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Nayuki 2023 Annual Results Conference Transcript

The respective meeting was held in Mandarin, and the English version is an automatic translation by a large language model for your easy reference. In case of discrepancy, the Chinese version shall prevail.

Lu Cheng: Hello and welcome to the 2023 annual results presentation of Nayuki Holdings Limited, I am Lu Cheng, Head of Investor Relations of the Company. Present at today's presentation are Mr. Zhao Lin, Chairman and Chief Executive Officer, Ms. Peng Xin, Executive Director and General Manager, and Mr. Shen Hao, CFO of the Company. The agenda of today's presentation is as follows. Mr. Shen will first give you a brief overview of the Company's results, and then we will open the floor for questions. Please welcome Mr. Shen.

(The following is the introductory section of the presentation deck. Please go to page 5 for the Q&A section)

Shen Hao: Distinguished online and offline friends, both old and new, good morning! Welcome to the Nayuki Tea Holding Co., Ltd.'s 2023 Annual Performance Press Conference. Investors can access our presentation materials through the company's investor relations website at ir.naixue.com. Please read our disclaimer before the meeting begins.

Today, my presentation will be divided into three main parts. Firstly, I will provide a brief overview of the Group's overall business performance over the past year. In 2023, we opened 544 new Nayuki's Tea outlets across the country, ending the year with a total of 1,574 directly-operated stores in 111 cities. This year, we plan to open another 200 directly-operated stores in prime locations of high-tier cities while closing some underperforming stores. We anticipate no net increase in the number of directly-operated stores this year. Furthermore, last year, we launched our first store in Thailand's Bangkok core area, which was warmly welcomed by Thai consumers and achieved sales exceeding one million RMB within its first month. In the future, we will continue to explore overseas markets.

In late July last year, we officially opened our franchise program, and upon announcement, received over a thousand franchise inquiries. By the end of the year, we had opened 81 franchised outlets. As of now, approximately 200 franchised stores have been established. In February this year, we optimized our requirements for franchisees, offering more flexible store formats and reducing the investment amount to 580,000 RMB, aiming to alleviate financial pressure on franchisees and support the continuous growth of our franchise business. Our goal is to achieve a scale of 2,000 to 3,000 franchised stores within 2-3 years.

During this year's Chinese New Year, many of you might have noticed newly-opened Nayuki stores in your hometowns. A considerable number of people have also approached us asking about how to join the franchise in different domestic and international cities. Currently, Nayuki's franchised stores have demonstrated quite impressive performances. For instance, the outlets in places like Xinghua, Jiangsu Province, and Lu'an, Anhui Province, have gained widespread popularity among consumers. Those interested in franchising can visit the official mini-program "Nayuki's Tea" on WeChat, tap the "Join Us" button in the lower right corner, and submit relevant information. Our franchise department colleagues will promptly get in touch with you.

In Q1 2023, following the decline of the pandemic, offline consumption rapidly rebounded. However, this trend did not persist into the second half of the year. We observed that traditional peak seasons such as Labor Day and summer vacation did not exceed expectations, showing a pattern of "sluggish peak seasons", and same-store revenues faced significant pressure in the latter half of the year. Due to the strain on revenue, store profit margins were affected. Particularly in cities like Beijing and Shanghai, where fixed costs such as labor and rent are relatively high, profitability during periods of low income fell below the average level. Conversely, markets in South China and Central China continued to show strong profitability, with operating profit margins reaching 25% in cities like Xi'an throughout the year.

We can see that the operating profit margin of the second type of tea drink stores located outside core malls or in residential and office areas stood at 20.4%, 2.1 percentage points higher than the first type, mainly benefiting from lower rents. Considering the rapid growth in the proportion of franchised stores, starting from our interim report in mid-2024, we will no longer distinguish between the first and second types of directly-operated stores but will continue to disclose the city tier breakdown on the right side, facilitating investors' understanding of the performance of high-tier directly-operated stores versus middle and low-tier franchised stores. It can be seen that currently, Tier 1 and Tier 3 cities, along with other cities, are performing relatively well, with both having an operating profit margin of 19.6%.

Regarding membership, thanks to adjustments in our price range and upgrades to classic products, more consumers have become members. By the end of last year, registered members exceeded 80 million, with an increase of 1.5 million monthly active members. The monthly repurchase rate for 2023 was 23.9%, up 0.9 percentage points compared to the mid-year period.

Product-wise, we have placed greater emphasis on consumers' demand for health and professional quality, further highlighting the charm of tea itself. During our overseas expansion, consumers equally prioritize health, and each market has unique demands. Nayuki possesses the professional capability to combine the excellent features of our products with local consumer needs. Last year, we engaged 80 million members in a selection activity, where consumers voted for the eight most representative "Nayuki Eight Fragrances" among our classic products, ultimately resulting in eight standout items, including the Bold Perfume Cheese Strawberry. The essence of our classic products lies in their tea aroma. To strengthen this experience, this year we conducted comprehensive formula upgrades to emphasize the tea aroma. Additionally, using tea culture as a theme, we launched online quizzes, promotional activities involving buying tea and receiving cultural and creative products, attracting over 10 million members to participate.

Moving on to our financial performance for the past year, details of which can also be found in our disclosed earnings announcements: In 2023, the Group recorded revenue of 5.16 billion yuan, growing by 20%. The flagship brand Nayuki's Tea accounted for 90.8% of revenue from directly-operated stores, bottled beverages contributed 5.2%, and Tai Gai and other brands made up 4%. Despite increased pressures in H2 2023, due to maintaining a good profit level in our stores, we managed to turn a profit for the entire year, achieving adjusted net profits of around 20 million yuan.

In 2023, the Group generated positive operating cash flow of 830 million yuan and nearly 300 million yuan in free cash flow for the year. This year, with plans to open 200 new directly-operated stores, our capital expenditures will significantly decrease compared to previous years. We believe there is a high probability that we will achieve positive free cash flow in 2024. By year-end, we held approximately 3 billion yuan in cash and deposits and have no plans for large-scale refinancing.

In terms of product offerings and sources of revenue: Sales of freshly-made tea beverages maintained a share of over 70%, while the proportion of bottled beverages and bakery products increased, with the bakery segment declining to 13.7%. Although bakery products are popular among many consumers and help differentiate us from other brands, we view them as having good long-term prospects. Therefore, we will retain our bakery product line and R&D capabilities, but do not plan to expand the bakery scale in the short term. The takeaway orders' share experienced a drop post-pandemic but later rebounded, currently stabilizing around 40%.

On the next page, we will discuss changes in various cost items.

In terms of the cost structure, we can observe that all major expense ratios remained relatively stable or decreased. Notably, the labor cost rate for Nayuki's stores dropped to 20.3%, and headquarters' labor cost rate declined to 7.3%; depreciation of right-of-use assets and other rental expenses combined, reflecting store rental levels, decreased significantly to 13.9%; delivery fees and other expenses also saw reductions. Despite revenue pressures in H2 2023, the company's cost optimization efforts proved effective.

Looking ahead to the new year and beyond, here are some key updates:

Firstly, we will focus on expanding our franchise and overseas businesses. As previously mentioned, we aim to open 2,000 to 3,000 franchised stores within 2-3 years. In February, we updated our franchise policy, lowering the investment amount from almost 1 million yuan to 580,000 yuan and decreasing the area requirement from 90 square meters to 40 square meters, significantly reducing franchisees' financial burden. Currently, 400 franchises have formally signed contracts, and it's expected that several hundred franchised stores will open by the end of the year. Overseas, we plan to open stores in Hong Kong, Macau, Southeast Asia, and countries like the UK and the US, initially focusing on direct operations but potentially considering franchising in the future. In 2024, we anticipate opening a low double-digit number of new stores overseas.

Secondly, there remains room for improvement in our store profitability. We are closely monitoring labor costs, rent, and delivery fees. In H2, influenced by the overall consumption environment, labor costs rose slightly, with annual store labor costs at 20.3%; we will strive to keep this figure under 20%. Thanks to lease adjustments in existing stores over the past two years and lower rents for new stores, actual rent costs stood at 14.5%, marginally better than our 15% target; the delivery fee ratio was 8.2%, still relatively high.

Raw material costs have remained stable, with utilities being a variable cost whose cost rate has stayed constant. Other depreciation and amortization expenses represent fixed costs, and with the introduction of more flexible store models and smaller footprints for new stores, the per-store capital expenditure is expected to decrease, alleviating depreciation and amortization pressures.

For 2023, the store operating profit margin was 17.7%, higher than in 2022, but due to the impact in H2, we fell short of our 20% target. This year, we will further optimize store models with the goal of achieving a 20% store operating profit margin. Concurrently, we will strictly control headquarters costs, with the absolute amount of headquarters costs in 2024 expected to remain flat or decrease compared to

2023.

Additionally, over the past period, the company's stock price has fluctuated due to a combination of factors, including fundamentals, macroeconomic conditions, and the capital market environment. We have maintained close communication with the market to ensure timely disclosure of fundamental-related information and address market concerns. We believe that normal fluctuations in stock prices caused by changes in fundamentals are not surprising. However, if irrationality persists in the market, we will act decisively to correct it. From January to February this year, we utilized general mandates granted by the market to repurchase 10 million HKD worth of the company's shares. In the future, we will continue to monitor market conditions and take all necessary measures to maintain market order when required.

Lu Cheng: Now, let's proceed to the Q&A session. When asking questions, please state your institution and name, and limit yourselves to no more than two questions each.

Question (Analyst from CITIC Securities): After the pandemic, the takeaway ratio has remained above 40%, and we also have online group-buying options available on platforms like Douyin and Meituan. How does the company view the future trend of the takeaway and online group-buying segments? Additionally, with the overall investment threshold for franchising lowered and the required store size reduced, what kind of store model should we expect in the future?

Peng Xin: Currently, our takeaway ratio is approaching 40%, which, when compared to our peers, suggests we are among the brands with a relatively lower takeaway proportion in the industry. Following the end of the pandemic, it was initially assumed that consumers would return to offline consumption patterns, yet last year, we discovered that online consumption has indeed become a habit for consumers. Regarding our stores, we consider them to be critical venues for brand experiences and spaces that continue to meet the needs of consumers for social interactions, leisure during shopping trips, and business clientele. While preserving these functions, we must also vigorously accommodate online consumer demands and continually find ways to reach them more conveniently, as these habits are driven by consumer behavior. As a brand, we must excel in both aspects.

Zhao Lin: With regards to franchising, we treat franchised stores similarly to our directly-operated ones. In the past, our equipment was not fully optimized; it was relatively large-scale, requiring substantial floor space. However, through ongoing upgrades to our equipment and streamlining the entire operational process, we have gradually reduced the space requirements and lowered staffing needs.

Initially, a store size of 40 to 50 square meters needed to be expanded to 70 to 80 square meters to be functional. Now, with continuous spatial optimization, although the functionality remains unchanged, the area has significantly shrunk. For example, we can open a store with just 38 square meters, like our outlet in Wanda Plaza, which presents an excellent image and can achieve both brand representation and a solid turnover. For those stores with poor image, small sizes, or failing to align with Nayuki's brand tone, we would not pursue them. Nayuki remains committed to maintaining our brand tone without compromise, yet we can enhance efficiency by optimizing workflows and utilizing space more effectively, thereby improving our overall footprint management.

Question (Analyst from Guosheng Securities): I have two questions to ask. Firstly, concerning the issue of industry competition, the competition in the milk tea industry is becoming increasingly fierce. What are Nayuki's core advantages and considerations for differentiation? And what is the brand's positioning and strategy going forward? Secondly, regarding franchising, what is the cooperation model between us and our franchisees? Are we functioning as a supplier earning revenue from supply price differences? If so, how do we envisage the contribution of franchisee income in the future?

Peng Xin: Post-pandemic, the competition and development in the entire industry have shown a favorable status, with the tea beverage sector remaining highly competitive within the catering industry last year. One thing is certain: the tea beverage industry continues to attract a vast number of consumers. At present, each brand showcases its own positioning and strategic thinking. Nayuki, as a brand entering its ninth year, is seeing its early consumers, many of whom are now in their 30s and 35s and older. As a brand, not only do we need to think about differentiation from competitors, but it is also crucial to understand current consumer behaviors and reinforce our brand image. Simultaneously, we aim to upgrade and reposition our brand to cater to our targeted young audience. At all times, we believe that consolidating our brand impression, adhering to our brand tonality, and maintaining our strengths are paramount. In our view, reinforcing qualities such as the premium perception of Nayuki's products, the reputation for superior tea, expertise in tea-making, the deliciousness of fresh fruit teas, the distinctive baking craftsmanship, and the use of high-quality and healthy ingredients are essential tasks at hand.

Zhao Lin: Since Nayuki started franchising, we have reaped significant benefits, especially given that we used to operate solely through direct stores. After engaging in franchising, we discovered that our team has developed dual capabilities – one in managing direct stores and another in supporting franchisees. When venturing into franchising, we identified potential opportunities that we once overlooked in our direct store operations. Similarly, while running our direct stores, we learned how to assist franchisees in improving their performance. This has greatly enhanced our organizational capabilities as a team and exposed us to more opportunities. A secondary benefit is that our headquarter costs were quite high relative to our store profits when we operated only direct stores. Upon introducing franchising, because all departments are already in place, adding a new business does not require additional manpower. Consequently, even if the profit margin from selling goods to franchisees is not particularly high, our overall profit remains satisfactory since our costs are already covered.

Question: I have two questions. First, regarding future growth. We see that in 2024, the direction for stores is focused on structural optimization of directly-managed stores, with the addition of 200 new ones but with no net increase in the total number. There's an initial strategy for franchising, and deeper penetration into overseas markets. Do you have any further planning for these three major areas? Is the current emphasis more on the franchising business? Second, concerning returns to the capital market, last year the company conducted some share buybacks and has a good cash flow situation. What are your plans going forward regarding buybacks, dividends, etc.?

Zhao Lin: For the first question, let me answer. Currently, we possess both direct operation and franchising models, and neither model is absolutely superior or inferior; rather, each is best suited to specific circumstances. Nayuki has the most directly-managed stores in the tea beverage industry, with over 1,600 such stores, while others either have none or very few. Our directly-managed stores are relatively concentrated in first- and second-tier cities, with limited presence in lower-tier cities. Across the country and globally, there is still massive untapped market potential. In this process, ensuring the success of franchisees requires us to first excel in our own brand. The disadvantage of direct operations is that when the network is not sufficiently dispersed, the difficulty of centralized management tends to decrease.

With our 1,600 directly-managed stores, we can continuously upgrade and optimize our brand image, product impressions, and store impressions in the minds of consumers, moving upward to communicate to our customers that we're constantly improving. Simultaneously, we empower our franchisees with our brand strength, and there's ample room for this, with a good cost-to-benefit ratio. Under these circumstances, the market space remains immense. Moreover, after weathering several years of the pandemic and undergoing extensive cost-cutting and efficiency-enhancing measures, we've discovered that we've gained some international competitiveness. Before the pandemic, we ventured overseas and found our brand was well-received, but our efficiency was lacking despite high popularity and turnover. Through years of optimization and adjustment, our organization has improved, and now, when we venture abroad, our competitiveness is robust - our products are loved by consumers, and our efficiency is notably high. Thus, the future growth potential is enormous; whereas we once had only the Chinese market, we now have a global market with vast opportunities. With our 1,600 directly-managed stores, we'll refine our brand image and expand store scale, potentially consisting of a smaller number of directly-managed stores and a larger number of franchised stores for growth.

Shen Hao: Concerning dividends and buybacks, the company currently doesn't have a specific timeline or amount planned for share buybacks. However, if the market were to experience sustained irrational downturns again, the company would definitely respond and conduct buybacks at appropriate and compliant times. Given the current challenging macro environment with weaker consumer spending and intensified industry competition, though the company has a large reserve of cash, we also recognize the vast global market potential and harbor ambitious plans for further market expansion. Therefore, we will exercise great caution in the use of funds. For now, there is no dividend distribution plan, but once we achieve sustainable profitability, we will definitely proactively consider providing capital returns to our investors.

Question (Investment Analyst from Huaxi Securities): I have two questions. Firstly, our leaders mentioned earlier that there will be ongoing upgrades and optimizations to enhance the brand's image in consumers' minds. Could you elaborate on the major moves planned specifically for brand power enhancement, and where the primary focus will be on the product side this year? Secondly, regarding the franchise business, there are currently around 200 franchised stores opened. Could you kindly provide some insight into the specific differences, including the profitability of these franchised stores?

Peng Xin: Reflecting on last year's market performance, Nayuki's most iconic and signature products are undoubtedly our fresh fruit teas, teas, and baked goods. Since Nayuki's inception, our foremost goal has been to encourage more young people to fall in love with tea. Whether they prefer fruit teas, classic teas, or pure teas, we aspire to offer every customer a drink they enjoy. Last year, we intensified our efforts in exploring and utilizing traditional teas, launching jointly developed Longjing and Dahongpao teas with tea masters, and six years ago, we pioneered the use of osmanthus flowers in green tea production within the industry. We have also introduced numerous traditional tea-based products and those featuring more Chinese elements, which have been warmly received by consumers. This year, we will further reinforce Nayuki's signature offerings by enhancing our professionalism in tea and developing a variety of innovative fresh fruit teas.

We've also noticed a growing trend: as consumers increasingly frequent tea beverage consumption, their demand for healthier options has escalated. Hence, our consumers have become more concerned about sugar content and overall healthiness. In terms of ingredients, Nayuki insists on using higher-quality raw materials, dairy products, and fresh fruits. Presently, we are exploring sugar alternatives, such as zero-calorie sweeteners derived from monk fruit, refining our formulations to create lower-calorie, better-tasting products. Recently, we partnered with the Shanghai Health Commission to initiate nutritional labeling for our fruit teas and milk teas, emphasizing the importance of producing healthier products and reinforcing the perception of healthiness. Focusing on fresh fruit teas, health consciousness, and tea quality, these three product lines will be our top priorities this year.

Zhao Lin: Regarding the second question, we've currently opened over 200 franchised stores and have learned a lot in the process. When we open franchises, we aim for a complementary advantage where, for instance, direct stores may face greater management pressure when spread too thinly, making centralized management more efficient. We value the management abilities of franchisees, while they appreciate our product strengths. Among these 200-plus franchised stores, we certainly hope that all franchisees can make a profit upon joining our brand. In practice, experienced franchisees with strong management skills can generate excellent profitability, given that even the best brands require diligent operation over time. Last year, our 1,600 directly-managed stores achieved a 20% store profit margin, meaning that with proper management and dedicated effort, franchisees can expect good returns. Of course, there are instances where some franchisees incur losses, which could be attributed to inadequate management ability, operational proficiency, poor site selection, or lack of experience. Profitable stores typically have better-managed store operations and higher responsibility, while unprofitable stores might suffer due to poor management or service quality, alienating customers. We are more cautious in selecting and serving franchisees to achieve a win-win situation. It's a long-term endeavor for us to guide and support franchisees facing challenges to help them improve and grow.

Question (Investment Analyst from Northeast Securities): I have two main questions here. Firstly, regarding our expansion overseas, including the selection of overseas markets, the consideration of overseas supply chains, and pricing in those markets. Secondly, I'd like to inquire about Nayuki Tea Academy, its expansion plans for this year, and its strategic position within the company.

Peng Xin: Zhao Lin and I toured Southeast Asia prior to last week. On one hand, our store in Thailand has been operating for a period of time, and we wanted to assess its progress. On the other hand, there are quite a few property owners expressing interest in having us open more stores and offering us prime locations. Our Thai store, situated right at the entrance of a relatively upscale shopping mall, has performed exceptionally well and garnered significant attention from property owners. To begin, I'd like to share our insights from Southeast Asia, which reflect our broader global considerations. We observed that, across various overseas markets, tea beverage prices generally do not lag behind coffee prices and in many cases, such as in the US market and the Southeast Asian markets we examined, tea beverages command a higher unit price than coffee. This presents a favorable condition for the industry as a whole. Regarding specific pricing strategies, while we take into account supply chain costs, we prioritize the brand impression we build locally and the scale of the market we aim to penetrate in the long run. Pricing decisions will ultimately be guided by our brand positioning and competitive landscape. Currently, in Thailand, our prices are set about 20% to 30% higher than in China. However, based on consumer feedback in Southeast Asia, where patrons generally regard our products as high-quality and appreciate our premium brand image, and are willing to regularly pay these prices, we adopt such pricing strategies. Our goal isn't merely to open a few stores in these countries but to establish a deep and comprehensive presence in cities, akin to what we've achieved domestically.

Zhao Lin: Regarding Nayuki Tea Academy, we have undergone two rounds of upgrading, and we're still in the process of further enhancements. Its performance has been commendable, giving us pleasant surprises. Concurrently, we have recognized the immense market potential. At present, we're not in a rush to aggressively expand because we see ample room for further upgrading. For a brand, the first impression is crucial and cannot be altered. Once the upgrading is complete, we hope Nayuki Tea Academy will impress consumers with a bright, beautiful image. That's why we're not in a rush for expansion, but instead focusing on refining the concept. Despite this, we can sense the vast market space that Nayuki Tea Academy can unlock in the future.

Question (Investment Analyst from Huaxin Securities): My first question concerns franchising. How are the 200 franchised stores distributed across different tiers of cities? Having opened franchising for a while now, what issues have we encountered in management or quality control, and how do we plan to address these problems going forward? My second question pertains to bottled beverages. We have achieved a 70% growth rate, reaching a revenue of 260 million yuan. Can you tell us what percentage of this comes from our flagship product, Nayuki's Lemon Tea, and what are the plans for product development and channel expansion in this regard?

Zhao Lin: Regarding the first question, we place great importance on the impression Nayuki's brand leaves on consumers. Whether it's a franchised store or a directly-operated store, we strive to ensure customers receive the same level of quality and experience. Both ourselves and our franchisees emphasize quality, health, and everything that our directly-operated stores prioritize. During the store opening process, we also involve our development team to assist franchisees in selecting suitable locations that do not compromise the Nayuki brand image or tone. Nayuki will never devolve into another brand; we cherish the beautiful brand impression we've built, and we won't forsake it. Even as we expand with franchised stores, including smaller ones, the overall Nayush impression will always be maintained. Our team is still learning, and encountering new challenges that we didn't face with directly-operated stores is beneficial, as it rapidly accelerates our experience and capability.

Peng Xin: Currently, our franchise partners share a similar philosophy with us, aiming to deliver excellent products, experiences, and services, which is something we're very pleased about. Many of our franchised stores are located in less penetrated lower-tier markets, presenting challenges to our supply chain. Nonetheless, we will promptly provide the necessary support. For us, this is indeed a valuable opportunity to enhance the capabilities of our backend team.

Shen Hao: Regarding RTD (Ready-to-Drink) beverages, I don't have the exact figures, but my rough estimate is that Nayuki's Lemon Tea accounts for roughly 30% to 40%. Please allow Zhao to introduce the overall situation.

Zhao Lin: Over the years, our RTD brand has gained significant recognition. Although it incurred a loss of over 40 million yuan last year, we firmly believe that the RTD market holds immense potential, and the product itself demonstrates strong staying power. We are determined not to slack off in the RTD market and have drawn lessons and gained experience from our journey thus far. In 2024, we will continue to invest heavily in the RTD line. I can confidently say that the extent of loss in 2024 will be significantly reduced compared to 2023, and I trust that this business segment will only get better.

Question (Analyst from Huachuang Securities): Firstly, what is the investment payback period for the currently established franchised stores? Have we conducted any calculations on what an ideal investment return period would be for franchisees? Secondly, given that there was some pressure on the average transaction value per customer in the industry last year, how do we anticipate changes in this metric for this year?

Zhao Lin: Regarding the first question, the payback period for franchisees varies significantly. An experienced franchisee who selects a prime location and manages their store effectively, conducting marketing activities and promotions, can recover their investment relatively quickly. However, there are also franchisees who, to date, are not profitable, and such stores do exist. The results truly depend on the individual. The same endeavor can produce different outcomes depending on who executes it. Our collective effort with franchisees at present is aimed at gradually enhancing their capabilities. I believe that all franchises in the industry are facing a situation where some stores are profitable while others are not.

Peng Xin: Amidst the current environment, we observe that the average transaction value per customer is trending downwards. However, we also note a positive phenomenon: consumer purchasing power and willingness to consume remain robust. At this stage, our primary strategy is to enable consumers to enjoy our products more happily and effortlessly. Despite a decrease in our average transaction value, our cost ratio has not risen compared to before, thanks to ongoing optimization efforts. This improvement is due in part to increased procurement volumes and deeper product development, as well as stronger cooperation with upstream suppliers. For us, offering competitive and consumer-preferred products remains crucial. Presently, consumers' ability to purchase easily contributes to their happiness. More importantly, our internal focus is on strengthening our core competencies within the upstream supply chain.

Shen Hao: Concerning the payback period for franchised stores, one can also refer to the performance of directly-operated stores since we are the sole company in the market with a substantial number of both direct and franchised outlets. Franchised stores mainly operate in third-tier cities, and their performance is comparable to that of directly-operated stores. Therefore, as a reference point, under good operational conditions, franchised stores might potentially achieve a higher profit margin due to the absence of depreciation and amortization expenses, as well as having some advantage in labor costs—these two factors could lead to a difference of around 5 percentage points. By referring to the performance of well-located and well-managed directly-operated stores, one can approximate a good benchmark for profitability.

Liu Cheng: Thank you to the investors who asked questions earlier. Prior to this conference, we received many inquiries from investors, most of which have been addressed during the event. However, there are still many friends who are deeply concerned about our overseas development, as numerous brands have already expanded internationally. Some investors feel that Nayuki might be a bit late to join the race and are interested in understanding Nayuki's advantages and how we view our competitiveness in the current international market. Let's invite the management team to address this matter.

Zhao Lin: Nayuki's approach to going global differs from that of other brands. I believe Nayuki is among the first beverage companies to utilize a direct-operated model when expanding overseas. Drawing from domestic experience, possessing dual capabilities is critical. When Nayuki ventures out, our team spends a significant amount of time and energy in foreign markets due to our commitment to direct operations. We follow a high-profile, aggressive strategy by first establishing our brand, ensuring that Nayuki's brand image takes root in the target country and city. Following this, we plan for rapid expansion to capture market share. We have chosen a path that starts with overcoming greater challenges, which, albeit harder initially, is considered more stable. Unlike other brands that may rely more heavily on capable franchisees or agents, whose performance can fluctuate according to their abilities, resulting in uneven market performance, sometimes flourishing in one country while failing completely in another. We have opted for a more steady, cautious, and secure route, which is also a long-term strategy. Rather than immediately seeking rapid growth through partnerships that might vary in effectiveness, we are committed to building a solid foundation for sustainable success.

Lu Cheng: Thank you for coming to today’s presentation. Due to time constraints, we have to conclude the meeting here. As usual, we will upload the transcript of the press conference to the Company's official website ir.naixue.com as soon as possible for your convenience. If you have further questions, all investors are welcome to contact us through the IR mailbox disclosed on the official website. This concludes today's conference. Thank you.