

Saga Communications, Inc.  
3<sup>rd</sup> Quarter 2019 Earnings Conference Call

November 7, 2019  
11:00 am ET

OPERATOR: Good morning, ladies and gentlemen, and welcome to the Saga Communications, Inc. Q3 2019 Earnings Conference Call. At this time all participants have in place on a listen-only mode. It is now my pleasure to turn the floor over to your host, Ed Christian, President and CEO of Saga Communications. Sir, the floor is yours.

MR. CHRISTIAN: Oh, Catherine, thank you, and this is so formal, we're more casual than that, but that's -- thank you so much. Hello, welcome for Q3. Sam is on the phone with me, and I will be turning it over to him shortly. He is going to review some numbers with you. Note the word adjusted is never used. Otherwise, UHY, our auditors would come in and severely reprimand him for doing so. You don't have any adjusted numbers, do you Sam?

MR. BUSH: I don't believe so. I'm looking very quickly just to make sure.

[Crosstalk]

MR. CHRISTIAN: All right, it's yours.

MR. BUSH: 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. This call will also contain a discussion of certain non-GAAP financial measures. Reconciliation for all the non-GAAP financial measures to the most directly comparable GAAP measure are attached in the selected financial data table. As reported in the press release for the quarter, our net revenue was \$31.3 million compared to \$31.7 million for the quarter last year. Note that gross political revenue for the quarter this year was \$96,000 compared to \$486,000 for the quarter last year, a swing of \$390,000. Without political, our revenue would have been approximately flat with last year. Station operating expense remained a strong point, with an increase of only \$171,000 for the quarter, including our picking up the expenses associated with our new stations in the Gainesville-Ocala market. On a same-station basis, our expense controls resulted in a \$779,000 reduction in station operating expenses for the quarter. Free cash flow was \$4.5 million for the quarter compared to \$5.2 million for the same period last year. Free cash flow was impacted by the reduction in Saga's deferred tax provision, primarily due to timing differences related to depreciation and amortization between 2018 and 2019. For the quarter, our deferred tax provision was \$400,000 compared to \$785,000 last year. Of the roughly \$1.5 million we spent on CapEx during the third quarter, almost \$400,000 was related to the continued progress in building a new tower in Norfolk, Virginia, while approximately another \$400,000 was spent finishing the upgrades to the existing studio buildings

in Charleston and Springfield, Illinois. For the 9-month period, political was \$351,000 compared to \$1.3 million last year. I really thought political would pick up as we went through the year, but so far, that hasn't happened. We're facing a soft fourth quarter with the headwinds of last year's political spending. In 2018, we had \$1.6 million of political in the fourth quarter. So far this year, fourth quarter's political has been very disappointing. Even with the additional CapEx-related expenses associated with our Charleston, Hilton Head and Gainesville-Ocala acquisitions, along with the Norfolk tower build, our CapEx for the first nine months was approximately \$4.7 million, \$217,000 over the same period last year. We expect CapEx for this year -- for the year to be between \$5.5 million and \$6 million. To better understand our calculation of free cash flow, net income and net income per share, we have included a couple of additional reconciliation tables as a part of the supplemental financial data section of our press release. At the end of the quarter, we had \$10 million in debt outstanding. Cash on hand at the end of the quarter was \$41.1 million. As of November 4, we had \$42.3 million in cash on hand. Including the recent \$0.30 per share dividend, which was paid on October 11, 2019, we will have paid almost \$68 million in dividends since December 3, 2012. We intend to continue to pay regular quarterly cash dividends in the future as well as considering special cash and stock dividends as declared by our Board of Directors. During the quarter, we repurchased 9,584 shares for \$276,000. For the year, we've purchased 20,691 shares for \$603,000. In 2018, we repurchased 53,713 shares for a total of \$2 million. Since we began our buyback, we have repurchased 2.1 million shares for a total of \$56 million. We expect same-station operating expenses to be flat to down 1% for 2019. We expect interest expense for 2019 to be around \$1 million. We expect our ongoing tax rate to be 29% to 30%, including an 8% to 9% deferred tax rate. And yes, we adjusted the deferred tax rate down by 1% or so. There you go, Ed. I worked in the word adjusted just to make you happy. And with that, I will turn it back over to you.

MR. CHRISTIAN: Thank you, Sam. For the past several days, I've been kind of puzzling over how to start the conversation with all of you. It needs to be a coach, and I really need to be cogent with the narrative and also factuals. Let's begin. It was kind of an unsatisfactory quarter for us. I was not pleased, and I needed to dig further with my analysis of both what happened at Saga and what's happening in the industry. Let me start with a strong premise, and that is that there is nothing wrong with radio advertising. It works. It's how it is being applied that is failing. I have a strong statement; we'll get to that. Radio revenue is and should be divided into multiple parts. Let me walk you through each, so that you have the beginning of an understanding of where we're going. National revenue has markedly changed. I mentioned this before, and I want to bring it up again. As I've said before, I was a national sales manager earlier in my career for radio stations. National always commanded a premium rate over local advertisers. In truth, there was no rational reason why, except that the radio industry thought that national advertisers had more money than local radio guys. Fast forward to today, and we have gone 180 degrees on this. Radio is on a downward trajectory on this. And the larger companies of scale are going for share rather than rate. And when I say downwards trajectory, it is strictly on rate. It's kind of akin right now what's happening to walking into an advertising agency with burlap bags and stuffing in all the commercials they can get even at low rates. And the little secret that is coming out now is that certain parties are offering much higher commission rates to agencies. If they get most or all of the budget and that's their prerogative. I have no problem with this. I don't condemn any one as every company has their strategy and needs. But at Saga, we believe in pride of product and providing value

instead of bulk distribution. Fortunately, for us, a lot of our markets are not reliant on national or regency agencies. But we still do both feel and absorb the pain of missing these buys as we're not rate competitive. And frankly, in our view, nor will we be. We just are not going to get into the fact of a diminution of pricing for the sake of acquiring commercials for the air. We would rather build a business by our working directly with clients, which we'll get into. Similar events are occurring at the local agencies across the country. Now perhaps, this is a result of a feeling or angst of uncertainty about the global economy. This, I do understand. And when I read headlines in The Wall Street Journal, such as US growth settles in low gear as business pulls back or an Associated Press article of growth slows in Q3. We certainly know about this as we do feel it especially in farm states. Our farmers are dealing with the efforts of the tariffs and weather, and it's been a tough year. However, the blame isn't entirely with the economy, but with the feelings of edginess and a tinge of fear of the unknown at a consumer level, especially in the international part. Now let's add another ingredient into the witches' brew and recognize according to The Economist magazine that just under \$1.1 trillion of revolving consumer debt, bills that are racked up by credit cards was outstanding at the end of August. It's a dangerous type of debt, high interest rates and enrollment in repayments didn't mean balances can quickly balloon. What we're finding is with our card stores, we're pulling back because they've a huge inventory, they still got to pull that out, but their spend is down, in some cases, markedly from last year. So, we're seeing this in a number of product categories, which is also affecting us. And this is coming in through the agencies that we're still dealing with. Now, we haven't abandoned advertising agencies, we haven't abandoned national, but we're definitely seeing less money or a downward pressure on the rates. Now, perhaps talking about the feeling of edginess or unease a little bit that's in the economy. This is why the pricing compression with national agencies and local revenue is occurring. After all, price does screw the market. One of the things I learned early on in the business here. Now what's the solution for companies like Saga. Two things come quickly to mind. First is that I tell this story to anybody who will listen. So, it's a short one. Vince Lombardi probably the most legendary football coach ever, was having a difficult season, and then had a particularly bad game where his beloved Green Bay Packers were severely trounced. Lombardi went into the locker room with his team and looked to his players and simply said, "Gentlemen, we need to get back to basics." He then picked up the pace and said, "Gentlemen, this is a football." Well, we need to markedly increase the training and teaching part with our sellers and practice, practice, practice. This is a priority that we're going to get into. Now this thought here of training and teaching and everything else was coupled with another thought that occurred to me about a week ago when I was kind of ruminating and reflecting back on a trip that I had to Iceland. And when I was in Iceland, I was there as -- for a meeting with the government as I'm the Honorary Consul for Michigan, Ohio and Indiana. I have been that for 25 years. And every five years, the government brings all 240 honorary consuls from around the world together to talk and discuss and see what's going on. And I'll tie this all together, please, so bear with me a little bit on this. The first session that we had was presented by the CEO of the largest shipping line in Iceland, Eimskip. And he is also active in a very big way with international fishing and sustainability. Again, be patient with me for a minute. And he started off his talk with the basic facts that globally, globally, only 50% of the fish is used, and 50% is thrown away. Fishing is Iceland's second largest industry, tourism is first. The challenge in Iceland is what can we do to expand this percentage. And now think about it, you could easily just say, "Well, listen, we've been for hundreds of years as a fisherman growing up, we cut off the

head, we cut off the tail, we take out their thorns, we skin the fish and sell the fillet, and that's it, and that's our business." Now, you can continue to do that or you can continue to start doing research and thinking what's going on. It took several years and currently Iceland fisheries utilized 74.6% of the catch. By the way, only in Iceland would you go with 74.6%, not sure they would say 75%. This is primarily as pharmaceuticals and cosmetics. And one of the most exciting finds was the use of cod fish cells. Yes, cod fish cellular makeup. Look up Kerecis, K-E-R-E-C-I-S. I was really blown away by this. It's a cellular fish skin graft that has regenerative bacterial properties of a cellular fish, basically it's a fish skin graft. The protein composition closely resembles that of human skin. It is conformal cover for severe trauma and burn wounds. In the presentation that was made, a US Army dud whose life was severely injured by a landmine in Afghanistan told a story that his wound would not heal. And after several years the docs advised him that the leg would need to be amputated. One of the other docs told him about Kerecis and try it. And after repeated applications, the leg healed. He showed it on a video recently. You can look this up. But what does this have to do with radio? Well, basically, we've been doing over and over and over again the same things. We might go outside and find new products that are not tangential to radio. We have to find new and different ways to expand our knowledge and our abilities and to not shirk or shrink our duties. We need to research and invent ways to expand and increase all parts of radio. A quick example is a technology you probably haven't heard of, DRM. It's the treatment of the AM spectrum, so that AM radio signals are sound quality of FM. Current DRM technology, which is digital issues, exclusively for AM radio in several European countries stations have turned their AM analog spectrum in for AM digital, and it's working. So, what we have here is an abandoned band on AM, except for new spot. And suddenly can be reborn with DRM. And India, Switzerland, Norway are already embracing DRM technology completely. Our commitment at Saga is to change our culture and focus on local direct business. Let me tell you why. This is how radio started and then it drifted in the local direct. I'm speaking specifically about hundreds and hundreds of categories that have not been either approached or well mined. The consultant sell must be applied, it is not about reach and frequency or even rates, it is about achieving results from local service providers and local merchants. No, I'm not talking about the proverbial mom-and-pop stores. But the companies, for instance -- an electrical company or a plumbing company with a dozen trucks. Frankly, the list goes on and on and on. These companies became disenfranchised when the death of Yellow Pages occurred. Think about it. We used to go to, all the time, go to Yellow Pages and look for -- lookup a product, lookup for it we're going to get answers. That's not available now, it's not -- at all. Radio can and does build this brand or their brand. It provides top of mind awareness. This requires effective and powerful copy, not price an item, it requires imaging. I'm going to ask you to think back for a second to a couple of decades ago when a movie came out. And it was a movie -- it wasn't about branding, but it was. And the one thing that they had in there, and the name of the movie is, "Who ya gonna call?" Ghostbusters. Everybody's heard that. They still know that. It's still used as part of the genre. It was just a line in the movie that was repeated over like an earworm that sticks in your brain forever. "Who ya going to call?" Ghostbusters. Okay. This is what I'm talking about radio can and should do this type of branding on an intense scale and provide new revenues to replenish the cheap dollars that are now permeating our industry. What are we doing? Well, for starters, we do have digital programs and platforms. Actually, we closed the former department that was located in an outlying market and rebuilt it from scratch and moved it to our corporate offices, where we can interact with the new staff as we push new products

into the -- in this field. Also, we've hired professional full-time people, whose sole function is to teach existing sellers and new hires, how to sell to retailers. What we need is a different approach and does require a paradigm shift in the sales thought process. Our mission is to teach, train, supervise, shadow, course correct and also mentor our sales staff into being superstars of local direct and local service companies. It will take time, months possibly. But once this is in place, we have returned to the basics of radio, which is to do compelling radio like a great copy, run it with frequency and know very well your client and smother them with service and ideas. Our smaller markets already know how to sell local direct because they're not reliant on agency revenue, and they have developed a skill set in presenting and closing longer-term business with local companies. To put this a little bit more into perspective. So far this year, through November 1, we, as a company, have produced creative spots for presentation purposes, numbering 3,227, actual count as of November 1. First of the year till now 3,227 new spots have been created for presentation purposes. I wish I could say that all of these have been converted into revenue. We're getting there, we will. But however, this resulted in \$1.4 million in additional revenue for the year, and we're just starting. As an example, our stations in Ocala, Florida, which are new to us. When we explain the concept and how it works and how you do when you get this produced 388 spots, and made sure they were played for the client. When they would go on cold-calls or presentation, "Hey, I have an idea. Well, I mean, I'll let you listen to something. I want to do it." Even in Milwaukee, which is a major market for us, our stations there are rapidly growing local direct product, and they produced 538 new commercials for clients that they were pitching in local direct. This emphasis is being accelerated in each of our markets. Frankly, there are some markets that are not so good, and these are finding that we are monitoring them for performance levels. Once this is implemented and enforced, it will most certainly help change the revenue levels and the culture and selling behavior. We are already experiencing great initial results with new clients. Let me tell you a story and that's just -- I've been telling stories. All right, Ed. I got a phone call several weeks ago from one of our managers in one of our midsized markets. He said, "Hey, I got to share this story with you. We just sold a new client, \$30,000 worth of radio advertising in one market." And I said, "What business was he in?" He said, "Ahh! Bedbugs." I said, "Bedbugs?" And he said, "Yes, you thought they were gone." I said, "Well, yes, I kind of did, because we really haven't heard about it." He said, "No, not so much in college towns." College towns and Airbnb are the two biggest problems for bedbugs. And he said that if you look at this college towns, the landlords aren't the most particular with their renters. This client in turn told our manager that even when he is fumigates a house and pronounces it's safe, the first thing that is said is, "Get rid of the mattress." So, we said, okay. Let's then go to a mattress store in town and tie them into the bedbug buy. So, at the end, we have anything where the mattress dealer is cooperating with a discount on the mattress and back and forth and cross-pollinating it. These are the ideas and promotions and things that we need to keep on doing. I think you see that where this is going. We are changing. We're expanding our thought process, and we're expanding what we do and discovering new uses for an old medium. New uses for an old medium. Well, stay tuned, there are still bumps ahead, but I do feel confident that our plan and actions are sound. We have 33 years under our belt as a company. And we haven't disappointed our investors yet. We are not about to. No question about this. My style is to think, create, do and execute. I expect immediate gratification, and that isn't quite occurring fast enough for me right now. We cannot sit idly by expecting the world to change around us for the better. We have a solid industry to help stimulate the economy for the better.

Effective now, Saga has adopted the paso doble style for our sales effort. By the way, for those who are really familiar with paso doble, it's a Spanish term, which is soldiers marching at 120 steps per minute, which is pretty fast. So, my byword here is paso doble to our sellers and to our people, let's get moving pretty fast. If you want to talk further, just call me, call Sam. We're around for the rest of the day. We've answered most of the questions, I believe. If there is one that we missed, pick up a phone and call us. And I do thank you for your time this morning. Sam, do you have anything that you want to add here?

MR. BUSH: I do not. I think that covers it very well. And I think, Catherine, we're now ready to wrap it up.

OPERATOR: Thank you, ladies and gentlemen. This does conclude today's conference call. You may disconnect your phone lines at this time and have a wonderful day. Thank you for your participation.

MR. CHRISTIAN: Thanks, Catherine.

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