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Accel Entertainment, Inc. (ACEL)

Q1 2022 Earnings Call

CORPORATE PARTICIPANTS

Derek Harmer

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Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

OTHER PARTICIPANTS

Chad Beynon

Analyst, Macquarie Capital (USA), Inc.

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

Steven Pizzella

Analyst, Deutsche Bank Securities, Inc.

Greg Gibas

Analyst, Northland Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. Thank you for attending today's Accel Entertainment Q1 2022 Earnings Call. My name is Tamiya and I will be your moderator for today's call. All lines will be muted during the presentation portion of the call with an opportunity for questions and answers at the end. [Operator Instructions] I will now like to pass the conference over to our host, Derek Harmen (sic) [Harmer] (00:00:32), General Counsel and Chief Compliance Officer. Please go ahead.

Derek Harmer

General Counsel and Chief Compliance Officer, Accel Entertainment, Inc.

Welcome to Accel Entertainment's first quarter 2022 earnings call. Participating on the call today are Andy Rubenstein, Accel's Chief Executive Officer; and Mat Ellis, Accel's Chief Financial Officer. Please refer to our website for the press release and supplemental information that will be discussed on this call. Today's call is being recorded and will be available on our website under Events & Presentations within the Investor Relations section of our website.

Some of the comments in today's call may constitute forward-looking statements within the meaning of the Private Securities Reform Act of 1995. These forward-looking statements are subject to risks and uncertainties, including those relating to COVID-19 and its variant strains. Actual results may differ materially from those discussed today and the company undertakes no obligation to update these statements, unless required by law.

For a more detailed discussion of these and other risk factors, investors should review the Forward-Looking Statements section of the earnings press release available on our website, as well as other risk factor disclosures in our filings with the SEC.

During the call, we may discuss certain non-GAAP financial measures. For reconciliations of the non-GAAP measures, as well as other information regarding these measures, please refer to our earnings release and other materials in the Investor Relations section of our website.

I will now turn the call over to Andy.

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Thanks, Derek, and good morning, everyone. Thank you for joining us for Accel's first quarter earnings call. Before we dive in, I would like to thank Brian Carroll for his hard work and dedication over the last eight years as our Chief Financial Officer. We would not be the company we are today without him. I would also like to congratulate Mat Ellis on his promotion to succeed Brian. Mat has played an integral role in our transformation into a public company and we're confident he is the right person to lead our finance organization as we continue to expand into new markets.

Turning to the quarter, I'm pleased to report we had another strong quarter despite the impact of Omicron. We reported revenue of \$197 million with year-over-year same-store sales growth of 3%.

When you think about the Omicron headwinds we experienced this quarter versus the fourth round of stimulus checks going out in March of 2021, the year-over-year growth we achieved further demonstrates the strength and resilience of our business. In the current inflationary environment, the cost of virtually everything is increasing. For example, it costs more to eat, travel, shop and commute. Our offering, however, has not increased in price, and our players usually live less than 15 minutes from our locations.

We believe local businesses will continue to invest in gaming due to the incremental profits they receive, and players will continue to choose our local, price-stable, high quality offering due to its appeal and convenience.

Looking at our number of locations, this is the first quarter where our number of locations dropped due to a change in regulatory practices. While we usually see an increase in closures after the holidays, the reason for this decrease is due to the IGB's recent enforcement of the 72-hour rule. The rule requires terminal operators to disconnect and remove their equipment from a location if there is no activity for 72 hours. In the past, we could leave our equipment if a location was temporarily closed for repairs, remodeling or an ownership change.

In addition, if a location went out of business, we could remove our equipment at our convenience. The 72-hour rule accelerated all planned removals for the next several months. As a result, we removed our equipment from approximately 30 locations totaling 150 VGTs. We view the drop as one-time in nature, and we expect to resume our normal growth trend going forward. More importantly, this change has almost no impact on our revenue.

On the expense side, just like most other businesses, we experienced higher-than-expected costs from COVID-related and macroeconomic-related impacts, such as increased expenses for overtime, fuel and parts. We're continually monitoring our spend and looking for ways to mitigate increased costs without sacrificing our best-in-class service. Our asset-light business model will allow us to quickly adjust to any further changes in the market.

Turning to Century. We believe we are on track to close at the end of May. Century continues to outperform our original estimates, and we're looking forward to combining the best practices of both companies. We plan to share more about Century at our next earnings call after the acquisition closes.

Sticking with M&A, our pipeline remains active and we are evaluating multiple opportunities in Illinois and across the country. Our long-term goal is to continue to increase the percentage of our revenue generated outside of Illinois. Century is the first step towards achieving our goal, and we hope to announce additional opportunities in the future.

On the organic front, our sales team continues to sign additional competitor in organic locations. For the first quarter, Accel was awarded 67 new licenses, or 35% of the total new licenses awarded. Our ability to continually win more licenses than our current market share is a strong testament to our sales capabilities, brand awareness and location owners believing in the Accel difference. When we look at the number of eligible businesses without gaming or the number of VGTs per capita, we believe Illinois still has a significant amount of highly visible growth.

Looking at other states, we remain cautiously optimistic that several states will consider distributed gaming in the future. We continue to work with the various stakeholders to educate them about the benefits of distributed gaming and the incremental revenues it generates for state and local governments, and small businesses alike. We are confident the growth playbook we built in Illinois can be replicated in any future market, and our leadership position nationally will create advantages for us.

Overall Accel is in a very strong position to capitalize on the future. Our hyper-local business model, low capital requirements and highly visible growth offers one of the best returns in gaming.

With that, I'd like to turn it over to Mat to walk you through the numbers in more detail.

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Thanks, Andy, and good morning, everyone. I've had the opportunity to connect with many of you on today's call and I look forward to continuing that relationship in my new role going forward.

For the first quarter, we had total revenue of \$197 million and adjusted EBITDA of \$35 million, year-over-year increases of 34% and 37% respectively. As a reminder, gaming was shut down for the first 18 days of January 2021. Location hold per day for the first quarter was \$811, a year-over-year increase of 3%. Considering the Omicron headwinds, perceived pent-up demand we experienced in the first quarter of 2021, as well as the fourth round of stimulus checks issued in March 2021, we believe 3% year-over-year growth further reinforces the strength of our business. As a reminder, the 3% growth only accounts for the days we were open in 2021, so it's an apples-to-apples comparison.

CapEx for the first quarter was \$7 million cash spent. As of March 31, we had 13,663 VGTs in 2,565 locations, year-over-year increases of 7% and 4% respectively. Location attrition continues to remain low and mirrored the pre-COVID historical averages. During the quarter, we removed 150 of our VGTs in 30 locations due to the 72-hour rule. As Andy mentioned earlier, we think of the drop as one-time in nature. When businesses shut down, we naturally remove our equipment at the appropriate time, but the 72-hour rule effectively accelerated our planned removals for the next several months. Going forward, we expect to resume our normal growth trend.

At the end of March, our average residual contract length was approximately seven years, a modest increase from last quarter. Our ability to increase this figure is a true testament to the strong and long-lasting relationships we built with our location partners.

I'd now like to provide an update on our share repurchase program. As you're all aware, we announced a \$200-million share repurchase program in November of 2021 as we find the opportunity to return capital to shareholders in the form of buybacks and attractive use of our significant free cash flow.

During the quarter, we purchased \$14 million of Accel's stock at an average purchase price of \$12.79 per share. In April, we purchased an additional \$6 million of Accel's stock at an average purchase price of \$12.17 per share. Given our relatively under-levered balance sheet and strong free cash flow, we are in a position to make exciting investments like Century, while thoughtfully continuing to return capital to shareholders. At the end of the fourth quarter, we had approximately \$147 million of net debt and \$745 million of liquidity, consisting of \$195 million of cash on our balance sheet and \$550 million of availability on our credit facility.

Turning to Outlook. As Andy mentioned earlier, demand in our revenue continues to be strong and consistent with our guidance despite Omicron. Q2 is also off to a promising start. That being said, like almost every other business, we are seeing somewhat higher expenses due to inflationary pressures and the tight labor market, the extents to which were not known to us back in November. Given this and the pending Century closing at the end of next month, we anticipate updating guidance at our next call.

Back to you, Andy.

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Thanks, Mat. We are pleased with our performance this quarter and even more excited for what the future holds. We can't wait to officially welcome the Century team to the Accel family, and we continue to focus on additional growth opportunities. We remain confident that our asset-light hyper-local business model creates a platform to outperform in difficult times and really thrive under normal circumstances, as demonstrated by our continued performance.

We aim to leverage our proven business model and extremely strong financial position to continue our expansion and return capital to shareholders. We've gone from operating in one state we went public in November of 2019, to 9 states after we closed Century.

Our success would not be possible without our dedicated employees and loyal customers. They are the true competitive advantages of our business and make Accel the preferred choice in our market.

We will now take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question is from the line of Chad Beynon (sic) [Beynon] (00:12:40) with Macquarie. Your line is open.

Chad Beynon

Analyst, Macquarie Capital (USA), Inc.

Hi. Good afternoon. Thanks for taking my question. Wanted to start with a high-level one. I know in the past, at the Investor Day, you talked about the difference between you and other land-based properties and the reward system. What we've been hearing from a lot of the operators is they're really pulling back on reinvestment rates, and I was wondering if this could be a potential positive for you guys, understanding that it's not in the near-term outlook, but, if this is something that could help you re-engage with some players that left, or reengage with players who just haven't frequented your locations, particularly in Illinois? Thanks.

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Thanks, Chad. Yeah, I mean, we have seen that benefit in the recent periods where we're developing relationships with players that we had not seen before, and they have recognized that our offering and our convenience is far superior to what they were – what they are receiving currently from the original brick-and-mortar offerings. And so, with a better product and the convenience, we continue to see the increase in player account, as well as a lot of new people, that basically didn't realize that our offering is very comparable to the brick-and-mortar business.

Chad Beynon

Analyst, Macquarie Capital (USA), Inc.

Thanks. And then, in terms of M&A, Andy, you mentioned in your prepared remarks that the pipeline remains active and you continue to look to diversify outside of Illinois. How does the changing of interest rates kind of affect how fast you could potentially do some more deals, given the cost of capital difference? Thank you.

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Hey, Chad, it's Mat. I can answer this one. I think the first thing to think about is we actually took some steps to protect against an increase in inflation rates. We took out a \$300-million four-year deferred premium cap, which protects us if LIBOR goes above 2%. The other piece of that obviously is we have relatively low rates on our facility and we'll look to continue to protect, but given our availability and that we raised that facility last year, I think, if anything, it puts us in a good position to get M&A done because we have the financing in place.

Chad Beynon

Analyst, Macquarie Capital (USA), Inc.

Thank you both very much and congrats on the appointment, Mat.

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Thanks, Chad.

Operator: Thank you, Mr. Beynon. The next question is from Steve Pizzella with Deutsche Bank. Your line is open.

Steven Pizzella

Analyst, Deutsche Bank Securities, Inc.

Hey, guys. Thanks for taking my question. I think Andy mentioned higher-than-expected costs due to COVID in his prepared remarks. Can you just kind of elaborate on those costs and do you expect those to fall off at all?

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Hey, Steve, it's Mat again. So, I think a lot of those costs are related again not to the business specific, but what we're seeing with the overall economy, particularly overtime, fuel and parts, when we look at it sort of just stepping back in terms of guide and everything, we now look at the company sort of on a combined basis and first and foremost, the revenue is remaining strong.

When you think about Omicron this year and sort of last year's stimulus checks, that 3% growth really reinforces the strength of the business. We've always sort of said that those 2021 levels are here to stay, and I think as the results come in, we continue to reinforce that. April and March are always two of the key months of the year and between March and as we said, Q2 is off to a promising start, we're pretty pleased with what we're seeing.

You know, kind of pooling it all back together to expenses, when we think about it in terms of guide, we're looking at things [ph] that are on a (00:16:57) combined basis and what I would say is that the increase in expenses has pushed us sort of to the bottom of that kind of pro forma combined guide. Obviously, we'll look for ways to mitigate those expenses, but many of these are sort of what everyone is dealing with throughout the economy.

Steven Pizzella

Analyst, Deutsche Bank Securities, Inc.

Okay. I appreciate it. Thanks. And then can you just talk us through what you saw in April, kind of relative to March, and are you able to delineate if you're seeing any degradation from kind of the lower-end consumer?

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

So, I would say as you remember, we – Player Rewards! is not live in Illinois, so we can't kind of track at the player level. We do look obviously per machine per day. The strength is still there. April was going to be a challenging month just given what was happening last year, but it came out very well. You'll obviously get the results from the IGB – or the numbers from the IGB in about a week or so.

Overall, you know, I think with everything going on, our offering remains very attractive. It's close to home, it's convenient, and as Andy mentioned earlier, it's a high-quality offering on par with some of the other options out there.

Steven Pizzella

Analyst, Deutsche Bank Securities, Inc.

Okay. I appreciate it. Thanks, guys.

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

Sure. Thank you.

A

Operator: Thank you, Mr. Pizzella. The next question is from Stephen Grambling with Goldman Sachs. Your line is open.

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

Hey, there. Maybe just following up on the macro question, I guess, has anything changed as you think about the relationship of the macro and some of the inflationary pressures, particularly as it relates to fuel on a location-by-location basis?

Q

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

You know, when you think about it that way, I would say again, what we're more focused on is the revenue in the play is stronger. Of course, fuel hits us, we have vehicles out on the road. I think that's hitting everyone, but when you think about our players and fuel, our locations are less than 15 minutes away. Fuel is not going to be a decision on whether they kind of go to one of our nearby establishments.

A

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Yeah. And if I build on that, they're more likely to go local than to a destination regional casino where they're driving 45 minutes to 1.5 hours. And the fuel actually in many situations is – the fuel increase in pricing is somewhat beneficial.

A

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

That's helpful. Then maybe if you can just give us a follow up or an update on some of the new market expansion, what you see out there. Are there any other new states that you've got your eye on that you could potentially expand into? Thank you.

Q

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Yeah. Unfortunately, the spring legislative sessions were not as productive as we hoped. We're seeing an opportunity of – to continue to expand the pilot that we're involved in, in Georgia and – so, I think we'll get some more locations involved in that pilot. The other states, I mean, there is a chance that legislation get passed. It's not looking that promising. And we continue to investigate and pursue some of the legacy states and hopefully, Century is the beginning of those efforts.

A

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

Awesome. Thanks. I'll jump back in the queue.

Q

Operator: Thank you, Mr. Grambling. [Operator Instructions] The next question is from Greg Gibas with Northland Securities. Your line is open.

Greg Gibas

Analyst, Northland Securities, Inc.

Q

Hey, Andy and Mat, thanks for taking the questions, and Mat, congrats on the new role. I guess, just wanted to confirm, you talk about seeing no impact from the decline in those – I guess the removal of those 30 locations. No impact on revenue. Is that essentially because they're just inactive locations?

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

A

That's exactly it. I mean, this is more of a change in methodology than anything. We've always reported the number of locations in VGTs by what the central system tells us. We're not going to make adjustments to that and those locations that are being disconnected were not generating revenue. So, it's – there's no real change on the revenue. It's just really we look at it as a change in methodology.

Greg Gibas

Analyst, Northland Securities, Inc.

Q

Got it. Thanks for confirming. And when I guess you think about expectations for new location license issuances from the IGB, maybe this year versus last, any thoughts there on how that might trend?

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

A

I think it's too soon to tell. I mean, where our focus is, is continuing to sign high-quality locations and get them into the backlog. I think the IGB is working hard to work through their queues to get stuff licensed. But, from our standpoint, it's let's sign high-quality locations and get them into the queue. A little too soon to tell on what sort of the ongoing licensing pace will be.

Greg Gibas

Analyst, Northland Securities, Inc.

Q

Got it. And I know you talked about readdressing guidance in Q2 after the Century acquisition closes. Are you withdrawing the current guidance, or just kind of waiting for that acquisition to close at the end of this month?

Mathew Ellis

Chief Financial Officer, Accel Entertainment, Inc.

A

I would say we've left it unchanged and waiting to provide an update next month after – or next quarter, excuse me, after Century is closed.

Greg Gibas

Analyst, Northland Securities, Inc.

Q

Okay. Sure. I guess last one for me, you know, you talked about eyeing a few other opportunities both within Illinois and other markets. What type of multiples do you maybe expect to pay on those future M&A opportunities?

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

It's a – it's a range and it really depends on the length of the contract, the nature of the leadership of that – that business and the opportunity for growth. So, traditionally, we're targeting around the [ph] \$7-ish million (00:23:52) range, but it all depends on the actual business.

Greg Gibas

Analyst, Northland Securities, Inc.

Okay. Appreciate it.



Operator: There are no additional questions waiting at this time. I will now turn the conference over to Andy for any concluding remarks.

Andrew H. Rubenstein

President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Yes. Thank you. I just wanted to thank everyone for joining us today. We have a very bright summer ahead of us, a lot of exciting things happening, and we look forward to updating you with a lot of good news the next time we get together. So, thank you for joining us and have a nice weekend.

Operator: That concludes the Accel Entertainment Q1 2022 Earnings Call. Thank you for your participation. You may now disconnect your lines.

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