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National Vision Holdings, Inc. (EYE)

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CORPORATE PARTICIPANTS

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Kate McShane – Analyst, Goldman Sachs & Co. LLC

Q&A DISCUSSION SECTION

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Okay. There we go. Thank you for joining us. Today, we are happy to introduce National Vision. We have Reade Fahs, Chief Executive Officer; and Melissa Rasmussen, Chief Financial Officer, here to answer some of our questions. Reade, I wanted to maybe turn it over to you first. We were talking before and I thought it might be helpful to highlight what you think is most misunderstood of the National Vision story and we'll go into this.

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Thanks for that. Because I do think there are some that fall, some things fall into that category. I'd say primarily is the state and the evolution of our remote medicine program. So much of what we do, we are a low cost provider of eyeglasses and eye exams and contact lenses. And our key point of value is we bundle the cost of the glasses and the contact lenses in with the eye exam. And generally, our entry offers two pairs of eyeglasses for $79 with the eye exam included in that, which is just a great deal. But you've got to be able to provide the eye exam to offer that great deal. It's been this way since the brand began bundling of the eye exam and the glasses.

And post-COVID sort of the market for any sort of medical professional out there, call it, optometrists or veterinarians or whatever, they're just less medical professionals out there and so the market for us, for optometrists, got smaller and that's what we need to provide the free eye exam. And we put together sort of a program soon after that saying, hey, we've got to deal with this shortage of doctors. And we worked out a way whereby doctors can be at home and do an eye exam on someone in the store. We gathered the data, we send it to them, they come on live in front of the patient and do the exam live synchronously. They say, do you like number one or number two? And the doctor presses the button and changes the lenses in front of them. It's a very cool lead experience. And guess what? You can hire plenty of doctors to practice from home and so recruiting and retaining those doctors is great and easy. And this program has been great for us. It's in the stores where we're doing it. It's 12% of exams and growing and that's pretty neat and exciting. But it has been – it was a startup and it's in an evolutionary state and growing in a really nice way. And I don't think people fully understand the potential of where this could eventually go in terms of really dealing with our capacity challenge. And so I'd like to talk more about that as we go in terms of the specifics of how it works. But I think that's the thing that's misunderstood in our story is the role remote can play in addressing the capacity challenges post-COVID.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

So yeah. So maybe we'll start there with some of our questions. Because it's such a unique part of your story. I feel like you mobilized it very quickly as well. So could you talk maybe a little bit about how differentiated this initiative is? Are you one of the only retailers offering this as an alternative to help you, again help with the optometrist capacity? Is there a goal of how many eye exams you think you can get to based on what you know today? And I know there are certain states that aren't necessarily allowing remote medicine yet and how does that play out?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Yeah. So this was designed around solving a problem. We had really stupendous success for about 19 years prior to COVID. But that's now ancient history now. So we live in a post-COVID world of new realities. We said that amidst these new realities, we would have to rapidly transform and creating sort of an Uber like eye exam experience was not in our skill set, but we did it and we've accomplished it and it's doing the job and really helping us now. It's not that it's – there are others that offer it but there aren't others that offer this bundled offering in the same way we do. So our need for exam capacity is heightened. We have what we believe is the largest network of employee doctors in America and we are doing a huge number of exams and that is the starting point for the eyeglass and eye exam purchase. So it is differentiating for us, because it solves that problem for us. It is not legal in all states yet. It's legal in 28 states. We were very pleased that the Texas came on board this year, and that helps us a great deal in that way. But there are sort of three to four evolutionary paths that are important to understand here. There's getting stores as productive with a remote doctor as with a live doctor. And we have a nice collection of stores that are as productive, but not all stores are. So we have a path there for that. Getting doctors, remote doctors more productive than in-store doctors and we have a nice collection that are and we believe ever more will be and that they should be more productive in that way. And so those are two key pieces, and then getting the balance right between supply and demand. And we also now have a collection of stores whereby the doctor, where a doctor in-store live, if there is a no show, a cancellation or if it's a slow day, can do exams in other stores, and thereby we aren't hiring an extra remote doctor at home. It's a doctor we're already paying for doing exams in places that are needed when they're not as busy, which would make the whole ecosystem all the more productive. But in the world we live in, in retail, you get a few stores, right, and you can eventually get all stores right. And we've got a nice collection of stores, right in terms of productivity relative to live doctors. Nice collection of doctors right in terms of more productive than in-store doctors and a collection of these hybrid doctors in-store doing exams in other places. And all of those are on a positive evolutionary path that gets better every quarter.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Well, that all sounds super exciting and very controllable in terms of taking things you can control?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Managing what you can control in a crazy world.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

So you're dealing with that. But you've also, along with the optometrist capacity, you also have some challenges with the macro and the consumer, because you do cater to a lower income consumer. And then there's the optical purchase cycle too that's been maybe a little...

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Disrupted, for sure.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Disrupted. So maybe could we take each one of those buckets? How can we start with the health of the consumer, the difference between what you're seeing between the managed care and the cash paying customer and just how you see that playing out for the rest of the year

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Yeah. So our customers are value focused. They are looking to save money on their eye exams and their glasses, and their contact lenses and we have always been a value positioned brand. In America, a little more than half of Americans have managed care benefits. They're generally employed and have nice jobs that give them good benefits and then cash pay consumers don't have benefits. When we bought America's Best, they did zero insured customers and we have gotten it up to over 35% of the business is insured customers and that is growing nicely. When it's insurance money and not your money, you are more apt to have a more normalized purchase cycle because it's not your money and that part of our business is growing at high single-digit comps. So that's pretty exciting

On the cash pay side, it improved in Q2, but it's essentially flat versus last year and the cash pay customers who are coming in are not buying as many added value products because they're watching their pennies as I think we're hearing throughout the day in so many businesses today. And we would expect the managed care customers to continue to improve, and we are – all of us in the industry are saying, when will the purchase cycle normalize for the cash pay customers? So many customers bought in2021 are generous. Government gave them all a lot of – gave Americans a lot of cash. And guess what? They went out and bought glasses. Wasn't that great? But they went out and bought the best pair of glasses they've had and the purchase cycle has not really normalized since then.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Okay. So we talked about where you comped prior to the pandemic, which is always at a very healthy mid-single-digit rate. And while comps have been improving because of all of your initiatives, we've not yet seen a return to mid-single-digit rate. Are you able to get back to these levels if the macro were to remain difficult with the cash pay customer, or are you at a place with remote health, the flexible optometrist schedules, marketing investment, where you could get back to mid-single-digit comp growth?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

So thanks for mentioning it. Yes, for 19 years, we had 72 consecutive quarters of positive comp store sales growth, averaging 5% within the last four years before COVID, averaging 7%. I do like to say that even though it's ancient history, yes, we believe we can, should, and will get back to mid-single-digit comps. We're very encouraged. We have had six consecutive quarters of positive comps. And in Q3 and Q4, we were in mid-singledigits, 4.7% and 6.3% in Q3 and Q4 of last year. We thought, hey, it's starting to feel back to normal. This feels the way we like it. The first two quarters have not been in the same way. Q2 was 2.4% for the company, 2.9% for America's Best. And what we said was, okay, we've been doing a lot of transformation, but we have to turn up the dial on transformation and we're doing it in a variety of ways. I've talked about the remote medicine program, helping us to get the capacity we need to address the demand that is there. We've implemented a lot of new promotions. I think, all right, you value conscious cash pay consumers, come on in. We had a 40% off single payer where you did have to pay for your eye exam program. And we just had finished up something called our Wise Buys program where we went back from our current two pairs for $79 and a free eye exam back to our historical two pairs and an eye exam for $69.

We said, hey, for a limited time, you can have that old offer that has drawn in a lot of folks and we also had a first time offer ever on progressives, which we have never tried before, two pairs of progressives for $129 and a free eye exam. Guess what? Lots of progressive wearers came in on that. That brought in new customers and we think that progressives offers are now going to be a part of our toolkit going forward.

We're doing some interesting things with new products and new product news that are driving traffic, but we are really very much in the mode of continued and heightened transformation to get us back to those mid-single-digit comps. Mid-single-digit comps yield mid-single-digit operating margins and that is our key focus and we are bringing fresh thinking and fresh ideas to get there.

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

And just to add one thing here. On the promotions, we were able to get some incremental data on our customers that we hadn't seen previously. So with these promotions that we were putting in place, we were able to evaluate the customer base that was coming in and the low income consumer that we had historically been seeing the most did come in during those promotional events that we were offering. So that tells us that they were sitting out based on macro constraints that they were facing. In addition to the progressives offer that Reade talked about, that was a very popular offer and we saw a lot of new progressive wearers that we hadn't historically seen come into our stores come in as well. So we did get some incremental data from those promotions.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

The promotions are working. How do you think about managing that and your margins until you do see return to a normal optical purchasing cycle?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

Yeah. So, with every promotion, you have to evaluate the increased traffic with the decrease in profit margins and that's something that we monitor very closely with the promotions that we put in place. So we evaluate where we are on, I guess, the level of increased traffic that it would take to offset the impact of the margin degradation from the promotion. And the promotions that we've put in place have been very successful so far. And so getting that customer to return during this economic period has proven to be beneficial

Now getting back to the mid-single-digits. To Reade's point, we have been in a period of transition or transformation, and we continue to be in that period of transformation. And to speed things up to his point, we did get some new talent, new leadership coming in to give some fresh perspectives in addition to the promotions and the new product offerings. And so we are taking some steps to speed this along as quickly as we can.

Kate McShane – Analyst, Goldman Sachs & Co. LLC
Maybe we can step back a little bit and talk about America's Best and Eyeglass World. There are two different banners. But maybe it would be helpful to walk us through what the key differences are between the retail banners, what they offer to the consumer, and just your thoughts about – I think remote rollout has been focused first on AB first and then will be Eyeglass World. But what is the path for remote for Eyeglass World going forward?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

So we have 1,200 stores, just over 1,000 America's Best stores. So that's the key part of the business and that is deep value. You come to us to save money and because we bundle in the eye exam. So that is all about savings. Eyeglass World, we have about 120 of those stores, bigger store, more brand focused. You have to pay for the eye exam and there's a lab in every store offering same day service. So it's a little bit more brand conscious, a little bit more speed conscious, still value and still you save money versus other places. But it's more the convenience of the same day service that is sort of driving a lot of the customers in.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

With the competitive landscape, I think it's been pretty clear from your results that it's in line with what we're seeing from other competitors in the space and you're not losing share. But how do you think about the opportunities to gain share? How do your stores compete against online only retailers for example and how have you been able to differentiate that experience for the customer?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

So the online is certainly a factor in our category and it's something we've monitored and even in the – the online category started just over 20 years ago. So, even in the pre-COVID days, that was something that we were competing against. The great news is, the process of purchasing a pair of eyeglasses, especially if you're a value conscious consumer, starts with an eye exam and that cannot be done online and so that is a key source of differentiation for us on that. And once you're standing in our store, having just received an eye exam and gotten your prescription, it's a lot easier, more convenient and you realize the financial savings because you're standing right there. So that's a benefit. It is believed all the data indicates that, during the COVID period, there was a spike in online purchasing. Guess what? People were at home. Of course, that happened. It then went down again and stayed relatively flat in 2022 and 2023. And you see a lot of folks who sort of are – you see some folks who came out saying online eyeglasses are going to be the way to g o, saying wait a minute, this is a product category that people buy in stores and then started opening stores.

One of the pieces of new product news that we're about to launch relates to this. There's a company called Pair Eyewear, which is an online only retailer. And what you do is you buy a base frame like this and then you can buy a lot of different tops to change your look. So it's a little magnetic thing and you can put it on top there. You can do it with sunglasses too, that sort of thing. And they came to us and said, hey, we realized that we're going to be limited because this is a category where people buy in stores and they say, we're not going to build stores. That's not in our competency. Would you like to be the exclusive provider of Pair Eyewear in store?

So we will be launching that in all of our America's Best stores in October, and they'll be doing their marketing saying, oh, you can now go try these on and buy them at America's Best. So it's a way that sort of we can leverage some of the online traffic. But knowing that consumers want eye exams and want the convenience of what stores provide. So you can get one pair of these with two tops for $129, great deal. October, okay, coming soon to an America's Best near you.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

And then just to wrap up the competitive landscape, I asked about online. But how do you differentiate yourself versus mass? Obviously, Walmart and Costco have their optical solutions and that's more value based as well. So what is the differentiating factor?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Key differentiator is the eye exam is free and bundled in with our cost. And most of those models are an independent leased optometrist who gets to decide what pricing they're going to charge and you can generally get two pairs of glasses for an eye exam for us, where often what the independent doctor is going to charge just for the eye exam in other places.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Got it. So, speaking of pricing, obviously, pricing compared to peers, there is a value equation here. I wondered how you thought about pricing gaps, and if there are any areas of your business where you feel like you can take more price without impacting demand?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

So with pricing, it's something that we look at all the time, that is top of mind. However, it is something that is not a broad stroke price increase with our industry. It's more of a scalpel precision that goes into it. And so, when we do pricing increases, we monitor them closely to make sure that what we are increasing prices on isn't driving new customer behavior. What we've seen recently is when we do have customers coming in, they're being a little bit choosier with the dollars they spend. So they're not upgrading to some of the items that they historically upgraded to. So they're not purchasing the nicer lenses, the add-ons such as warranties and things like that. But we do monitor how closely the spend is.

And as we put in place in December to offset some of the Walmart profit gap with our exam pricing. So we increased exam pricing and that was a sticky price increase where we've had continued increased traffic in addition to the increased revenue from the overall pricing increase. So it is something that we monitor, and we evaluate where we are in the market versus our competitors, because we still do want to be able to provide a quality product for a good value. But at the same time, we need to make sure that we're offsetting cost increases that we're receiving and being as profitable as we can be.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Just given some of the softness we've seen in the last couple of quarters with your comp. I think some people are asking about just if it's still the right time to grow stores. And so I wondered if you could maybe talk about how you're viewing unit growth in the short-term. But then also, I think you recently did a white space analysis that noted that you could add even more stores than what you originally thought. So could you maybe walk us through the kind of the shorter view on unit growth and the longer-term?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

So we did at their white space. We talked about that earlier this year. And while we're going through and evaluating our white space, we're also at the same time doing a fleet optimization. And the fleet optimization is a separate endeavor than the white space. That doesn't impact the white space opportunity. However, pruning our fleet is something that we're looking to make sure that we do on an ongoing basis. It is something that we have historically done. However, some of these stores have not met our profitability metrics, so we're looking to take action on those.

The pandemic period, the tolerance coming out of that for how long we would wait for a store to turnaround has certainly changed. And with that, we're taking action on the less than 5% stores that we talked about. As we think about filling incremental white space, moving into 2025, we had talked about opening stores. We'll still be a unit grower. However, we are going to look at opening a little bit fewer stores in 2025 versus what we historically have between the 65 and 75 stores. And one, we're doing that, we're going to certainly be evaluating and scrutinizing each and every real estate site very closely so that we can make sure that these are the best sites that we do open as we go through and do this fleet optimization.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

And that leads us to one of our last questions here about margins. You recently modified the operating margin outlook for fiscal year 2025 from mid-single-digits to flat with 2024, so closer to 3%. We wondered if you could back up a little bit and just talk about your cost structure and how it compares versus 2019. And how long do you think it could take you to get back to normalized margins in the context of this higher cost structure?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

Yeah. So the cost structure, if you're looking at 2019 versus 2024, very different time periods. In 2019, we didn't have the remote capabilities. So we didn't have the increased structure that goes along with managing that. In addition, there have been increases in occupancy. There have been wage increases. And so there have been a lot of cost pressures throughout the years between those two periods. And as we go through and mitigate those cost pressures, we're looking to put in place various initiatives including digitization of our stores, digitization of our back office, so that we can be ever more efficient at executing these processes to be able to get to the margin level that we had historically operated at even if we aren't at mid-single-digit comps. However, mid-single-digit comps is where we've historically leveraged our cost structure, because it is a high structure or a high cost structure with the manufacturing facilities, with the fleet, with all of the retail associates and back office.

And so, as we go through that, when we talked about 2025 with the revision downward in our outlook for the back half of 2024, we had also talked about 2025 would be in line with 2024. And part of that is, as we go through 2024, we are not performing where we had expected to be this year, meaning that we're getting a tailwind from incentive compensation. Because of the performance, we are getting a tailwind currently from that. Next year, we would look to reinstate that incentive compensation. So we'll be facing a headwind next year as we roll into 2025.

With that, there are plenty of puts and takes. We've got the fleet optimization that we're working through which we expect to be accretive to overall margins and that with the headwind of compensation plus we've got or, yeah, the incentive compensation. And we've got other puts and takes that we'll talk about as we release our 2025 guidance. But those are really the big drivers.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Is it possible you can see some kind of improvement in op margin once you do have your store optimization strategy – I'm sorry, evaluation completed or is that 3% more taking into account what could happen with the store fleet optimization?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

There are several puts and takes. And so we do expect the fleet optimization to be accretive. That being said, the incentive compensation headwind coming next year is going to be a substantial headwind that we'll have to offset through other measures.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Okay, okay. We're asking five questions of each company that is presenting at the conference. We've touched upon some of them already, but we wanted to start out asking about just the expectations for the consumer environment in the second half of 2024 relative to what we saw in the first half. Do you expect things for the consumer to be the same, better, or worse?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

We're expecting continuation of the same.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

And then on the topic of margins, which we just kind of talked about, there are other costs, such as like materials and labor and tariffs that I feel like has been a little bit more of a tailwind for the industry at least for the last year. Do you expect this to be the same, better, or worse than 2025?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

We're expecting basically the same in 2025. That's been our planning assumption.

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

And we've made some nice progress in diversifying our supply chain outside of China as well over the past few years.

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

And while we did see the recent information that you all just put out about 2025. We're taking the conservative approach. Until we see things turn around, we're operating conservatively.

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

But we're hoping you're right

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Maybe if I could sneak in kind of a part A on the topic of cost pressures. Tariffs, I do think you felt this a little bit in 2018 and 2019. Can you just quickly remind us how much of your materials were impacted by that and what kind of response, pricing response was the result of tariffs in 2018, 2019?

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

It was about 10% that was impacted by the tariffs in 2018 and 2019. And what we did with that, we had diversified our supply chain and reduced as much as we could coming out of China. And so we expect to be in a better place if we end up in a place where we're having to navigate those tariffs again in the future.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Okay. Our third question that we're asking is just about consumer behavior of looking for value. And again, you cater more towards the lower income consumer who's probably always looking for some kind of value. But we were wondering just your view on is this a cyclical trend, a testament to the macro, or do you think there's been some secular trend how the consumer looks towards value?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

For us, we have always been a value consumer. Our consumer base has always been seeking that. We believe our category is evolving more towards value in a good way. But for us, that's just going to be a consistent over time. That's why people, that's why we exist to provide better value than the majority of the industry.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

And our number four question, we talked about more or less points of distribution. You guys are growing still, so there'll be more points of distribution next year. And then promotionality, we've talked about a little bit as well. I guess relative, do you expect your company to be more or less promotional this year versus last year? And what's your expectation for the industry when it comes to promotions?

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Okay.

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

With promotions, in second quarter this year, we started running more promotions than we had historically been running, and that was in large part to try to determine what was going on with our consumer. Was it that they were sitting out, was it that they were going somewhere else, was it that they were just purchasing different things? And so, with the promotions, we were able to get some incremental data points. And so as we go forward, we'll continue to run some promotions. I think as Reade said with the progressives offer, that was something that spoke to a customer that we had not seen as significantly in our stores. And so we'll continue to run something with the progressives offer going forward. But the two Wise Buys offers that we were running did end in August. And going forward, we'll figure out a new promotion to run.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

All right. That's all we have.

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Well, I have two things. One, as you know, we give out company socks to everyone in our company so that we don't get too focused on this part of the body. And I noticed you weren't wearing socks. And I think these will go really well with those shoes of yours. And two, if I had to just summarize since we have a minute or two left here, remarkably successful for 19 years. The world changed. We realized we had to transform and adapt to the new realities of the market. Champions adapt. We did big hard things like remote. It is in its early innings and is going to continue to get better and better for us. We are trying different new, and different promotions that are driving traffic, although still sometimes not quite the average sale we want, because people aren't buying as many of the higher value lens add-ons as normal. And we're trying neat new product offerings like Pair to leverage some pieces of the online category and get in new and different customers to us. And we think the combination of those things are on the road to help us get back to mid-single-digit comps which deliver mid-single-digit operating margins. And if your economic forecasts come true, that should come true for us. We'll be remaining conservative until we see it really take off. But the transformation continues at National Vision.

Kate McShane – Analyst, Goldman Sachs & Co. LLC

All right. Thank you so much for joining us today

L. Reade Fahs – Chief Executive Officer and Director, National Vision Holdings, Inc.

Good, good.

Melissa Rasmussen – Chief Financial Officer, National Vision Holdings, Inc.

Thank you

Kate McShane – Analyst, Goldman Sachs & Co. LLC

Thank you.