TOPGOLF CALLAWAY BRANDS CORP.
SECOND QUARTER 2024 EARNINGS CALL PREPARED REMARKS

Katina Metzidakis, Vice President of Investor Relations and Corporate Communications

Thank you, operator and good afternoon, everyone. Welcome to Topgolf Callaway Brands' conference call announcing our intent to separate into two independent companies. I'm Katina Metzidakis, the Company's Vice President of Investor Relations and Corporate Communications. Joining me as speakers on today's call are Chip Brewer, our President and Chief Executive Officer, and Brian Lynch, our Chief Financial Officer and Chief Legal Officer.

Earlier today, the Company issued a press release announcing its intent to separate its business into two independent companies. We have also published a presentation which, along with our press release, is available on the Company's Investor Relations website under the "News and Events" tab under "Webcasts and Presentations." The purpose of this call is to address the contemplated separation of Topgolf and, therefore, we will not be discussing any intra-quarter trends nor providing any other company updates during this call.

Aside from revenue, the financial numbers reported and discussed on today's call are non-GAAP measures. We identify these non-GAAP measures in the presentation and reconcile the measures to the corresponding GAAP measures in accordance with Regulation G. Please note that this call will include forward-looking statements that involve risks and uncertainties that could cause actual results to differ materially from management's current expectations. We encourage you to review the safe harbor statements contained in the presentation and the press release for a more complete description.

With that, I would now like to turn the call over to Chip Brewer.

Chip Brewer, President and Chief Executive Officer

Good afternoon, everyone, and thank you for joining us today. As you have seen in our latest press release, we announced that Topgolf Callaway Brands intends to separate into two independent companies with the goal of maximizing shareholder value and driving the full potential of each business. While we expect that a spin-off of Topgolf into a standalone public company is the most likely separation path, the Company will continue to evaluate other options for separation to maximize shareholder value.

This transaction is an important milestone in our company's history. Since our founding in 1982, Callaway has always prided itself on delivering innovation that makes the game of golf more fun and accessible. Over the last decade, we have re-established ourselves as the leading brand in golf equipment, with the #1 U.S. market position in golf clubs, and the #2 position in golf ball, combined with a strong, complementary active lifestyle business. Since our merger with Topgolf, we have both improved and grown this business to over 100 U.S. and international venues. We have transformed the technological capabilities of the business, installing Toptracer in all venues and rolling out a system-wide digital bay inventory management system and new consumer data platform. These investments in Topgolf have created a scaled business with the capabilities necessary to achieve its growth opportunity as a standalone entity. Importantly, during this period, Topgolf has significantly expanded its market leadership position. This expansion, along with Topgolf's impressive venue level EBITDAR margin improvement, has allowed us to outperform our original EBITDA and free cash flow expectations for Topgolf.

Post-transaction, Callaway will be well positioned to continue its journey as a leading, and more focused, golf equipment and active lifestyle business that we believe will be well understood and valued by the market. Topgolf will remain the category leading, high-growth, pure-play venue-based golf entertainment business, empowered to pursue its own distinct long-term strategy and value creation opportunity.

Over the last year, we have conducted an extensive strategic review of both the Callaway and Topgolf businesses. We believe that a separation will maximize shareholder value, with each business greatly benefitting from enhanced strategic focus, a strong balance sheet and optimized capital allocation policies, a simplified operating structure, and, importantly, a distinct investment thesis.

This transaction will create two strong, focused operating companies with industry-leading market positions.

At Callaway, our vision is to be the leader in golf equipment along with highly complementary businesses in Active Lifestyle and, post separation, in range technology. Callaway's portfolio of leading brands would include Callaway, Odyssey, TravisMathew, OGIO, Jack Wolfskin and Toptracer.

The Callaway business, including Toptracer, generated approximately $2.5 billion of revenue in the last twelve months through Q2 2024.

As an industry-defining brand, Callaway continues to solidify its legacy as a leader in golf equipment. Our ongoing innovation has enabled us to maintain our leading market share position in golf clubs. Additionally, our substantial investments in golf ball have resulted in steady share gains, reaching a record 22% of US dollar market share in July of this year. As a standalone business, there are significant opportunities for growth as golf is enjoying long term tailwinds. We have demonstrated strong operating abilities over an extended period of time, and we will be positioned to continue to invest in our core strengths as well as new capabilities. Additionally, Toptracer will provide a long-term opportunity for deep engagement with avid golfers and to transform the driving range experience.

Callaway's golf equipment business will be supported by a strong portfolio of popular apparel and accessory brands. Our Active Lifestyle brands are complementary to our Golf Equipment business in that they support each other and provide operating leverage across our global resources and scale. These brands all hold leading market share positions in their respective categories and are well positioned for future growth.

Callaway will continue to leverage its world-class product development and supply chain capabilities across its businesses.

In terms of future capital allocation priorities, Callaway will retain the existing Topgolf Callaway financial debt (including our term loan and convertible debt) and would initially utilize free cash flow, as well as any retained stake in Topgolf, to de-lever before considering the return of capital to shareholders or other capital allocation priorities. In this manner, we intend to reduce our leverage to 3 times or lower net debt to EBITDA within 12 months of separation. And, at the same time, Callaway will be well positioned to continue to reinvest in its market leading positions to drive future growth.

Importantly, Callaway will be a business that has historically been well understood and valued by the market.

At Topgolf, we will continue to build on our success to take full advantage of the significant white space opportunity in venue-based golf entertainment, where we are the clear market leader.

As we have discussed in the past, Topgolf is expected to continue to benefit from shifting consumer trends, supporting the increasing popularity of off-course golf in the U.S. and globally. In 2023, an estimated record 32.9 million Americans participated in off-course golf, representing an 18% year-over-year increase and a 41% increase since 2019.

Topgolf's portfolio will initially include over 100 U.S. and International venues, and they will seek to grow their footprint against a backdrop of significant whitespace, identified as approximately 250 venues in the U.S. and 250 internationally. The team's multi-year track record of successfully identifying and opening venues that consistently achieve our ambitious financial return rates is nothing less than extraordinary. This capability has been built up over multiple years and reflects the high level of talent within our real estate and our venue operations teams.

The Topgolf business, excluding Toptracer, generated approximately $1.8 billion of revenue in the last twelve months through Q2 2024.

The enduring strength of Topgolf is the unique nature of the venue experience, one that consumers continue to enjoy and that both builds upon and leverages the positive momentum of golf overall.

While the recent macro trends have certainly pressured same venue sales, we view these trends as largely cyclical as we are working through a period of slowing consumer spend, along with a post-COVID reversion in corporate events. At the same time, we are taking clear action to further strengthen the ability of the business to drive positive same venue sales as conditions normalize. We believe the longer-term trends for golf and experiential entertainment such as Topgolf remain positive. Furthermore, historical data shows that even prior to the improved capabilities we are now putting in place, for instance from 2015 through 2019, the business was able to deliver positive same venue sales performance. More recently Topgolf delivered 7% positive same venue sales in 2022 and the 1-2 bay consumer portion of our business, which represents approximately 80% of Topgolf's venue revenues, delivered 4% same venue sales in 2023.

Turning to our improvement initiatives and how we are going to come out of this period even stronger: as I discussed on our second quarter call, we are making investments in our internal and front-end digital capabilities, leveraging our recently launched consumer data platform and digital bay inventory management system. We believe these actions will allow us to enhance the user experience and deliver more tailored offerings to customers, ultimately driving revenue growth. In addition, we are placing increased emphasis on newness and the experience in the venue – via new games and other surprise and delight elements such as the launch of our new "Sure Thing" golf club – as we believe these will ultimately drive both new and repeat visits. Lastly, we will continue to look to partnerships to increase awareness as well as traffic.

In response to our actions, the fun scores, registered after guests play, have steadily improved. Fun scores are a leading indicator of future growth and have historically been highly correlated to our consumers' likelihood to both return to and to recommend Topgolf. Returning to same venue sales growth will take time, but we are confident that we are putting the right plans and teams in place to execute it.

Looking ahead, as same venue sales growth resumes and the profitability of our venues steadily increases (as we have a proven track record for driving venue profitability improvement throughout the business cycle), we expect our already attractive venue returns to improve even further. With these expected improvements in venue returns, coupled with the on-going capture of our significant whitespace opportunity, we believe Topgolf is well positioned to drive durable top- and bottom-line growth.

And I should note that while these are the pillars of our immediate action plan today, I look forward to the Topgolf team providing greater detail on the Company's ambitions as we get closer to the separation.

As we have discussed on prior calls, the team at Topgolf has driven significant improvement in venue economics over time. In 2019 compared to LTM Q2 2024 we have increased EBITDAR per venue from $5.8 million to $6.7 million, EBITDAR margin from 29% to 34% and rent coverage, defined as the EBITDAR to rent ratio from 2.6x to 2.8x. We know our venues are capable of generating even stronger economics and returns, but their performance today already drives significant embedded cash flow that will create financial flexibility and reinvestment capital going forward.

As we look towards the planned separation, we are committed to positioning Topgolf to deliver against its white space opportunity as a standalone business, while at the same time delivering positive free cash flow and maintaining a strong financial position

To this end, Topgolf will be well-capitalized at the time of separation, with a cash balance of approximately two hundred million dollars and no financial debt. Looking ahead to 2025, to appropriately balance growth and free cash flow during this transition year, we intend to reduce Topgolf's new venue growth plans for 2025. Our current estimate would be for a mid-single digit number of new venues. We believe this change will further improve Topgolf's already strong financial position and will likely be well received by most shareholders in what will be a newly independent entity. One of the advantages of Topgolf's current scale, embedded free cash flow, and strategic position is this optionality on when and how we build new venues, thereby allowing us to balance our mutual goals of growth and positive free cash flow. Accordingly, we expect Topgolf to be free cash flow positive in 2025, just as it was in 2023 and as it is forecast to be in 2024.

And, to be clear, our return metrics remain strong, as does the quality of our venue pipeline.

Looking further forward, it is our expectation that continued improvements in existing venue performance and continued venue unit growth can drive meaningful improvement in profitability as the business matures.

As a result, we are very excited about the financial prospects of Topgolf as a standalone company. As outlined here, it will start out in a well-capitalized financial position with the clear expectation of continued positive free cash flow performance. Over time, we believe that its core fundamentals, supported by a significant whitespace opportunity, will create substantial value for shareholders.

Beyond the attractive fundamentals of the two new businesses, Topgolf and Callaway will continue to partner to unlock further value. Post-transaction, Topgolf and Callaway will enter into ongoing, value-creative commercial agreements with one another. As an example, Callaway is expected to remain the exclusive golf equipment partner for Topgolf.

Now, I would like to turn the call over to our Chief Financial Officer, Brian Lynch.

Brian Lynch, Executive Vice President, Chief Financial Officer & Chief Legal Officer

Thank you, Chip. Turning to the transaction details, it is the Company's intent to spin at least 80.1% of Topgolf to obtain the desired tax-free treatment of the spin-off for U.S. federal income tax purposes. The Company will also consider retaining a limited ownership position in Topgolf for a period of time. Existing shareholders of Topgolf Callaway will receive a pro-rata allocation of shares in the new Topgolf company.

We expect these new Topgolf shares to be listed on the New York Stock Exchange, and investors will receive detailed information on the business of the new Topgolf company. This transaction is subject to customary approvals to be secured prior to the separation. This type of transaction can generally be completed in approximately 9 to 12 months from the time of announcement. Based on what we know to date, we would expect to complete our transaction in the second half of 2025. For internal purposes we are targeting July 1, 2025.

Prior to separation, we plan to establish independent organization structures, complete audited financials and finalize capital structure and capital allocation policies for the two separate companies. As previously mentioned, all financial debt, including our term loan and convertible notes, will remain with Callaway. Topgolf will retain its venue financing obligations, but will have no financial debt. Topgolf will also be funded with a significant cash balance, our current estimate of this would be approximately two hundred million dollars. Both companies are expected to be free cash flow positive from the outset and would have strong financial positions. From a leverage perspective, at the time of the spin, Topgolf with no financial debt would not have any financial leverage and Callaway is expected to be at 3 times or lower Net Debt to EBITDA within 12 months.

Prior to closing, we will seek to obtain a private letter ruling from the relevant tax authorities and/or an opinion from tax counsel and would seek the U.S. Securities and Exchange Commission declaring effective the registration statement related to the spin-off. We would also seek to obtain other customary approvals, as well as final approval from our Board of Directors.

Callaway will continue to be led by Chip Brewer. Topgolf will continue to be led by Artie Starrs, Chief Executive Officer of Topgolf. Further details about the management teams will be announced later in the transition.

While the Company expects that a spin-off of Topgolf is the most likely separation path, we will continue to evaluate other options for separation to maximize shareholder value.

The following information is meant to provide clarity into the components of the two businesses going forward and other ongoing and one-time expenses that will be incurred as part of this transaction. As we have mentioned, the new Callaway would consist of the existing Golf Equipment and Active Lifestyle segments plus the Toptracer business. The new Topgolf business will include the existing Topgolf segment, less the Toptracer business.

In the last twelve months through Q2 2024, the existing Golf Equipment and Active Lifestyle segments generated $2.4 billion of revenue and $267 million of Adjusted EBITDA. During this same period, the existing Topgolf segment generated $1.8 billion of revenue, $333 million of Adjusted EBITDA and $245 million of Adjusted EBITDA less venue financing cash interest. During the last twelve months through Q2 2024, Toptracer's results were included in the existing Topgolf segment results and consisted of revenue and EBITDA of $46 million and $1 million, respectively.

As part of this transaction, we expect approximately $25 million of net dis-synergies, with slightly more than $25 million incurred at Topgolf and a net benefit at Callaway. We also expect one-time transaction expenses of approximately $50 million.

I will now pass it back to Chip to close our prepared remarks.

Chip Brewer, President and Chief Executive Officer

Thank you, Brian.

We firmly believe that our announcement today is in the best interest of our fellow shareholders. Both companies will enter this next period with strong financial positions and clear strategic direction; and following the separation, both businesses will benefit from more focus, a simplified operating structure and a more distinct and compelling investment thesis for investors. Most importantly, after a thorough analysis with the full involvement of our board of directors, and the counsel of multiple outside strategic advisors, including both Goldman Sachs and Centerview Partners, we believe that this separation will unlock significant shareholder value.

And to be clear, we believe both companies will be financially strong from the start and both companies are expected to generate positive free cash flow in 2025. Topgolf in particular, will retain its venue financing obligations, but will have no financial debt, be funded with a strong cash balance of approximately two hundred million dollars and is expected to be free cash flow positive in 2025, just as it was in 2023 and is forecast to be in 2024.

I am sure you have many questions; and, as I hope you understand, we will not have all the answers today. We will be sure to continue to provide updates as appropriate in the coming months. As we get closer to the separation, both Topgolf and Callaway will deliver more detailed presentations on their business plans and investment thesis.

Thank you and operator, please open the lines for Q&A.