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RCII - Q2 2017 Rent-A-Center Inc Earnings Call

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OVERVIEW:

Co. reported 2Q17 consolidated total revenue of $677.6m and net diluted loss per share, excluding special items of $0.01.

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PRESENTATION

Operator

Good morning, and thank you for holding. Welcome Rent-A-Center's Second Quarter Earnings Release Conference Call. (Operator Instructions) As a reminder, this conference is being recorded, Thursday, July 27, 2017. Your speakers today are Mr. Mark Speese, Chief Executive Officer; Maureen Short, Interim Chief Financial Officer; and Daniel O'Rourke, Vice President of Finance, Investor Relations and Treasury. I would now like to turn the conference over to Mr. O'Rourke. Please go ahead.

Daniel B. O'Rourke - *Rent-A-Center, Inc. - VP of Finance Analytics & Reporting*

Thank you, Jack. Good morning, everyone, and thank you for joining us. Our earnings release was distributed after market close yesterday, which outlines our operational and financial results for the second quarter of 2017. All related materials are available on our website at investor.rentacenter.com..

As a reminder, some of the statements provided on this call are forward-looking statements, which are subject to many factors that could cause actual results to differ materially from our expectations.

Rent-A-Center undertakes no obligation to publicly update or revise any forward-looking statements. These factors are described in our earnings release issued yesterday, as well as in the company's SEC filings.

I'd now like to turn the conference call over to Mark.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Thank you, Daniel. Good morning, everyone, and thank you for joining us. Today, we'll discuss our second quarter results and go into detail on the progress we are continuing to make on our strategic plan. Needless to say, our focus remains on the key elements of this plan, which are strengthening the core U.S. business, optimizing and growing the Acceptance Now business, and leveraging technology investments to expand distribution channels that integrate our retail and online offerings.

We're encouraged by the results we are seeing. We implemented a number of new initiatives during the quarter to drive our business forward. While, it will take time to fully realize the benefits of the actions that we have taken, given the portfolio nature of the rent-to-own industry, we remain on track and reiterate our expectations to achieve the 2018, 2019 targets that we laid out as part of our strategic plan.

Let me remind everyone, we have said, it would take several quarters before these results showed up on the top and bottom lines, and from a portfolio standpoint, the second and third quarters historically, perform lower.

That said, we believe the monthly key operating metrics reports will continue to provide visibility into our progress, and we are committed to holding ourselves accountable for our performance.

Now, I'd like to review the results of the second quarter. Our core U.S. business showed solid progress in the second quarter. We continued to enhance the value proposition of the business through these targeted initiatives.

As I mentioned, last quarter, we implemented a new competitive offering in February with the goal of increasing customer satisfaction and retention, increased ownership to shortened terms and an increase in the early purchase discount, all while improving the life cycle of inventory, and enhancing our return on investment.

As a result, we saw further improvement in Q2, including a 9% decrease in returns year-over-year. We are also starting to see an increase in ownership as well. But the full impact of this initiative will take some additional time. As we continue to increase ownership levels, our inventory turns will accelerate and in turn, our cash flows will improve.

In Q2, we also continued our focus on optimizing our inventory mix to better meet the demands of our customers and grow the portfolio. As a matter of fact, over 65% of the products we ship to our stores during the quarter were higher end, aspirational products as the portfolio balance improved. In addition, the year-over-year change in merchandise on rent improved by 380 basis points. While this will continue to take time, shifting the mix towards the higher end, aspirational better and best products will drive stronger economics for Rent-A-Center.

In fact, as noted, in the June's monthly metrics report, delivery APU, again this is the average monthly rate of new agreements, improved 5.7% year-over-year, as a result of the continued optimization of the value proposition and higher end inventory in our system.

We've also reduced the overall amount of Acceptance Now returned product in the core, by over 30% this year, as a result of our efforts, to increase sell-through rates through targeted sales initiatives. These include a reduction in the remaining inventory value of these products when they are transferred into the core and an overall reduction in Acceptance Now returns.

We also enhanced the quality of the portfolio against the prior period. This was part of our improvement in account management practices. It is a key part of our overall strategy. Delinquencies improved by 410 basis points over the prior-year period. In order to optimize or to continue to optimize our business, we are stabilizing and upgrading our talented workforce. To reaffirm our commitment to the co-workers, we also implemented a profit sharing program in April to align the co-workers with the ultimate goal of enhancing stockholder value.

This new plan captures the full P&L, and in addition, profit sharing now includes the assistant managers. We strongly believe that this plan will decrease turnover and increase engagement.

Further, our focus on P&L management and training for managers will improve our overall business. I'd also like to highlight our new mystery shopper program, this is designed to improve the customer experience. This program will provide the salesforce a critical feedback on in-store, web, and phone-based customer interactions. Importantly, detailed training is integrated into the tool to help co-workers significantly improve their interactions.

In regards to our core store footprint, we continue to employ targeted initiatives for our underperforming stores. As we have shared with you in the past, we expect underperforming stores to show signs of a turnaround by the end of 2017. We are continuing to evaluate individual store performance and rationalization. And as part of that, we have engaged a third-party to help us better understand the potential role of franchising, and what it would take to become a world-class franchisor. Now, this work is well underway and we believe it can play an integral role in the future of Rent-A-Center.

Turning now to the Acceptance Now segment. We saw strong same-store sales in the quarter. To be clear, there are now only approximately 500 locations in the Acceptance Now same-store sales calculation, due to the remainder having been removed from the calculation, due to receiving accounts and the revenues from the closed Conn's and h.h. gregg stores. While delinquencies were unfavorable compared to the prior quarter, primarily due to seasonality, and the transferred agreements from those closed stores, same-store sales remained higher than last year due to a larger portfolio in those respective locations. This growth is being driven by a maturing store base and stronger average ticket as a result of the initial actions that we've taken to date to optimize the value proposition in this segment as well.

We also continue to improve our decision engine, and the risk analytics to increase our return on investment through improved ownership by implementing consistent risk assessment policies and strategies across all ANow locations. The overarching goal is to reduce returns, increase ownership and increase the return on capital. This increase in inventory -- the increase in inventory held for rent in the ANow segment, and you will see that in the segment reporting that the held for rent went up. This was temporary or is temporary and it was intentional, as we work to move the excess inventory in the core, which we have done and at the same time, we opened 2 regional resale locations to sell excess products through. Those are now operational and inventory is once again flowing through all channels.

Turning to the third pillar of our strategy. We are focused on leveraging our technology investments to expand our channels to reach new customers. As part of this, we are focusing on opportunities to capitalize on strong growth prospects in emerging rent-to-own channels, particularly, in Acceptance Now and e-commerce. We are in the late innings of developing and deploying a mobile application, which will bring Rent-A-Center to our consumers anytime and anywhere. RAC mobile will provide more choices to our consumers with the ability to make payments and manage their accounts, while allowing us the opportunity to engage and improve customer retention and satisfaction.

With respect to the balance sheet, we are focused on improving the return on our inventory investments and we've continued to pay down debt and position the company for growth and value creation. We were pleased to have closed the amended credit facility during the quarter, which we believe provides us with sufficient liquidity and flexibility to execute on our initiatives and drive value for stockholders.

We are pleased with the good progress we have made on our strategic plan during the quarter, delivering sequential improvements in same-store sales in both the Core U.S. and Acceptance Now businesses. As we laid out when we announced this plan, our transformation of the business will take 7 quarters and our work is not yet done. However, I am optimistic about what we have achieved so far and we remain on track with our plan.

Finally, I also want to thank all of our 20,000 coworkers for their hard work and all that they continue to do to stay focused, and execute on our strategy.

And with that, I'll turn the call over to Maureen.

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Thanks, Mark. Good morning, everyone. Now I'll walk through the financial performance for the second quarter of 2017, and will present the results excluding special items, compared to the same period of the prior year or to the first quarter of 2017, as we measure sequential improvement against our strategic plans.

Consolidated total revenues for the second quarter were $670 -- Sorry, $677.6 million, down 9.6% versus prior year. Adjusted EBITDA was $28.9 million, and EBITDA margin was down 20 basis points versus the first quarter. Net diluted loss per share excluding special items, was $0.01.

In our Core U.S. segment, total revenues were down 13.9%, driven by a same-store sales decline of 10.2% and a 5% reduction in average store counts. The same-store sales decline is primarily due to a lower portfolio balance versus prior year.

As Mark mentioned, we continue to make progress on the portfolio. Same-store sales improved sequentially by 230 basis points, driven by value proposition changes and the higher monthly rate of new agreements, which was 5.7% above prior year in June. The year-over-year change in merchandise on rent improved sequentially by 380 basis points, which shows that we are making up ground versus last year on the portfolio. We continue to expect sequential improvement in same-store sales every quarter of 2017, and to achieve positive same-store sales in the fourth quarter, when the benefits of our initiatives become more significant.

Gross profit margin in the Core U.S. business was 69.6%, 260 basis points lower than last year due to value proposition changes and targeted pricing actions to rightsize the inventory mix. These changes will continue to put pressure on margins for the next 2 quarters. However, they are expected to drive higher retention and ownership rates. Core merchandise held for rent was up sequentially driven by an increase in the average cost per unit, due to the shift towards more better and best product. The number of idle units were down sequentially, partially driven by fewer Acceptance Now returned product in the Core stores. Store labor expense was down $19.4 million versus last year, driven by lower store count and lower insurance expenses.

Other store expenses were down $17.6 million, driven by lower store count and lower skip/stolen losses. Skip/stolen loses in the Core business were 2.4% in the quarter, compared to 2.9% last year. And our expectation is that losses will remain at lower levels, given the improvements made in delinquency rates and the quality of the rental portfolio. While store expenses benefited in the first half of the year, from stores that closed in 2016, we will have fully [elapsed] the closures in the second half of the year.

On a sequential basis, core EBITDA dollars improved 21%, and EBITDA margin improved 210 basis points.

Now, turning to the Acceptance Now business. Total revenues increased by 1.9% due to higher same-store sales of 6.7%, which was partially offset by store closures. In Q2, 262 Acceptance Now staffed locations were closed and merged into existing locations, primarily due to the closures of Conn's and remaining h.h. gregg locations. The company also opened 70 new staffed locations within the quarter.

Acceptance Now revenues for the full year is expected to be similar to 2016 revenue, since the growth in the first half of 2017 will be offset by the store closures. Gross margin was 51.1%, down 170 basis points from last year, driven by lower gross profit on merchandise sales, due to a focused effort to encourage ownership and reduced returned product by negotiating a buyout amount in lieu picking up product for select customers. We expect this gross margin trend to continue going forward and will likely build aspects of this into our future value proposition changes.

Skip/stolen losses for Acceptance Now were 9.4%, which was a 70-basis-point improvement versus prior year. Acceptance Now EBITDA was $25.6 million (sic) [$25.0 million] in the second quarter, and sequentially EBITDA margin decreased by 60 basis points. Corporate expenses increased compared to last year, primarily driven by incentive compensation accrued at a higher rate than last year and higher depreciation resulting from the implementation of our new POS system. Corporate expenses for the remainder of the year are expected to be flat to slightly above prior year.

Now turning to the balance sheet. Last month, we announced the completion of an amended credit agreement with our existing bank group. Under the new agreement, maintenance covenants were replaced with a monthly fixed charge coverage test. If our fixed charge coverage is less than 1.1x, we must maintain $50 million of excess availability on the revolver. The revolver size is $350 million, with an expansion feature of an additional $100 million. Pricing is substantially the same with an additional pricing tier above 4x leverage. The amended credit facility provides us with more than adequate liquidity and flexibility needed to execute on our strategic plan.

At the end of the second quarter, we had $73.8 million in cash and cash equivalents, and reduced total debt by approximately $16 million during the quarter. Our total debt balance was $647.4 million, with $55 million drawn on the revolver. For the quarter, the company's fixed charge coverage was 0.8x, leaving approximately $140 million of available capacity on the revolver, taking into account the additional $50 million necessary given the fixed charge coverage rates. Year-to-date, we have generated approximately $112 million of cash from operations, and continue to expect to end the year with a lower debt balance.

With that, let me turn the call back over to Mark before we open up the lines for your questions.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Thank you, Maureen. Yes, before we open the line for questions, I want to discuss a few other items related to our business. We've made a number of exciting personnel additions to further strengthen the leadership team. In May, Joel Mussat rejoined the team as Executive Vice President, Chief Operating Officer. Many of you know or have met with Joel in the past, having spent 11 years working here at Rent-A-Center. It's great to have Joel return and we look forward to his contributions as we enhance our operational capabilities. We also appointed Martin Evans as Executive Vice President, Chief Human Resource Officer. Martin brings an outstanding people skill set, and more than 20 years' experience shaping high-performance cultures at Fortune 500 companies. Most recently, Martin was Head of HR at Exeter Corporation, where he reshaped and defined a new mission brand and values for the company, reducing turnover, restructuring benefits and cultivating a unified values-based culture.

I also want to reiterate my personal commitment to my role at Rent-A-Center. As a founder of the company, and CEO, I have the utmost confidence in our strategic plan and future prospects. As I've outlined this morning, the initiatives underway, as part of our plan, are already delivering substantial progress in key performance metrics, including improved same-store sales and reductions in delinquencies. I look forward to continuing to share our progress in the quarters ahead.

I also want to briefly address recent media reports regarding the company, and unsolicited indications of interest. The Rent-A-Center Board and Management Team are focused on maximizing value for all stockholders. The Board is well advised, remains open-minded and regularly reviews Rent-A-Center's strategic priorities and opportunities, and is committed to acting in the best interest of the company and all stockholders.

Beyond that, we won't be commenting further on this topic. And I'd refer you to our previous public statements. As I've shared with you this morning, my focus is on expeditiously executing our strategic plan, to restore growth and improve profitability.

So with that in mind, and this being our quarterly call, we ask that you limit your questions to items pertaining to the results that we have reported today.

With that, I would like to now go ahead and open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Budd Bugatch of Raymond James.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

I guess first question is regards the gross margin, the value proposition that you talked about. What would be the normal and how do I think about the gross margin versus what you've done to eliminate some unproductive inventory? How do you -- how do we think about the quantification of that differential in gross margin?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I want to make sure I understand your question. And you're saying, how should we think about it relative to what it might be in the future, the way the value proposition was positioned compared to how it's being reported today, given the discounting and acceleration of moving through the prior promotional inventory, in other words?

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Yes. Give us a flavor of what the two parts were in the results just reported and then how does it look going forward. What's kind of a target margin for the Core and for Acceptance?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Yes, Budd, so today the 260-basis-point change year-over-year within the Core business was driven by two things: The value proposition changes, which are recurring and aggressively trying to move through older idle product, in order to make way for the new more aspirational products. So the margin should improve going forward, given that we won't need to be as aggressive in moving through idle inventory, because we've already started buying the new inventory, and we've moved through a lot of that inventory already.

So going forward, we will see margin improvement from the second quarter. However, we will still see some pressure year-over-year, given the changes that we made within the value proposition.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Yes. And of the 260, what was the value -- of the 260 basis points, what was the value proposition portion and what was the discounting portion [indiscernible] moved through the inventory?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I think, well, yes. No, I understand what you're trying to ask. I know I've said before, I think everyone recalls the average piece of inventories in our system about 18 months. So I think, where you really got to start is, how long is it going to take to move through it.

And then, where does this ultimately settle? To Maureen's point, sequential third quarter will show some pressure compared to last year, fourth quarter likely will. As we get into '18 and beyond, it is when you're going to start to see that settle into where it could be or should be on a normalized basis.

Now, you're asking is that 100 points lower? Or 200 points lower? Or what from where it is right now? And the answer is yes, it's somewhere in between there.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Okay. And my next question is regarding inventory productivity. Inventory on rent per store has -- continues to move down, although it looks like the deceleration may be at least moderating sequentially. But that's kind of a future revenue basis for the Core. What are we -- where are we in that process? How should we think about that going forward? And if you talk about Core expectation for revenues, I apologize, I was a little tardy in getting on the call, because I was on another call. If you can help us for the balance of this year?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

So are you asking with the on rent inventory, what are our expectations are going forward within the core business?

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

No, Maureen, that inventory on rent per store, per average store, it looks like it continues to fall, which is the basis of additional revenues or recurring revenues going forward. So that's kind of the revenue -- that's kind of the fuel for the engine. Where are we in that process? When does that start to rise? What's the expectations for Core revenues?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Yes. No, that's -- you're right. It's a portfolio business. Everyone should recall that the first quarter, although, it looks really good on the top line, you have all of these payouts, you generate all this additional revenue from the payout, but that's at the expense of the portfolio shrinking, the contracts have left the system. And that shows up in the second quarter, which is to your point, that the portfolio shrunk a little bit. And again, that's the portfolio nature of the business and the first quarter the implications of all the payouts, which is why I said the second and third quarters tend to be the softest. So in that comment that I made about second and third quarter tend to be the softest, you might see something similar in the third quarter in terms of the portfolio performance.

We said all along that we felt that the fourth quarter is when accounts were going to turn positive and that the results of these initiatives were going to start to show themselves, that would suggest that you would also then start to see that turnaround in Q4 and beyond.

Operator

Your next question comes from the line of Laura Champine with Roe Research.

Laura Allyson Champine - *Roe Equity Research, LLC - Senior Analyst for Consumer and Retail*

It's Laura Champine with Roe Equity Research. I wanted to ask about keep rate, because I think a higher keep rate is part of the strategic plan. Can you give us where that was in Q2 and where it needs to be in 2018 to hit your margin expectations as laid out in the strategic plan?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Yes. We said as part of our strategic plan, our goal is to drive it ultimately, up to approximately 40%. Historically, it's ranged in the mid-20s. We are approaching 30%. Part of that is driven through the account management, the value proposition change. I will be clear, and we said then, it's going to take a little more than what we've done in the past to drive it to 40%. And we recognized that. And we are going to do things to do that. I'm going to give you a specific example.

We are working on enabling technology to give a greater visibility at the store level to help them make decisions around account management. Today, everyone knows that all the account management is handled at the local level, they do a great job, but they have somewhat limited visibility on the customers' life cycle. They have visibility on to that customer's current agreement, and their behavior and their payment, and length of time on rent. They don't have full visibility into the customer's life history with us. And that's a critical piece that's missing. Because we need to understand more about the customer and have that form our decisions around account management. And we believe by introducing that as one example that will help us move closer to that number.

Operator

Your next question comes from the line of Kyle Joseph with Jefferies.

Kyle M. Joseph - *Jefferies LLC, Research Division - Equity Analyst*

Actually, just a follow-up to prior question. I was just wondering if you have ever discussed the keep rates between segments. So at ANow versus other stores, and is that 40% target for both segments?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

No, no, it is not. And I think we have talked about the Acceptance Now in the past. The numbers are almost inverted. So if it's 25% or so in the Core. It's 75% plus in the Acceptance Now. And again, we've mentioned earlier this year, as part of our strategic plan, we felt and still feel, that there are some value proposition enhancements that can be made in that business model also, and we are driving to increase that keep rate something closer to 85%. And we believe there is opportunities to do that following the same rationale that we described in the Core, in terms of pricing and terming, coupled with consumer insights, and analytics, and underwriting and so forth.

Kyle M. Joseph - *Jefferies LLC, Research Division - Equity Analyst*

That's very helpful. And then Maureen, I know, you gave some commentary about corporate expenses. I know they were up sequentially. Was there anything onetime there, I did hear your Guidance for sort of FY '17?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Yes, it's mainly driven by the fact that we're more on track this year versus our bonus plan than we were last year. And so we're still accruing at 100% bonus for the year. That's driving the overwhelming majority. There were a couple of small, I would call nonrecurring items and some true-ups, and lower insurance expenses, which can be choppy from time to time. But generally, it's driven by that incentive compensation change year-over-year.

Kyle M. Joseph - *Jefferies LLC, Research Division - Equity Analyst*

Got it. And then, just there's some moving parts in Acceptance Now. So just a little help modeling there. Can you give us sort of like the average remaining term on the legacy Conn's and H.H. Gregg contracts?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Yes. I don't have the exact number in front of us. And I think what you're getting at, Kyle, understandably, is how do you think about the revenue falloff, right? And so we closed down the stores, we've transferred the accounts. There's an annuity associated with the accounts. How long is that annuity going to run and what does it look like? I know Maureen said in her comments, that you felt that -- that we feel strongly that the revenue portfolio ought to match last year.

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Right. Yes. And then we understand it's challenging to model this, and so we are giving some more color around what we believe 2017 revenue within Acceptance Now will be, and we are saying that it will be very similar to 2016 levels. We've seen higher revenue growth in the first half. However, because of the falloff of the store closures in the back half, it will be, we won't see that year-over-year growth. And so overall for the year, Acceptance Now revenue will be fairly similar to 2016 revenue.

Kyle M. Joseph - *Jefferies LLC, Research Division - Equity Analyst*

Got it, that's helpful. And then last question, apologies, but I also hopped on a little late. Did you give the write-offs by segment in your commentary earlier?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

We did, but I can do that again.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

2.4% in the Core, skip/stolens.

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

And 9.4% in Acceptance Now.

Operator

Your next question comes from the line of Brad Thomas with KeyBanc Capital.

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

I also got a little bit late here. So I apologize if I'm repeating anything. But just a quick follow-up on what you said on Acceptance Now, Maureen. So your guidance for 2018 Acceptance Now revenue is to be similar to 2016, so around the $818 million that you posted that year?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Yes. This is guidance for 2017, yes. So we had $818 million in '16, we expect to be similar to that in 2017.

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Got you. And then in '18, we will likely have a big falloff, or at least a falloff from the loss of h.h. gregg and Conn's? Is that still a reasonable expectation?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

In 2018, we typically see more of the falloff upfront, so there will be less falloff from those accounts in 2018 than there was in '17. We also have opened 70 new Acceptance Now staff locations this year, and we should continue to see benefits from those even more so in 2018.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Coupled with any others that we continue to open throughout this year and/or next year for that matter. So...

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Right, right. Perfect. And so, Mark, just a question on the Core. It's been about 6 months that you've been back in the CEO role. You're clearly helping to drive an impact on the business in areas that you can control. But it's still tough out there. Where are you seeing the greatest signs of encouragement and where are you seeing the biggest challenges? How confident are you today that you can actually get this business back to comping positive and when might that occur?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I will tell you, I've been very pleased with what we've accomplished year-to-date in the Core. It is, as I said, reiterated our belief and the outlook for the balance of this year, 2018 and beyond. We said, initially, and I reaffirm, again, today that we believe the fourth quarter is when you're going to see the positive comps come. The team has done a remarkable job of managing, the account management. If you think about the portfolio, there's been a heightened sense of urgency around the P&L. We've gotten -- we've introduced some additional new training, the introduction of the secret shoppers, our selling skills, [what about] customer retention, and clearly, we are doing a better job satisfying the customer. Products are staying on rent longer. Returns have gone down. Ownership has gone up. So I'm very encouraged on those -- on what we're seeing on that front.

The opportunities that are still in front of us, and it addresses maybe some of the things outside of your control, or what's going on in the broader market, how are consumers going to market, how and where do you meet the customer, where they want to be met. And we're very mindful that we've got -- as we think about emerging technologies, and whether it's the mobile wallet, e-commerce. E-commerce is new for us. I'm excited to say and pleased to say, we've actually extended our isle. I think we nearly doubled the SKUs that we are now offering through e-commerce in the second quarter. And that will continue to expand, as we get -- there's things that have to be further developed and/or worked out. But those types of initiatives are going to be important for us to execute and put in place, in order to do the things that we believe we're capable of doing.

As we said here today, there's nothing to suggest, we won't be able to do that. And we're taking steps and so I do feel really good, Brad. And as I sit here today, reaffirm, that based on everything we are seeing today, and where we are positioned today, would expect the comps to turn positive in the fourth quarter in the Core.

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Got you. And then one last question, if I could Mark, and you may have addressed little bit of this in your prepared remarks. But obviously, the company and the media have disclosed at least interest from outside parties in buying the company. Obviously, the Board has a different composition today than it did when you joined back in the CEO role. I guess, could you give us some more insight into the Boards view today on maybe why a review of strategic alternatives isn't appropriate at this time?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I would tell you that, again, the Board does regularly evaluate opportunities to drive an enhance value. It assesses them against a wide range of strategic options. They are well advised. And based on where we are today, the Board believes that it is not the right time to conduct a process as we execute on our plan, and the Board strongly believes we'll drive greater shareholder value.

Operator

Your next question comes from the line of Anthony Chukumba with Loop Capital.

Anthony Chinonye Chukumba - *Loop Capital Markets LLC, Research Division - Analyst*

Just had a quick question for you. Any update on the CFO search?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I'm sorry, you broke up Anthony. Any update on, I'm Sorry, what?

Anthony Chinonye Chukumba - *Loop Capital Markets LLC, Research Division - Analyst*

The CFO search?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

CFO search. I'm Sorry. Yes, I can give you a brief update. We haven't, obviously. First of all, I want to reiterate, Maureen has done a wonderful job. And I mean that in all sincerity. Obviously, there's been an awful lot going on over the last several months, no work had really been done at that point. Now, with the onboarding of Martin, the new Chief Human Resource Officer, with some of the other things behind us, if you will, that process will begin in the near future.

Anthony Chinonye Chukumba - *Loop Capital Markets LLC, Research Division - Analyst*

Okay. And then just one quick -- later follow-up, aside from the CFO, I guess, with this new -- with this onboarding, with these new executives that you mentioned earlier, any other major sort of openings from a Senior Management perspective?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I'm considering to evaluate a couple of areas. I feel very comfortable where we are. There's nothing pressing, I'll put it that way. Having said that, there's one or two areas that I'm continuing to evaluate, whether they're necessary and how they may fit in and so forth, but I'm not, beyond that I really don't have any, anything I'm willing to share, any strong view. I mean, the important takeaway is with Joel rejoined, and Martin joining, and so forth, and some other realignment that we have done internally. I feel really good about where we're positioned and the team that we have here. And I will share with you, because I think it's an important note. There's not been any turnover in the Senior Team in the last 4-plus months, 5 months. So people are aligned, committed and focused.

Operator

Your next question comes from the line of John Rowan with Janney.

John J. Rowan - *Janney Montgomery Scott LLC, Research Division - Director of Specialty Finance*

You guys spent a lot of time talking about better decision analytics both from the Core and in Acceptance Now driving better keep rates. Just give me an idea, though. How do you guys see those strategies changing your approval rates. And does that, a kind of embedded in, Maureen, the guidance that you gave for flat Acceptance Now revenue in '17 versus '16?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

The decision engine changes, we continue to make and enhance the approval process within Acceptance Now. And so yes, we consider any kind of enhancements that we are making through our decision engine in any guidance or results that we show.

We do believe that we will continue to make those enhancements. Will they necessarily mean, stricter, more restrictive approval rates? I don't think necessarily it has to mean that. What we're really focused on, and what you can see in the results in the second quarter, within the Acceptance Now channel, is that we've started really looking at select customers, those that have paid in quite a bit on their agreement and if there's some kind of negotiation or discounting that we could do to hold on to that customer and provide a positive customer experience, without taking the returned product. So we're continuing to make more decisions around how we best go about doing that. And we'll continue to do so going forward.

John J. Rowan - *Janney Montgomery Scott LLC, Research Division - Director of Specialty Finance*

So let me get this straight, to make sure I understand. So the decision analytics are not necessarily, when someone comes up and want to -- in Acceptance Now location to buy something, whether or not they approve that customer, it's more so about customer outreach and getting through to people who might be a few days delinquent, or whatever might be in renegotiating the terms of their rental agreement?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

No, no. It's kind of all of the above, John. It is on the front end. So when you come in, we're getting smarter and smarter. I mean, the more customer data points that we have, as the portfolio grows, and as the channel grows, you just get that much more intelligence in terms of customer behaviors. That does feed, what is they're likelihood to pay, what is there likely hood to keep, and so forth. And so all of that does just like any lending institution, all of those things go into: a, do we want to underwrite you? And for how much? And so it will play a role in the approval process. To Maureen's point, it can also further play a role in behavior -- or managing the account after the fact. And so we're trying to come at it from both angles.

The big opportunity, and I'll -- we've talked about this, but I think it's an important point to drive home here. Obviously, initially, and a lot of time focus and effort around the Core, given the size and what happened last year, and we talked a lot about the value proposition, all of the initiatives and really getting things stabilized there, and again, I compliment them, they've done a wonderful job of doing that and the results speak to it. We've made good progress in the Acceptance Now segment, but our work there is not done and we've talked about opportunities that we believe still exist in that segment, specifically, around the value proposition. And how do we think about the terms and the pricings, and I believe, that there are some structural things that we can do that will actually give us a greater return on our investments, while improving the value proposition to the customers, which will also reduce our losses and our risk and the downstream effect, whether that's a return back into the Core or write-off and so forth.

But like the Core, this is a portfolio business. So these things will take a little bit of time also, but the decision engine, I mean we make enhancements, we have a small committee that once a month gets together and we get output. So we get learnings and behaviors and then that influences, do you turn the dial a little tighter to the left, or can you go a little looser to the right based on these -- under scenarios and so forth. But there's a lot of opportunities still to be had in the Acceptance Now channels.

Operator

Your next question comes from the line of Carla Casella Hodulik with JPMorgan.

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

One follow-up on the Acceptance Now just to understand. So the sales are actually better than we expected, that's great. Inventory is lower than expected. So is it just better managing the inventory within that channel? Or is there less -- and actually, this is merchandise on rent. Or is the pricing? Is there's -- the disconnect doesn't make sense to me completely?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

You're talking the inventory on rent within the ANow segment, it's dropped.

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

Yes. It's down about $30 million from the last quarter.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

That's the falloff of h.h. gregg and Conn's. So as Maureen said, we closed all the stores, right? We [indiscernible] in the surviving stores, so you got the portfolio shrinking and yet at the same time, because you're not in those stores, you don't have the new growth coming on. Part of that was offset by an increase and that it is important, so yes, it's come down for that reason. But we have been driving the pricing up a little bit. So but the on rent, just the value is because of the h.h. gregg Conn's closures coming out and the annuity running down.

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

Okay, great. And how do you look at new business for Acceptance Now? Are you seeing any change in kind of competition or the manner of competition to get the new accounts?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

In Acceptance Now?

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

Yes.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Well, we had a successful second quarter. We opened 70 new locations.

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

Yes, that's great.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Despite the decisions that we made and what happened with h.h. gregg, not a decision and then Conn's, but we were able to add 70 additional. So we continue to have interest out there, and we are continuing to open new store fronts.

Carla Marie Casella Hodulik - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

I guess I'm trying to understand here. Are you having to get -- how you have to be more aggressive with your pricing or contract terms in gaining those? Or has the market stayed about the same that you're just having more success, given the initiatives that you put in place from a merchandising front?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

It's the latter. We have not enhanced the deals so to speak, to get the deal. So no, it's just the folks doing a good job of selling our value proposition and so forth to the retail partner and what it could mean for them with our manned solution and those types of things.

Operator

Your next question comes from the line of Budd Bugatch with Raymond James.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Yes, I had a couple of follow-up's if I could. Just labor, you've changed the labor model in the Core, I'm just curious now, how to model? What do you think about modeling the labor in the Core going forward and how to think about that, now that you've made those changes and have we fully -- had fully implemented them?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Yes, so from a labor perspective, we've been benefiting in the first couple of quarters of the year from the closures that were made in the second quarter of last year. So that no longer will be a benefit going forward. We talked about investing in our frontline coworkers earlier in the year. And trying to minimize turnover and increase the talent within the workforce at the store level.

And so in the back half of the year, you will start to see that investment that we've made, since we're no longer comping over the store closure benefit. And so from a run rate perspective, we will see an increase versus what you've seen within the second quarter.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

So I think it was like 30.4% in the second quarter, so you think the lever rate is going to be higher as a percentage of sales, and as you go down and maybe what you think in the quantification of that, Maureen?

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

Yes, it will be above 30%. We talked about the third quarter from a sales perspective, it's typically one of the lower quarters. So maybe a little bit higher than that versus the fourth quarter, which will be more in line with the second quarter, given the higher sales, primarily.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Okay. And you also talked -- and you've given the monthly metrics, which I think is great, that the fact that the monthly rate is up 5.7%, I think, in the third month of the quarter. Can you give us what that rate is? What is the agreement rate now on a monthly basis?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I don't think we've provided the actual amount before, Budd. I don't...

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

I understand, I was hoping you would. So don't let us stop you, Mark.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I don't have the exact number in front of me. So let me give it thought, see if I can find it. And then we'll share it with everybody when we decided to.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Okay. And my last question is, is the ANow sales effort, that was regenerated about a year or so ago. I guess the 70 locations are a bit of a process for that, or a product of that. What looks -- what's the pipeline going forward for new locations for ANow?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

It's a little harder to quantify, right? I mean, when you think about opening [Denoble] brick & mortars, you could very much -- or certainly, more so control that. In this case, it's not just finding, it's negotiating -- going through the whole sorts, so it's really hard to put an exact number on it. I can tell you, and I will say comfortably, that we have a pretty active pipeline going right now. And so I feel confident that you'll continue to see nice numbers of new stores being added throughout the rest of this year.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Any thoughts about direct versus staff, you still...

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

These are still manned solution, and we continue to make progress on the unmanned. And that again, that's an important opportunity. Yes, that's a big opportunity for us. And we're committed to having a very viable user-friendly scalable unmanned solution at some point in the future. But what we're talking about here are the manned.

Beryl Bugatch - *Raymond James & Associates, Inc., Research Division - MD and Director of Furnishings Research*

Okay. And just, you went to a 50/50 proposition in the Core versus 70/30 for EPO. I think -- can you talk about what's that doing to help, you -- your keep rate?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Well we're very early into it. But as I said, we are pleased that our returns, the pickups are down 9% year-over-year. The keep rate, where the time on rent so there's a lot of ways that we measure this, but the time on rent has in fact extended, so they are staying out longer. Our purchase options or those that are going to ownership, that percent is actually up.

And as I said, we were historically -- I already answered you, we were historically, 25%, and we're pushed 30% in the second quarter. So now, there's a lot of things moving in there. I believe, we are trying to move through some older products so those had shortened terms. And I just want to be clear, we are 90 days into that. So -- but directionally, all the leading things, number of weeks on rent, the returns, all of those are trending in the right direction, gives us -- makes us feel good about all of that.

Operator

Your next question comes from the line of Anthony Chukumba with Loop Capital.

Anthony Chinonye Chukumba - *Loop Capital Markets LLC, Research Division - Analyst*

I just want to make sure that I heard correctly. Did you say that you opened two facilities for Acceptance Now to dispose of return product? I just wanted to clarify that.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Yes, what I was alluding to, is if you happen to look at the segment reporting on the balance sheet, you will have noticed that the held for rent inventory in the Acceptance Now segment went up sequentially. And I was saying that, that was intentional and temporary, and that we were kind of -- assume that normally what happens that product gets picked up and almost immediately within a matter of 2 weeks, it's dispersed into the Core stores, moved through that channel, if you will.

Given the influx of inventory we had and some other things we wanted to work through, we slowed down the process of moving that product into the Core, so that we could address some immediate issues in terms of the quantity that we had. We were opening up, I said, those two clearance centers to relieve pressure. And, so we let it back up a little bit, intentionally in the ANow to put some other things in place. All of that has been done, so that channel is back open. What I'm trying to suggest is that you can expect to see that number come back down to its historical, and hopefully, over time, even below historical as we improve some of the other outcomes and so forth.

Anthony Chinonye Chukumba - *Loop Capital Markets LLC, Research Division - Analyst*

Okay. But with, so these, sort of, Acceptance Now clearance centers, this is just -- it's just sort of a temporary thing. It's not going to be sort of like an ongoing strategy?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

You're breaking up a little bit, Anthony, but I think you are questioning the clearance centers, and if those are an ongoing strategy. It's to be determined. We went in there with a temporary, so we have short-term leases. They have options to renew. We like what we are seeing at this stage. Again, we've really only been into it about 6 weeks on average. We have two standing. We are considering maybe a third. I don't think it would be any more than that.

And then whether they are there, it will depend. If it proves to be that this is another successful way to move product more quickly, and get the return on the investment and so forth, then perhaps, it's got a longer life.

On the other hand, if we can self-solve some of these other issues, and the demand or the need is not as great, then they very well go away. So it's -- right now, we went into it with more of a temporary mindset, i.e. a year or less kind of on the onset.

Operator

Your next question comes from the line of Bradley Thomas with KeyBanc Capital.

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

A lot of follow-up questions here this morning clearly. Thanks you for taking mine. Just wanted to clarify, I think there were some comments that you all made about Core same-store sales expectation for the third quarter and if I heard you right, did you say that you thought it was going to be similar to how 2Q played out, down 10%? Did I hear you right there?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

No, we didn't. No, what we said -- Well, we didn't say anything about the third quarter, that it was going to continue to improve and that we felt by the fourth quarter you would see a positive number, and candidly for us to get to a positive in the fourth quarter, has to imply that there is going to -- we are going to continue to step down, right? So the first quarter, I don't remember the exact, was 13%, I think, and then we improved 200, 300 basis points in the second quarter, as it going to be a similar?

Again, we haven't given specific numbers or guidance on that, but what we have said is that we believe and still believe that we will turn a positive comp in the quarter, during the fourth quarter. So to do that, one would have to assume that it will continue to improve between here and there.

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Got you. That's what I had thought you would have said. But I misheard you earlier. And then just, I'm just trying to connect the dots to operating income in the Core, and really for the whole company. The margin comparisons do get easier here, the sales comparison is get easier as well. Clearly, if you comp positive in the fourth quarter, one would think you're operating income would be up in the fourth quarter. I mean, how are you feeling about the likelihood that you might be able to actually increase operating income dollars and EBITDA dollars in 3Q?

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

In Q3?

Bradley Bingham Thomas - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Yes.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

I think, Maureen, didn't you say that you expected it to be somewhat similar. I said earlier that Q2 and Q3, seasonally, have always been our most difficult. And you can go back and look at all the prior years, there may have been one year exceptional when they rolled out cell phones. But otherwise, Q2 and Q3 have always been the most challenging given the portfolio nature and they tend to slip a little bit and then it's the fourth, when it sprints.

Maureen B. Short - *Rent-A-Center, Inc. - Interim CFO*

In the third quarter, we will see more of that labor increase that I spoke about earlier, with the investment that we've made within the store base, of trying to stabilize the turnover. So we will see -- still continue to see a challenging third quarter. But the fourth quarter is when many of the initiatives that we've rolled out, will become a more substantial piece of the portfolio. And so that the fourth quarter is really when we expect to see that revenue growth and the profit growth.

Operator

We have reached the allotted time allowed for the question-and-answer session. I would now like to turn the call back over to CEO, Mark Speese, for closing remarks.

Mark E. Speese - *Rent-A-Center, Inc. - Co-Founder & CEO*

Thank you, and thank you all for your time and interest. Let me reiterate, that we are pleased with the progress and the results. We believe that we are positioned to continue to execute our plan, and we reaffirm our belief in 2018 and beyond.

Thanks, again, for your support. And we look forward to providing you our monthly metrics reports, and we look forward to visiting with you again next quarter. Thanks, and have a great day.

Operator

This concludes today's conference call. All participants may now disconnect.
