



Luckin Coffee, Inc.
Q1 2023 Earnings Conference Call
Transcript

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PARTICIPANTS

Jinyi Guo *Chairman and CEO, Luckin Coffee*

An Jing *CFO, Luckin Coffee*

Alicia Guo *Investor Relations Director, Luckin Coffee*

PRESENTATION

Operator

Ladies and gentlemen, welcome to Luckin Coffee's first quarter 2023 earnings conference call. All participants will be in listen-only mode during management's prepared remarks, and there will be a question-and-answer session to follow. Today's conference is being recorded.

At this time, I would like to turn the call over to Ms. Alicia Guo, the head of Investor Relations of Luckin Coffee, for prepared remarks and introductions. Please go ahead, Alicia.

Alicia Guo

Investor Relations Director, Luckin Coffee

Hello, everyone, and thank you for joining us on today's call. Luckin Coffee announced its first quarter 2023 financial results earlier today.

Today, you will hear from Dr. Guo Jinyi, Chairman and CEO of Luckin Coffee, and Ms. An Jing, CFO of Luckin Coffee. After the Company's prepared remarks, the management team will conduct a question-and-answer session based on questions submitted via the Company's webcast.

We will be referring to a slide presentation on today's call, which can be found via a conference call webcast link as well as on the Company's IR website. The IR website link is investor.lkcoffee.com.

During today's call, the Company will be making some forward-looking statements regarding future events and results. Statements that are not historical facts including, but not limited to statements about the Company's beliefs and expectations are forward-looking statements. Forward-looking statements involve inherent risks and uncertainties. Further information regarding these and other risks is included in the company's filings with the SEC.

With respect to any non-GAAP measures discussed during the call today, the accompanying reconciliation information related to those measures can be found in the earnings press release issued earlier.

During today's call, Dr. Guo will speak in Chinese, and his comments will be translated into English.

Now I would like to turn the call over to Dr. Guo Jinyi, Chairman and CEO of Luckin Coffee. Dr. Guo, please go ahead.

Jinyi Guo

Chairman and CEO, Luckin Coffee

(Translated) Hello everyone, welcome to today's earnings conference call, and thank you for your continued support of Luckin Coffee. I am Luckin's Chairman and CEO, Guo Jinyi.

In the first quarter of this year, with the adjustment of pandemic prevention and control measures, the restaurant industry recovered rapidly, and market competition gradually intensified. Despite the very competitive environment, we still achieved rapid growth in both revenue and profit, with the numbers of stores and customer reaching record highs. By the beginning of April this year, the second anniversary of the launch of Coconut Latte, sales of our Coconut Latte have surpassed 300 million cups, making it a well-deserved "Innovative Consumer Product of the Year". Our strong performance in 2022 and the first quarter of this year is a testament to the effectiveness and resilience of our business model, the efficiency and growth potential that comes with scale, as well as our consistent product quality and high brand recognition. In the future, we are determined to expand our market share and prove to the market that we have strong and efficient operational capabilities. To achieve our strategic goal of increasing market share, we will accelerate the pace of store openings, launch more "delicious and affordable" products, and give back to consumers with higher quality products, more convenient services and friendlier prices. We will adhere to the principles of healthy and sustainable development of our business, maintain a long-term perspective, stay grounded, and build a world-class coffee brand.

Looking at the numbers, the first quarter not only sustained the good growth momentum from the previous quarters, but the outstanding performance also demonstrated the scale advantage of our business. In particular, total net revenue increased by 84.5% year-on-year to RMB 4.4 billion, with a GAAP operating profit margin of 15.3%. The self-operated store profit margin was 25.2%, and the same-store sales growth rate was 29.6%. Additionally, there were 1,137 net new store openings, bringing the total number

of stores to 9,351, and the cumulative number of customers reached 150 million. The number of average monthly transacting customers was 29.49 million.

CFO An Jing will provide further details on the financials later.

In 2023, we will seek to strengthen and systematically implement sustainable development across our entire business, building on the foundation of our sustainable development breakthrough from "zero" to "one". We aim to pursue long-term value, actively take on social responsibilities, and promote the healthy development of the industry. While we continue to promote the establishment of a sound sustainable development management framework and mechanism, we will comprehensively carry out the formulation of sustainable development strategies and objectives.

In the first quarter, we officially started to take carbon inventory of our entire business. In order to ensure the efficient and effective implementation of the related work, our Sustainable Development Committee has established a subcommittee on climate change and carbon neutrality, which is responsible for the overall planning of our company's carbon peaking and carbon neutrality, as well as the identification and control of climate change risks and opportunities. Under the leadership of the subcommittee, we have established working groups that focus on the key areas of our business, which will help us develop a comprehensive plan for achieving carbon neutrality that is both scientifically sound and can be effectively implemented.

Our corporate vision is to "create a world-class coffee brand and making Luckin Coffee a part of people's daily lives". At the end of March this year, Luckin Coffee opened two new stores in Singapore, which are in the trial stage. The two stores are located in the fashionable and trendy area of Singapore and have already been widely praised by young consumers since their opening.

The launch of Luckin Coffee's Singapore stores is an important first step in our expansion into international markets and is the starting point of our internationalization strategy. By establishing a presence in Singapore, we aim to fine-tune our entire IT and operation system and test our business model in the overseas markets. Our goal is to make Luckin Coffee's high-quality coffee accessible to consumers worldwide, by leveraging our brand's professional, youthful, fashion, and healthy image and our new retail coffee business model.

In terms of brand, we continue to enhance our brand identity by positioning ourselves as "professional, young, fashion, and healthy," which has been successful in attracting new customers. As of the first quarter, our cumulative transacting customers reached 150 million, and the number of average monthly transacting customers has reached 29.49 million, which is double the figure from the previous year. In March, the number of Luckin Coffee's transacting customers exceeded 30 million, a record high.

In terms of products, we are not only focused on creating innovative and popular beverages but also on strengthening our professional capabilities in research and development, supply chain management, and expansion. In the first quarter, our BILUOCHUN Flavored Newer Latte sold 4.47 million cups in its first week, and our Minty coconut latte, launched in April, sold over 6.66 million cups in the first week, generating over 240 million in revenue.

We are also committed to increasing our investment to produce high-quality coffee. In March, we launched the "Global Coffee Bean Search Plan," led by Anthony Douglas, the 2022 World Barista Championship champion, and ten certified Q-Grader Luckin R&D personnel. Their mission is to explore high-quality coffee beans for Luckin Coffee consumers in the world's six major high-quality coffee-producing regions.

As of the end of the first quarter, we remain the largest coffee chain in China in terms of the number of stores, and we aim to continue to grow at a rapid pace. We had 9,349 stores in 240 cities, with 1,135 net new store openings in the first quarter. As competition in the coffee market in China intensifies, we will continue to expand our presence in high-tier cities and accelerate our penetration in new markets through our partnership model.

We will also continue to invest in our supply chain to maintain our competitive edge. Following the official groundbreaking of the Luckin Jiangsu roastery last December, the Yunnan Baoshan green bean processing plant will break ground at the end of this year. Our investment in the supply chain has created higher barriers to entry and deeper moats, and also allowed us to optimize our costs.

These are the key highlights of our performance in the first quarter. Next, we invite CFO An Jing to present the financial data and commentary.

An Jing

CFO, Luckin Coffee

Thank you very much, Jinyi

Good morning, afternoon, and evening everyone. Thank you for joining us today. Our team has delivered a stellar quarter, and I am excited to share our results, but first, I want to recognize our hardworking employees, loyal customers, partners and investors for their support. Without you, our rapid growth would not be possible, so thank you.

Before I begin my financial remarks, I would also like to point out changes to the definitions of certain metrics that will be mentioned today. First, delivery fees derived from self-operated stores paid by our customers has been added to revenues from self-

operated stores, on top of the previously included revenue items. Second, commissions to third-party platforms related to self-operated revenues has been deducted from store level operating profit of self-operated stores, in addition to the previously reported deductions of cost items. Please note that the historical comparative metrics have been adjusted to reflect these definition changes.

Now, I will take some time to highlight our 2023 first quarter results in detail.

Let me begin with a high-level overview of the quarter. Our exceptional first quarter results were not only a product of our team's hard work, but also propelled by the net positive economic factors. During the first quarter of 2023, although there were some indications of uncertainty in the macroeconomy, we benefitted from the positive trends in China. We have also seen a clear rebound in consumer spending with the lifting of COVID restrictions in China, which encouraged consumption as people across the country gradually returned to their pre-COVID routines. We believe that China's strong economic fundamentals and supportive policies provide a favorable backdrop for our business operations, and we look forward to continued success in the Chinese coffee market. As for Luckin in particular, business has improved both quarter over quarter and year over year, and we continue to see a positive trajectory. Since the start of February, we were pleased to see consumption trends bounce back to a more normalized level, and our store operation rate has recovered to pre-COVID levels.

In addition to the supportive macro factors, Luckin's store and menu expansion has driven strong results, and we are delighted to report that our business demonstrated robust growth and improved profitability in Q1 2023.

We reported a record-high first quarter with RMB4.4 billion of net revenues, an increase of 84.5% compared to the same period of last year. If we take a closer look, we see growth across all our revenue streams. Following the updated definition as mentioned above, net revenues of our self-operated stores reported 74.9% YoY growth with a SSSG for self-operated stores of 29.6%; meanwhile, our partnership revenues grew by 106.7% in the first quarter and currently amounts to 25.6% of our total net revenues.

We have also enhanced our profitability and recorded an operating profit margin of 15.3%, compared to 0.7% in the first quarter of 2022, a result of the team's efforts to improve our profitability structure, through quickly expanding scale to meet the growing market needs while efficiently controlling costs.

Our team also made excellent progress in customer engagement during the quarter, with the lifting of Covid restrictions and consumer confidence increased, achieving year-on-year growth in average monthly transacting customers of 84.6%, an increase from 16.0 million in Q1 2022 to 29.5 million in Q1 2023.

We are very confident in the excellence of our products, as well as the strength of our business strategy, which has clearly produced results for our stakeholders. Across various market cycles, we have proven the robustness of our business model and our capacity to withstand difficult circumstances. At the same time, we are excited by the momentum of our growth and expansion, which continues to persist.

To meet the continued demand for our products, in the first quarter, we had 1,135 net new store openings, covering 240 cities in China and two new stores opened in Singapore. Moreover, as discussed above, our store operation rate has normalized with recovering consumer demand. We now have a footprint of more than 9,300 stores as of March 31, 2023, which provides us with significant benefits of scale. This has resulted in an enhanced profitability structure and increased revenue and operating margin.

In terms of store mix, we opened 658 net new self-operated stores this quarter, including two stores in Singapore. For our partnership stores, we opened 479 net new stores and entered into more areas in the lower-tier cities. As of March 31, 2023, we had more than 6,300 self-operated stores and over 3,000 partnership stores.

Our expansion plans are strategic and aimed at increasing our presence, brand awareness, revenue, and efficiencies of scale. Our strategy is to increase store density in tier 1 and 2 cities while rapidly penetrating lower tier cities, to further improve store coverage and better meet consumer needs. We are pleased to see the steady execution of our expansion strategy unfolding as it continues to contribute to the building of value for all our stakeholders.

I would like to take some time now to discuss the details of our improved profit profile. Our reported overall operating margin in Q1 was 15.3%, a significant increase when compared to 0.7% in Q1 of prior year, mainly driven by strong business growth and improved efficiency from cost controls, technology-driven operations as well as enhanced benefits of scale. Also, I would like to point out that by leveraging our operation efficiency, our operating expenses as a percentage of net revenues decreased to 84.7% in the first quarter of 2023 from 99.3% in the same quarter of 2022. In addition, our achievements in scale, costs, and efficiency trickled down to our bottom line, and we are pleased to report that our net margin achieved double digits in the first quarter at 12.7%.

Following the updated definition as mentioned above, store level operating profit margin of self-operated stores maintained its growth momentum and reached 25.2% in the quarter compared to 18.5% in the same period of last year. We believe the improvements were primarily driven by our active approach to new product launches, store expansion, and operation efficiency, which are really the three largest buckets that

are moving the needle in how we expect to further improve the margin in the coming years.

For partnership stores, as mentioned in previous quarters, we don't disclose any metrics on profitability. However, as illustrated in the ER issued earlier today, revenue contribution from partnership stores increased 106.7% year-over-year to RMB1,135.4 million during the quarter.

In addition, we are glad that our overhead expense ratio continued to be more efficient and resilient during the quarter.

Our general and administrative expenses, on an absolute value basis, increased by 11.7% year-over-year, which was mainly a result of the increase in payroll costs for headquarter staff, tax surcharges, R&D investments in IT initiatives, and expenditures for office supplies, while partially being offset by the decrease of share-based compensation for restricted share units and options issued to management and employees. The G&A expense as a percentage of revenue decreased from 13.3% in Q1 last year to 8.1% this quarter.

The sales and marketing expense ratio was stable at 4.5% this quarter, while the absolute value increased 84.0% year-on-year. We continued to spend more on strategic branding investments through various channels, more on subcontract service fees to support our e-commerce business as well as on commissions to third-party delivery platforms which are in-line with the increase in the number of delivery orders.

Expenses related to the previously reported fabricated transactions and related restructuring amounted to 0.1% of net revenue in the first quarter of 2023, compared to 1.6% of net revenue in Q1 of the prior year. This is largely due to the successfully completion of our provisional liquidation in March of 2022 and overseas investor litigation settlements that are near completion. We believe the expenses related to the previously reported fabricated transactions will continue to diminish.

During the first quarter, we experienced positive operating cash flow of RMB1,072.6 million, compared to RMB107.7 million in the same quarter of 2022.

In terms of our balance sheet, we now have no interest-bearing debt and our cash position remains very strong with about RMB4.4 billion of cash and cash equivalents, restricted cash and short-term investments, which is around USD638.7 million as of March 31, 2023. We have a healthy balance sheet and we will regularly evaluate our liquidity requirements to ensure that we can meet our business needs and further optimize our capital structure.

I'll now turn it over to Jinyi for concluding remarks followed by Q&A.

Jinyi Guo

Chairman and CEO, Luckin Coffee

(Translated) The outstanding achievements of Luckin Coffee today are only possible with the love of our customers, the support of our partners, and the trust of our investors. We express our heartfelt gratitude to all of you! We will continue to deliver better quality and better prices and provide you with coffee that is "delicious and affordable". We will continue to focus on the long-term value of our brand and strive to make Luckin Coffee a world class and centennial brand with enduring prosperity, and we work towards achieving long-term, healthy, high-speed, and sustainable growth.

Thank you. Now, we would like to open the floor to questions.

QUESTIONS AND ANSWERS

Operator

Ladies and gentlemen, we will now begin the Q&A session. I will turn the call over to Alicia Guo at Luckin Coffee who will moderate today's Q&A session.

Alicia Guo

Investor Relations Director, Luckin Coffee

Thank you. Now, let's begin with the first question.

How does the company perceive the competition in the Chinese coffee market and what actions does it plan to take in response?

Jinyi Guo

Chairman and CEO, Luckin Coffee

(Translated) Thank you for your questions.

Over the past three years, the Chinese coffee market has seen rapid growth, leading to intense competition among brands. We welcome this competition as it brings vitality to the market and offers consumers more choices, leading to a higher market growth

potential. At the same time, we plan to vigorously compete by focusing on customer value and providing competitive prices.

We have established significant scale and cost advantages through years of effort. This has allowed us to maintain a reasonable profit margins while offering competitive prices and cup volumes that are difficult for other brands to match. We are confident about our ability to beat the competition.

We recently launched a "RMB9.9 store celebration event" for some stores to continue to improve customer acquisition and operation capabilities through innovative marketing activities. The event also serves as a way to give back to the large number of consumers who have supported and loved Luckin Coffee over the years. The participating stores have seen a significant increase in overall cup volume and revenue, benefitting more consumers. We plan to continue this event in the long term to further drive the growth of the coffee market in China. And it is also an important embodiment of putting consumers first.

Alicia Guo

Investor Relations Director, Luckin Coffee

Thank you, Dr Guo. Let's move on to the next question.

Congratulations on the solid first quarter results. We noticed that in this quarter, the Company's operating profit margin achieved double digits again. Could you please share more color on this? What are key drivers behind this?

An Jing

CFO, Luckin Coffee

Thank you for the question.

As I have mentioned before, our OP margin achieved a record high of 15.3% and our store level operating profit margin of self-operated stores maintained its growth momentum and reached 25.2%. I believe there are three key drivers:

First, with the lifting of restrictions and the gradual recovery of the economy, we saw incremental sales from our expansion of stores and menu. In the first quarter, we opened over 1,000 net new stores and launched 24 SKUs. Our average monthly transacting customers reached about 30 million. In this quarter, the newly launched BILUOCHUN Flavored Newer Latte has sold 4.4 million cups within the first week since

launch. All the above achievements contributed to our total sales, meanwhile, enhancing our branding power and facilitating our sustainable growth.

Second, in addition to sales growth, our OP margin also benefited from the improved efficiency from cost controls and technology-driven operations. We were glad to see our technology-driven operation success reflected in our G&A operating leverage ratio at this quarter. The G&A expense as a percentage of revenue decreased to 8.1% this quarter from 13.3% in Q1 last year.

Lastly, the decrease of expenses related to the previously fabricated transactions and related restructuring. This expense decreased to RMB5.9 million, or 0.1% of net revenue in this quarter, compared to RMB37 million or 1.6% of net revenue in Q1 of the prior year. This is largely due to the successful completion of the debt restructuring and near completion of overseas investor litigation settlements.

In the future, we will continue to expand our stores and menu, meanwhile, continuing to invest in the technology-driven operations to enhance our operating efficiency. As coffee becomes a daily ritual for more and more Chinese customers, we are confident that we will continue to experience the benefits of our expanding scales, the strengthening awareness of our brand, and the advantages of our operating leverage.

Alicia Guo

Investor Relations Director, Luckin Coffee

Thank you, Ms. An. The next question is:

Could you please update the company's store opening targets for 2023 and comment on the pace of future store openings?

Jinyi Guo

Chairman and CEO, Luckin Coffee

(Translated) Thank you for your question.

Currently, it appears that our goal of opening 10,000 stores will be achieved in the first half of this year. This will make Luckin Coffee the first coffee chain brand in China to exceed 10,000 stores. Over the past three years, we have built a leading digital site selection and store expansion management system. After systematic analysis and assessment, we believe that there are still many potential locations that meet our site selection criteria in both first and second-tier cities, as well as lower-tier cities. The market space is far from saturated, and with the acceleration of coffee consumption in

China, the space for opening stores is still expanding. We are confident in the future expansion of our store network. We will closely monitor market changes, maintain a strong competitive pace of store openings, and continuously improve Luckin Coffee's store coverage density to better meet consumer demand.

Alicia Guo

Investor Relations Director, Luckin Coffee

Thank you, Dr. Guo and Ms. An. That is all the time we have for today's earnings conference call. We thank you for your participation on today's call. We look forward to providing you with regular business updates and look forward to speaking with you again next quarter.

Operator

This concludes our call today. You may now disconnect.

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