm not seeing anything that's standing in our way from us making those investments other than we must find the right deals. I'm not doing deals to do deals. I'm only doing deals if they meet our requirements and we get the cash-on-cash returns that I see versus buying back our stock.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you so much, Joe, for those questions. Before we bring up our next questionnaire, I'd like to encourage everyone to re-tweet and share this space. If you have a question to ask, please raise your hand and we would bring you up as a speaker. Next up, we have Jason Scheurer of Orchard Wealth.

Q: Good quarter. My big thing that I wanted to get some clarity on is you guys obviously keep acquiring the real estate in these prime areas, Texas, Florida, and also Colorado. Do you have any idea what the underlying property values that you've been buying have accumulated by? How much in those respective counties is commercial property going up year after year, which you don't record on your balance sheet, as those properties move up?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

We're not allowed to take step-up basis. We have cost basis accounting under GAAP. But I would guess in certain markets, there's always people out trying to buy your properties. Anybody that owns property knows your phone rings off the hook, 'I want to buy your house,' 'I want to buy this.' We get those calls on a regular basis, we've gotten some offers. We bought Tootsie's property, 2015 maybe, for $15 million. I've got an unwritten offer, verbal over the phone, would I take $24 million for it. Of course I laughed. I was like, 'If you add a zero, we can sit down and talk. We own the club.' 'Oh, we thought you could just move that tenant.' 'No, we are the tenant.'

I think we have about $250 million plus in real estate, last time I did everything. We have $100 million written on the sheet, I think about $120 million some in real estate debt on slide 14.

Q: I keep looking at the fact that your borrowing cost on this real estate that you've had over the years, it seems to be growing at least equal to what you're paying out in interest on these properties.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Probably, easily. Our weighted interest rate now on our real estate is only 5.41%. Our overall is 6.52%, but our real estate finance is a little over a point cheaper. So that's highly possible. A lot of this real estate that we bought, we've done some pretty major improvements to the properties as well, so that never hurts with the value.

Q: And then about what percentage of the entire business do you own real estate and what percentage is leased?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Bradley and I just did this the other day -- 85% or 83% owned and 15% to 17% leased. The only reason we have so much leased now is because of the restaurants and the Lowrie acquisition. It's pretty close to 85% and 15%, I believe.

The new locations that we're getting ready to open like Rowlett and Lubbock, Austin, Texas; Florida, Colorado; Downtown Denver, Colorado -- all those locations are owned. As more locations open, the percentage of owned properties are going to go up versus leased properties. We haven't added any leased properties recently. Not that we won't. If we find the right location and if we can lease them cheaper than we can buy it, then we may tend to lease. It really depends on how much capital we have to put into the location as well.

Q: At the new casino location, when that goes in, you're going to have a steakhouse and you will have a club in there. Are there any other clubs in that area?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

There are the five clubs we own, which are about an average of about 45 minutes away.

Q: Okay. So the idea being is if somebody is on vacation and I've got a bunch of guys then we'll head up there and we're looking for something, you are the only game in town when it comes to that?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I'm about the only game in town for you to eat after 11:00 PM at night up there, other than 24x7 at Monarch. It's amazing to me, because it's a gaming town, all you can do is gamble. In summer, there are some things to do, but in the winter their numbers die down. You've got the opera, you've got a lot of art galleries in Central City. But for Black Hawk, other than the new distillery area that they're opening, and the casinos, they barely have lounge acts. I saw some ads for this summer, they're bringing in some lounge acts. I was like, wow, finally a live band of some kind, something. Because literally, there is no entertainment in that marketplace right now, and that's what was so exciting to me.

We can take Central City and turn it into the Fremont Street of Vegas with all the entertainment. The strip is 0.9 miles away and has zero entertainment. Come 11 o'clock at night, midnight, you're on a table and you're not doing very good, you're not feeling it, you've got two choices -- you drive back to Denver or you go to bed in your hotel room. Nothing else to do out there.

I'm going to give you a third option. ‘Hey, let's go see the girls at Rick's.’ As we continue to look at properties out there, we may build a nightclub of some kind. Other things to create an entertainment zone for the thousands of people, especially Thursday, Friday, and Saturday, that are out there and gaming. If you’re winning, you want to stop and go do something else; if you're losing, you want to stop and do something else. I want to give them those other options. And if you want to game still, you still can, which I think will be a big part of our deal. You may come to the casino to gamble and end up seeing an entertainer and ending up in VIP. You may come to see the entertainers, end up in VIP, and then decide, hey, let's go play blackjack for a while.

So I think there's going to be a lot of synergies between the two businesses. I know it hasn't been tried before, and I know I'm going to have a learning curve. But the beauty of it is both businesses are so profitable that I'm still going to be paid very, very well while I'm working through my learning curve. That's what you see in our analysis. We said the first year, let's say we only do half the money, we only do three point some odd million. It takes us the full year to learn and get to the point where in the second year, we earn the $7.5 million zone, and we're still a 50% cash-on-cash return on this investment.

I haven't seen anything that's excited me like this since 2004 when I bought Rick's Cabaret on 33rd Street in Manhattan. That was a bigger company deal at that time. We did $6.7 million of total revenue the year before. Then we paid $7.6 million for a single club, and within four days of owning, I tore it down. There was nothing left, but three brick walls, and then we spent $3.8 million rebuilding it, which was an unbelievable amount of money for us at that time, but that's what created the RCI we see today. I think the Central City property for a very small investment of $10 million has the chance of taking this company to a whole different level than where it is today.

Q: On a different pivot, when you take over clubs over the last five years or so, when you take over the business, what's the RICK's premium that you guys are able to squeeze out on average from what they were doing numbers-wise to what you think like in a year, year-and-a-half of you being there, you can get it up to? Is it like 15% improvement, it's 20% improvement?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Typically, about 20%. I think we're at 17.4% on the trailing 12 months through December 31st. I know through December 31st or maybe that was through March 31st, we were up 17% or 18%. I think 20% is a pretty good number for us. We tend to increase revenues and EBITDA by about 20%.

Q: So when you're purchasing the clubs for three times to five times, it is three times to five times their numbers, but then you come in and you're finding another 20% on top of that, which obviously lowers your acquisition costs, but you don't realize that until a few years later?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

Typically, that's what we're seeing. Sometimes we see it in the first year, sometimes we see it right away. When we bought Tootsie's in 2007, we bought $18.8 million in revenue and they were doing $8.8 million in EBITDA. We paid $25 million for it. In the first year we did $23.8 million in revenue and $11.4 million in EBITDA.

Denver probably would have been pretty immediate, had we not been coming out of COVID. There were employees to hire because they'd only been open for four weeks in Denver when we bought it. Some of the other clubs had been open a little bit longer, but they were in markets that all opened late COVID. There were a lot of issues we had to work through, so it took us almost six months to realize and see the gain there.

Q: When you showed us the universe of the 2,200 total clubs that are out there, give or take, what percentage of them are owners that have, let's say four or more clubs? When you go to the industry events, I seem to run into people that own like six, four, five. Sometimes you know there's a bunch of ones and twos, but it seems a lot of the participants at these club events are usually the guys that own multiple clubs.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I think EXPO is definitely a lot of multi-club owners and I think it's anywhere from 2 to 25 that these guys own. Of course you've got a couple of the big boys that own lots of clubs like us, but there's not very many of those. I think only one other club owns the same number or probably more clubs than we do. Most of them are smaller, between 4 and 10 clubs is an average.

There's plenty of people out there for us to purchase clubs from. There are a lot of one-offs that we can do throughout time. The key is running them.

We just made a major acquisition. People are worried about Bombshells, and one single location in the last acquisition does more annual EBITDA than all the Bombshells combined. Why don't we focus on the important stuff, which is the clubs? Everything else is just bonus ways for us to come up with the money, build additional free cash flow, and put money to work, while we're waiting for the next club acquisition.

Our Director of Operations for RCI Management Services is in Dallas right now. He is working on getting the new club out. His team is putting the teams together, putting our POS systems in, getting our culture ingrained in the acquisition, in the clubs that we acquired and that takes time. It's a three-month to six-month process.

People say well, can you go buy something else? I could probably go buy something else right now, but why stretch our management team? Our pace has increased over time because our ability to manage them has increased over time. As our ability to manage and absorb more acquisitions increases, we'll make more acquisitions. In the meantime, it's nice to have a couple of other things to put our cash flow into and keep the machine running.

Q: Great. Thanks.

Mark Moran - Chief Executive Officer, Equity Animal

Thank you so much for those questions. Next up, we're going to bring up Adam Wyden of ADW Capital, the largest institutional shareholder of RCI Hospitality Holdings, Inc.

Q: On the steakhouse and casino, you guys talked about conservatively taking two years to get from $3.7 million to $7.4 million. I know your slot revenue anticipation is less than half in Black Hawk, which is really conservative, so if you can match Black Hawk, that's a lot more EBITDA, it is probably another $4 million. But can you talk a little bit about the table games? I know there's also supposed to be a steakhouse there, you're talking about digital sports betting, but also potentially in-house sports betting. It might be helpful to give the other layers, to outline the other buckets and how big they could be.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I'm not making any guess on any of those other revenue sources at this time, because I just don't know. I think the steakhouse is actually part of the club revenues. So the only thing you really have that we didn’t include is table games, which we have no clue on at this point. We’ve got some preliminary numbers. You can go to the Colorado Department of Gaming website, you can download every casino’s numbers, you can download our combined casinos’ numbers, you can download by city. You guys can go look at all those things yourself and put together models. I am not sharing my models at this time, I think it's way too premature for that.

As far as the sports betting goes, an online sports betting group partners with a casino for their skin and those range anywhere from about $7.5 million to $10 million over 10 years on a contract revenue share basis with minimum payments. We are not including any of that at this time. We don't have a signed contract at this time with any other group. We have been negotiating with groups and I think within 30 days after our license is issued, we will have a full time partner. That'll be immediate income as well.

I don't want to speculate on where we're going to be or what that revenue is going to be at this time. I just showed you that if I make zero off of all those other things, I make 50% a year for two years. That's anticipating that I am going to be so behind the learning curve that I'm only going to do 50% of the revenue in the first year that we anticipate. I think it's a conservative number.

I don't need to go out on a limb. I don't need to say we're going to make $20 million or $15 million or anything else to justify the investment. I wouldn't even be trying to justify the investment, but I have a lot of calls and a lot of people saying ‘Why are you doing this’ and I wanted to put out there why we're doing it. This is our take. This is our map. This is the way we see it happening. If we can make 50% cash-on-cash returns, I’m not going to invest when I have the certainty of an investment like this. The backup with table games and with online sports betting and an actual sportsbook on the premises as well. I can make my 50% returns that easily.

Q: That was my point, that you beat the crap out of the numbers and still do a 50% cash on cash. Those are the best types of investments, where everything goes to hell in a handbasket and you make 50%. I was just trying to lay out the other buckets for folks, so they understand that if you execute on this, like you've done on other things, there's a lot of upside, but that's helpful.

<u>Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.</u>

I'll give you a little color on slots, for example. Central City is $129 a day. I think the Black Hawk average is about $100 more and something a day. If you take your top casinos over there, they are running over $400 something a day. So if we can come in somewhere between $129 and $300 in the middle of that zone, that means millions of more dollars.

I think there's a lot of uniqueness to our project. I believe that with our properties in Denver, our properties around the country, we will be able to market a lot of packages to not only our employees and entertainers and our guests of our existing clubs around the country, but they'll bring friends. This will become a very unique market for us.

Q: Got it. I don't know if anyone has asked about M&A. I know you're digesting Burch and you did Lowrie. Have you commented at all about these little clubs that you're renovating and repurposing so the ramp up of those or any of the other smaller M&A opportunities and what that looks like?

<u>Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.</u>

We've talked about the three properties that we have in various stages of construction right now. That will probably all be opened in 2024. We’ve talked about free cash flow generation on slide 23. That's how much cash we have. We're still looking to invest $200 million a year. We’re showing where this cash is going to come from. We talked about the bank loans that we're still able to get on our real estate, how we have about $20 million, $25 million in cash out that we can do if interest rates drop back under 6%. We'd probably immediately cash that real estate out on new real estate loans. All the pieces are in place. We just have to continue to do what we do.

Q: I noticed that you updated your buyback slide for different fiscal year '24 ranges with free cash flow. Obviously, these are on the consensus numbers, I suspect not where you think you are, but it gives people a band of outcomes in terms of where the buyback is. Looking forward to hopefully seeing some of that as well. But I'll hop back into the queue and if I have more questions, I'll raise my hand.

Mark Moran - Chief Executive Officer, Equity Animal

Thanks so much for the questions, Adam. Next, Stagflation Season from Twitter.

Q: Thank you, Mark, and congratulations to Eric, Bradley, and the RCI team for a great quarter. As a frequent customer, I wanted to ask you guys the following question, which is, what systems do you guys have in place to ensure club quality stays consistent as expansion continues to grow?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

We just put our system in. We put our culture in. If you follow @Reardon_Dean1, that's our Vice President of Operations. He posts all the parties. He takes the teams to lunches and dinners and posted the DJ meeting the other day, where we had a big MMA star as a surprise speaker on the call. Those are the things we do. We build our culture, and our culture keeps everything else in line, because people want to be a part of it.

Q: Thank you.

Mark Moran - Chief Executive Officer, Equity Animal

I have a question that was submitted anonymously so I'd like to encourage anyone who has questions, who is listening, who would like to ask them, that you can go to the form, at the top of this space and type them in, they'll be relayed to me or you can DM me. This question is, Eric, what's the go-to-market strategy for you guys to expand into sports betting in an already crowded sportsbook app market. What is the main product differentiation?

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

The beauty for us is, it's not our product. We're being paid a minimum fee to use our license in the State of Colorado. You've got to remember, sports betting may be crowded in certain markets. In other markets, it's not as crowded because you have to have a license in that state in order to take bets. Currently in the State of Colorado, there are only 31 possibilities, maybe 21 or 24, I can't remember the number, I'm sure you can find it on the Colorado gaming department's website on how many of those licenses they actually are using a skin. They call it skinning.

When you bet on, say, Bet on Sports on PENN Play, you're actually betting through the Ameristar casino in Black Hawk, Colorado. You're on their license; everything is done through their license through the skin of Bet on Sports. That gives you an idea. There's still plenty of those gaming companies. All those gaming companies aren't licensed in the state of Colorado and any that aren't licensed could reach out to us, because we have two skins at this point that should be available sometime around the first year. So, in fact, I am going to go to a gaming convention tomorrow afternoon and market those skins as well.

Mark Moran - Chief Executive Officer, Equity Animal

Thanks. And with that we are going to be concluding our Q&A session. For those who joined us late, you can meet management tonight at 7 o'clock at Rick's Cabaret New York, one of RCI's top revenue-generating clubs. Rick's is located at 50 West 33rd Street between Fifth Avenue and Broadway, a little in from Herald Square. If you haven't RSVPed already, you can ask for Eric Langan or me at the door. After 9:00 PM, however, I will be busy implementing my own capital allocation strategy. I'm going to pass off to Eric to say one more thing, but on behalf of all of us at the company and our subsidiaries, thank you so much. Now, Eric with the last word.

Eric Langan - President & Chief Executive Officer, RCI Hospitality Holdings, Inc.

I just want to shout out to Antonio Brown, who brought the camels and the goats to Houston at the visit with me for a couple of days. And thank them personally for inviting me to their barbecue, at their meet and greet. It was a great event. I had so much fun, and I look forward to next year's meet and greet, the camels in Denver, where I plan to host you guys again and hopefully, we set up some other companies for you guys to visit while you are out there, so you're not just learning about us. Thanks again for inviting me and sharing your time.

And with that, I thank everyone for your time today. Look forward to another great quarter, as we move forward and hope to talk to everyone again soon. Thanks.