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AHC - Q1 2018 A. H. Belo Corp Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to A. H. Belo Corporation's First Quarter 2018 Financial Results Conference Call. (Operator Instructions) As a reminder, today's call is being recorded. I will turn the call now over to Ms. Katy Murray, Chief Financial Officer. Please go ahead.

Mary Kathryn Murray *- A.H. Belo Corporation - CFO, SVP, Treasurer & Assistant Secretary*

Good morning, everyone. This is Katy Murray, Chief Financial Officer of A. H. Belo Corporation. Welcome to our first quarter 2018 conference call. I am joined by Jim Moroney, our Chief Executive Officer, who will assist me in leading today's call; Grant Moise, Executive Vice President of A. H. Belo Corporation, and Publisher and President of The Dallas Morning News; and Robert Decherd, who was previously announced will become our Chief Executive Officer effective May 17, will also available for Q&A.

Before the market opened this morning, we issued a press release announcing our first quarter 2018 results. We have posted this release on our website under the Investor Relations section.

Unless otherwise specified, comparisons used on today's call measure first quarter 2018 performance from continuing operations against first quarter 2017 performance from continuing operations.

Our discussion today will include forward-looking statements. Forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those statements. The company assumes no obligation to update the information in this communication except as otherwise required by law. Additional information about these factors is detailed in the company's press releases and publicly available filings with the SEC.

Finally, today's discussion will include non-GAAP financial measures. We believe that non-GAAP financial measures provide useful supplemental information to assist investors in determining performance comparisons to our peers. Reconciliations to the most directly comparable financial measures presented in accordance with GAAP are provided on our website under the Investor Relations section.

Before I review the quarter, I wanted to update everyone on the 2 new accounting pronouncements we adopted effective January 1, 2018. The first pronouncement is Topic 606 regarding revenue recognition. We adopted a modified retrospective approach, which means we are not restating historical financials, but are adopting this prospectively starting with this quarter. The primary impact for us is, we will now be reporting revenues, we've once reported on a gross basis, on a net basis. I will be calling out the impact of Q1 in my commentary below. The second pronouncement change is where we record net periodic pension expense or benefit, we have adopted a retrospective approach and all prior periods have been restated reflecting this pension expense or benefit below operating income or loss versus including that expense or benefit above the line in operations. For both of these items, we've provided detailed information in our GAAP to non-GAAP reconciliation, again provided on our website under the Investor Relations section.

This morning, we reported a net loss of $4 million or $0.19 per share compared to a net loss of $4.4 million or $0.21 per share reported in the first quarter of 2017. For the first quarter of 2018, we reported an adjusted operating loss of $2.5 million and this compares to the $834,000 adjusted operating loss that we reported for the first quarter of last year.

Turning to revenue highlights, for the first quarter, we reported total revenue of $49.5 million, a decrease of $11.4 million or 18.8% when compared to the $60.9 million reported in the first quarter of 2017. Approximately $3.1 million of this decline is attributable to the new accounting standard Topic 606. Adjusting for this change, total revenue declined by $8.3 million or 13.7%.

Advertising and marketing services revenue of $25.7 million reported in the first quarter of 2018 is down $9.5 million or 26.9% when compared to the $35.2 million reported last year. $2.9 million of the decline was due to the adoption of the new revenue guidance, requiring certain transactions to be recorded net versus gross. Excluding the impact of the new revenue guidance, advertising and marketing services revenues decreased $6.6 million or 18.8% when compared to the prior year period. In addition, $700,000 of the year-over-year decline was related to the sale of the Denton Record-Chronicle in the fourth quarter of 2017.

Circulation revenue of $17.7 million reported in the first quarter of 2018 declined by $1.4 million or 7.4% when compared to the first quarter of last year. Approximately $300,000 of this decline was the result of the new revenue guidance. Home delivery declined $900,000 or 5.5% from the first quarter of last year and single copy declined by $200,000 or 9.8% from the first quarter of 2017. The decline was primarily due to lower home delivery and single copy volumes.

Other revenue decreased $600,000 or 8.7% to $6 million for the first quarter of 2018. $200,000 of this decline was related to the sale of Proven Performance Media in the fourth quarter of 2017 and $300,000 of the decline was related to declines in commercial printing.

Total consolidated operating expense for the first quarter of 2018 was $55.7 million, a decrease of $10.2 million or 15.5% compared to the prior year. Excluding the $3.1 million decrease related to the adoption of the new revenue guidance, consolidated operating expense decreased $7.1 million or 10.8% when compared to 2017. The decline was primarily due to decreases of $4.1 million in employee compensation and benefit expense, $1.4 million in distribution expense, $600,000 in newsprint expense, $400,000 in consulting expense and $400,000 in temporary service expense.

Adjusting for the new revenue standard, pension benefit, severance expense, depreciation and amortization expense and asset impairments, adjusted operating expense, for the first quarter of 2018 was $55.1 million, a decrease of $6.7 million or 10.8% compared to $61.7 million of adjusted operating expense reported in the first quarter of last year. The significant year-over-year reduction in adjusted operating expense was a result of cost reduction initiatives enacted throughout last year, including staff reorganizations, outsourcing of design and pagination functions and elimination of unprofitable single copy outlets. As of March 31, we had headcount of 1,046, which reflects a decrease of 204 or 16.3% from the 1,250 we had at March 31, 2017. Most of this decrease was due to job eliminations last year.

Turning to the balance sheet, as of March 31, we had approximately $54 million of cash and no debt. As of April 30, we had approximately $55 million in cash and cash equivalents. For 2018, we expect total capital expenditures to be approximately $5 million. In the first quarter, we reported a tax benefit of $1.3 million. We expect that our cash tax for this year will be approximately $1.2 million and related primarily to the Texas margin tax. I will now turn the call over to Jim.

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

Thank you, Katy, and good morning, everyone. I want to acknowledge that the first quarter was a particularly challenging one for our print advertising revenues. The greatest decreases were felt in retail and national display advertising. Preprints and TMC were also down more than we are accustomed to seeing. However, as you may know, for 2018 a large national grocer pulled out all of their preprint business from every newspaper nationwide. They were our largest print advertiser in 2017. If we take their revenue out of 2017, rather than preprints and TMC being down 21.9%, the year-over-year decline in preprints and TMC would have been 10.7%, which cuts the decline nearly in half. Grant can add more color to the decline in print advertising revenues in the Q&A portion of this call.

As we've stated before, our #1 strategic priority is to grow our paid digital subscriber base. And I'm pleased that in the first quarter, we grew our digital subscriber base by 8,036 subscribers or 44.2% compared to the first quarter of 2017. We ended the quarter with 26,206 paid digital subscribers. On a sequential basis, we grew our digital subscriber base by 2,741 or 11.1% when compared to the digital subscriber base on December 31 of last year. In the first quarter, we recorded approximately $800,000 of digital-only subscription revenue, an increase of $200,000 or 33.8% over the same period in 2017. The recently hired Head of Digital Audience, Dan Sherlock and his team have been singularly focused on growing our base of paid digital subscribers and we are very encouraged by the growth they have achieved. From the work we've done to date, we know that the journalism that best converts our digital audience to paid digital subscribers is local, relevant, original journalism. So we will continue to focus on publishing relevant and original quality local journalism for which consumers have demonstrated they are willing to pay. We are confident that the growth in digital-only subscription revenue will be a more and more meaningful part of our company's profitability going forward.

In addition to our digital subscriber strategy, we continue to focus on the growth in our digital marketing services offered by Belo and Company. The Dallas Morning News sales team generated 528 sales to Belo and Company in the first quarter of 2018. This compares to 325 sales generated in the first quarter of 2017, an increase of 203 sales or 62.5%. We continue to leverage our legacy customer relationships to drive revenue growth in the companies that we build and buy. In the first quarter, total gross digital and marketing services revenue was $11.8 million, which represented 41.1% of total gross advertising and marketing services revenue, a 430 basis point increase over the same period in 2017. In addition, total gross digital and marketing services revenue accounted for 22.4% of total gross revenue of $52.6 million, representing an increase of 110 basis points over the same period last year.

As always, I'm proud of our relentless pursuit of quality in the journalism that we publish. We made an outstanding showing in the National Headliners contest, which is one of the communication industry's most prestigious and oldest honors. This year 6 of our journalists received awards; among those honored were photographers, Tom Fox, who took best in show, and Louis DeLuca, who won 2 first-place awards. In April, the Dallas Morning News won 9 first-place awards at the Texas Associated Press Managing Editors 2017 awards ceremony. We won first place for both newspaper of the year and online newspaper of the year. In addition, Dallas Morning News' editorial writer, Sharon Grigsby, was 1 of the 3 finalists for this year's Pulitzer Prize for editorial writing for her work on sexual assault issues at Baylor University.

Lastly, if you indulge me just for a minute or 2, I would like to address my announced -- the announcement my decision to retire. In the latter part of 2016, which marked my 15th year as Publisher of the Dallas Morning News, I told the board I would like to retire in 2018. After so many years as Publisher, I was certain that it was time to turn the reins over to the next generation of leadership. In 2015, I was able to accomplish the transition to a new editor of the Dallas Morning News with the hiring of Mike Wilson, who succeeded Bob Mong, the company's editor for the previous 14 years. In the first quarter of this year, we hired Brendan Miniter, who succeeded Keven Willey as the editor of our editorial pages; Keven had edited those pages for 15 years.

And finally in March of this year, I turned the leadership of the Dallas Morning News over to Grant Moise, who had been the General Manager for 1 year and in that time demonstrated to me that he had the talent and the drive to lead the organization. These 3 key leadership changes assured me that the 133 legacy of the Dallas Morning News would be in excellent hands going forward.

Also, I am very proud of our company's industry leadership in diversifying our sources of revenue, so that we can lower our dependency on print-related revenues. And now with the addition of digital subscription revenue to our mix of revenue sources, I believe that we're at the very good execution of this initiative that company has the mix of revenues from which they can rebuild a sustainably profitable business. So it's a good time for me to turn over the operations of the Dallas Morning News to Grant and to Tim Storer to head-up Belo and Company.

In closing, we know that to be successful we must continue to deliver the excellent journalism that our subscribers are accustomed to, we must continue to grow our digital subscriber base, we must deliver a differentiated digital and marketing services solutions that our customers need and we must continue to make prudent investments in our print franchise that will enhance the duration of its profitability.

John, we are now ready for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And over the line of Barry Lucas with Gabelli & Company.

Barry Lewis Lucas - *G. Research, LLC - Senior Analyst*

Just to make a comment before the questions. And thank you, Jim, for all the many years of service and our frequent conversations. And welcome back to Robert, a little bit unexpected, but nice to have you back aboard, Robert. One just a kind of numerical question, you gave us the sequential increase in digital-only subs and you gave us the year-over-year change in digital-only subscription revenue. What was the sequential change from December to March in digital-only?

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

Barry, we can get it to you. But I don't think I've got it right of at my -- tip of my fingers.

Mary Kathryn Murray - *A.H. Belo Corporation - CFO, SVP, Treasurer & Assistant Secretary*

I can get that to you, Barry, if we did know, and I don't have it from a quarter-to-quarter perspective.

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

Maybe we can get it while -- before the call ends or if not, we'll get it back to you.

Barry Lewis Lucas - *G. Research, LLC - Senior Analyst*

Then let's -- and maybe go bigger picture with Grant and Robert there, as you think about the decline in the core business and exclusive of the large advertising loss to the grocer. But you look at our ongoing declines -- trend lining those, as well as the digital increases, if you had a choice of dart, when might we see an inflection point where the digital business can make up for the balance of the print losses and we could see some growth. And just secondarily, as that business grows, what's the margin -- what do you think the margin profile on that business will look like as it starts to mature?

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

Barry, I'll lead off and I'll let Grant and if Robert wants to chime in as well. The accelerated decrease in the first quarter with print makes that question of when will that happen, harder to answer because it was -- for us, at least as a company and I think you know kind of what our trends have been on both advertising and total revenue growth greater than we had expected. I think the answer to that question, it all hinges on a couple of things, whether or not we end up making any acquisitions to the Belo and Company profile of services, its offers and how say rapidly how we can grow our digital subscriber base. The digital subscriber base is virtually 100% incremental profitability because there is just no incremental cost in adding one more digital subscriber. So as we grow that base, the answer to your margin question is a lot better. But as you also know, as we lose display advertising, we lose also there a very high-margin revenue -- piece of revenue. So I think the question again is going hinge on how well we can build our digital marketing services revenue and how quickly we can continue to build up this digital subscriber base. And then, if we can see a little moderation to what we saw in the first quarter from the print side, then that will make that equation easier, but I don't think we have right now a date certain that we could tell you that. It depends on execution and performance and a little bit of help on the secular decline piece that is related to the print advertising revenues, particularly. You want to add anything?

Grant S. Moise - *A.H. Belo Corporation - Executive VP, President & Publisher of The Dallas Morning News*

Yes. Hi, Barry; it is Grant. I will add a little bit of color just to kind of what I saw on the print side in the first quarter is -- Katy and Jim mentioned in the script, there is the national kind of retail impact of what we saw. Let me give a little bit more color to that. When decisions are made locally, meaning that Dallas-Fort Worth is the entire customer base of a client. we've seen our even our print decline be somewhat moderate. However, when decisions are made nationally, whether that be by department stores or electronics retailers or even at the banking sector, those declines we've seen in print are about 3x larger than when it is a local -- just a local placement. So it's interesting, a lot of these national decisions and kind of some of the national strategies, we have seen that trend kind of accelerate in terms of decline in the first quarter and what we are doing right now is just rebalancing our resources and our efforts to double down on the local, which is seeing a great deal of -- more value in that print product then some of these decisions that are just made nationwide. And so that's really the biggest shift that we saw in the first quarter. It's not necessarily categorically as much as it is local versus national change in trends.

Mary Kathryn Murray - *A.H. Belo Corporation - CFO, SVP, Treasurer & Assistant Secretary*

And Barry, back to your question on digital subscriptions and the growth sequentially from Q4 to Q1, it was a 7.3% increase quarter-over-quarter, which was approximately an addition of 1,800 digital subscriptions.

Operator

(Operator Instructions) Next, we go to David Cohen with Minerva Advisors.

David P. Cohen - *Minerva Advisors LLC - President and Chief Compliance Officer*

Could you comment at all on the Austin American-Statesman transaction and what you think that might say about franchise value of the DMN?

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

Well, what I would tell you is that the purchase by GateHouse tends to be based on their willingness and ability to take out a lot more expense than most of the other suitors for properties like the Austin American-Statesman. And so I think you may get a bit of an exaggerated look at what a multiple might be on average when you take those companies that would be willing, if ever, to buy a large metro like the Dallas Morning News, which GateHouse has not demonstrated or at least indicated an interest in doing so. I think that the mid and small markets that they have targeted are probably seeing larger apparent multiples based on the synergies that GateHouse believes it can get out of the properties that they acquire.

Operator

And with no further questions, I'll turn it back to the company for any closing comments.

James M. Moroney - *A.H. Belo Corporation - Chairman, President & CEO*

No. I thank all of you all for being on the call. We appreciate it and we look forward to talking to you after the second quarter. And thank you, John.

Operator

Ladies and gentlemen, that does conclude your conference for today. Thank you for your participation. You may now disconnect.