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Saga Communications, Inc. *(SGA)*

Q4 2011 Earnings Call

CORPORATE PARTICIPANTS

Edward K. Christian
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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Fourth Quarter 2011 and Year End Results Conference Call. At this time all participants are in a listen-only-mode. [Operator Instructions] As a reminder, this conference is being recorded.

I'd now like to turn the conference over to Ed Christian. Please go ahead.

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

Thank you, Linda, and welcome, everybody, to our conference call today. Joining me on the call is Sam Bush and Warren Lada. And without further ado, Sam will have the executive summary.

Samuel D. Bush
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

This call will contain forward-looking statements about our future performance and results of operations that involve risks and uncertainties that are described in the Risk Factor section of our most recent Form 10-K. Actual results may differ materially from those expressed in this conference call.

This call will also contain a discussion of certain non-GAAP financial measures within the meaning of Item 10 of Reg SK. Reconciliation for all the non-GAAP financial measures to the most directly comparable GAAP measure is attached in the selected financial data table.

We just wanted to point out today that even with the continued economic volatility, free cash flow grew 8.2% to $22.9 million in 2011. That is an increase of $1.7 million and takes into consideration that we spent $5.6 million on CapEx this year versus $4.4 million in 2010.

Net revenue for the year was down less than 0.5% and net of political gross revenue was up 1.6% for the year. For the year we had $1.4 million in gross political revenue compared to $4.1 million for the same period last year. For the fourth quarter, we had $651,000 in 2011 and $2.4 million in 2010.

Radio, including the networks, had $512,000 this quarter of gross political revenue compared to $1.8 million for the same period last year. TV's gross political was $139,000 during the quarter this year compared to $577,000 last year. Political is always a hard category to project and it is so dependent on where both parties decide to spend their time, money and effort.

Looking back to the 2008 presidential election year, we did $6.9 million in political revenue compared to $4.1 million in 2010. We expect a good bump in revenue from political in 2012, although it is difficult to put a firm estimate to it.

National accounted for approximately 17% of gross revenue for the quarter compared to 16% for the same period last year, and 16% for the year in 2011 compared to 14% for the year in 2010.

Our networks' net revenue of $1 million was down from the $1.3 million we reported last year for the quarter. We had $316,000 gross political revenue for the quarter last year compared to $130,000 for the networks this quarter.

For the year, the networks reported $4 million of net revenue this year compared to $4.5 million for 2010. Political for the year was $283,000 this year compared to $814,000 in 2010.

From an operating standpoint, station operating expense was up less than 1% in 2011. Overall, we continue to monitor expenses diligently and expect overall station operating expense to be up 1.5% to 2.5% in 2012. A big determinant of what we end up spending will be based on how we see our revenue growth as the year progresses.

In the other income or expense area, you will see that we saw a nice reduction in our interest expense for both the quarter and the year. This is primarily due to the continued reduction in the level of our outstanding debt, a meaningful reduction in the interest rate we're paying, and a reduction in the amortization of the bank fees. We paid down $27 million in bank debt this year and so far in 2012, we've reduced our debt by another $7 million. This does not include a net cash set off as we had $7 million in cash on hand as of the end of year. Currently we have between $4 million and $5 million of cash.

Keep in mind a couple of unusual items when comparing this year's numbers to last year's. We've reported in the first quarter of 2010 as other income a $3.6 million a one-time payment for a frequency coordination of one of our FMs, adding to our 2010 income. Also this year in the second quarter we completed a new senior debt facility, which resulted in the write-off of $1.3 million in previously unamortized bank fees.

As reported in the press release, capital expenditures in the quarter were $1.4 million compared to $1.1 million last year. For the year, they were $5.6 million compared to $4.4 million in 2010. Tax law allowed us to take a bonus depreciation deduction in 2011 on qualifying purchases, which results in the items' total cost being expensed in 2011 from a tax perspective. We're planning to spend between $4.5 million to $5.5 million in CapEx in 2012. Again, the final determinant will be based on how we see the year going from a revenue perspective.

Two other quick items for 2011, we expect interest expense for the year to be between $2.3 million and $2.6 million. Our anticipated total tax rate going forward will be 39% to 40%. We anticipate deferred taxes for 2012 to be between $3.4 million and $3.6 million. Current taxes will vary based on the income in each quarter.

Once again, we asked for your questions to be submitted via e-mail prior to the call. Ed and I and Warren will respond to those questions that we feel we can appropriately respond to later in the call.

Ed, I'll turn it back over to you.

Edward K. Christian

Chairman, President & Chief Executive Officer, Saga Communications, Inc.

Thank you, Sam. I'm not an apologist for last year. I think we did well considering the environment that we faced on it. Just our – where – one of the things that we were able to negotiate in to our new credit facility was that our loan does not amortize once we're below two times EBITDA. We're at that point right now.

The current plan is to probably pay down the revolver, which we can borrow back on but not touch the basic structure of the ARM itself, and then that would allow cash to build. I'll answer this right up front, is what we do with cash is determined upon the market condition. Certainly we have three different or four different scenarios. We can just sit on cash, like a lot of companies do. Secondly, we could reduce debt further, but we don't really believe that, because I think we're at a point in time where we recognize that a certain amount of debt is healthy for the enterprise and that's where we are now.

We could do dividends or we could do acquisitions. And interestingly enough, we've been waiting for several years to watch the transaction market, and if you talk to anybody in our industry, they will tell you that the transaction market has been frozen for three years. If you add up the number of deals in 2008, 2009, 2010 and 2011, it's paltry compared to historic precedential deals that occurred in radio.

I think 2012 is the turning year for this. We're going to see a lot more inventory come on the market. What's happened over the last three years is that there are a number of, pardon the expression, what I call zombie companies that appear to be radio companies that are operated as radio companies, but indeed they have been taken over by their equity holders or, in some cases, banks or whatever it might be.

Management remains in place, but the companies behave as if they are being marched through a [indiscernible] (7:36) nights with whips. And there has been no expense on CapEx or other things. Appearance sake, they're fine, but now we are beginning to see that the fact is that because there is a comfort level in the economy coming back a little bit, that some of these companies are coming to market. I mentioned this strictly because it might provide some opportunities for us, and other broadcast companies to strengthen our portfolios. Going into companies like this is always somewhat problematic because their ideas of cash flow and their ideas of CapEx are entirely different from ours. So those have to be measured, so there is no assurance that any of this will come to fruition. But I do like the deal market. I think you're going to see as many deals – actually I was talking with a broker friend of mine the other day who made a statement that he felt that 2012 will have as many deals as 2008, 2009 and 2010, and that's the reality. So we are watching that part of the market, and that's kind of the X in the equation if that happens, it happens; if it doesn't, it doesn't.

Where we are for this year, and where we see where we are going. Boy oh boy, I read this morning the estimates, and they go anywhere from [ph] Zenex (8:50) Media 4%, up to [ph] Marcy Wideker (8:59) zero to me at plus two. I think that [ph] Marcy (9:02) might be low, I think [ph] Zenex (8:57) could be right, any of our numbers could be correct.

If we look at how we are in first quarter, we are low single-digit, low to kind of mid, somewhere in there. It depends because March is not done yet, even though historically March is done, but we got to get the final numbers in yet.

I don't think 2% is unrealistic. I think historically radio has kind of grown along with GDP, though we can show some aberrations over the years. But what we are facing right now is a disconnect that the GDP is growing by 2%, and we're reducing unemployment by 200,000 plus jobs each month, there is a disconnect between the unemployment rate which has always marched with GDP. And I haven't figured that out yet, so this is something we have to watch and track. Why? Because if we look at the employment rate GDP should be higher than it is right now, so we have to kind of analyze that. I'm not sure why that is, but it's a thing that I ask you all to kind of think about and ponder because radio really marches with the economy. We're tied into the well-being of how people feel, we're tied into the well-being of how our advertisers feel.

And the more that they feel sanguine about the environment, the better they are in terms of spending, and that's kind of how I look at this on this. There is a disconnect, and we need to kind of measure that out.

Secondly, while I have the floor here for a moment, I've been listening to a lot of conference calls and also reading the transcripts on them, and I guess that I'm not an apologist because I tell you that we are an old technology company and we are radio and television, been around for a long time. And we talk about that because that's our bread-and-butter, that's where the money comes from, that's why the famous bank robber Willie Sutton said I rob banks because that's where the money is. Well, we do radio and TV because that's where the money is.

But a lot of companies recently have been focusing on the icing of the cupcake and rather than the cupcake itself. And we like to think of if this is a cupcake, it has icing, not icing itself is a cupcake.

So you'll apologize – you'll excuse us, that is, if we don't apologize for being a radio company and spend a lot of other time on other areas. Yes, they are important, interactive streaming, non-traditional revenue. Interactive and streaming account for about 4.5% of our revenue now. We're not as bullish as some of the other companies. One company is quietly telling people that they feel they'll be doing about 40% of their revenue in interactive in a few years. We don't see how you do that. And that's okay because we know that we can make a lot of money and have a lot of free cash flow as a radio company.

So I ask you to understand when you're listening to things that everybody talks about, there are other initiatives, and talks about streaming and talks about what they're doing in other areas, online or through different transactional or non-traditional business.

But the meat and potatoes of this still is radio, still is television, and that's what's going to pay the bills for the foreseeable future. And in our markets here that's what we track on. We do not ask our sellers to not sell anything else. But in – with the crowded menu of items that they have of multi-platform radio stations and everything else, we know that to mandate growth in a particular area comes at the diminishing of our core competency and our core product. And it's a fine balance that we tread and we're aware of it. And rather than trying to get people to – or sellers to go on out there and do this and take money from traditional methods of sales in radio or television and apply it to interactive Internet or streaming or whatever it might be. So really just shifting dollars within the category and not creating. There is in any market a certain fixed amount of revenue and we can talk about all the new things that happen, but you're not going to be able to push past that point.

So we always at Saga believe comp – to spend your time on your core competency on that and be realistic in your goals, because if you force your sellers into a back, tight situation, they'll just shift the dollars and make you feel good, but that's not what's going to happen. We are an old technology company, been around forever, so has television been around forever, and our foreseeable future, it's not going to change.

Been talking with Sam this morning and Warren, and I should – we don't apologize for being an old technology company. We wouldn't expect Warren Buffett to do a conference call and say, you know I have this, this new method of transportation where using lightweight of aluminum rails we're doing this, we're doing that, we're doing the other thing. And the total in the light of day it really comes down to he runs a railroad, and there is there no apologizing for being in the railroad business and the same with us in broadcasting.

Let me move on from that. One of the things that I think I should mention is and keeping with this, there is a story that [ph] Frank Sacks had in Inside Review (14:39) today about how Arbitron is looking at measuring no longer just radio, but measuring audio. And I think once again there is a lot of pressure from within our own industry to measure audio, to measure Internet streaming, to measure whatever it is. And we run into a fine line of changing the perception of what we do. Radio and television have been measured – radio by Arbitron for 60 some odd years, and it's disquieting even though we are not an Arbitron subscriber, to see a statistical research company trying to shift their measurements to audio when there are still problems in their fundamental development of audience measurement with PPM. And I would hope that at some point in time we'll find our people that use their technology to help us, the industry, set rates through measurement, find ways to enhance their product rather than just spread their parting up in to other areas that really isn't the best interest for broadcasters at this point in time.

Jim Seiler, who started Arbitron, American Research Bureau many, many years ago, 60 some odd plus years ago, had it right when he said we measure radio and TV stations. They dropped TV but they're still there. And remember we still have the split methodology between PPM and diaries, which is another issue for us to deal.

So this hurts our industry, you know, it should help us, in having split methodologies and split problems with PPM technology and further fragmentation is not in the best interest of broadcasters. I'll leave my feelings on mixed methodology alone right here. We should probably go into some of the questions we have, and see what we have at that point of time.

QUESTION AND ANSWER SECTION

Samuel D. Bush A
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

We've got a number of questions. Some of them we've already addressed in our comments, such as pacing for the first quarter and so forth.

Edward K. Christian A
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

We didn't knew that, well, we did – we kind of -

Samuel D. Bush A
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

A little bit anyway.

Edward K. Christian A
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

Yeah.

Samuel D. Bush A
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

We've heard from other broadcasters that auto is driving the growth so far in 2012. Are you seeing the same? How are your other categories faring?

Edward K. Christian A
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

Warren, do you want to try to -

Warren S. Lada
Senior Vice President-Operations, Saga Communications, Inc.

A

Yeah, I would say that nothing really has changed in the business. Automotive is still a very significant part of what we do, as is telecommunications, retail, banking, financial sector and so on and so forth. So I don't really see any significant changes in categories, at least with Saga, as to who we're tapping into. Automotive has come back; it hasn't roared back. It has the potential of increasing over time, but I don't see any real shift from what we've seen in the past five years. So I'd say, business as usual in that regard.

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

A

Sam?

Samuel D. Bush
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

A

Very good. We've addressed a number of the other questions, Ed, as we already talked about. I know one that's near and dear to your heart, any thoughts on radio royalties? You talked about that a little bit as well, I believe, already. So do you have any other comments on that?

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

A

Well, I didn't really get into radio royalties. The industry reached a very friendly and good agreement with ASCAP that is signed, it's in effect. It re-set the rates. It shifted the industry back to a percentage of revenue rather than on a fixed fee basis, which was a seminal event and reversed things from many, many years ago. It had been on an assured revenue basis for years and then in an experimental basis it switched over to the other, but we were able to reach a very friendly and favorable deal with ASCAP. And I must compliment them for reaching out to us and coming up with something that we believe worked for both parties. And there's nothing like a win-win situation.

BMI is still left out there. I believe that BMI is working hard at what ASCAP did. And it's always a very difficult thing for one performing rights organization to change the metric from another and I think that that's where we are at this point in time. BMI is a good organization, just like ASCAP, they both have wonderful composers, authors and publishers. The industry recognizes that they are the gatekeepers for music and for composers, authors and publishers and we recognize that there is a lot of issues that performing rights organizations face. But yeah, we have to license our music and I think that meetings with BMI will be very productive in the future and once precedent is set by ASCAP, it's very difficult to really change that back to a different way. It's always difficult to measure on market share because that's a moving metric that switches from month-to-month to year-to-year, and which is why we prefer to have based on a revenue share of what we do and with our music and what we don't do.

So I hope in the next few months that – that we could do something with BMI – and I am speaking here as chairman of the Radio Music License Committee and not as Saga. Indications are that that could occur, and it would be a wonderful thing to put both of these issues behind us.

Samuel D. Bush
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

A

The – I've got a fairly lengthy question here, but I think it all comes down to one thing, which you've talked in previous conference calls about, and I know the philosophy of Saga, but is radio still a people business with local characteristics important, or is it a big business that scale and centralization should realistically trump local management, local sales and local programming? And then that goes on to say, is there anything wrong with valuable national programming talent like Ryan Seacrest or Mike Huckabee being on thousands of stations since TV and cable already does it?

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

A

Well, I think I'll take the last one. I think Ryan Seacrest is a good product; there is no localism in his show. Mike Huckabee is a national product and there's certainly room for national products, whether the Huckabee v. Rush Limbaugh has traction, we'll have to wait and see. I don't know the answer to that. But in terms of the question here, I would answer it: both. And it depends on the size of the market. Certainly we believe that localism wins, we believe that direct contract with our – contact with our advertisers wins, we believe that relationship building is what's important about it and we believe that understanding the needs, wants and desires of our advertisers and the needs, wants and desires of our local community make us superior broadcasters in the market in which we serve.

However, with that said, in larger markets, because of the necessities of quick processing of business, it becomes a rate business and we are seeing that then, and I wish I could say that I think that PPM has helped to increase rates, but I don't see that because there's still a diminution. And I suggest that if a study were done, we might find that in certain markets, the number of units per hour has been added to stations rather than decreasing, which would then suggest why the average unit rates are coming down and the cost per point is coming on the end markets.

So I think doing the business in a larger market, which is not where we intend to play, is totally different from how we conduct our business. So I can empathize with those larger markets who feel the frustration of being held hostage to numbers from a rating service which is trying to sort itself out and using these as a metric for buying and selling.

So in the larger markets, yes, to the fact that if big business wins out; in the secondary markets, yes to the fact that the entrepreneurial spirit is alive and well and gaining money and share.

Samuel D. Bush
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

A

Okay. One final question for you, Ed, and this is very general, but what keeps you up at night, if anything, about the industry in the near to mid-term?

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

A

I guess, the only thing I – again, I do not apologize for being an old-style technologist. I think what I look at, and if I had to say anything about it, it's the fact that right now everybody is trying, as I said initially, to morph themselves into something they're not, and we need to really refocus and spend our time concentrating on winning the hearts and minds of the people that we serve as broadcasters.

That all the other information and everything else that they talk about, the new initiatives and everything else like this, are fine, but they're still unproven. I mentioned earlier to Sam and Warren that I still have my pets.com puppet here and if anybody goes back to that time when pets.com did their IPO, they raised $345 million, of which they dissipated within two years. They paid the highest amount for a Super Bowl commercial and everybody got behind it, yes, this is the way we are delivering pet food online. I think the only profit they ever made was by selling the image of the pets.com puppet for about $145,000.

And one thing I remind everybody is the pets.com puppet doesn't have any clothes on today and didn't have any clothes on when it first came out as a little hand puppet, but nobody seemed to notice back then. So the more history lives, the more it repeats itself. But I will tell you that radio and television are safe bets.

One final thing, just to show you that the TV still is a growth industry. I think that we – through retrans money this year, we're able to achieve close to a 300% increase in the dollars that were coming in. Now admittedly some of those are shared with the networks, so that's not a true metric. But it shows that this is an area in television that everybody should be ever mindful of, that that money is real and it will continue to grow.

Warren, have you got anything else that you want to bring up?

Warren S. Lada
Senior Vice President-Operations, Saga Communications, Inc.

A

No, and Sam asked that question about what keeps you up at night. I think the other part to that is the potential of something happening that is beyond anyone's control, and whether it's high gas prices, whether it's a war, whether it's a terrorist attack, whatever. I mean, those things, obviously we can't do anything about them and could have an impact on our day-to-day.

And going back to the question, Sam, that you asked earlier about local versus national control and all of that. I agree with Ed that it's a little bit of both, but fundamentally our business is driven by local effort, and the relationships that we garner with our advertisers and with our listeners, and the ability for the local market to reflect specifically what it is about that community that's important to them is, I think, a hallmark of our business and I think we do a pretty good job with that.

Samuel D. Bush
CFO, Treasurer, SVP & Head-Investor Relations, Saga Communications, Inc.

A

Well, we obviously do, because only 16% of our revenue was driven nationally last year.

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

A

Yeah, and that's where it's been. I would frankly like to see it down so we increase our local down to less. The only thing I can tell you, and I'm not really that familiar with the exact quotation in the Serenity Prayer, but it's basically Lord, give me the ability to control what I can control, and that's what we try to do at Saga each and every day. But that said, Linda, if you're here, if you want to do a wrap up. I think we're done for right now.

Operator: Thank you. Ladies and gentlemen, that does conclude our conference for today. Thank you for your participation and for using AT&T executive teleconference. You may now disconnect.

Edward K. Christian
Chairman, President & Chief Executive Officer, Saga Communications, Inc.

Thank you, Linda.

Operator: Thank you.