Trading Under the Symbol: ISDR

Transcript of
RCI Hospitality Holdings, Inc.
First Quarter 2018 Earnings Call and Webcast
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Participants
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Gary Fishman – Investor Relations

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Frank Camma - Sidoti & Company
Marco Rodriguez - Stonegate Capital Markets
Ishfaque Faruk - WestPark Capital
Darren McCammon - ProActive Financial LLC
Jason Scheurer – Orchard Wealth & Legacy Management
Steven Martin – Slater Capital Management

Presentation

Operator
Greetings and welcome to RCI Hospitality Holdings Fiscal 2018 First Quarter Conference Call and Webcast. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions]. As a reminder, this conference is being recorded.

It is now my pleasure to introduce Gary Fishman, who handles Investor Relations for RCI. Gary, please go ahead.

Gary Fishman - IR
Thank you, Kevin. Please turn to slide 2 everybody. I want to remind you of our Safe Harbor Statement that is posted at the beginning of our conference call presentation. It reminds you that you may hear or see forward-looking statements that involve a number of risks and uncertainties. I urge you to read it. Actual results may differ materially from those currently anticipated. We disclaim any obligation to update information disclosed in this call as a result of developments that occur afterwards.

Please turn to slide 3. I also direct your attention to the explanation of non-GAAP measurements that we use and are included in our presentation and news release. Finally, I'd like to invite everyone in the New York City area who is listening to join us tonight at 6 o'clock to meet management at Rick's Cabaret New York, Manhattan's number one gentlemen's club. You can also tour its sister club, Hoops Cabaret and Sports Bar, next door. Rick's Cabaret is located at 50 West 33rd Street between Fifth Avenue and Broadway around the corner from the Empire State Building and down the street from Madison Square Garden. If you haven't RSVP'd, ask for me at the door. And right now, looking out the window, the snow doesn't look that bad. So, don't let that be an excuse.

Now, I'm pleased to introduce, Eric Langan, President & CEO of RCI Hospitality. Eric?

Eric Langan - President & CEO
Thank you, Gary. Good afternoon, everyone. Please turn to slide four.

I'd like to start this call again by thanking everyone for sticking with us, for believing in us, and for helping us to maintain the value of our stock. As we promised on our February 14th call, we have been working diligently to complete our first quarter 10-Q in order to get back on schedule by the second quarter.

We are pleased to report that we filed the 10-Q after the market closed today and we are now current with all of our SEC filings. We are also pleased to report another quarter of strong core results. GAAP results were a profit of $1.47 per share. In line with previous announcements we have made, that included a $9.7 million tax benefit due to a reduction in our deferred taxes as a result of the new tax bill. It also included $827,000 in added interest expense, covering debt issuance costs and prepayment penalties related to our new debt refinancing. On a more comparable non-GAAP basis, EPS increased 71% year-over-year, to $0.53 per share, and free cash flow increased 47% to $7.5 million.

Our outlook continues to be positive for the year. Favorable revenue trends have continued to-date, and with our first quarter performance, free cash flow is on track for our recently upwardly revised $23 million target.

Please turn to slide 5 for an analysis of our first quarter operating performance. Total revenue increased 22% year-over-year. This reflected a 16% increase from new units and a 6.9% increase in same-store sales.

There was not a lot of differences between GAAP and non-GAAP operating income. So, for consistency, I'll focus my comments on the non-GAAP results. While revenues increased 22%, non-GAAP operating income increased 44%. That reflected increased operating leverages from higher sales and an overall improved portfolio of clubs and restaurants.

As part of our operating results, we incurred about $500,000 in additional expenses. These related to the cost of transitioning to our new financial management system and work towards completing our year-end audit. The end result was that non-GAAP operating margins expanded 340 basis points year-over-year to 22.5%.

Please turn to slide 6. Sales have been performing very well. Same-store sales have now increased year-over-year for seven straight quarters. Total Nightclub and Bombshell segment sales are also up seven quarters in a row. The largest gains began in the third quarter and fourth quarter of last year. That reflected the acquisitions of Scarlett's Miami and the St. Louis club in the third quarter and the opening of Bombshells 290 Houston in the fourth quarter.

We are working very hard to continue to growing sales year-over-year. Keep in mind, our seasonally strong periods are Q1 and Q2, and that business is generally softer in the third and fourth quarters. Also keep in mind, same-store sales increases go in waves. They go up a period of quarters, then they subside, and then we grow again.

Please turn to slide 7 to review our cash generation metrics. We continued to do very well in the first quarter. Adjusted EBITDA increased 39% year-over-year to more than $11 million. This was the highest quarterly level in the last two years. Actual cash on hand as of December 31st increased 21% to $12 million as compared to the end of September 2017. As noted on our opening slide, free cash flow increased 47% year-over-year to $7.5 million.

Please turn to slide 8 to review our long-term debt. Last call, we showed estimates as to our December 31st debt positions and rates. At the time, we wanted to show you the favorable impact anticipated from our new bank loan. This slide shows you the actual impact, which is very close to our estimates and continues to be highly favorable.

Please turn to slide 9. Here, we show you our debt maturity schedule along with our occupancy costs. The debt maturity schedule is similar to what we showed you on our last call. As you can see, our amortization and the few relatively small remaining debt balloons are very reasonable for us to handle, given our cash flow. If you recall, we calculate occupancy expenses, one of our largest cost areas, as rent plus interest as a percentage of revenues. As you can see on the slide, although we have acquired additional clubs and underlying real estate with debt over the years, our occupancy costs have dropped dramatically. They were 9.4% in fiscal 2014, and as of the first quarter, they were down to 7.7%. As we sell off non-income producing real estate and make the Scarlett's balloon payments, we should see occupancy expenses decline a little more.

If you'll please turn to slide 10, we'll review our capital allocation strategy. As you know, there is a key metric we look at to determine whether to buy, open or close units, buy back shares or pay down debt. That is our free cash flow yield on our market capitalization. At the target $23 million free cash flow for fiscal 2018 and the recent $28 stock price, the yield works out to about 8.5%. According to our capital allocation strategy, if the yield is in double digits range, we would likely buy back shares. If it is below that, we would likely buy or open new units, but only if we can achieve our cash on cash returns of 25% to 33% buying strategic rationale.

Now, for the longest time, we have been saying that the stock would have to be trading at substantially higher prices for to be worthwhile to pay down even our most expensive 12% debt. At a 37% effective tax rate, the after tax yield on paying down 12% debt was 7.6%. With $23 million of free cash flow, that would be like buying back stock at $31, some $3 above our current market price. However, the new tax law changes that dynamic. With our effective tax rate at 23%, the after-tax yield is 9.2%. That's like buying back shares at 26, $2 below current price. That's far more attractive. This is not to suggest that we'll necessarily pay down our debt faster, but it shows you the rationale fits with our capital allocation strategy.

Please turn to slide 11 for an update on how things are going so far this year. The second quarter is continuing to do well from a sales point of view. As we mentioned in the last call, January was good despite tough weather in some markets. February was good primarily due to traffic benefiting from the pro football championship in multiple markets. We are hopeful about March with something like half a dozen major college basketball tournaments in New York City and Charlotte, where we have a total of four clubs, including two of our largest ones.

As I mentioned on previous calls, we have three new Bombshells in the works in the greater Houston area. The Pearland unit, which will be our largest Bombshells ever is now just awaiting the gas hookup. We continue to target opening it by the end of this quarter. The other two Bombshells, one on I-10 and one on the Southwest Freeway, continue to be slated for opening in the fourth quarter of this fiscal year and the first quarter of fiscal '19 respectively. For modeling purposes, all three are likely to open towards the end of their respective quarterly periods.

As for operating expenses, we still have some residual costs for IT transition and year-end audit. I continue to hope to see more normalized operating expenses by the third and fourth quarters. Insurance costs were up 34% year-over-year in the first quarter versus 22% sales increase. We've already started to work on ways we could potentially reduce this expense. We've also begun to see salary and wage pressures around the country, so we will have to be cognizant of that as well.

On the upside, the new tax bill is already helping the bottom line. During the first quarter, we had a gain of $9.7 million. Excluding that, our effective tax rate was 25.4%. Some of our analysts may still be using a higher effective tax rate. For the full-year fiscal '18, we anticipate the effective federal tax rate of 24.5% and the total effective tax rate of 26.5%, which includes state and local taxes.

To wrap up, I'd like to review our three-year goals for any new investors on the call. So, please turn to slide 12.

One, we want to grow our free cash flow per share at 10% to 15% on year average and grow our total free cash flow to approximately $30 million. Two, acquire more great clubs in the right markets. On average, over the years, we have made more than one club acquisition per year and we are currently in discussions with multiple potential candidates. Three, continue to expand the number of Bombshell company-owned stores. Our target is three per year over the next three to five years, which would give us a total of 14 to 20 units. And four, while we are in growth mode, we will not be pressured into deals that we don't like for the sake of growth. We will work to make sure that each new acquisition or restaurant is right for us, that it meets our requirements and adds to achieving our long-term goals and not add undue risk or stress on our systems.

Thank you for listening and thank you to our staffs around the country for all their hard work and for all those that were involved in closing out the quarter and making us current with the SEC.

Now, let's open the call for questions.

Operator
[Operator instructions]. Our first question today is coming from Frank Camma from Sidoti. Your line is now live.

Q: A couple questions if we could flip back to slide 11. First, right at the top, the college basketball events, you were talking about the March Madness. Will it be different from last year, like as far as the timing, is that why you are calling this out or is it wasn't in the New York—

Eric Langan - President & CEO
Yes. We picked up a few more. The Big Ten, Big East, and NIT in New York. The ACC is in Brooklyn this year. So, there are a few more tournaments than we're normally used to.

Q: Okay. I see. So, you'll have a benefit of that.

Eric Langan - President & CEO
Good for us. Yes.

Q: And the second question is on Bombshells. How has the trend been with the one that you most recently opened? Did you go through that typical trend of a honeymoon period and sort of sell—I don't know if you call it sell off, but like where the revenues sort of—

Eric Langan - President & CEO
I'd called it drop-off. The drop-off has been compounded a little bit with freeway construction on the weekends. And I think once that freeway construction is completed that we are going to get, I think, a second little honeymoon period at that location. But, I think, it'll decline a little bit here, but then I think it will pick up considerably when the road closures are going to be done. But, I know they are moving traffic on the weekends. They are flipping it from the old roads to the new roads right now and they'll go tear down the old roads and rebuild and then finally get it all done. But, I think, we should see some pretty strong return in probably May and June as that construction at least stops being on the new and moves to the other side.

Q: Okay. And when you are talking about insurance cost, is that property insurance or liability insurance? I was just trying to figure out what type of insurance we're talking about.

Eric Langan - President & CEO
Yes. It's a little bit of everything. Mainly, we're seeing an uptick in our liability cost per thousand dollars of revenues. And so, we're in the process of looking at a few other options including some type of captive that we'd operate ourselves. So, there are several—

Q: You have like reinsurance behind it basically.

Eric Langan - President & CEO
Exactly, yes, we would basically. So, basically right now, we self-insure the first $100,000 of all claims. But, what we would do is maybe some kind of captive where we would maybe self-insure the first $1 million of all claims through the captive and then reinsure on top of that.

Q: Okay. And my last question is to salary and wages, because, I mean, the nice thing is exclusive of the Bombshells and you're somewhat insulated from this in the fact that a lot of your entertainers are not employees, right, for the most part. But does it put wage pressure on the group as well since there is competing forces there? Can you just talk about that?

Eric Langan - President & CEO
I think with our actual club level employees, there are not a lot of wage pressures; it's more upper management or office and clerical staff. A lot of our club employees work on tips. So, obviously, the clubs are busy and we're grossing more money. Our employees are tending to make their share of the money as well. So, their pressures are not directly related to us but more on the customer experience.

Q: Okay. So, it's not as extreme as other restaurant companies would have, obviously, because that's a direct hit.

Eric Langan - President & CEO
It's like I said, it's just more management based and non-tipped employee base.

Operator
Our next question today is coming from Marco Rodriguez from Stonegate Capital Partners. Your line is now live.

Q: Hi. Yes. This is Marco Rodriguez from Stonegate Capital Markets. Thanks, guys, for taking my questions here. I just wanted to dive in a little bit more on the Nightclub side, the same-store sales obviously really strong here for last three quarters for you guys. Are there any sorts of clubs that are helping drive this that are showing some really strong same store sales or is it kind of broad-based, any color there?

Eric Langan - President & CEO
It's fairly broad-based, I'd say in the 3% range. We are getting the bonuses. Tootsie's in Miami is doing extremely well for us. And we have a few other clubs here and there that are coming back a little bit stronger. The Odessa clubs, for example, year-over-year. Oil is back up, so we are seeing some nice increase in that market year-over-year. But basically, it's just about everywhere. I mean, we are seeing some nice increases everywhere.

Q: And are you seeing the spend in the Nightclubs? I mean, the spend being driven more on the service side or are you seeing kind of a better mix from food and beverage, any sort of color there?

Eric Langan - President & CEO
Well, we are seeing it everywhere. Obviously, the service revenues are higher. You can see in our breakdown an increase year-over-year on service revenues, which is our high-end spend. But we are also seeing more bodies through the door in our blue collar clubs which helps their numbers. So overall, I think it's just generally people are feeling better about going out and having more fun and little more secure that their paychecks are going to be bigger, or of course we have more employment out there. So, as that continues, I hope to see our numbers continue to grow, and maybe we can keep a nice streak of same-store sales growth going. We are

seeing a very strong quarter so far in January, February and March. Typically, we run strong through about mid-April when tax time hits. And then we get a little bit of a slowdown and hopefully we will see that nice recovery in May like we are supposed to, then we keep it running all the way through the summer.

Q: And then, in terms of Bombshells, just wanted to clarify here the timing of the Pearland open. I think I heard you say in your prepared remarks that the three additional Bombshells that you will be opening will be end of quarter. So, should we be thinking that there's really no impact in the quarter from a revenue standpoint?

Eric Langan - President & CEO
Correct. I think our goal right now is to hopefully be open around the 27th, do a soft opening of Pearland around the 27th. So yes, you won't see any real revenue till the April, May, June quarter. And the way that everything is pushing now, we were wishing to go to the beginning of the quarters originally, we were going to open in January but with the hurricane in Houston and the flood issues and of course the amount of workers, not being able to get construction workers because of so many insurance companies spending so much money to have people tear out houses and do flood remediation, we basically are pushing everything about 60 days. So, instead of opening at the beginning of the quarters we are probably going to be opening in the end of those quarters is what we are looking at right now.

Q: And last quick question, I know on the last call we talked a little bit about the franchise opportunity, I think in your response to one of my questions there you thought you might have some more of an update in terms of the franchise opportunity going forward, maybe now if not by end of May. Just kind of wanted to follow up to see if there are any changes there.

Eric Langan - President & CEO
Yes. There has not really been much change and we're really cutting back our expenses, we're cutting our costs, we're not really spending much money pushing franchising right now. I think until we see restaurants as a whole and casual dining as a whole rebounding that there is not going to be much interest for other groups to come in and open our restaurants at this time. We're going to focus on our own core operations, spend our money on that, maybe take some of the money we were spending on franchising put into some more marketing, especially in the Houston market where we are becoming very dominant as we open these next three stores, and we're going to focus on that right now. We are still registered; we're going to stay registered to sell franchises. And if something comes along, we're definitely willing to talk to people, but I just don't think that's where our management energy and focus should be right now. I think we should be focused on our core stores and opening our own new stores at this time.

Operator
Our next question is coming from Ishfaque Faruk from WestPark Capital. Your line is now live.

Q: A couple of questions for me. In terms of Bombshells, the same-store sales were a very big uptick. Is it like seasonality or was it like one-time things or—

Eric Langan - President & CEO
If I had to blame on any one thing, I'd have to blame it on the Houston Astros.

Q: Just like Houston Astros or there is a little more too it.

Eric Langan - President & CEO
Yes, the Houston Astros definitely made a big difference all those home games and away games, both were big for the restaurants. The city was definitely behind the Astros and out in force watching the games and what not.

So, I'm hoping, as opening day hits, I think April 2nd in Houston, the restaurants will see a nice uptick coming in April again from the Astros being back to playing.

Q: My second question, Eric, you mentioned in your prepared remarks and the slides that you are looking at the right clubs and the right markets. Do you have a sense for geographical limitations in terms of acquisitions that you are looking at right now?

Eric Langan - President & CEO
We're looking close to where we already operate of course, and then just new markets where we feel that we can buy the number one or number two clubs in the market and get a nice foothold in. That's really what we're looking at right now. But, we're looking at everything, I mean, right now, it's about pricing and our management team is very, very strong. We've closed some underperforming locations and what not, so our guys aren't stressed right now. So, really we could do an acquisition anywhere, provided that the numbers make sense.

Q: Okay. In terms of the size of the club, are the clubs skewed primarily towards higher-end clubs or is it like across the board?

Eric Langan - President & CEO
We're looking at everything right now. Like I said, right now, it's more about pricing and getting the return. Obviously we favor the larger Scarlett's type acquisitions. But the St. Louis acquisition, at $4 million, was still a very good acquisition for us. And so, we'll look in all those price ranges. I think, anywhere right now we would probably be looking at $1 million to $40 million in acquisitions, whether it's multi-club or single club. Those are the kind of numbers we are looking at that's easy for us to do right now. We have bank financing for the real estate side of it, and then some cash on hand right now to do the rest, and our debt is very easily manageable.

If we sell off a few pieces of this non-income producing real estate, hopefully we can eliminate this additional $250,000 in payments to take our loan to value down to 65% on our existing real estate, which will free up $250,000 a month in cash as well. So, there are a lot of opportunities over the next few months as we kind of get used to this. And as I said, we just have to get back to normalized expenses. The 10-K being late and the extra work and focus on all of that was a lot for our internal accounting people and for me as well. So, we had management basically focused on operations, existing operations and kind of put acquisitions on hold.

But, we've been talking with people, with candidates, and we'll get very, very serious as we move in, now that we are current again and we are back to a more normal flow. We're used to our new accounting system, because even our accounting systems took management's time as well, changing systems and getting used to the new way we have to do things. With all of that, I think it should normalize through the end of this month to the end of March. And as we move into April, I think we are going to be ready to be back out there and getting very serious about new acquisitions. We have got two Bombshells under construction right now. Pearland is almost finished. I-10, we are getting close to pouring foundation, and we will start putting steel up here in the next few weeks. The building permits are on second review, I think, first or second review, I think they're coming to second review in the city for the 59 location. And so, if everything goes right, we will start construction on that property in early April, which should put us open in November, but maybe December depending on weather this summer.

Operator
[Operator instructions]. Our next question is coming from Darren McCammon from ProActive Financial LLC. Your line is now live.

Q: Hey, guys. Not to sound like a broken record, but congratulations on another fine quarter.

Eric Langan - President & CEO
We are trying. We want to keep that broken record playing.

Q: I want you to too. Along those lines, okay, so, you've had seven in a row here. You talk a little bit about lapping yourselves in Q3 and Q4. In other words, your numbers getting a little tougher. What can you do to make sure that those are same-store sales increases also?

Eric Langan - President & CEO
Well, like I said, hopefully the Astros are going to help us in Q3, which have helped with the Bombshells. We are just going to keep doing what we are doing and we hope the economy stays strong, and as the big customer spend continues. Obviously, if the big customer spend dries up, there is not a lot we can do to bring the big customer spend in. We can, if we actually go to recession, we can go into discounting and stuff we have done in the past, but right now I think that everything is hitting on all cylinders. I just want everyone to be prepared. It's very rare that we just continue to blow it out, and blow it out, and blow it out. So, I just want everybody to be prepared for that one quarter or two quarters where we step back a little bit. I don't think it will be this quarter. January, February and March has been very strong for us.

And I anticipate moving forward, there is nothing out there that scares me right now, but I just don't want everybody to think this is going to be the norm that we are going to keep doing 6% or 7% same-store sales increases. It could easily fall back down to the 3% range, which is, I think, a little more normal and we can have a hiccup here or there depending on if there is a big sporting event or something in the past or a big fight or something we had in the past that we don't have in the quarter going forward. But overall, everything has been very strong. And I think we are going to continue to do that, but I just don't want people to get so used it that it shocks if we have an off quarter.

Q: Okay. So, what I heard is you guys are expecting 8% to 10% increases going forward?

Eric Langan - President & CEO
Yes, I wish. No, like as I said, I think, we will return to a more normalized 3%. The Bombshells in this quarter I don't think will be as strong as they were in the last quarter. I mean, the Astros definitely made a big difference. But, as we open up the new store and we're going to start some new marketing in Houston that we've never done in the past, maybe we will see some increases again going into the summer. We're going to try to make a pretty decent push going into the baseball season this year.

Q: Okay, I heard you. I won't get too crazy on the modeling. So, you had scheduled basically the LD Micro Conference and it got canceled because of the fires?

Eric Langan - President & CEO
Yes.

Q: Are you planning on doing any road shows or conferences like that this year?

Eric Langan - President & CEO
We're going to be at the Sidoti conference in March here in New York. We're still talking about whether we are going to go out to LD in June or not. We don't normally do that summer conference, but we're thinking about it very seriously right now. I haven't had a chance to talk to Chris to find out exactly what the deal is going to be on the summer conference, but I'm thinking about that one as well. And definitely, we will probably be out in April and May on some non-deal road shows, meeting with some investors in specific markets, just try to get the story out there again and get everything ready, especially as some of our acquisitions heat up, we want to make sure that were keeping attention on the stock.

Q: And you had mentioned the 12% debt or 11.8% debt. Is there any reason why you couldn't pay that off early?

Eric Langan - President & CEO
No.

Q: If you wanted to?

Eric Langan - President & CEO
We can definitely pay it off. In fact, we used $2.9 million of the bank loan to pay off $2.9 million of the 12% debt, and we kept the amortization schedules, the payment the same. So, rather than keeping the amortization schedule long, we've shorten the amortization schedule by keeping the same payment on the debt as if we hadn't paid off the $2.9 million. So, we are accelerating that 12% debt. It just makes sense. It's not quite 10%, but it's close enough to 10% return on our money that we're definitely watching it and paying attention to it. And we have a ton of cash. I mean, by the time we did the loan, we were sitting on almost $15 million in cash on hand. So, I think as long as we stay in the $12 million to $15 million range, we probably won't accelerate that. But if we start getting more than $15 million cash on hand, where it's sitting in the bank, not earning us any interest at all, we will probably put that to work because we can always go and borrow the money again.

Q: So, that actually leads me to my next question. If you got $15 million now and you got $10 million coming in real estate sales and another $23 million in free cash flow, I mean you are looking $40 million plus by the time this year's over.

Eric Langan - President & CEO
You're e little high on all that cash. Remember, we have to service the debt. So, we have a $3 million balloon payment in May and about $8 million a year that we service. So, that's about $11 million in debt servicing we have to do out of that $23 million. And we have to sell the $10 million in real estate and we have to pay off some debt against that $10 million in real estate. It's not all free and clear. You say $40 million. I've seen an article you did and I think we are probably closer to $25 million year-end if we do nothing. Just because we have to service that debt and we have some debt against that real estate.

What we hope to do is sell that real estate, pay 100% of the proceeds to the loan, so that we can get down to 65% LTV and drop that payment from $870,000 or $825,000, whatever it is, down to about $500,000 and some thousand so we free up that quarter of a million dollars every single month on a go forward basis. And then, our debt service won't be $8 million and it will drop down to about $5 million, which will free up free cash flow on a go forward basis or give us that money to take on additional debt if we want to do acquisitions with, without actually increasing our debt load.

So, those are the things we are looking at right now. But yes, to answer your question, we definitely are going to have to by end of the year, consider paying off a considerable amount of our debt or making some acquisitions. And of course, acquisitions are our preferred method to use that cash. Because I'm not going to sit around with $25 million cash in the bank, I mean, that doesn't make a lot of sense for us when we have 12% debt that gives us almost a 10% yield.

Q: Nice problem to have, huh?

Eric Langan - President & CEO
Exactly. We have worked hard to get here, and we've stayed the course. Trust me, there are a lot of deals popping up at me that are tempting, but just not quite right. They want a little too much money for them and they

want to me stretch and we are going to just sit here and wait, and if they want to come to us and be in our model, great. We are not really ready to stretch too much yet. We may start stretching a little though—3.5 may become a more norm than 3 if the market is rewarding us for the growth. But, I don't see us getting to crazy numbers, which could put us to 4.5 only if it's a very specific acquisition with great grandfathered licensing, no competition, and those types of things. So we may look at raising our prices that we are willing to pay a little bit, but we are just not there just yet. The markets are going to have to see that there's a definite reward for that.

Otherwise, I think we're just going to stay here, stay in our three times model. There is plenty of stuff out there we are looking out right now in that price range. And we have just been busy with the Q and the K and the new accounting system and everything to keep pushing them down the road a little bit. We are down the road. You are going to start seeing us be more active I think through March, April, and May. I don't know when we'll actually get something papered. It does take a little time. But, we are actually going through financial statements of acquisitions now where we haven't been able to, because our financial people have been very busy. But that will start over the next few weeks. We have several coming in over the next week or so that I finally made requests from the brokers and the sellers and said give me the information, we're ready to start looking. So, we will start looking very hard. We will start doing some negotiations. And in the past, we've been able to close several deals, so I'm sure we will continue to do so as we move forward.

Operator
Our next question is coming from Jason Scheurer. Please proceed with your question.

Q: I just wanted to first compliment you on your capital allocation strategy. I pretty much feel like if you went up to every CEO out there, I don't even think one in ten would be as committed to it as you guys have been over these last couple of year—

Eric Langan - President & CEO
It took us a long time to get here. It's a learning experience. But, once we've gotten used to it—and of course we had to build the cash flow. We have so much cash flow; we have to be careful with it. Otherwise, like we did for three years, where we kept growing and growing, but our stock kept going down, and we were doing deals to do deals, we weren't doing the right deals. And so, now, we are very focused to make sure we do the right things. We want to add to the cash. What really got me started on it is someone told me one time, "Take risks to get rich, not to get poor." And I started looking at some of the things we were doing and we were taking risk and we weren't making money from it. So, to me, that's taking risk to get poor. We don't want to do those things. So, I appreciate it. We're going to keep working on it.

Q: Yes. Let me just circle back to this thing here. How many Scarlett's type of operations are out there in the space?

Eric Langan - President & CEO
I don't know, I mean Scarlett's types clubs that do $15 million?

Q: Yes.

Eric Langan - President & CEO
Maybe 50, 100, 150, I don't know. The problem is none of the clubs give you their data. So, it's hard to tell. The data is not public. I didn't realize Scarlett's was doing as much money as they were, till I got all their numbers. And they were doing considerably more a few years back. So, I mean, there is more than we know about for sure, and we're starting to find out about a few more. And now we've done an acquisition in that price range, we are getting guys with some bigger clubs that are getting older that are giving us calls and saying, "Hey, do you think we could do something on this club?"

I think there are a lot more clubs that are making a $1 million to $3 million a year for sure that we can pick up for $3 million to $9 million, $10 million, plus the real estate values. They are probably a lot more of those deals out there than the big Scarlett's deals. But, I know, there are more Scarlett's deals out there for sure. And I know a few of them. We've actually talked to owners that just aren't ready to sell yet. So, we're definitely keeping our eye on it. And, I think, if guys get ready, hopefully we will be their first call.

Q: I'm assuming with the Bombshells that you guys are working on, I'm assuming all of them are out of the flood plains, so that we don't have to worry about that again if there is any other problem come a year from now.

Eric Langan - President & CEO
Well, none of our Bombshells flooded. That was the beauty. It did get right up to the doorsill on our Southeast Houston location, but nothing got in the building. Yes. I mean, where we are, we actually have flood insurance now because the new bank loan requires it, on four of our properties and none of them are the Bombshells locations.

Q: Do you see any limit to like how many Bombshells that you guys would actually be owner/operators of?

Eric Langan - President & CEO
No. I don't think we're going to do more than three or four a year but at the same time I don't think there is any limit to how many we can operate. I mean, the nice thing about restaurant operations, there is a lot of restaurant management out there and a lot of guys we can hire to help us run restaurants. Actually it's more difficult and not as difficult. How is that? Because there are just so many more people, it's a much more complicated business than our clubs, because of the food service and the quality of food and those types of things, and there's more employees, period, than say our typical club. But it's something we've learned over the last five years. And I don't think we would have any problem. In fact, the more restaurants we have, I think they become easier and easier to operate just like the clubs. When you have three restaurants, you lose a manager, it's a third of your staff. When you have 30 restaurants, it's 3% of your staff. So, you have plenty of other people to call out and step up when you are larger.

Operator
Next question is coming from Steven Martin from Slater. Your line is now live.

Q: Couple of questions. As you add the Bombshells, do you expect to get leverage within the Bombshell system because you are adding a high percentage of units?

Eric Langan - President & CEO
We are already seeing that with some of our food purchasing. We are seeing some of that with our liquor purchasing, especially the liquor combined with the clubs. So, I'd say, definitely, we will pick up more and more leverage as we are selling more and more of our product and hopefully be able to negotiate better prices, and if we can't then our menus may change up a little bit and we will use products where we get that leverage. And definitely with management, we are paying a director of operations for our restaurants to oversee five restaurants right now when he could oversee 15 easily. He needs staff underneath him, but I think that as we have done with the clubs, we will continue to grow more and more free cash flow with less and less corporate overhead costs.

Q: Is there an update on the New York market? I know some clubs have closed and you had the 60-40 thing hanging around. What's going on in the New York market?

Eric Langan - President & CEO

Everything is rumors. Like you said, it's fluid right now. There are clubs that have gone. I don't think anybody new is opening. The city would definitely not allow that at this point under a 60-40 deal. I have heard that they are going to give them until January, this coming up January, to get in compliance through one group but then I've heard another group say that the city is going to do something sooner. I think their cases are out of court. Unfortunately, we're not involved in any legal aspects of it, so I don't know where the lawyers are. I think they have a federal case going now or something, I've heard. A couple of groups have or a couple people have, but I don't know that's the clubs or the bookstores. It's very hard to get information because everybody is being pretty hush-hush about it because obviously they don't want competitors to know what's going on, or their own employees and what not as well. I will say, I don't think that the 60-40s three years from now will still be around. I think they will at some point have to close their doors. The city definitely has got the legal power to do so. It's just a matter of now creating the willpower to do so.

Q: And one last one, when you look out at acquisitions now that you're sort of refocusing, when you look geographically and by type, what are you thinking about?

Eric Langan - President & CEO
We are looking at the East Coast of course. We like the East Coast better. We are definitely not looking much in California at all. We are not looking in Texas a whole bunch. We'd like to build more brand recognition, more revenues in Florida. Florida is a great market for us. Even though Tootsie's is a big portion of it, I think we would definitely do more in Florida. But we're really looking all up and down the East Coast. We're looking in Central U.S. right now, a couple of smaller locations similar to the St. Louis type location. But, basically, we're looking everywhere. We do have some Western United States stuff on the table that we are looking at, but basically right now, we're going to look at what makes the most sense as far as cost, ability to finance, using some of our cash. If we're getting a really good deal on it, we'll put up more cash obviously. But obviously, the less attractive the deal is, the less of our actual cash we want to put up because we want to stick with that whatever cash we put in. We want to make that money back in three or four years, so we can turn around and do it again.

Q: Just as an aside, I think you've done a great job on managing the cash. And I don't think any of us have a problem with you sitting with a little extra cash while you are waiting for the right pitch.

Eric Langan - President & CEO
We are not really sitting on too much extra right now. I mean, even at $15 million, we're up to about $8 million in operating cash now with Scarlett's. Scarlett's is a big cash operator, and the New York clubs are big cash operators. Of course, we own all of our own ATMs, so there is several million of float in the ATMs as well. So, I mean you are talking about $7 million in extra cash if we get to $15 million. But we have the $3 million balloon payment coming up in May, so we want to make that out of cash flow without borrowing money again. And I call that kicking the can down the road, so to speak, because basically we've taken over Scarlett's.

We only have $2 million in Scarlett's right now and that's the payment we made in November because we borrowed 100% of the funds to buy Scarlett's. And so, it's time to build some equity up in Scarlett's a little bit. So, we're making the free cash flow out of it. So, basically we're going to use that cash flow to make those balloon payments. And I like those types of structured deals because we get a nice look at those deals and the leverage is fantastic for us. And if we get into a jam, we have the free cash flow to cover any of these type payments that would come up, especially now if you look at the debt schedule you'll see, everything, all of our balloons until 2022 I think are all related to Scarlett's, the $5.4 million and the $3 million are both Scarlett's related.

Q: And I'm betting to that some of those debt-holders would be very happy if you extended it?

Eric Langan - President & CEO
Yes, they will. I'm sure.

Q: All right. Thanks a lot and great quarter.

Eric Langan - President & CEO
In extending them, but I don't see us hurrying to pay them off either. We're just going to ride it out and pay them when they become due and continue to build the company.

Operator
[Operator instructions]. If there are no further questions, I'll turn the floor back over for any further or closing comments.

Gary Fishman - IR
Thank you, Eric. Thank you, Kevin. We've included a couple of supplemental slides in our appendix. Slide 14 is our calendar. A few things coming up. For those of you who dialed in a little bit later, tonight, you can meet management at Rick's Cabaret in New York from 6:00 to 8:00. It's at 50 West 33rd Street between Fifth and Broadway. If you haven't RSVP'd, ask for me at the door. We will also be providing tours of Hoops Cabaret and Sports Bar next door.

And as Eric mentioned during the call, on March 29th, we are scheduled to present at the Sidoti conference in New York City. Registration is free for professional investors. We encourage our tri-state area professional investors to attend our presentation or sign up for a one-on-one. For those based out of town, we would like you to consider it as a reason to come into New York City to see us and other interesting small-cap companies. To make it worth your while, we are also considering having a meet management that night at Rick's. And on April 10th, we will be reporting second quarter Nightclubs and Bombshells segments sales.

On behalf of Eric, the Company and our subsidiaries, thank you and good night. And as always, please visit one of our clubs or restaurants. Thank you.