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Saga Communications, Inc. (SGA)

Q3 2013 Earnings Call

CORPORATE PARTICIPANTS

Edward K. Christian

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

Samuel D. Bush

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

MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Third Quarter 2013 Results Conference Call. At this time, all participants are in a listen-only mode. [Operator Instructions] I would now like to turn the conference over to your host, Mr. Ed Christian. Mr. Christian, you may begin.

Edward K. Christian

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

Thank you very much and thanks to all of you joining us on our third quarter conference call. As historic with us, here is Sam with the obligatory announcement and some commentary.

Samuel D. Bush

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

Thank you, Ed. 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 Factors 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 S-K. Reconciliation for all the non-GAAP financial measures to the most directly comparable GAAP measure is attached in the selected financial data table.

During the quarter, we had \$206,000 in gross political revenue compared to \$1.5 million last year. Excluding political revenue, our gross revenues increased 5.2% for the third quarter. Net revenues increased 1.6% this quarter. We experienced nice growth in both national and local this quarter. We increased our gross local revenue 4.6% or almost \$1.2 million over third quarter last year. National increased 11.9% or \$539,000 over the same period last year. National accounts for approximately 14% of gross revenue for the quarter compared to 12.8% for the same period last year.

We will have a challenge with revenue in the fourth quarter as will every other broadcaster. Fourth quarter of 2012 was a great revenue quarter for Saga with net revenue increasing 10.3% over 2011, principally due to the \$4 million in political revenue we received. Without the political revenue this year, we are expecting to be down mid to high-single digits. We are working on a number of initiatives to stimulate revenue in the quarter, but even with these efforts, we don't expect to be able to make up the \$4 million in political.

In the fourth quarter of 2012, political revenue accounted for over 10% of our gross revenue. Our current expectations are for us to receive between \$4 million to \$6 million of political revenue in 2014 as the tide turns back to more elections.

As stated in this press release, station operating expense increased \$1.2 million for the quarter. Approximately one-third of the increase was due to an increase in healthcare costs as we had several large claims hit our stop-loss limit, thus increasing our healthcare cost significantly in the quarter. We don't expect future quarters to repeat this increase, but since we are self-insured we were subject to variations, sometimes bad, sometimes good quarter-to-quarter.

A number of other areas showed increases as well, including sales compensation expense going up \$170,000 and programming salaries going up \$196,000. The sales compensation expense increase was due to our improved sales performance while the programming salaries increase is a matter of reinvesting in our people supporting our future performance.

We continually monitor our expenses to make sure that each and every expense is justified and will benefit our ongoing performance. Currently, we expect fourth quarter station operating expenses to be up 1% to 3%.

Retrans revenue in our TV division was \$582,000 in the third quarter, up from \$480,000 last year. Retrans payments to the networks were \$133,000 in the third quarter compared to \$104,000 last year. We expect retrans revenue of \$2.2 million for all of 2013, with a corresponding expense of \$600,000 for a net of \$1.6 million to Saga. The net should increase somewhere between \$200,000 and \$300,000 for 2014.

In the other income or expense area, we continue to see a nice reduction in our interest expense for the quarter. Interest expense for the quarter was \$308,000 compared to \$381,000 for the third quarter of 2012. This is primarily due to the reduction in the amount of debt we had outstanding. As of today, we have approximately \$29 million in cash on hand. As reported in the press release, capital expenditures in the quarter were \$1 million compared to \$1.4 million last year. We currently expect our CapEx for the year to be between \$5 million and \$5.5 million.

Two other quick items for 2013. We expect interest expense for the year to be between \$1.3 million and \$1.5 million, given the existing interest rate environment. Our anticipated total tax rate going forward will be between 40% and 41%. We anticipate deferred taxes for 2013 to be between \$3.3 million and \$3.6 million.

As usual, we asked for your questions to be submitted via e-mail prior to the call. We had six questions, all of which we have responded to or will respond to in Ed's and my comments. Ed, back to you.

Edward K. Christian

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

Thank you, Sam. Sam and I talked about what Q4 is going to be like and I think that that's a safe assumption that he said, obviously, we're going to try and do a little bit better in that, but it's a tough putt for that with political, as much as it was last year. But look, in Q3, we were plus 5% if you factor political out, and even with that was 1.6%. And in an industry that seems to be growing at 2%, I think we're doing okay.

Okay is not good, I admit that. Actually, I think 1.6% is a little bit shy. My personal projection was for 2% for the quarter, and we should have done a little bit better. A couple of things factoring into that, we have probably a couple of assets that we have targeted it on, and we've talked to [indiscernible] (06:05) before and they're still in a workout mode, kind of – that's just a tough word to say.

Our networks, we've been hit there with some soft revenues. They're occurring because of a downward swap pressure on the entire sector. Candidly, our industry is awash in barter spots during the years of 2009, 2010, 2011

and 2012, and even carrying forward, a lot of companies on our industry elected to go with barter in lieu of cash with some good and services which created this giant cauldron of spots which becomes available every day and then disappears unused at night. And when you have that kind of inventory and you dump it on, while I use the arcane term, unwired part of the business or wired in the case of our networks, it does hurt.

I think it's going to change next year. In fact, I know it's going to change with the political year because state radio networks do very well on that. That's going to be a good year for us and during that time, it'll allow us to again focus and find out what we can do.

The problem we really have too is the quality of the advertisers because of the amount of revenue or the inventory that's available now. I think that there has been a degradation in the quality of advertisers that are using radio because we still have – the traditional ones are very good, but there was a new category kind of, how do I say this delicately, different and unusual or non-traditional advertisers that are using the barter inventory to reach stations. Anyway, it's the unwired networks or the wired networks are still a good business to be in. It's just that we are in a little bit of a slump right there.

The only other problem is one that is suffering in – one of our markets is suffering in a sales issue. And we have put that under a laser-like focus and it's under active watch with a plan that we have instituted on that.

And let me just talk for a second about this because this is something that I think the industry should be getting too focused on and analysts or holders should look at. And one of the metrics that we use and it's been quite reliable to us is how many accounts around the station in a given month. We can always sit and talk about our revenue. We can talk about our cash flow. But what we really have to get down to is, what is the level at which you push yourself into the high profit mode?

One of our managers, Alan Beck, in Champaign is really spending a lot of time developing. This is kind of a matrix for us to use and to look at things. And for instance, in Champaign, Illinois where we have over 200 accounts on a year and we break them down into local or into national, local agency and then local and we really look at having 200 local accounts is a threshold number for us. So the station comes in and we do the analysis each month, which we now have the ability through Marketron, which we worked with them to develop a report that's available to any Marketron client. Now I believe, I know it's available to us, where we can actually sit down and look on a weekly basis or, if we want, a daily basis as to how many active accounts are on the year or that month.

That's the matrix that we'd look for in terms of developing how much dollars we're pulling into it. Obviously, the more accounts, the better the salespeople are doing. It allows us to goal set with the salespeople. It allows us to monitor how they're doing if we see a salesperson. With the limited number of accounts and high volume count, we know that they have time to develop others. It's not disrespectful to a salesperson to expect them to have 20, 25 active accounts a month.

I mean if you look at the number of hours available in the [ph] neighbor (09:54) sales in prospecting a new – and if we know that they're falling behind that, that means that they can go out and into a developmental mode. That's working out very well for us and we're using it as a tool and where we see the problems every time it's been verified by the number of accounts looking on a year as to what's going on there.

Sam said our expenses are up. We talked about the medical. We've also been spending more in research and markets and this is really paying off for us in the respective marketplace. And we've added marketing and promotional hours to promote our brands through other media. And for a while during the dark years, shall we say, I think that everybody pulled back from that and there's always a need. If we believe in advertising, then we have to find other ways to advertise and support our own brands.

Sam mentioned the cash on hand, the \$29 million plus closer to a shy below \$30 million, tad shy of \$30 million. Our debt is \$51 million. Our debt to EBITDA is 1.38. If you look at where we are – because there's a good deal of excess cash, we know that there's like – we need about \$5 million just on hand to run the enterprise. And what we do with the others – the other amount of money is, well, last year, we paid a dividend, about \$7 million for our first time out.

Our board is meeting in December to look at the best source and use for what we do because there's a responsibility towards shareholders and to everybody else to look and it's exactly the same. And the ways that you can utilize some of the cash on hand is through a stock buyback. If the price is appropriate, the repurchase of stock.

Dividends are certainly one way to reward the shareholders. The other way is by a reduction in debt, which also increases the value of the enterprise and through acquisitions. And we've been looking quite often at acquisitions of late. We've missed out on a couple and we have a small tuck-in one which we feel we can probably get into our organization in the near term. But that certainly is part of our thrust too is finding the acquisitions that make sense and holding them in. We think it's a good time if you can find the right stations to buy, which is why we like to have certain cash on hand to do that. But certainly, our growth is it's time for us to begin kind of a growth curve in the company.

Let's talk a little bit about industry health for a second here. There's a lot of discussion of what's going on in the industry and where are we right now. Remember the cartoon with the guy walking around with a sign that says, "The end is near," the guy with the big beard and the robe. Well, we had several of these guys walking around [indiscernible] (12:56) a few years ago. And frankly, they've left the room for right now which is good. I think they're hanging around some of the Internet streaming companies that are dependent upon advertising to pay for their bills and wearing the same signs that say, "The end is near." But they've left us alone and we have escaped the size of them doing that.

But really times are changing and it's challenging. I don't know how many of you saw Barron's last Saturday when it came up. They had a wonderful cover story. The headline was Slowing to a Crawl and it was written by – let me see right here – Jonathan Laing. And if you haven't read it, it's a great article yet it's a troubling read. I do suggest that if you can get it yourself or go online or find a copy and check it out. Essentially, the article makes a cogent case with vivid examples of why GDP growth could slow to 2% for possibly decades down from our historic 3.5%. As the article says and there's a quote right here, "Lackluster GDP gains will put the U.S. economy in a perennial state of near-stall speed."

Well, so let's say that some of the doomsday sayers are wrong and rather than crashing, we need to adapt what we do to ensure the financial viability of our broadcast industry. If we accept the reality, then maybe that we are in a slowing economy, as I mentioned last month or in the last quarter. If we accept that as a reality, and I think by looking at the earnings of all the industries, and not just picking and broadcasting, you find that this is pretty much what's happening in there. We need to adapt what we do to ensure the financial viability. This is changing and we got to get there.

One major broadcast executive – I was reading the transcripts of some of the other calls – mentioned that he feels that a renaissance is coming. That would be good. That'd be very good, but for that to occur really the fact that we also need a rectification of our current problems. I work in the industry right now and I think that if we have this to really get to where we need to be, to place us in perspective as a broadcast industry, we need to have a rectification of our current problems.

I work at it as like setting a goal. It sounds a little bit corny to say we need another Golden Age of Radio. No, I'm not talking about studio orchestras or guys with their hand over their ear cupped before a microphone or something like that. But I'm talking about a golden age in the century in which we live.

I'm talking about rebuilding our image but a great deal of it is our own internal understanding and we really have to focus on the fact, as an industry, that we can't clone a plant and just pick it up and put that plant in another area and have it produce the same product. That works in manufacturing; I don't think it works in radio. Our business is all about people, people doing compelling broadcasting in their service area. And you have to have lots of people to do that, if we get our product right, if we focus on that.

Well, there was a conference in Detroit a couple of weeks ago on the dashboard on the connected car [DASH The Connected Car Audiotainment Conference]. My son-in-law is a designer with a major U.S. car company. And I said to my son, why don't you go to this? We had our director of engineering go and it was a pretty well-attended conference. And he went and I talked to him afterwards and I said to him, okay, Peter, if you have to look at this, what are some of the takeaways that you got?

And he said to me, he said people definitely want a radio in their car. That's good to know. And the other one is people like radio. I said, people like radio? He said, yeah. It was apparent in all the research and everything that's coming up. People like radio. Well, that certainly is important to know also. Now, like is good but I think there is really is a three-part deal that also has like, trust and respect. I use this all the time. The three winning combination is like, trust and respect.

People have to trust radio and also respect it and I'm wondering if the trust and respect – liking a product is one thing but trusting and respecting is another. And I think that's [ph] where we come (17:44) and I think it takes people doing great jobs to create the reality that we are in a community. And I said this – and I don't want to be preachy here, but if we blend the community – and you got to try and community any way that you like them. If we blend the community and we blend radio into one, we'll continue to survive and to prosper even in a 2% GDP world. That's what is going to happen and that's where we can work out.

Again, I don't want to sound too impassioned on this, but I spent over half a century in this business, so I have some pretty strong feelings about what it's like and what we should do. This is a great business. You really can do – I'm watching these commercials of late on TV that for a card company and they talk about and/or like, well, it's good that we don't have to choose between sweet or sour chicken, or sweet and sour chicken, or sweet or sour chicken and chosen getting served sour chicken.

In our business right now, you can treat people with respect and make money. It's as simple as that. We can do both. But we have to have the people that we have to have the commitment and we have to do this and if this is the case and we do it well, then there's nothing to worry about with our industry. Our industry will continue to grow and prosper. Our investors will be happy. The communities that we serve will be happy. Our stock price will be stable and rise and we can continue on doing what we're doing.

I truly believe about the industry, but we as an industry need to make a commitment to get behind it and do the right thing and do these things right and that's it. Sam, I don't mean to be preachy though. I just got carried away in the...

Samuel D. Bush

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

No, you're passionate about the industry and that's one of the things that people like about Saga.

Edward K. Christian

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

Well, Saga will continue to be passionate about the industry, not just me but the company will reflect...

Samuel D. Bush

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

Everybody. Yes.

Edward K. Christian

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

I think we answered all the questions. Was there one that we didn't touch on? Are we pretty good there?

Samuel D. Bush

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

No. We took care of everything in either your or my comments.

Edward K. Christian

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

Okay. As usual, Sam and I are around if anybody has any further comments or something we didn't answer. We, as you know, love to talk about our business and love to talk about Saga. So please feel free to contact us, and we will see you in 90 days.

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

Samuel D. Bush

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

Thank you very much.

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