Q3 2019 New Media Investment Group Inc Earnings Call - Final

3,574 words
31 October 2019
CQ FD Disclosure
FNDW
English

Presentation

OPERATOR: Ladies and gentlemen, thank you for standing by, and welcome to the New Media Third Quarter Earnings Call. (Operator Instructions) Please be advised that today's conference is being recorded. (Operator Instructions)

I would now like to hand the conference over to your speaker, Ashley Higgins, Investor Relations for New Media. Please go ahead, ma'am.

ASHLEY HIGGINS, IR, NEW MEDIA INVESTMENT GROUP INC.: Thank you, Zetania. Good morning, everyone, and thank you for joining our call today to discuss New Media's third quarter results as well as our pending acquisition of Gannett. During this call, we will discuss both the Gannett transaction and New Media's financial results for the quarter. If you navigate to the New Media website, you will find that we have posted an earnings supplement in addition to our earlier press release. We will not walk through the supplement on today's call, but it can provide you with additional detail on this quarter's performance should you have interest.

Before we begin, please let me remind you that this call is being recorded. In addition, statements made during this call with respect to future results and events, including the proposed acquisition and related transactions, are forward-looking statements that are based upon current expectations. Actual results and events could differ materially from those discussed today. We encourage you to read the forward-looking statements disclaimer in the presentation as well as the risk factors described in New Media's filings made with the SEC.

In addition, we will be discussing some non-GAAP financial measures during the call today, and the reconciliations of those measures to the most directly comparable GAAP measures can be found in the earnings supplement.

Lastly, I would like to remind you that nothing on this call constitutes an offer to sell or solicitation of an offer to purchase any interest in New Media. The webcast and audiocast is copyrighted material of New Media and may not be duplicated, reproduced or rebroadcasted without our consent.

With that, I'd like to turn the call over to Mike Reed, New Media's Chairman and CEO.

MICHAEL E. REED, CHAIRMAN, CEO & PRESIDENT, NEW MEDIA INVESTMENT GROUP INC.: Thanks, Ashley, and good morning, everyone. Thanks for joining our call this morning. In addition to reviewing our third quarter results with you, also we'll take the opportunity this morning to update you on our pending acquisition of Gannett, how that's gone so far, and I'll discuss the incredible opportunity we think it brings for creating shareholder value and reiterate why we believe you should vote in favor of our transaction on November 14.

Starting with the quarter, first. Our third quarter financial performance delivered on as adjusted EBITDA and cash flow, but was lower than our expectations on revenue. We announced our Q3 dividend earlier this month on October 16 of $0.38 per share, and that will be paid on November 12 to shareholders of record tomorrow, November 1.

There were 2 factors that challenged our quarterly revenue performance. First, Hurricane Dorian impacted some of our southeast markets, which caused a loss of approximately $1.5 million to revenue, as adjusted EBITDA and free cash flow. Second, market rumors and the eventual announcement on August 5 of our agreement to acquire

Gannett inevitably caused some distraction from operations, which impacted our revenue primarily across print and digital advertising. However, since the announcement, we have worked hard to refocus and have stabilized performance by the end of the quarter.

Another positive note on revenue is that we have seen a meaningful improvement in UpCurve's revenue trends starting in mid-September and continuing into October, moving back toward our targeted revenue growth range for the year. Very encouraging. In Gatehouse Live, our events and promotions business had another strong quarter with revenue up 49.6% to the prior year. On the events side, we hosted the Best of the Best Community's Choice Awards during the quarter, which outperformed our expectations. We also had a great quarter for the endurance races, hosting over 66,000 participants. And on the promotions side, September was the best month yet for revenue. Gatehouse Live is on track to earn over $60 million of revenue in 2019. I think we had previously guided closer to $55 million earlier this year. And keep in mind, we started this business from scratch, 0 revenue 4 years ago. This homegrown, fast-growing business is meaningfully contributing to our diversification away from declining revenue in traditional print advertising.

We were also really pleased with our subscriber growth trends in the quarter. Our digital-only subscriber growth, again, more than offset our print subscriber decline, growing 64.9% to the prior year, up to 217,000 digital-only subscribers. Our ability to sustain subscriber growth is putting us on a path to a much more sustainable circulation revenue stream over the long term.

As I mentioned a few minutes ago, as adjusted EBITDA and free cash flow for the quarter were very strong. These results reflect our efforts to further centralize our infrastructure, much of which was implemented earlier this year.

I'd like to turn now to our pending acquisition of Gannett, which we believe is an incredible opportunity to create shareholder value. To recap, we announced an agreement to acquire Gannett on August 5, subject to customary closing conditions, including regulatory clearances and shareholder approval. As of last week, we have obtained all of our required regulatory approvals and are now focused on the shareholder meetings that both New media and Gannett will hold on November 14. Assuming we receive shareholder approval, we would plan to close the acquisition shortly thereafter. We are financing the purchase price with financing that, while expensive, can be repaid without penalty at any time. And I'll say more about the financing in just a minute.

Another important component of the acquisition is the changes to our management agreement with Fortress. An independent committee of our Board negotiated an amendment to our management agreement effective as of the closing of the acquisition. The amendment fixes the termination date for the management agreement as of December 31, 2021, and reduces the incentive fee rate for the remainder of the term. As part of the amendment, we were able to eliminate the cash termination payment, otherwise payable to fortress upon termination in exchange for the issuance to Fortress of about 4.2 million shares of New Media common stock. There will also be 3.2 million options issued to Fortress struck at a premium to where New Media's current trading price is. Finally, Fortress will be restricted from selling its shares until after the termination of the management agreement.

As I said before, the opportunity to acquire Gannett is an incredible opportunity to create value for our shareholders. Our companies will be much stronger together than either is today on a stand-alone basis. There are several primary reasons for that. Before I go through those reasons, one note I would share with you is since New Media's inception in my tenure as CEO of the company since its inception, this is the single biggest and best opportunity our company has had. I haven't seen more upside associated with the transaction for our shareholders than I see with this one. I'm extremely excited about it.

Now, first, this acquisition creates the best path for our combined company to stabilizing top line revenue trends and then realizing growth. We realized that we could pursue growth through other avenues, but we strongly believe, as I just said, the acquisition of Gannett is the best option with the most upside.

Second, the acquisition presents significant cost reduction opportunities that can be achieved with greater size and a faster time line than either company could achieve on a stand-alone basis. We previously announced expected annual run rate synergies of $275 million to $300 million. Since our announcement on August 6 -- August 5, we have been working hard on integration planning, and we are now even more confident in our ability to realize the high end of the range in savings and within the 18- to 24-month period we previously stated. We feel great about the synergies.

Third, the acquisition creates the leading U.S. print and digital news organization with deep local roots and national scale. Scale is a necessity for a digital business, and our size will enhance our earnings potential. Our ability to generate substantial cash flows will allow us to deleverage the balance sheet quickly and to return capital to shareholders through dividends, in addition to investing for growth that will drive revenues.

One area of the deal that we know investors have had questions about is the financing for the acquisition. We view this loan as bridge financing. Before selecting this financing, we did a comprehensive analysis of other financing options available in the market. The financing we settled on has several positive features to it. It has no financial covenants other than a minimum liquidity requirement. And importantly, we can prepay without penalty at any point. We see a clear path to aggressively paying down this facility with Apollo and bringing our leverage ratio to under 2x in 2021. At this level, we believe we could refinance into a traditional bank financing at a much more attractive rate while maintaining the flexible covenants.

As we have kicked off integration planning in earnest, we are increasingly excited about the future prospects of the combined company. Our teams have complementary strengths and experiences and are planning to leverage the best practices of both companies to help us transform our business model to create a more agile and dynamic organization. We announced on Tuesday the members of our combined Board, and they bring a strong understanding of the media industry and our legacy companies. In addition, they bring us expertise in finance, digital, marketing and business development. I can't emphasize enough that New Media has a much larger opportunity to grow and will be a much stronger company immediately when combined with Gannett. We believe this acquisition is the single best path for creating significant shareholder value over many years to come. We are extremely excited about the future and hope that we have your support for this transaction so that we can take advantage of the opportunities we see before us.

Now let me turn and talk about a very important part of our business, our journalism. Sustaining local journalism is the reason that we are fighting so hard to transform our business model so that we can ensure our local communities have trusted, high-quality journalism for the next 100 years. In the quarter, we have a new partnership with the Midwest Center for Investigative Reporting that is funding an agricultural data journalism fellowship. It will allow our reporters to access the center's data sets and allow us to further develop products targeted at our rural audiences. The Austin American-Statesman was awarded first place for Best Digital Presence and Best Section by the Society for Features Journalism. And our reporter, Alex Kuffner, in The Providence Journal won a first place award from the Society of Environmental Journalists for his coverage of invasive jellyfish in Rhode Island waters. Congratulations to you all, and thank you for your continued service, commitment and hard work on behalf of our communities.

Now I'd like to open the line for questions.

ASHLEY HIGGINS: Zetania, you can go ahead and open up the queue.

Questions and Answers

OPERATOR: (Operator Instructions) Your first question comes from the line of Jason Bazinet with Citi.

JASON B BAZINET, MD AND U.S. CABLE & SATELLITE ANALYST, CITIGROUP INC, RESEARCH DIVISION: I guess in your prepared remarks, you mentioned you'd received all regulatory approvals for the merger, just waiting on the shareholder vote. I think there was some news item, can't remember when it came out, around the FCC sort of questioning the Apollo financing, given the cross ownership of TV stations and newspaper assets. And I was just wondering if you could comment on whether or not that is still an outstanding issue or if that's behind you now.

MICHAEL E. REED: Well, the FCC has no jurisdiction in our transaction, Jason. We're -- we don't have licenses that are being reviewed for transfer by the FCC. And so we have committed financing from Apollo that's not subject to the FCC review and approval, and our transaction is not subject to any review or approval. So I think that was more rumor than fact-based. And we have -- there's been no alteration to our plans for a November 14 vote and a closing shortly thereafter.

OPERATOR: Your next question comes from the line of Lee Cooperman of Omega Family Office.

LEON G. COOPERMAN, PRESIDENT, CEO & CHAIRMAN, OMEGA ADVISORS, INC.: When I listen to you, Mike, on the call, I'm reminded of the deceased comedian, Rodney Dangerfield, who used to complain he gets no respect. And so I look at Page 88 of the S4, the proxy statement that came out and connects with the merger. And if I take the numbers there, the stock is presently trading at 2.7x EBITDA. And this assumption -- so nobody believes the numbers, no, on the resized dividend, the stock gives 9%, your 2.7x EBITDA. In 2021, you're going to fix the financing. Nobody believes it. And I think part of the problem is Gannett's total revenues have been declining at over 9% over the past few quarters. New Media's revenues have been declining at around 7%. In fact, I think the Q3 was 7.9%. Post merger, you're projecting declines 3.5% in 2020, 1.5% in 2021 and down 0.4% in 2022. As regards margins, they're running 11% to 12% currently. Post merger, you're expecting 15.6%, 18.6%, 21.3%, '20, '21, '22. Now I can understand the margin expansion stemming from the synergies, but I don't understand how we go from revenue declines that are 7% or 8% to 3% or 4%. What is behind that and how confident they are that this is going to be the case?

MICHAEL E. REED: Yes. Thanks, Lee. I'm highly confident that, that's going to be the case. And what's really driving the historical declines, which you'll see reverse as we go forward is print advertising. And in the combined company over the next 3 years, print advertising is projected to go from over 30% to less than 15% of the total revenue. So 85% of our revenues will be driven by categories that we feel we can have either stable or growing. So we feel very confident over the 3-year period that the biggest driver of declines, print advertising, will be a very small portion of our overall business. And that leads to the continuous revenue improvement you see on the page you noted in the proxy. That's why we feel confident. And you're exactly right on margin. As we stabilize the top line, the synergies that we realize will improve our margin.

LEON G. COOPERMAN: How quickly in the new year, 2020, will you be able to generate asset sales or it'll become clear to the public that the projections that you have are realistic and that you can start paying down debt dramatically. What kind of asset sales, order of magnitude, do you anticipate in 2020?

MICHAEL E. REED: We're working on those things right now, Lee, so I would expect that you would see asset sales throughout the entire year, beginning in the first quarter and continuing through the fourth quarter. We'll begin to realize synergies immediately. So you'll see those in the first quarter as well. So I would expect shareholders would be able to see, both in our financial statements and through asset sales, our performance relative to the plan as well as our ability to delever quickly.

LEON G. COOPERMAN: Great. I know we're happy to get rid of Fortress, but I got to tell you, and I probably shouldn't say this but I will say it because that's my nature of speaking what's on my mind. Basically, I was in the hedge fund business for 26 years. I only got paid when I made money for investors. The kind of money that Fortress is walking away here with -- and I know it's not your doing. They brought this public in 2014 at $16 a share. The stock is $8.5 and they're going to walk away with hundreds of millions of dollars. It's just morally wrong and they shouldn't even take the money, given what they've done here. But I'll pass on the question to the next person. I just want to get that on the record. It's just terrible.

OPERATOR: Your next question comes from the line of Jeff Bernstein of Cowen.

JEFFREY M. K. BERNSTEIN, VP, COWEN INC.: Yes. Could you just talk a little bit about the digital business? It looks like it's basically been flat here for about a year. It had been a really good source of growth. And I know the combined company is going to have a much, much bigger digital footprint. So maybe you could make some forward-looking statements about the kind of growth rate you'd like to see in the digital side in the combined entity.

MICHAEL E. REED: Yes. Thank you. The third quarter is a one snapshot in time, so I wouldn't read too much into that. If you look at the first half of the year, we produced much better revenue growth on the digital side, and we expect that going into fourth quarter as my remarks indicated this morning. There definitely was some distraction in the third quarter due to the rumors about the transaction, and then, of course, the announcement of the transaction and synergies and so forth.

We also had a management turnover in the UpCurve business during the second quarter, which we're addressing, but that led to some slowdown early in the third quarter. So it's a very -- it was a very small snapshot in time. I wouldn't read anything into it. The overall digital trends we have produced, we think we will continue to produce. As we look forward, we would expect to continue to grow digital revenues at more than double-digit pace in the combined company.

OPERATOR: There are no further questions. Mr. Reed, you may proceed with any closing remarks.

MICHAEL E. REED: Thank you. So just to reiterate, we are excited and confident about the future and believe bringing together the best of management from both companies as well as best practices and products will greatly enhance our ability to grow revenues and cash flow. Scale matters in the digital space. And this combination really enhances the scale of both companies, which we believe improves and speeds our ability to grow.

This deal also gives both companies a stronger and longer bridge to cross as we transform our business. This results from a more significant structural cost reduction opportunity when combined than either company could create on a stand-alone basis. We are much stronger together with a viable path for growth for our shareholders, our employees and for sustaining journalism. We hope you'll be supportive of this transaction on November 14. And I thank you all for your time this morning and look forward to updating you soon on our progress. Thank you.

OPERATOR: This concludes today's conference call. You may now disconnect.

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