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Accel Entertainment, Inc. (ACEL)

Q2 2020 Earnings Call

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CORPORATE PARTICIPANTS

Mathew Ellis
Senior Vice President-Corporate Strategy, Accel Entertainment, Inc.

Brian Carroll
Chief Financial Officer, Accel Entertainment, Inc.

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

OTHER PARTICIPANTS

John DeCree
Analyst, Union Gaming Research LLC

Greg Gibas
Analyst, Northland Securities, Inc.

Stephen Grambling
Analyst, Goldman Sachs & Co. LLC

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the Accel Entertainment Q2 2020 Earnings Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

I would like to now hand the conference over to Brian Carroll (sic) [Mathew Ellis] (00:35). Please go ahead.

Mathew Ellis

Senior Vice President-Corporate Strategy, Accel Entertainment, Inc.

Welcome to Accel Entertainment's second quarter 2020 earnings call. Participating on the call today are Andy Rubenstein, Accel's Chief Executive Officer; and Brian Carroll, 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 and Presentations within the Investor Relations section of our website.

Some of the comments on 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 and the current health conditions. 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.

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During the call, we may discuss certain non-GAAP financial measures. For a 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 Mr. Andy Rubenstein.

Andrew H. Rubenstein

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

Thanks, Matt. Good morning, everyone. Thank you for joining us for Accel's second quarter 2020 earnings call. It was a very quiet quarter due to the statewide shutdown, but we have seen strong results since video gaming relaunched.

As a reminder, on March 16, the Illinois Gaming Board shut down all video gaming terminals across the State of Illinois. In late June, the IGB announced gaming would relaunch on July 1 and issued protocols requiring one of the following actions: VGTs to be spaced 6-feet apart, or dividers to be installed between VGTs, or if options 1 and 2 cannot be achieved, disable the VGT.

Once again, the Accel team went above and beyond preparing for relaunch, and we are pleased to report that we had a successful first month. We brought back most of our employees a little more than a week before our locations could reopen. And on day one, more than 80% of locations were live and by day three, more than 90% of locations were live. In addition, less than 3% of our VGTs were disabled due to the IGB protocols. More importantly, our players were also excited for gaming to resume and July gaming revenue was near our pre-COVID-19 budget.

During the shutdown, our team did an excellent job in maintaining close contact with our business partners to not just understand how we would work with them to implement the new guidelines, but also to help support them in these unprecedented times. We are encouraged by both the recent performance and the limited number of our locations that have closed due to the pandemic.

Recent policy decisions in Illinois have also given us confidence that we should be able to avoid a similar statewide shutdown. On July 15, Governor Pritzker further divided Illinois from 4 regions to 11 regions. We have analyzed the regions and determined no region has more than 20% of Accel's gaming revenue.

It's also important to note, Chicago, a municipality that prohibits video gaming and has been more impacted by COVID-19 than rest of the state, is a separate region. We will continue to work with the Governor's office, the IGB, the local municipalities and our establishment partners to follow the latest COVID-19 ordinances and guidance.

During the second quarter, we also announced that we had agreed to acquire Tom's Amusements, a Southeast amusement operator and Master Licensee in the State of Georgia, led by Emily Dunn. The acquisition closed on July 22, and our teams have been busy integrating the companies and working with Emily to grow her brand.

This is an important milestone to our vision of expanding nationally. The Georgia market is large and underpenetrated, and we believe that the Accel playbook will help us grow the market and allow us to take significant share. We are encouraged by other discussions that additional state expansion may occur even faster than we had previously anticipated.

Finally, on June 16, we announced the redemption of all public warrants to purchase shares of our common stock for a redemption exchange rate of 0.25 shares of common stock per public warrant. We followed this

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announcement several weeks later with an exchange offer to the private warrant holders with the same redemption exchange rate.

94% of the private warrant holders, including myself, and all members of our Board of Directors signed an agreement indicating they would participate in the exchange offer. The redemption and exchange offers were made to simplify the company's capital structure and reduce the potential dilutive impact of the company's warrants.

Unfortunately, with operations suspended, we recorded minimal revenue and adjusted EBITDA loss of $9 million for the second quarter. However, the strengths of our business model are reflected in these results as we were able to quickly adapt and ensure the long-term prosperity for Accel. Our balance sheet remains strong with net debt of approximately $220 million and total liquidity of $199 million. We emerged from the shutdown in a strong position and look to continue executing our growth plans.

With that, I'm going to turn it over to Brian Carroll, our CFO, to walk you through the second quarter results in more detail. And then we will open it up for questions.

Brian Carroll

Chief Financial Officer, Accel Entertainment, Inc.

Thank you, Andy. As of June 30, we had 11,108 VGTs in 2,335 locations. Year-over-year increases of 33% and 37%, respectively, and that is probably the right metric to focus on for our growth potential.

The small decrease in locations in VGTs from the prior quarter was primarily due to lower performing locations closing their business due to the impact of COVID-19 as well as the IGB not having two meetings, thus delaying the normal addition of locations.

At the end of June, our average residual contract length was approximately 6.8 years, and on a standalone basis, excluding Grand River, our residual contract length was approximately seven years. With re-launch, we've been able to resume upgrading Grand River's equipment and expect that these improvements will increase the hold per day of these locations.

We have installed more than 556 VGTs and expect to install a total of 1,000 by year-end. To-date, approximately 8% of our game titles have been updated to higher bet limits.

The majority of our VGTs will be receiving additional updates for the remaining game titles during the second half of this year. Of the updates, approximately 50% of our VGTs will require an on-site update, which we began this week and expect to complete by year-end.

We had total revenue for the second quarter of $0.4 million due to the statewide shutdown and an adjusted EBITDA loss of $9 million. CapEx remained limited with approximately $0.3 million cash spend in the second quarter compared to $5 million in the second quarter of 2018. Given the pandemic, we deferred purchases, and more importantly, we were able to work with major vendors to defer payments until operations resumed.

At the end of the second quarter, we had approximately $220 million of net debt, and $199 million of liquidity, consisting of $149 million of unrestricted cash and $50 million of revolver availability. We are in full compliance with all our bank covenants.

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And earlier this week, we executed an amendment to our credit facility, which provides covenant relief through Q1 of 2021 to ensure we have adequate flexibility in the current environment. While this was not necessarily needed, this amendment provides us with the flexibility to continue operating sensibly without the overhang of the shutdown.

Back to you, Andy.

Andrew H. Rubenstein

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

Thank you, Brian. With one of the toughest quarters in our company's history behind us, I'm pleased to be focused on continuing our mission to be the leader in route gaming. I have been extremely proud of how the Accel team has responded to the current environment and continue to provide the same great customer service that we have been known for.

We will now take your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of [indiscernible] (11:09) from S&P Global. Your line is now open. Your first question comes from the line of [indiscernible] (11:21) from S&P Global. Your line is now open.

Our next question comes from the line of John G. DeCree from Union. Your line is now open.

John DeCree

Analyst, Union Gaming Research LLC

Q

Good morning. Good afternoon, everyone. Thanks for taking the questions. I had a couple, I guess, kind of housekeeping items first, Andy. So you mentioned by day three, about 90% of your locations were live. I was curious if you could talk about the balance in the other 10%. What your expectations are there? Are those eventually going to come back online? Have some closed? And just broadly speaking, what is the outlook for those remaining locations?

Andrew H. Rubenstein

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

A

Thanks, John. As far as the remaining balance, we have experienced a continual growth toward probably 90 – the mid-90s, low to mid-90s locations that are now open. There are some that have closed, and every day, one or two are trickling in as not reopening.

Our expectation is as some of the locations weren't quite ready to open initially or wanted to wait and see how the recovery in the hospitality industry would occur kind of postponed or open. We're seeing, at the same time, a couple open every day.

So, although we don't have a target number of where we think the ultimate percentage will be, I think we're slowly kind of migrating up into the mid-90s. And our expectation is that there will be some that don't ever open as we see these closures occurring every day.

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John DeCree
Analyst, Union Gaming Research LLC

Q

As a follow-up to that, Andy, and it maybe a little premature as everyone's still just getting reopening and under social distance and protocols. But, have you had any conversations with locations that have previously not considered adding VGTs to their location as an additional source of revenue, and I would say outlook for kind of new openings or new locations in the state that might come online as they look for maybe new revenue sources given the kind of dining business has been so disruptive?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

Our sales team had some pretty good traction in July with new opportunities. And I think we'll continue to see that occur throughout the rest of the year. I would caveat – by the caveat that there are – the expectation is that there will not be as many new businesses opening up in the next six to nine months, until we see some certainty or more certainty on how the pandemic is going to be controlled and whether there's a vaccine that will be implemented later in the year.

So there have been a few businesses that have decided to add VGTs. We've seen a couple situations where one business closed and a new person takes over the business. And I think that will continue throughout the third and the fourth quarter and into the first quarter. But I don't expect a significant increase in the rate of new business openings occurring over the next six to nine months due to market uncertainty for those small business owners.

John DeCree
Analyst, Union Gaming Research LLC

Q

Yes. That's great. And if I could sneak one last one in, on your view for revenue per day, so far hold per day. It's early, but we've heard a lot of talks about the benefits of stimulus checks and expanding unemployment. Wondering if you have a sense on how the trend of kind of coin into the machines is going, if it's been relatively consistent since you've reopened or if you've seen some volatility there? And that's it for me. I'll hop back into the queue. Thanks, Andy.

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

Yeah. Thanks, John. The – I would – there has been some consistency. We haven't seen a lot of volatility. And the stimulus and the unemployment does provide a little bit of a lift, I think. The greater impact that we're seeing is that people are not using their disposable income for travel and other types of entertainment, and therefore, normally, July and August are months where there is a lot of travel and there is more of a kind of a drop in our business, I think that's making up for some of the shortfalls in the fact that there are people that are reluctant to go out into public. A lot of our players are older, and they still are cautious.

And the other thing that's – as we stated earlier, there is not as many of the establishments in our portfolio that are open as opposed to what would be a normal time period. So I think the balance of the lack of options or alternative entertainment is balancing out some of the negatives.

John DeCree
Analyst, Union Gaming Research LLC

Q

Thanks for all the additional color.

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Operator: [Operator Instructions] Our next question comes from the line of Stephen Grambling from Goldman Sachs. Your line is now open.

Stephen Grambling
Analyst, Goldman Sachs & Co. LLC

Q

Hi. Thanks for taking the questions. Maybe looking towards Georgia, what have you learned since the deal closed? And how do you think about the growth rate potential in that region?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

Thanks for the question, Stephen. The – it's really, really early for us to give any kind of real perspective on it. And I wouldn't anticipate any near-term growth as the current market has some challenges that we're trying to understand. So Georgia is one that we have little near-term expectation, and we're in more of a learning phase and as well as an integration mode.

Stephen Grambling
Analyst, Goldman Sachs & Co. LLC

Q

And then whether it's in Illinois or otherwise, I guess, are you hearing or seeing any kind of operator distress that could create opportunities for their consolidation, either in Illinois or otherwise?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

I would say that we haven't really seen distress. We've seen people interested in partnering with us, and that's always a theme in our business. As far as the operators that kind of are looking for kind of a transition, there's definitely interest, and I wouldn't put it any greater than normal, but we're continuing conversations with a lot of the different operators and opportunities that we've seen over the last year or so, and I think that will continue going forward into the fourth quarter and early next year. And as far as distress, I don't think we've seen that explicitly in the marketplace.

Stephen Grambling
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thanks so much.

Operator: Your next question comes from the line of [indiscernible] (20:08) from S&P Global. Your line is now open.

Greg Gibas
Analyst, Northland Securities, Inc.

Q

Yeah. I'm guessing this is me. Can you hear me, okay?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

Yes.

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Greg Gibas
Analyst, Northland Securities, Inc.

Q

Okay. This is Greg Gibas from Northland. So must have had the wrong name in there at some point. So sorry about that. Sorry about the confusion. But we're just hoping to follow-up on a few things. First, I guess, a little bit more color on how July has trended from a hold per day perspective, maybe relative to pre-COVID times? Is there anything you can share there?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

Yeah. Thanks, Greg. The July numbers, as I mentioned earlier, were pretty strong considering what we were coming out of. And the fact that we didn't have as much of our inventory of locations operating. So the hold per day was consistent with where we thought our business would be in our projections pre-COVID, maybe slightly below because of a lot of the locations not being open. But I think, like as I said, the lack of entertainment alternatives and people staying closer to home, were very advantageous for us in terms of performance.

Greg Gibas
Analyst, Northland Securities, Inc.

Q

Sure. That makes sense. And then, I guess, could you – I think you already provided this on the call, but what percentage have been updated with the new betting limits? And then also the percentage of locations that had their 6 VGT installed at this point?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

So the – as far as the betting limits are concerned, we have installed in the IGT portfolio, the basic software upgrade that was provided through the system update pretty much throughout the portfolio. That was only a few games, not the entire portfolio of games on each machine. The rest of that portfolio has not been updated. As it was just recently released, we're in the process of doing that. So on a given machine only, call it, 10% to 15% of the games has the higher bet limits and the bigger jackpots. We'll see that on the IGT portfolio increase pretty rapidly over the next six to eight weeks.

The Sci Games software is very different and that needs to be loaded on to each individual machine by visiting location. You can't do it through the central system. So very, very few have experienced that upgrade. And the expectation is, it will take some time probably into the fourth quarter before those machines all get upgraded.

So it's a process. I don't think we've gotten anywhere close to a critical mass on that upgrade and probably we'll give you better insight at the end of the third quarter. Then what's the second part of your question?

Greg Gibas
Analyst, Northland Securities, Inc.

Q

It was the percentage that have had their 6 VGT installed?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

So I think we're probably in a – somewhere between 25% to 35% that will accomplish by the end of the third quarter. I mean, it's a very dynamic number that obviously increases every day. And you'll see that lift as you

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monitor the amount of machines every month – the monthly report that comes out from the IGB, you'll see our numbers increase.

Greg Gibas
Analyst, Northland Securities, Inc.

Q

Okay. Got it. That's helpful, Andy. And I guess the last one from me. Just to be a follow-up on the general health of your establishment partners, I know you already said that on day three, they were 90% open again, which is pretty good. I guess I would just ask, how many do you think will maybe permanently go out of business? I imagine you're pretty close with their health, maybe day-to-day or at least month-to-month. And then maybe with respect to the pace of new licenses being issued from the IGB, I mean, how do you think that will be impacted by the shut down?

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

A

The total amount of locations that won't come back is obviously a guess. What we saw during the pandemic was a lighter amount of business closures than normal. And I think that's attributed to the fact that a lot of the locations were receiving government support, so they stayed open while they were – they refused – they didn't declare their closure during that time in order to receive the government support. So on a normal basis, we lose, call it, 7 to 10 locations that are closing every month, just in the course of our normal business. That was a light – we experienced a lighter number in the pandemic period of closure.

We're now starting to see slightly accelerated as some of those locations are making declaration that they're not reopening. I think we'll see that impact probably through the first quarter of 2021 as locations will make the effort of trying to reopen and see how the business goes. Usually, January is a high closure month as businesses want to get through to the holidays kind of as a last draw. And so I think you'll see a higher-than-normal closure rate beginning, let's say, this month through probably the end of February.

Greg Gibas
Analyst, Northland Securities, Inc.

Q

Okay. Got it. Thank you.

Operator: There are no further questions at this time. I will turn the call back over to Andy Rubenstein.

Andrew H. Rubenstein
President, Chief Executive Officer & Director, Accel Entertainment, Inc.

Okay. Well, thank you, everyone, for joining the call. We look forward to continuing to help our small business partners reopen their business, just in fact to survive in this period, because obviously, they are restrained in the ability to serve indoors. And fortunately, this is occurring during a warmer weather period that a lot of them are expanded their outdoor service. And so the gaming has helped supplement that revenue. And we look forward to updating you after the third quarter with kind of continual growth. And hopefully, everyone stays healthy and safe and wears their masks, because that is essential to the support of a lot of these small businesses. So thank you for taking the time, and we look forward to talking to you in a few months.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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