Operator

Good Morning and welcome to the Innovative Food Holdings Second Quarter 2024 Earnings Conference Call. My name is Ronit Wallerstein and I'll be moderating today's call. With me on today's call for Innovative Food Holdings is Bill Bennett, our CEO; Brady Smallwood, our COO; and Gary Schubert, our CFO. Throughout the conference, we will be presenting both GAAP and non-GAAP financial measures including, among others, historical and estimated EPS, adjusted EBITDA, which is net income before costs associated with amortization, depreciation, interest and taxes, and excluding certain one-time expenses; and adjusted fully diluted earnings per share, using the weighted average shares outstanding for the quarter ended 6.30.24.

These measures are not calculated in accordance with GAAP. Quantitative reconciliation of certain of our non-GAAP financial measures to their most directly comparable GAAP financial measures appear in today's press release.

I would also like to remind everyone that today's call will contain forward-looking statements from our management made within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended, concerning future events.

Words such as "aim", "may", "could", "should", "projects," "expects", "intends", "plans", "believes", "anticipates", "hopes", "estimates", "goal" and variations of such words and similar expressions are intended to identify forward-looking statements. These statements involve significant known and unknown risks and are based upon a number of assumptions and estimates, which are inherently subject to significant risks, uncertainties and contingencies, and many of which are beyond the Company's control.

Actual results, including without limitation, the results of our Company's growth strategies, operational plans, as well as future potential results of operations or operating metrics (and other matters to be addressed by our management in this conference call), may differ materially and adversely from those expressed or implied by such forward-looking statements.

Factors that could cause actual results to differ materially include, but are not limited to, the risk factors described and other disclosures contained in our filings with the Securities and Exchange Commission including the risk factors and other disclosures in our Form 10-K and our other filings with the SEC, all of which are accessible on www.sec.gov. Except to the extent required by law, we assume no obligation to update statements as circumstances change.

With that, I would like to turn the call over to Mr. Bill Bennett. Please go ahead.

Bill Bennett

Hello everyone and good morning. I'm happy to welcome you to our Q2 2024 earnings call.

Hopefully you saw the press release this morning with some highlights from the quarter. We will also file our full 10-Q shortly, for your reference.

As I've mentioned several times before, we remain in the "Stabilization" phase of our three-phase plan. Accordingly, we mentioned last quarter that Q2 would be our toughest quarter of the year from a revenue perspective, and in fact, our Q2 results reflect those expectations. Total revenue declined 10.1%. 62% of this decline was driven by our intentional ramp down of the direct to consumer e-commerce business, which saw a 52.2% decline. 37% of the decline was driven by our Specialty Foodservice business, which declined 4.3%. We've continued to face headwinds with a large customer's technology platform transition, which we have very few levers to address, while the majority of the remaining core business continues to advance nicely. Our Artisan Specialty Foods business in Chicago continues to grow in the high single digits, as does our business with Gate Gourmet. Between the growth in these other core businesses, and the other incremental growth we're expecting, we continue to be on track to grow Specialty Foodservice revenue in the back half of the year.

Let me offer a bit more color around the three buckets of incremental growth mentioned in the press release.

First, we're making progress with the newly announced customers. We announced that one of these was a top five U.S. broadline distributor. With this customer, we launched the business with our non-perishable items, which have gotten off to a strong start, and we were very excited to hear recently that they're now pulling in our perishables assortment, which will further accelerate our growth trajectory with them. As we've said before, this business has the potential over time to grow to be as large or larger than the business we have today with U.S. Foods, so it remains a top priority and area of focus for us.

Second, we continue to uncover new opportunities to leverage our platform in new channels and with new customers. As an exciting example, we recently launched a ten store test with one of the largest retailers in the U.S. where we are managing their gourmet cheese assortment. Similar to our other large customers, this sales channel would require little to no marketing, a very small amount of capex, and comes with a built-in base of customers. Retail does require lower margins than foodservice, but it also provides immediate scale since shelf space guarantees awareness and sales. This is a sales channel our leadership is deeply experienced in, so it's great to see our network and experience bring new opportunities to the company. It's also exciting to see that although we are selling off our igourmet.com business, we can still leverage our cheese sourcing and processing capabilities to grow business in other sales channels. This opportunity too could be as big or bigger than the business we have today with U.S. Foods.

Third, we're seeing growth from our reallocation of resources as we shift focus away from our consumer e-commerce business. These changes are driving sales increases at our business with

Amazon, the airline caterers, and within our Chicago Artisan Specialty Foods business. Brady will speak to some more details here.

Now, as our specialty foodservice business gets back to growth in the back half of the year, the progress we're making on margins and SG&A will start to bear fruit. We continue to pay close attention to our pricing and sourcing efforts, and while GAAP gross margins declined 41 basis points as we've been clearing out inventory related to the sale of the igourmet.com business, our adjusted gross margins increased 36 basis points this quarter. Similarly, GAAP SG&A as a percent of sales weakened 62 basis points, but after removing non-cash expenses such as stock compensation and depreciation and amortization, it actually improved by 166 basis points. It's tough to achieve SG&A leverage while revenue is on the decline, yet we're achieving it with the scale of savings we're delivering. So we're putting in place the right business model that we expect will generate profit growth as our revenue returns to growth.

Brady and Gary are going to speak more about the details of the igourmet.com transaction, but I just wanted to highlight here what an important strategic step forward this is for the company. In the 6 years that IVFH has owned our consumer e-commerce businesses, we've lost in excess of $12M. To put that in context, that far exceeds our entire outstanding long-term debt as a company. Removing that profit headwind is a critical step in our evolution and turnaround efforts. When I got here, this was the main focus of the company's efforts. Go read the press releases from that time period – everything was focused on the consumer e-commerce business – the people, the marketing dollars, the growth efforts. I remember a leadership team dinner early on in my tenure where the team was discussing a new growth idea for the consumer e-commerce business. I started pushing them on how much time they'd have to invest to bring it to life, how much it would actually drive in sales if we were successful, and ultimately how much money we'd make, and we agreed it would bring in less than $3,000. I couldn't believe I had 8 people around a table brainstorming ideas for driving only $3,000 in profit on a business losing millions of dollars, but that's where they had been asked to focus. Contrast that with how we operate today. I sat through hours of our weekly Monday meetings this week, and not once did I hear anybody even mention the e-commerce business. We are fully focused on growing the profitable, meaningful parts of the foodservice business, and we're doing it with a third less people than we had a year ago.

With the sale of igourmet, we've now completed the divestiture of the businesses we set out to eliminate. Of the 10 operating businesses I inherited when I took this role, we have now closed or sold off 6 of them, including: igourmet, Mouth, plantbelly, Grow Brand Management, the Haley Group, and Food Hatch. In fact, as a funny aside, I recently looked at the back of my business card where I have these brands listed, and realized I need to remove 6 of the 10, as well as change our headquarters address on the front of the card. I guess it's time to get a new business card!

I wanted to wrap up by thanking our board for facilitating the recent stock transactions to cover taxes on the leadership team's stock grants. It's great to see their continued support and confidence in the future of the company.

Now I'll turn some time over to Brady to talk in more detail through some of the specific actions we've taken in the operation of our business this quarter. Brady?

Brady Smallwood

Thank you Bill, and good morning everyone. Today I'll provide some updates on a few of our major transformation initiatives, including ecommerce, resource reallocation, M&A, and sourcing.

Since I joined, I've consistently shared updates on our evolving consumer-focused ecommerce business, and as highlighted in our recent press release, we signed a definitive agreement on August 6th with a strategic buyer for our last remaining direct-to-consumer business, Igourmet. We anticipate closing by month's end, followed by a one-month transition period during which we'll temporarily serve as a third-party fulfillment provider for the buyer. The assets in this transaction primarily include digital assets and the customer base, while we retain our warehouse, supplier relationships, and inventory, which we can continue to leverage in our B2B sales channels.

As Bill mentioned, shedding these brands has allowed us to reduce SG&A overall but also reallocate resources to our foodservice business, where we see multiple opportunities for profitable growth. A prime example of this is the revitalization of our previously stagnant Amazon business focused on foodservice items. Until recently, our assortment was outdated, digital content was lacking, and pricing was poorly managed. This quarter, we shifted our Amazon expertise from Igourmet to foodservice. Within weeks, we activated over 1,600 new items, updated product content and pricing, and ramped up customer service. The results have been immediate, with the business now showing triple-digit year-over-year growth. We have seen similar results in our airline catering business, entry into retail, and Artisan local distribution—when we strategically align resources to our growth opportunities, we execute better and realize more growth.

This streamlining also positions us to redouble our M&A efforts. As Bill noted last quarter, it's been over a decade since the company's last acquisition in the foodservice sector, and we are being conservative in our approach to the next. Our leadership team has extensive experience in acquisitions—collectively involved in more than a dozen acquisition negotiations or integrations at large companies—while our board has been involved in many more deals than that, especially in the micro-cap segment. This expertise underpins our prudent investment framework that Bill outlined last quarter, which to summarize was 1) a business that's already profitable, 2) fairly valued not considering synergies, 3) significant and obvious synergies, and 4) the right size given our current size and cash position. We have reviewed dozens of deals and been in advanced talks with three different companies. We have passed on most for not fitting our framework. We do still have active M&A discussions though and our goal is to execute our first acquisition this year.

Lastly, we have also continued to progress on our sourcing initiative to strengthen key categories, reduce our costs, and reduce prices to chefs. This project is still in early stages, but we have already been able to expand our fresh seafood offering and other specialty proteins such as wagyu beef, foie gras, and lamb. This has led to new restaurant relationships and this new, compelling assortment is at the center of pitches we are making to new, larger business customers.

In summary, we are excited about both the organic growth and M&A opportunities that we see, and with our streamlined and focused organization, we are well-poised to execute on these opportunities going forward.

I'll now hand the mic over to Gary.

Gary Schubert

Thank you, Brady.

Hello, everyone. In addition to the Sales, Gross Margin, and SG&A results that Bill highlighted earlier, I would like to present some more financial outcomes for the second quarter of 2024.

Beyond the Sales, Gross Margin, and SG&A results that Bill outlined, the Company recorded a GAAP net loss from continuing operations for the second quarter of $103K. This is compared to a net income from continuing operations of $83K during the same period in the prior year.

I'll now share non-GAAP metrics that we believe offer a more precise evaluation of our ongoing operations. Our Adjusted Net Income, a non-GAAP metric, was $553K or $0.011 per fully diluted share. This is compared to $819K or $0.017 per fully diluted share in the prior year

Our Adjusted EBITDA, another non-GAAP metric, for the second quarter was $821K, compared to $1.2M in the prior year. Additionally, the Adjusted Free Cash Flow, yet another non-GAAP metric, for the second quarter was $597K, compared to $926K in the prior year.

As of the end of the second quarter, our net working capital, excluding assets held for sale, stood at $6 million. This is a slight decrease from Q1 at $6.1M. Our Current Assets increased by $550K, with the most notable change being an increase in accounts receivable by $1.1M as we replace our e-commerce customers paying by credit card with professional chefs who operate on terms. Subsequently, this does also result in a delay in cash which reduced by $386K. The increase in Current Assets was offset by an increase in Current Liabilities of $695K. The most notable increase was the increase in stock appreciation rights of $413K, which is revalued each quarter based on Black-Scholes to determine current liability.

On August 6, the Company signed an agreement to sell intangible assets of its consumer e-commerce business, igourmet, generally consisting of customer lists, domains, and trademarks for cash of $700,000. The Buyer also assumes gift card liabilities of approximately $330,000. And the net cash proceeds after closing costs and other adjustments are estimated to be approximately $400K. As a result, over the next 12 months, we expect to experience sales headwinds of approximately $8-9M and add back approximately $300-400K of net profit improvement.

In addition to cash totaling $3.9M, the Company continues to have access to an untapped $3M revolving credit facility with MapleMark. With the company's operational performance on the rise and our balance sheet having undergone restructuring, we are confident that our existing funds, in conjunction with our credit line and the anticipated proceeds from the sale of igourmet's intangible assets, will provide adequate capital to execute our three-phased growth strategy.

And now, I'd like to thank you for your time and turn it back to Bill.

Bill Bennett

Thanks, Gary. Hopefully you can get a sense that we're in a great position to stabilize the company this year, cement a much stronger business model, and prepare to begin investing for the future.

With that said, we're happy to take some Q&A, so I'll turn it back to Ronit to moderate the Q&A for us.

Operator

We'll now move to the Q&A section of the call. If you'd like to ask a question, please use the Zoom function to "raise your hand" or dial *9 if you are calling in from a phone. Please limit your comments to one question and one follow up if needed, and keep your comments professional and respectful. We've allocated approximately 20 minutes to this portion of the call.

JD Abouchar

Great progress on turning the company into a new direction. First question would be on the uniqueness of the Chicago model, opportunities still within to grow it within the Chicago metro area. And then how do we replicate that in other major cities? And do you have your eye on any in particular?

Bill Bennett

Yes. Great question, J.D. Thank you. It's something we've thought a lot about and is an integral part of the M&A strategy that we're now pursuing.

If you go back to 10 years ago, when we acquired the Artisan business, -- they were actually our largest supplier to the drop ship portion of the business that we had at thetime, mostly just with US Foods. So it was sort of like a vertical integration play. What's happened since then, though, is the business has doubled in size. So they started around $10 million. They do about $20 million today, split roughly half-half between serving the local Chicago market and servicing the drop ship business. So that's a really unique synergy that we can bring to any kind of regional distributor that we may acquire.

And so that's a lot of the focus of our M&A efforts now is finding the right size and the right type of small regional distributor that could fit nicely in our portfolio where the hope would be we can take their existing assortment, get it listed on our drop-ship sales channels and fairly quickly get them incremental sales that they wouldn't have otherwise had access to, improve the throughput of their warehouse and leverage their assets in a way that they weren't able to before.

So it's definitely a compelling model, while continuing to grow that local distribution business as well. So yes, all of those remain opportunities for us, and we'll continue to be open and candid with investors as we come across those opportunities.

Operator

All right, our next question is from Joel Gold.

Joel Gold

First, congratulations Bill, toyou and your team for the outstanding performance you've done and for positioning the company for a very exciting future. So I'm really delighted, very happy to hear everything that's going on, and the ability to diversify the company so that we are -- I guess -- and maybe this is a question -- a statement that ends up as a question, continue to lower the percentage of our revenue from US Foods while continuing to increase the dollars that we do with US Foods. So is that a fair estimate in terms of where you see the foodservice opportunities going to Bill?

Bill Bennett

Yes, thanks for the compliments, Joe. I really appreciate it. We've got a phenomenal team and I am super blessed and lucky to have them as a part of the effort. So I appreciate that.

Yes, the way you described the path forward with US Foods is exactly where I'd like to be. Decreasing our reliance on one customer, I think is healthy for the business. It's healthy for all of us. And ideally, we'd love to do that through -- while still growing the USFoods business, right, so we’re growing everything else at such an exponential rate that it drops as a percentage of the total. We do have to disclose our sales of US Foods, as you can see in our quarterly filings. Of course, our current Q will be out in the next hour or so. But what you continue to see over the quarters is that our business with them has been shrinking. And so while I'd love to get them back to growth the reality is that it's been shrinking in the most recent quarters. So that's definitely a focus of the team. It's our biggest dollar, still our biggest customer as of today is still U.S. Foods. So it's a focus for us to strengthen that business again. But the reality today is that they are declining. Does that answer your question? I think you've gone back on mute, but I hope it does. Thank you, Joe. Appreciate the question.

Operator

Our next question is from Ian Cassel.

Ian Cassel

I guess my first question would be about 1 of the things you highlighted in your prepared remarks, which was but the large national retailer, the 10-store test that you're doing with gourmet cheese. Can you talk a little bit more about that, how that opportunity came about and what exactly you're providing them?

Bill Bennett

Yes. So, we've said all along that our goal is to have many lines in the water to use a fishing analogy. We want to have lots of opportunities that we're constantly pursuing, realizing that many of them won't work out. And so the more we have in the water, the more chances we have of something going big and becoming a material part of our business. So this opportunity, in particular, we've been working on for – I think we're just hitting 12 months now. So literally, very early in my tenure, we kicked off the efforts and the discussions with this retailer to build some kind of business together.

And like I said all along, any kind of B2B business just takes time, right? You have to build a relationship before they’re going to take a risk with you. And I think, especially in a retail environment where building a relationship eventually means getting shelf space the retailers taking a risk, too. So there's a lot of relationship building there that has to take place, which is why the lead time for something like this is long.

The nature of the business is that we are -- like Brady mentioned, we're actually able to leverage the capabilities, equipment and supplier relationships that we've developed over the years from the ecommerce business to now implement a cheese business with this retailer. So this is a space where we're physically taking ownership of the inventory. We are cutting and wrapping the cheese and then delivering it to those 10 stores as part of this pilot. So that's sort of how the business works today.

One thing I really like about this is that it's a focused assortment. So historically, with igourmet, we carried upwards of 600 varieties of cheese. When you think about any retail environment, we're not going to be anywhere close to that quantity of SKUs that we need to carry, keep track of, forecast, order and store. So I think the focus here is going to help us tremendously, which again, goes back to our B2B strategy.

I'd so much rather be in the business of creating these big partnerships and relationships where we go deeply together and we're not spending marketing dollars on every single customer and trying to convince them to come back to us again. If you remember, I think this was last fall in our earnings call, when we laid out the case to ramp down our e-commerce business, we mentioned that it cost us $25 to acquire every new customer into the e-commerce business, and we only had a 5% retention rate. So you're literally -- you're losing money hand over fist, just trying to grow the top line. The big difference with retail or with Broadliners, but in this situation with retail, there's none of that marketing expense involved. You've got a built-in base of customers in that store traffic. And once you've got shelf space, you've got people guaranteed to be walking by your product and seeing it and that sort of ends up being your marketing effort to gain visibility. So very excited about that.

We'll continue to do press releases and update it on quarterly calls as that pilot progresses. Does that answer your question, Ian?

Ian Cassel

Yes. Maybe just one follow-up: what's the delivery cadence on something like that? That cheese is obviously perishable. Is that like once every 3 days, you're dropping the pre-sliced cheese off of those individual stores? Or is it longer than a week, what does that look like?

Bill Bennett

Today, we're hitting a cadence of about once a week, but all of that can be malleable, right? We've got shipping capabilities, of course, because of the e-commerce business that we historically have run, and so it's very easy to go faster. One thing our partner has really appreciated is that, especially in this 10-store test, we just can't afford to be out of stock on anything. And so when sales have done well, we've been able to overnight products and get it to the store quickly so that we stay in stock and continue measuring the results accurately. But in the long run, we want to be efficient and move it through their supply chain as much as we can, so that we're keeping as much cost out of the system as we can.

Ian Cassel

And one last question. I saw about an hour ago, Performance Food Group acquired Cheney Brothers -- and I think those are 2 logos on your slide presentation. Just wondering how you think about that.

Bill Bennett

Yes. Performance Foodservice Group acquired Reinhart a few years ago, who we also have a relationship with-- and that's really done wonders for helping us get our foot in the door more with PFG as the depth of the relationship grows. So I would hope that a similar thing happens with Cheney Brothers, but I too am one hour into that news headline. So lots to be discovered still as we have conversations with Cheney and understand the implications of the acquisition.

I had a question come through as a direct message in the chat. So this is from -- I'm actually not sure how to pronounce it: Paul Tschischik.

“Bill, in the prepress release you mentioned regarding specialty foodservice, headwinds in the legacy drop-ship business partially off set by growth in Artisan Specialty Foods business, airlines business and the new late customers. Could you elaborate on growth rates in each of those sub businesses? And what's the current revenue contribution of each stream?”

That's not something that we've released before, Paul. So I'm hesitant to kind of going into that level of detail. But I mentioned in my prepared remarks today that both artisan and the airlines are growing in the high single digits. Of course, with the size of our largest customers, the net effect of all that together is still negative. But the fact that those other core businesses are growing are an important part of the story for how we're going to get back to growth in the back half of the year. I will say, too, we're starting to rethink the revenue segmentation that we give in our public filings. Historically, we've broken out specialty foodservice, e-commerce, and our services business. As e-commerce goes away, of course, it's going to be important that we rethink the level of detail we're showing. So I'm not quite ready to sort of reveal a new structure, but you can count on additional visibility going forward. Thanks for your question, Paul.

Bill Bennett

All right. Thanks, Ronit, for moderating. Thanks, everyone, for your questions today and for your attendance and engagement on the call. It's really inspiring to see the level of interest in Innovative Food Holdings. As always, I'm happy to make myself and my leadership team available to connect with investors who have further questions about publicly available data. Please reach out to Gary Schubert, whose contact info is included in our press release, if you'd like to schedule a touch base. Take care, and we look forward to continuing to update you on the progress of our strategy at our Q3 update later this Fall. Thanks all, and have a great day.