

Papa John's Reports Second Quarter Earnings

2008-08-06

Domestic comps increase 2.4%, 2008 earnings guidance reaffirmed

Highlights

Second quarter earnings per diluted share of \$0.27 in 2008 vs. \$0.23 in 2007

Comparable second quarter results, excluding the consolidation of BIBP, were \$0.41 in 2008 vs. \$0.40 in 2007, an increase of 2.5%

Domestic system-wide comparable sales increase of 2.4% for the quarter

32 net Papa John's worldwide unit openings during the quarter

Earnings guidance for 2008 reaffirmed at a range of \$1.68 to \$1.76 per diluted share, excluding the impact of consolidating BIBP

Papa John's International, Inc. (NASDAQ: PZZA) announced revenues of \$283.4 million for the second quarter of 2008, representing an increase of 10.6% from revenues of \$256.3 million for the same period in 2007. Net income for the second quarter of 2008 was \$7.6 million, or \$0.27 per diluted share (including an after-tax loss of \$4.1 million, or \$0.14 per diluted share, from the consolidation of the results of the franchisee-owned cheese purchasing company, BIBP Commodities, Inc. ('BIBP'), a variable interest entity), compared to 2007 second quarter net income of \$7.0 million, or \$0.23 per diluted share (including a net loss of approximately \$5.3 million, or \$0.17 per diluted share, from the consolidation of BIBP).

Revenues were \$572.4 million for the six months ended June 29, 2008, representing an increase of 10.7% from revenues of \$516.9 million for the same period in 2007. Net income for the six months ended June 29, 2008 was \$16.3 million, or \$0.57 per diluted share (including a net loss of \$9.3 million, or \$0.32 per diluted share, from the consolidation of BIBP), compared to last year's net income of \$20.2 million, or \$0.66 per diluted share (including an after-tax loss of \$5.5 million, or \$0.18 per diluted share, from the consolidation of BIBP).

"Given the brutal commodity and consumer environment, our second quarter comps were very encouraging and our earnings and cash flow yield remained strong," said Papa John's president and chief executive officer, Nigel Travis. "As the commodities market and operating environment remain both difficult and unpredictable, we will continue to look for ways to assist both our corporate and franchise operators through this difficult period while driving top line sales."

Revenues Comparison

Revenues were \$283.4 million for the second quarter of 2008, an increase of \$27.2 million, or 10.6%, over the corresponding 2007 period. The increase in revenues for the second quarter of 2008 was principally due to the following:

Domestic company-owned restaurant revenues increased \$14.2 million or 11.9%, reflecting an increase in comparable sales results of 3.6% and an 8.3% increase in equivalent units due to the acquisition of 42 domestic restaurants during the last six months of 2007.

Franchise royalties increased \$1.0 million, primarily due to the increase in royalty rate from 4.0% to 4.25% for the majority of domestic franchise restaurants effective at the beginning of 2008.

Domestic commissaries revenues increased \$10.1 million due to increases in the price of certain commodities, primarily cheese and wheat. The commissary charges a fixed dollar mark-up on its cost of cheese, and cheese cost is based upon the 40 lb. cheddar block price, which increased from \$1.38 per pound in the second quarter of 2007 to \$1.75 per pound in the second quarter of 2008, or a 26.8% increase. The cost of wheat, as measured on domestic commodity markets, has increased more than 100% for the first six months of 2008, as compared to the corresponding 2007 period.

International revenues increased \$2.4 million reflecting the increase in both the number and average unit volumes of our company-owned and franchised restaurants over the past year.

For the six-month period ending June 29, 2008, revenues increased \$55.5 million, or 10.7%, principally due to the reasons mentioned above and due to a first quarter increase in other sales from expanded commercial volumes at our print and promotions subsidiary, Preferred Marketing Solutions, Inc.

Operating Results and Cash Flow

Operating Results

Our pre-tax income for the second quarter of 2008 was \$12.2 million, compared to \$11.1 million for the corresponding period in 2007. For the six months ended June 29, 2008, pre-tax income was \$25.8 million compared to \$31.8 million for the corresponding period of 2007. Excluding the impact of the consolidation of BIBP, second quarter 2008 pre-tax income was \$18.5 million, a decrease of \$900,000 or 4.5%, from the 2007 comparable results of \$19.4 million and pre-tax income for the

six months ended June 29, 2008 was \$40.0 million, a decrease of \$400,000, or 1.1%, from the 2007 comparable results. An analysis of the changes in pre-tax income for the three- and six-month periods ended June 29, 2008, respectively (excluding the consolidation of BIBP), are summarized as follows (analyzed on a segment basis -- see the Summary Financial Data table that follows for the reconciliation of segment income to consolidated income below):

Domestic Company-owned Restaurant Segment. Domestic company-owned restaurants' operating income decreased \$400,000 and \$800,000 for the three- and six-month periods ended June 29, 2008, respectively. The second quarter of 2007 included a \$600,000 pre-tax gain associated with the termination of a lease agreement. Excluding the \$600,000 gain associated with this termination, operating income increased \$200,000 in the three-month period ended June 29, 2008. The six-month 2008 operating results included a \$1.2 million loss on the anticipated sale of company-owned restaurants (see further discussion in the Refranchising Initiative Update section below) and the costs associated with the closing of five restaurants during the first quarter of 2008, compared to a loss of approximately \$100,000 in the prior year. Excluding both the incremental \$1.1 million loss associated with the disposition of restaurants and the prior year gain on lease termination noted above, domestic company-owned restaurants' operating income improved approximately \$900,000 in the six-month period ended June 29, 2008 as compared to the same period in 2007. This improvement in operating results is primarily the result of the acquisition of 42 restaurants during the last six months of 2007 and the fixed cost leverage associated with increases of 3.6% and 3.1%, respectively, in comparable sales for the three- and six-month periods ended June 29, 2008, substantially offset by the significant rise in commodity costs during the three and six months ended June 29, 2008. Restaurant operating margin on an external basis, excluding the impact of the consolidation of BIBP, decreased as a percentage of sales 1.3% and 1.1% for the three- and six-month periods ended June 29, 2008, respectively.

Domestic Commissary Segment. Domestic commissaries' operating income decreased approximately \$300,000 and \$1.9 million for the three- and six-month periods ended June 29, 2008, respectively, reflecting a reduction in gross margin percentage resulting from increases in the cost of certain commodities and increases in distribution costs due to higher fuel prices.

Domestic Franchising Segment. Domestic system-wide franchise sales for the second quarter of 2008 increased 2.3% to \$372.6 million from \$364.1 million for the same period in 2007 and increased 1.9% to \$754.4 million for the six months ended June 29, 2008, from \$740.5 million for the same period in 2007, primarily resulting from increases of 1.9% and 1.6% in comparable sales for the three- and six-month periods, respectively. Domestic franchising operating income increased \$1.0 million, to \$13.1 million, for the three months ended June 29, 2008, from \$12.1 million in the prior comparable period and increased \$2.5 million to \$27.6 million for the six-month period ended June 29, 2008, from \$25.1 million in the prior comparable period. The increases for both the three- and six-month periods were primarily the result of the 0.25% increase in our royalty rate implemented at the beginning of 2008 (the royalty rate for the majority of domestic franchisees is 4.25% in 2008 as compared to 4.0% in 2007). The increase in the royalty rate was a part of the franchise agreement renewal program announced in the fourth quarter of 2007. This program was completed during the first quarter of 2008, with over 95% of our domestic franchisees renewing under the new form of franchise agreement. Our equivalent franchise units for both the three- and six-month periods ended June 29, 2008 were relatively consistent with the corresponding 2007 periods as net unit openings substantially offset the previously mentioned acquisition of 42 restaurants by the company during the last six months of 2007.

International Segment. The international segment reported operating losses of \$1.5 million and \$3.3 million for the three and six months ended June 29, 2008, respectively, compared to losses of \$2.0 million and \$4.4 million, respectively, in the same periods of the prior year. The improvements of \$500,000 and \$1.1 million in operating results reflect leverage on the international organizational structure from increased revenues due to growth in the number of units and unit volumes.

All Others Segment. The operating income for the 'All others' reporting segment increased approximately \$300,000 and \$1.8 million for the three and six months ended June 29, 2008, respectively, as compared to the corresponding 2007 periods. The increases are primarily due to improvements in operating results of our print and promotions subsidiary, Preferred Marketing Solutions, Inc., resulting from increased commercial sales and related margin improvement.

Cash Flow

Cash flow from operations was \$29.3 million for the first six months of 2008 as compared to \$26.2 million for the comparable period in 2007. The consolidation of BIBP decreased cash flow from operations by approximately \$14.3 million and \$8.7 million in the first six months of 2008 and 2007, respectively. Excluding the impact of the consolidation of BIBP, cash flow from operations was \$43.5 million in 2008, as compared to \$34.9 million in the corresponding 2007 period. The \$8.6 million increase was primarily due to an improvement in working capital, including income and other taxes, accrued expenses and accounts payable.

Form 10-Q Filing

See the Management's Discussion and Analysis of Financial Condition and Results of Operations section of our quarterly Form 10-Q filed with the Securities and Exchange Commission for additional information concerning our operating results and cash flow for the three- and six-month periods ended June 29, 2008.

Domestic Comparable Sales and Unit Count

Domestic system-wide comparable sales for the second quarter of 2008 increased 2.4% (composed of a 3.6% increase at company-owned restaurants and a 1.9% increase at franchised restaurants). Domestic system-wide comparable sales for the six months ended June 29, 2008 increased 2.0% (composed of a 3.1% increase at company-owned restaurants and a 1.6% increase at franchised restaurants). The comparable sales percentage represents the change in year-over-year sales for the same base of restaurants for the same calendar period.

During the second quarter of 2008, 29 domestic restaurants (five company-owned and 24 franchised) were opened. On a year-to-date basis, we have opened 55 domestic restaurants (nine company-owned and 46 franchised) and 46 restaurants were closed. Our total domestic development pipeline as of June 29, 2008 included approximately 350 restaurants scheduled to open over the next ten years.

At June 29, 2008, there were 3,270 domestic and international Papa John's restaurants (670 company-owned and 2,600 franchised) operating in all 50 states and 28 countries. The company-owned unit count includes 127 restaurants operated in majority-owned domestic joint venture arrangements, the operating results of which are fully consolidated into the company's results.

International Update

Highlights:

During the second quarter, we opened 38 restaurants (two company-owned and 36 franchised) while five restaurants were closed. On a year-to-date basis, we have opened 60 restaurants (five company-owned and 55 franchised) while seven restaurants were closed.

International franchise sales increased 30.1% to \$55.3 million in the second quarter of 2008, from \$42.5 million in the prior year comparable quarter and 31.6% to \$107.7 million for the six months ended June 29, 2008, from \$81.8 million in the prior year comparable period.

As previously announced we entered into an agreement with Berjaya Pizza Company Sdn. Bhd. for the development of 100 restaurants over the next ten years in Malaysia. The first restaurant is scheduled to open later this year.

We recently entered into an agreement for the development of 20 units in the Dominican Republic over the next nine years, with the first opening scheduled to occur this year.

At the end of June, we reached the milestone of over 500 restaurants operating internationally ten years after the opening of our first restaurant outside of the U.S.

As of June 29, 2008, the company had a total of 501 restaurants operating internationally (18 company-owned and 483 franchised), of which 160 were located in Korea and China and 109 were located in the United Kingdom and Ireland. Our total international development pipeline as of June 29, 2008 included approximately 1,100 restaurants scheduled to open over the next ten years.

Refranchising Initiative Update

At year-end, the company announced the implementation of a formal refranchising initiative, the goal of which is to increase the percentage of franchised units in the domestic restaurant portfolio over time. The company's goal is to reduce the percentage of domestic-owned company units to below 20% in the next few years (23.5% at June 29, 2008).

The company is working to complete the sale of 21 company-owned restaurants located in two markets. Our goal is to complete the sale of these restaurants during the third quarter of 2008, subject to satisfactory completion of due diligence and finalization of third-party financing by the buyers. The company plans to continue to review additional divestiture opportunities over the next several months.

Share Repurchase Activity

The company's board of directors has authorized the repurchase of \$50.0 million of common stock during 2008. The company repurchased approximately 664,000 shares of its common stock at an average price of \$27.13 per share, or a total of \$18.0 million, during the second quarter of 2008, and 768,000 shares of its common stock at an average price of \$26.40 per share, or a total of \$20.3 million, during the first six months of 2008. A total of 26,000 and 50,000 shares of common stock were issued upon the exercise of stock options for the three- and six-month periods ended June 29, 2008, respectively. Subsequent to quarter-end, through July 30, 2008, the company repurchased an additional \$6.9 million of common stock (255,000 shares at an average price of \$26.99 per share). At July 30, 2008, \$22.8 million remains available for repurchase under the repurchase authorization.

There were 28.7 million diluted weighted average shares outstanding for the second quarter of 2008, as compared to 30.6 million for the same period in 2007, a 6.2% decrease. Approximately 28.3 million actual shares of the company's common stock were outstanding as of June 29, 2008.

The company's share repurchase activity increased earnings per diluted share, excluding the impact of the consolidation of BIBP, by \$0.01 for the three and six months ended June 29, 2008.

2008 Earnings Guidance Reaffirmed

The company reaffirms its previously announced 2008 earnings per diluted share guidance in the range of \$1.68 to \$1.76 for the year. The projected earnings guidance excludes any impact from the consolidation of the results of BIBP and reflects our expectations of continued commodity price pressures, most notably cheese and wheat, as well as increased fuel costs. We expect that net worldwide unit growth will more likely be near the low end of our previous guidance of a range of 160 to 190 units due to the possibility of reduced unit openings and/or increased unit closings as a result of continued pressures on operating margins related to increased commodity, labor and energy costs. We also reiterate our guidance for domestic system-wide comparable sales to increase in the range of 1.25% to 2.75%.

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