Conference Call Transcript
1Q24 Results
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Arcos Dorados First Quarter 2024 Earnings Webcast

Dan Schleiniger

Good morning everyone and thank you for joining our first quarter 2024 earnings webcast. With us today are Marcelo Rabach, our Chief Executive Officer, Luis Raganato, our Chief Operating Officer, and Mariano Tannenbaum, our Chief Financial Officer.

Today's webcast, which is being recorded, will consist of prepared remarks from our leadership team, which will be accompanied by a slide presentation, also available in the Investor section of our website, www.arcosdorados.com/ir.

As a reminder, to better view the presentation on the webcast platform, please scroll over the upper left-hand part of the screen and click on the arrows to maximize the slides. After we conclude our opening remarks, we will answer your questions, which you can submit using the chat function on the left-hand side of the screen. You will need to minimize the slides to access the chat function.

Today's call will contain forward-looking statements and I refer you to the forward-looking statement section of our earnings release and recent filings with the SEC. We assume no obligation to update or revise any forward-looking statements to reflect new or changed events or circumstances.

In addition to reporting financial results in accordance with Generally Accepted Accounting Principles, we report certain non-GAAP financial results. Investors are encouraged to review the reconciliation of these non-GAAP financial results, as compared with GAAP results, which can be found in the press release and unaudited financial statements filed today with the SEC on Form 6-K. Marcelo, over to you.

Marcelo Rabach

Thank you, Dan. Good morning everyone and thank you for joining us. The strength of the results we reported this morning demonstrate how far we have come as a Company over the last decade. They also reinforce the strength of the Arcos Dorados business model, with solid US dollar growth to start 2024, even in the face of a very challenging economic environment in one of our main markets. This is a testament to the importance of operating responsibly and managing the business with a long-term mindset.

In the last ten years we diversified the business, reducing the weight of any single country. While Brazil remains our biggest market, NOLAD now contributes a growing share of sales and EBITDA, much of it in hard or very stable currencies. And, within SLAD, markets like Chile, Colombia and Uruguay have also increased their contributions to consolidated results.

Our objective is to generate sustainable profitability growth over the long term. To this end, the business model and the 3D's strategy are working well together. Everything starts with sales, and our balanced approach to managing pricing, product mix and guest volumes is driving above inflation comparable sales growth. The most critical driver of sustainable sales growth is guest volume. And the McDonald's Brand continues to capture the highest volume per restaurant in our region, by far.

The Region's growth potential is huge, and we are still accelerating restaurant openings. In fact, we plan to invest in the McDonald's Brand for many years to come, and our investments will foster a virtuous cycle of growth in our communities and local economies. In turn, this will support our long-term expansion plans while insulating the business from short-term volatility.

Before getting into the specifics of first quarter results, I want to take a moment to express how saddened we are by the severe flooding in Brazil's southernmost state, Rio Grande do Sul. Fortunately, all our employees in the state survived the flooding.

In the short term, we are focused on supporting our employees and their families, including with basic necessities and by guaranteeing their job security, until the situation improves. We have also begun distributing food within the communities we serve as well as to first responders. Moving forward we will be working on several initiatives, in coordination with local governments and NGO's to continue supporting our people and to aid in reconstruction.

Finally, I should also note that our business exposure to the state is relatively limited and, so far, Brazil's second quarter trends have not been materially impacted by this situation.

Turning now to the first quarter, performance in Brazil and NOLAD more than offset the impact of the devaluation of the Argentine peso on consolidated results. Total revenue rose 9.1 percent in the first quarter, supported by the twelfth consecutive quarter of positive comparable guest traffic at the consolidated level. Systemwide comparable sales rose above inflation in nearly all markets as well and were up 2.2 times blended inflation for the entire Company, excluding Argentina. McDonald's Brand visit and spend shares remained more than 2 times our nearest competitors and the Brand attributes we track are at, or near, all-time highs across the region.

The digitalization of the Arcos Dorados business also remained on track in the quarter, with Digital channels generating 55 percent of systemwide sales. Total digital sales growth of 30 percent in US dollars was driven by Delivery, self-order kiosks and mobile order and pay sales.

Notably, this quarter, we signed an agreement to become a regional sponsor of Formula One in Latin America. Over the years, this global sport has become popular among families within the region, bridging all demographic, gender and socioeconomic groups. In addition to providing a significant boost to our brand presence in the region, this sponsorship will focus on further leveraging the successful Three-D's strategy, including the synergy with the precision, teamwork and speed of service of our industry leading Drive-thru business.

Finally, restaurant openings continued to accelerate. We added 22 EOTF restaurants,19 of them free-standing. Brazil opened 11 restaurants, including 10 new free-standing units. Luis will now take us through an overview of sales performance in each division.

Luis Raganato

Thanks Marcelo and good morning everyone. As Marcelo just mentioned, we believe sales growth above inflation is the most sustainable way to increase profitability.

Brazil’s comparable sales rose 9.4 percent, on top of 13.8 percent in the first quarter last year. This year’s growth was 2.2 times inflation in the period, with higher volume and average check contributing to the result. Digital sales grew 38 percent and accounted for 65 percent of total sales in Brazil. Importantly, 26 percent of sales were identified. As a reminder, these are transactions where we not only have customer data, but where customers have explicitly authorized us to track and use their data. Additionally, the Meu Méqui loyalty program continued to gain traction in the market in the quarter.

Brazil’s marketing plans and campaigns became the “talk of the town” during the first quarter, with the continuation of the successful “Méqui Me Pega” campaign and the launch of Big Tasty Turbo Cheese. We engaged with Gen Z customers by, once again, sponsoring the Lollapalooza music festival in São Paulo as well as the country’s most popular primetime TV show, Big Brother Brasil.

We also drove brand excitement and customer engagement across all sales channels by bringing back the McFish sandwich as a limited time offer, selling out in a very short time. Finally, the dessert category included the introduction of the McFlurry “Chocrocante” with an iconic Brazilian chocolate, Diamante Negro.

NOLAD’s comparable sales grew more than three times blended inflation in the quarter, with guest volumes driving almost the entire result. Every single market in NOLAD grew comparable sales above inflation in the quarter, with strong volume growth as the main driver. Performance was particularly impressive in Mexico, with comparable sales up in the teens, driven primarily by guest volume growth. I should note, that the quarter’s result also benefitted from the extra trading day due to Leap Year as well as from Holy Week, particularly in Mexico.

Key marketing activities in Mexico included the launch of the new value platform “Elige tu Fav”, which allows guests to choose between delicious beef or chicken combos at an attractive price. Notably, Digital channel sales in Mexico doubled versus last year and the McDonald’s App is now the most downloaded, and used, App across the country’s QSR industry. Panama implemented a strong value platform, coupled with one of the biggest brand equity scores in the region, to accelerate the business in that country. In Puerto Rico, we gained significant visit share as the new brand campaign “Saca tu Encanto” resonated well with guests.

Finally, as Marcelo mentioned, we signed a regional sponsorship of Formula One that resonates across our footprint, with special meaning in NOLAD given the popularity of Mexican driver, Checo Perez.

Comparable sales grew below blended inflation in SLAD due to the significant economic slowdown in Argentina in the quarter. However, except for Argentina and Ecuador, the other large markets in the division generated comparable sales growth well above local inflation. This included Chile, Colombia and Uruguay, where guest volume growth was robust. Comparable sales were up 1.8 times blended inflation in SLAD, excluding Argentina.

The silver lining in Argentina was that, while consumption was down 20 to 30 percent in the country, Arcos Dorados’ volumes declined at about half that rate in the period. The local team delivered this impressive result by continuing to offer consumers the best value proposition in the market’s QSR industry. This led to significant market share gains against our main competitors and improvements in our brand equity scores, which should position us for a strong rebound once the economy stabilizes.

Similar to Brazil, the SLAD division strengthened brand affinity and excitement among younger consumers, by sponsoring the most relevant music festivals in the region, including "Lollapalooza" in Argentina and Chile, as well as "Estereo Picnic" in Colombia. We brought menu innovation to SLAD's markets with the launch of the Quarter Pounder Western BBQ in Chile and Uruguay, Quarter Pounder Cheesy Jalapeño in Ecuador and the Grand Tasty Spicy in Argentina. These new product launches were all met with strong guest responses, helping drive restaurant traffic and average check growth.

SLAD also continue making inroads in the chicken category, with the launch of the McCrispy Chicken platform in Uruguay and the McCrispy Chicken Legend in Colombia, which is quickly becoming a guest favorite.

All the marketing efforts related to menu favorites, music and sports are generating tangible results. Market share performance in the quarter was strong throughout the Arcos Dorados footprint in both visit and sales share. We also measured 2.5 times Top of Mind and 1.5 times Favorite Brand scores against our main competitors, on average, across the geography. This was supported by all the markets we track with quarterly data in NOLAD and SLAD, which gained important market share in the period.

In Brazil, where we continued to strengthen the Brand's leadership position, we achieved an all-time-high visit share score over the trailing 12 months. According to our research, Brazil reached record high scores in brand equity, including top of mind, while remaining the country's Favorite QSR Brand by a wide margin. Notably, we measured favorable gaps against our main competitor in all the brand attributes we track, covering experience, taste, community impact, family environment and affordability, among others. Over to Mariano for a closer look at consolidated and divisional profitability in the quarter.

Mariano Tannenbaum

Thanks Luis. Good morning everyone.

First quarter Adjusted EBITDA growth was in-line with revenue growth in the period, highlighting the diversity of our operation and the resilience of the cost structure, even following the significant devaluation of the Argentine peso. As we mentioned on our last call, we expect to generate EBITDA growth primarily through revenue growth, while capturing efficiencies and margin opportunities over the long run.

The Consolidated EBITDA margin was flat with lower Food & Paper and G&A offset primarily by higher Occupancy and Other operating expenses as a percentage of revenue. A consistent value proposition and a lower cost environment led to the improvement in Food & Paper, and significant revenue growth leveraged G&A. Meanwhile, below inflation growth in Argentina was the main cause of lost operating leverage in fixed expenses. For full year 2024, we expect the favorable cost environment to continue and will focus on gaining efficiencies in other line items.

Divisional results reflect this dynamic, with Brazil extracting almost 27 percent higher US dollar EBITDA and 90 basis points of margin expansion from its strong topline growth. Importantly, Brazil's solid margin expansion included lower Food & Paper, Payroll and G&A expenses.

NOLAD also turned its impressive sales growth into almost 21 percent US dollar profitability growth, and 30 basis points of margin expansion.

SLAD's US dollar EBITDA decline in the period was driven almost exclusively by the reduced consumption in Argentina and the translation impact from the Argentine peso's significant devaluation at the end of 2023. The resulting volume reduction in the Division's largest market caused sales and operating leverage to decline, which reduced margins as well. To a lesser degree, SLAD's results were also negatively impacted by the effect of the unrest in Ecuador.

Looking ahead, the macroeconomic environment continues to be challenging to predict in the short term. But we remain focused on generating the strongest possible full year results in each of our markets, leveraging the diversity of our operating footprint to drive consolidated US dollar profitability higher than last year.

Luis Raganato

The driving force behind our results for the last three years was the Three D's strategy of Digital, Delivery and Drive-thru. The work to digitalize the business is far from over, and the results of the first quarter demonstrate how this strategy still has plenty of room to drive performance across the entire Arcos Dorados footprint.

Digital, which includes sales from the Mobile App, Delivery and Self-order Kiosks, grew 30 percent in US dollars versus the prior year quarter. These channels accounted for 55 percent of systemwide sales and allowed us to identify 22 percent of sales in the quarter as well. In Brazil, digital channels generated 65 percent of sales, including 26 percent identified sales with actionable customer data.

Delivery and Drive-thru sales combined, were up 14 percent year-over-year in US dollars. These two channels, that make up "off premise" sales and heavily leverage the Company's free-standing restaurant footprint, accounted for about 44 percent of systemwide sales in the quarter.

Brazil's Delivery sales grew by more than 44 percent in US dollars and was more than four times the nearest competitor's delivery sales in local currency terms, according to publicly available information. NOLAD's results also benefited from strong Digital sales, particularly in Delivery and self-order kiosks, as we continue the digitalization of these markets.

The Loyalty Program we launched in Brazil and Uruguay, so far, has grown to more than 8 million registered members as of the end of April 2024, up from 3.2 million at the end of last year. We should have Loyalty in two more markets by the next earnings call, and we expect to be fully implemented by the end of 2025.

Loyalty boosts the power of the Mobile App by taking customer data from identified sales to offer an increasingly personalized guest experience. We have been very encouraged by the accelerating growth in registered members and a very positive trend in 90-day active customers. Together, these drive frequency significantly higher than non-Loyalty customers, which also increases the customer's lifetime value. We are already seeing this in both Brazil and Uruguay, and the roll-out of Loyalty in each new market will benefit from the learnings we are gaining in existing Loyalty markets. Mariano.

Mariano Tannenbaum

Let’s take a look at our Capital Structure and investments in growth.

Our net leverage ratio remained at a very healthy 1.2 times at the end of the first quarter. I am also pleased to report that, a couple of weeks ago, Moody’s upgraded Arcos Dorados’ corporate and senior debt rating outlook from Stable to Positive, re-affirming the Ba2 rating, based on our liquidity condition and latest operating performance.

Over the last 12 months, cash from operations remained in-line with the prior period. We have been deploying excess cash primarily to support restaurant growth and modernizations as well as expanding digital capabilities. We continue to expect to fund this year’s capex plan with cash on hand and cash from operations.

In the first quarter, we opened 22 restaurants, which is on pace to meet full year guidance, and we deployed about 61 million dollars for capital expenditures for restaurant openings, modernizations, and maintenance as well as for Digital and IT enhancements. Marcelo, back to you.

Marcelo Rabach

In the next few days, we expect to publish our 2023 Social Impact and Sustainable Development report. You will be able to download the report by visiting the Recipe for the Future website. Let me give you a preview.

This will be our tenth annual ESG report, which is also the industry’s only report to include audited content. This latest edition will showcase all the progress we made last year across the six pillars of our Recipe for the Future.

Among the highlights were the hundreds of thousands of training and job opportunities we offered to the region’s young people. This is one of our most important contributions to the economic development of the communities we serve, given that almost two thirds of our employees are younger than 24 years old. We are also proud of the diverse and inclusive workplace we offer, having received more than 40 awards and other forms of recognition just last year, from a variety of governments and NGO’s.

On the environmental side, more than 30 percent of the energy Arcos Dorados uses now comes from renewable sources and this number continues to rise as we sign more agreements for this type of energy, providing an incentive for these energy producers to continue investing in the countries where we operate. These are just a few examples of the important work we are doing for the benefit of our communities and the environment.

I opened today’s call by saying that first quarter results demonstrate how far we have come over the last decade. Before we move to Q&A, I would like to leave you with some final thoughts.

The strength of the Arcos Dorados business model is evident in the first quarter’s results. We operate across a diversified geographic footprint, generating a growing amount of cash flow from stronger and more stable currencies and markets than ever before.

Sales growth remains solidly above inflation, supported by positive guest volumes at the consolidated level. This is driving profitability growth in a way we believe is sustainable over time and we are capturing incremental operating efficiencies as well. Most importantly, all the levers we have pulled to generate these results are far from over.

The Brand continues to capture significant market share. Our menu is constantly evolving to meet customer preferences. The digitalization of all markets is, and will aways be, an ongoing process. Our pricing tools are increasingly sophisticated, further balancing sales growth and margins. The operation is already the industry standard, and it's getting better. And we still have a huge opportunity to accelerate restaurant growth across the entire region.

These are among the many reasons we are confident in our ability to continue generating significant shareholder value in the years to come. Thank you, once again, for your interest in Arcos Dorados and ongoing support of our business. Dan, over to you to start the Q&A session.

Dan Schleiniger

Thanks Marcelo. In order to get started, please minimize the presentation slides so that you can access the chat function on the left-hand side of the webcast platform. Please limit yourself to one or two questions so that I can read, understand and convey them to our speakers. We will now pause briefly to compile your questions.

Thiago Bortoluci, Goldman Sachs

Good morning, Arcos team. In Brazil, can you provide a breakdown between ticket and traffic that drove the comparable sales growth in the country?

Marcelo Rabach

Good morning, Thiago. Thank you for joining us today. We had an excellent 1Q in Brazil. And as you know, comparable sales are a function of guest volume, pricing and product mix, and we had a positive contribution of each of these drivers.

In terms of guest volumes, they rose low single-digits in the 1Q24. So, they were positive again in Brazil in the 1Q. Pricing was basically in line with headline inflation, and product mix improved thanks to the higher participation of digital and loyalty sales versus the prior year. So, the three components of the comparable sales had contributions to the figures we saw in Brazil in the 1Q.

And importantly, according to CREST, we gained both visit share and sales share in the 1Q and over the trailing 12 months, with some of the smaller players in the industry losing share.

In fact, over the last 2 years, if you take a look at Brazil's numbers, 1Q comparable sales have grown more than 24% in the cumulative 2 years. And of those increases, around 40% came from volume, and 60% more or less came from average check.

So, we are in the strongest position in Brazil to capture additional growth in coming years, and this will generate for sure significant shareholder value, thanks to our very strong position.

Thiago Bortoluci

The delivery sales channel is growing at 44% year-over-year. It seems that this was the main driver of same-store sales growth, while on premise performance was lower in the quarter. Can you share comps by channel in Brazil?

Luis Raganato

Of course, delivery keeps on surpassing our expectations with an impressive growth of 44%. But having said that, we had a very good sales quarter in Brazil, with all channels growing positively in the mid-teens.

Specifically in delivery, we are leveraging from our freestanding restaurant portfolio; the strength in operations and marketing execution; the close relationship that we have with 3POs; and the recent launch of our loyalty program.

Thiago Bortoluci

What was the contribution of the channel mix to our gross and EBITDA margins in the quarter?

Mariano Tannenbaum

Perfect. Thanks, Thiago, for the question, and hi, everybody. Of course, the contribution was very positive. In the 1Q of this year, EBITDA grew almost 27% from US$59.5 million in the 1Q23 to US$75.4 million in the 1Q of this year. And EBITDA margin was up 90 basis points from 15.9% to 16.8%.

We are extremely happy to see that this increase in margin was reflected in several lines, mainly in food and paper. So, we are improving gross margin; in payroll, which is improving as well; and G&A, which are the 3 main cost lines in our income statement.

Thiago Bortoluci

Can you comment on how beef and potato are trending? And how would this impact gross margin?

Mariano Tannenbaum

We see a benign food and cost environment, and we are optimistic with the outlook for 2024. In particular, we see a better outlook on beef with reduction in costs. We see some pressures on potato, but overall there is a positive trend, and we are expecting, everything else equal, a better gross margin than what we had last year. So that's the outlook that we have for 2024.

Thiago Bortoluci

About Argentina, any comments on the traffic in the region? And how has it been evolving throughout the quarters?

Lorena Reich, Lucror

What are our expectations for the rest of the year in Argentina?

Marcelo Rabach

Consumption in Argentina declined between 20% and 30% in the 1Q. But, as we mentioned during the opening remarks, Arcos Dorados volumes declined only about half that rate. These volumes have been evolving modestly; in a positive way, sequentially since then.

I would say that our local team has been doing an excellent job in terms of remaining close to consumers, offering them the best value proposition in the country's QSR industry by far. And as a result of that effort, we have gained significant market share and further strengthened our brand attributes. And this should put us in a very well position for when the Argentine economy begins its expected recovery.

It is still too soon to know how all the macroeconomic factors will evolve during the year, but we are working very hard in order to navigate the current situation as well as possible, and always with the long-term mindset. So, challenging context in Argentina.

But remember that the beauty of Arcos Dorados is that we operate in 20 different markets. So, we have another 19 markets. And our business today is very diversified, with significant contributions coming from Brazil, from NOLAD, and from other markets of the SLAD division. So, we are very confident that this diversification will continue driving consolidated profitability growth in full year 2024, and in coming years.

Thiago Bortoluci

How does the scenario, maybe higher for longer interest rates, impact our near-term plans around expansion?

Mariano Tannenbaum

In this case, we have a long-term plan of investments, openings, mainly freestanding units in many of our markets. In LatAm, we have the long-term plan also to modernize our existing stores with EOTF. We are also deploying investments in non-development, mainly in technology, to continue improving our digital platforms. And this will not change.

We are seeing above average returns in general, mainly in our freestanding units, well above our cost of capital. And this will not change. So, we will remain with our investments and we are very pleased with the results we are seeing so far.

Felipe Cassimiro, Bradesco

Could you shed more light on the evolution of the competitive landscape in Brazil and Mexico with heated competition from other listed players? And how are you adapting to fiercer competition in the QSR segment?

Marcelo Rabach

We gained more than 1 p.p., in fact, 1.1 p.p. of market share across our main markets in the 1Q24, according to our research. And I would say that competition has been mostly rational although, as you mentioned, we have seen increased promotional activity in some markets, particularly in Brazil.

But we are focused on offering a very compelling value proposition with competitive pricing and, most importantly, an unmatched restaurant experience. So, this is driving volume growth in recent quarters, and this helps us to leverage our fixed cost structure.

This year, for example, we have a more favorable cost environment that should help us to continue improving our margins while we respond and we react to competitive pressures as needed. Given the fact that we are the leaders in all these markets, particularly in Brazil, we have the ability to react and to put pressure in some competitors if we feel that that's the correct answer that we need to give them. So, we are very well positioned and gaining share in most markets.

Felipe Cassimiro

Tax rate was substantially higher than our estimate. Could you elaborate the main reasons of the effect of tax rate of around 40%? And how should we think about this over the course of 2024?

Mariano Tannenbaum

Felipe, thanks for the question. On a quarterly basis, the effective tax rate can be volatile, given the various rules governing the calculation of this liability in each of our markets. Remember, we operate in 20 different markets, plus our holding companies, as well as within our overall structure.

So, for the 1Q24, we had an effective tax rate of 39.7%. This compares with 35.8% in the 1Q23. So, looking ahead for the full year, even if it is difficult to predict, we believe in that a consolidated ETR between 35% and 40% is a reasonable level to expect for the full year.

Felipe Cassimiro

How should we think about the evolution of the royalty rates in Brazil? Should we still see a growth support offsetting this line in 2024?

Marcelo Rabach

Thank you, Felipe. We have in place an agreement with McDonald's for the growth support incentive that goes through the end of this year. So, we expect royalty rates on consolidated levels to stay in the same range that they were in this 1Q, around 6.3% of sales. And given the fact that we already agreed with McDonald's with the support for the full year, we do not expect this number changing materially during the year.

Daniel Schleiniger

It's probably fair to say that it's a fixed amount of gross support, and sales have been above expectations. So, it's a little bit less of impact on growth.

Felipe Cassimiro

The supplier days dropped 5 days to 80 days in the 1Q24, which is back in line with 2018 and 2019 levels. Could you elaborate on the reasons behind the reduction? And how should we think about supplier relationships and potential benefits with lower costs on a move forward basis?

Mariano Tannenbaum:

Traditionally the 1Q is the worst quarter in terms of working capital for the Company due to seasonality. Remember that in this particular quarter, we also accelerated the openings. Remember, this year we had 22 openings compared with only 8 openings last year.

And this is what we are trying to do in terms of avoiding having all our CAPEX backended. That could have had an impact on our accounts payables, because usually development suppliers have shorter terms than other suppliers. So, I wouldn't expect a change in our account payable terms in the short or in the medium term. And if so, it would be for the better and not for the worse. That means, if anything, we will expand payment terms and not reduce it.

In some cases, of course, there are opportunities to have reduction costs by changing the outstanding days, but those are very specific things and negotiations, and we cannot expand that to the whole bucket of our suppliers.

Julia Rizzo, Morgan Stanley

Can you give us an update on sales trends in the key markets for the 2Q to date?

Marcelo Rabach

I would say that, as I mentioned before talking about Argentina, the figures that we are seeing in the 2Q are in line with what we saw in the 1Q. Remember that the 1Q was very strong. It was in fact, our 12th consecutive quarter of comparable guest count volume growth. So cumulative sales trends are about in line with these numbers in the 2Q, although we will not benefit this quarter from an extra trading day, and we will compare with Holy Week that last year was in the 2Q.

We remain focused on delivering great value to our guests all across our menu, and we expect this to help us deliver comparable sales growth at or above inflation in the full year 2024 in most of our markets, with a balanced contribution from pricing, product mix and guest volume, as has been the case so far this year. So that's what we are seeing today in terms of volumes.

Julia Rizzo

Can you give more color on delivery performance? How much does delivery representative sales in Brazil?

Luis Raganato

Thank you, Julia. In Brazil, delivery represented around 20% of systemwide sales. And, about the delivery performance, we operate delivery in more than 80% of our restaurants in 14 different markets. Delivery sales rose 27% in USD and represented 18% of systemwide sales.

And about the evolution, delivery has surpassed our expectations so far. We believe that there are still good opportunities to keep on capturing market share, because even with the best course in speed and accuracy, we still have a big room to improve our operations. And we believe that the channel has not reached full maturity yet. And because of this, we believe that our strategies and our operating models will continue to evolve.

Our strategy will keep on focusing on strong operational execution. We are going to keep on working in innovations in digital capabilities and targeted marketing campaigns specific to this channel to keep on strengthening the strategic partnership with 3POs and own delivery, that represents today about 10% of our total delivery sales.

Julia Rizzo

About delivery, after growing so much and achieving significant sales representativeness, how is this channel profitability versus consolidated figures in Brazil?

Mariano Tannenbaum

Well, thanks, Julia for the question. In fact, all our channels are accretive to the business, and they are generating good returns and contribution towards EBITDA. You can see that delivery has grown a lot in the last several years, representing now relevant part of our business. And the margins continued to increase overall as well.

So that means that delivery, even though there's a delivery fee that the Company pays to the 3POs, there are many other impacts in our cost lives that benefit the margins overall and are helping to improve the overall margins of the Company. Remember last year, we had a record EBITDA margin and, in this quarter, you can see that margins are improving as well.

Lorena Reich, Lucror

Good morning. Congrats on the strong performance. Can you comment on the cash burn during the quarter, which is still very healthy, but below US$200 million versus usually having above that figure?

Mariano Tannenbaum

Thanks, Lorena, for the question. I already answered a part of the question about working capital seasonality being the 1Q the worst of the 4 quarters we have. And this is because in January, usually we pay all invoices related to the end of the previous year. And being December, our highest month in terms of sales and CAPEX development. In January, there's an impact on our working capital.

On top of that, this year in particular, the quarter ended on Easter Sunday, which is a 4-day holiday weekend in many of our LatAm countries, that resulted in a temporary increase in the account receivables that were automatically collected on the next business day, Monday. That's the Monday of the 2Q. So, these 2 effects, of course, have an impact on the cash flow dynamics of the 1Q.

On top of that, I already mentioned as well in a previous question that this year we accelerated CAPEX on the 1Q, having opened 22 new restaurants compared with 8 new restaurants of the previous year. So, these dynamics are impacting the cash flow generation on the 1Q. But if you look at the trailing, 12 months. So then excluding seasonality, the operating cash generation remain in line with the prior period and we expect a cash conversion similar to last year.

Lucas Ferreira, JPMorgan

How have restaurants operational KPI's been involving in Brazil, such as turnover, drive-thru speed, et cetera?

Luis Raganato

Hello, Lucas. Thank you for the question. The evolution on operational KPI's in Brazil specifically have been very positive. We focused for the last 2 years, for example, on 90 days turnover. We focused on people. People is the base of our operations plan. And specifically in that KPI, we have seen a reduction of our turnover in about 20%. So, that is very positive.

Our crew, our managers are the base of our operations, and we rely on that to have an excellent execution. And talking about speed and accuracy in the rest of the channels, and talking about delivery, even front counter, the improvements have been very significant. But having said that, we still have a huge room to keep on improving.

I would say that the main focus is to equalize operations, and equalization means that we try to work with low performance stores, and markets, even. We benchmark and leverage the best practices that we have in those that are high performance stores and markets. And that's the beauty of having 20 markets, the geographic diversity that we have. So, in summary, we are pleased with the results, with the evolution of these KPIs, but we are obsessively focused on the continuous improvement.

Robert Ford, Bank of America

Good day, everyone. Can you discuss some of the system's more successful CRM strategies in terms of activation and transaction sizes and some examples of your early successes?

Luis Raganato

Thank you, Bob, for the question first. Yes. And I am going to go a little bit deeper into digital. And you know that we are pleased with the evolution of digital sales. About the performance, we have rose 30% in USD accounted, as we said, for the penetration is 55% of total systemwide sales and this includes 22% of identified sales. So, we are very pleased with the performance and we are very confident that we are going to be able to maintain our growth trend.

Digital sales. The growth of the channel was driven by 3 main factors: the implementation of new functionalities to our app, the expansion of our customer base and a great trend in active users. And loyalty was a booster of the sales because we use the customer data and identify sales to offer or to try to offer a more personalized experience.

So, we have 3 main KPIs to evaluate the program: its visit frequency, average check and 90-day active user. And what we are seeing is an acceleration growth in registered members.

Like I said before, we launched the program in Uruguay and Brazil in October 2023. By the end of December of last year, we had 3.2 million registered members and by the end of April, we had 8 million registered members. That is a significant growth. And we are seeing that today, in the last weeks that is still going on.

And so, we do not only see that growth in registered members, but a positive trend in active customers. And this steady increase reflects the growing engagement and interest that our guests have with it.

And talking about redemptions and the margin that we can see in the future of this program is that, we see a positive impact since redeemed products have on average, a higher margin because these transactions are incremental. For example, a dessert after lunch or associated with a new sale.

And you know that another advantage that the program has is that it enables us to analyze customer behavior as average check and number of visits. When I talk about that, it’s the average check and number of visits to manage the customer lifetime value.

So, we are going to keep on investing on that. We are encouraged about the early results and we are going to implement it in 2 more markets by the next earnings call, by August, and we intend to cover the whole region by 2025.

Robert Ford

How will Arcos prove to be more or less digital versus other global markets? Thank you.

Marcelo Rabach

Thanks, Bob, for the question. And I think you referred to other McDonald's global markets. I would say that the digitalization of the Arcos Dorados business is strategic for us. It has been that way for many, many years now. That's why 55% of our sales during the 1Q were digital.

And the investments that Luis was mentioning, they have had great returns. All of them have had great returns. A positive impact on our sales, a positive impact in terms of average check, and finally, a positive impact in terms of margin.

So, we continue to benchmarking against the best markets within the McDonald's system. For example, China is one of the leaders in terms of digital within the McDonald's system. We continue to benchmark with them and trying to get the best practices and the newest tools that they are using in order to leverage all the efforts that we already have done in terms of digital within Arcos Dorados. So, this will continue to be a focus for us in coming years.

Daniel Schleiniger

Great. Thanks, Marcelo. And that was actually the last question we received from the investment and analyst community. So that's the end of the Q&A session.

Thanks again for all your interest in Arcos Dorados and joining us in today's webcast. We look forward to speaking with you again in the middle of August on our 2Q24 earnings webcast. And until then, stay safe and have a great day.

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