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OUTFRONT Media, Inc. (OUT)

Q3 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the OUTFRONT Media Third Quarter 2021 Earnings Conference Call. At this time, I would like to turn the conference over to Linda Murad, Vice President of Financial Planning and Analysis. Please go ahead.

Linda Murad

Vice President, Financial Planning & Analysis, OUTFRONT Media, Inc.

Good afternoon, and thank you for joining our 2021 third quarter earnings call. With me on the call today are Jeremy Male, Chairman and Chief Executive Officer; and Matthew Siegel, Executive Vice President and Chief Financial Officer. After a discussion of our financial results, we'll open the lines up for a question-and-answer session. Our comments today will refer to the earnings release and a slide presentation that you can find in the Investor Relations section of our website, outfrontmedia.com. After today's call is concluded, an audio archive will be available there as well.

This conference call may include forward-looking statements. Relevant factors that can cause actual results to differ materially from these forward-looking statements are listed in our earnings materials and in our SEC filings, including our 2020 Form 10-K, our second quarter 2021 Form 10-Q and our September 30, 2021 Form 10-Q which should be filed tomorrow. We'll refer to certain non-GAAP financial measures on this call. Any references to OIBDA made today will be on an adjusted basis. Reconciliations of OIBDA and other non-GAAP financial measures are in the appendix of the slide presentation, the earnings release and on our website, which also includes presentations with prior-period reconciliations.

Let me now turn the call over to Jeremy.

Jeremy J. Male

Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

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Thanks, Linda, and thanks to you all for joining us today. I'm excited to be on this call and sharing the results of our continued recovery and the positive outlook we have for our business. This quarter we've had a key milestone with our billboard revenues surpassing our 2019 third quarter level and transit showing very steeper quarterly growth. As you can see on slide 3, total revenue grew 41% which was again above our expectations. This impressive growth was across the board with US billboard up 32% from last year and transit revenue up 95% from last year, markedly higher than our earlier expectations. Our recovery was initially led by our mid-sized markets, and we are now seeing acceleration across all of our regions with very few exceptions.

While transit isn't yet back to 2019 levels, we're encouraged by ridership gains and national advertiser interest in reaching the millions of people who utilize our various franchises. It's good to see that our key transit markets revenue return is starting to over index the gradual ridership recovery. This revenue improvement carries through our financial statements as OIBDA and AFFO posted growth rates well above our revenue growth percentage. With this performance and current Q4 visibility, we now feel confident we will outperform our previous full year guidance by a significant margin, and we expect this momentum to continue into next year. I'll leave Matt to give you more details on that good news in a few minutes.

Let's turn to slide 4 for a more detailed look at our US Media revenues. As mentioned earlier, billboard revenues were up 32%, reaching 102% of third quarter 2019 level. Transit revenues were up 96%, almost double the third quarter of 2020, which was heavily impacted by the pandemic. Transit ridership in New York City and Boston has now passed 50% of equivalent 2019 levels with return to school and people starting to return to their offices again. This improvement in audience has driven a steady improvement in revenue.

Turning to slide 5 and to look at US sources of revenue. You can see that national business growth has accelerated with a 55% gain. This is the first time since the start of our recovery that national grew faster than our local business. This is a great indicator for the future as our asset portfolio is strategically built to meet the growing demands of large advertisers and agencies. We expect this trend will continue over the next few quarters. Our local US business also performed particularly well with a 33% increase this quarter. And more importantly, the billboard portion of our local business is 7% above the comparable 2019 third quarter level.

This robust revenue recovery and shift in business mix towards national advertisers has driven yields higher across our billboard portfolio as you can see on slide 6. We were delighted to see a total yield of over $2,400, up 34% from last year, once again, above our 2019 third quarter level. We anticipate further yield improvement for the remainder of the year. Our digital business continues its strong recovery as you can see on slide 7. Digital billboard grew 65% in the quarter, more than 2.5 times the impressive static growth rate of 23%, and digital transit grew almost 200%, albeit from a very low base in 2020. These growth rates are eye catching, and we firmly believe digital will be a key growth driver of our business in the future.

To complete the revenue picture on slide 8 is our other segment, which is primarily Canada. Performance across the board almost matched our US business with growth of nearly 40% as Canada continues its rebound from tight government restrictions.

Let me now hand it over to Matt to review the rest of our financials.

Matthew Siegel

Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

Thanks, Jeremy. Good afternoon everyone. Thanks for joining our call today. Please turn to slide 9 and I'll start with our expenses. Overall, our total expenses were up $68 million year-over-year, similar story to our second quarter, with the cost increases primarily result of the continued recovery in our sales performance. The largest

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cost bucket is billboard lease expense, and here we see a modest 7% increase, which, when compared to our revenue growth, highlights the operating leverage inherent in the largest portion of our business. Most of our real estate expense is subject to long-term leases with an average life of approximately 10 years. So we don't expect to see a material impact from inflationary pressure on this expense line anytime soon.

Transit franchises likewise are subject to multiyear agreements, and margins are not likely to be materially impacted by inflation in the near term. Transit franchise expense continues to have the largest cost variance due to high increases in revenue, and thus revenue share across most of our franchises around the country, and from the MTA performance, which will remain beneath its guaranteed minimum annual payment level for all of 2021 as compared to 2020, when our amended contract permitted us to defer the MAG and paying only revenue share from the second quarter on. Our second largest cost bucket is SG&A which grew 34% in the quarter, largely as a result of higher compensation costs from the stellar performance of our teams.

Our operating leverage is demonstrated by our OIBDA performance this quarter as total expenses increased 31%, 10 percentage points below our revenue growth, even with the headwind of the MTA minimum annual guarantee payments. You can graphically see this improvement in OIBDA on slide 10 as our 41% revenue growth drove OIBDA up 82%. Of course, this is our highest quarterly OIBDA since the end of 2019, and our OIBDA margin of 27% is near our historical level. There are a number of contributing factors to our improved OIBDA margin. One is shift in business mix with transit forming a lower than historic portion of our revenue. Two, a higher relative growth in our smaller markets and faster growth in digital inventory, and successful efforts from our real estate teams addressing some challenging leases.

Looking at the breakdown of OIBDA on slide 11, you can see 70% growth in US media billboard, which is also surpassed our 2019's third quarter level. We are enjoying the recovery in sales momentum, and as Jeremy said, these results not only show we turned a corner, but have also have paved the way for the future. Transit OIBDA is historically much smaller than billboard and has just turned positive, another pleasing hurdle in our recovery. The MTA performance remains below the minimum annual guarantee level, but has the potential for extremely high incremental margin as performance recovers toward its MAG level in the future. The franchise costs remain fixed and the variable costs are only those associated with selling. So we expect to see sequential improvement in transit gross margins again in the next quarter.

Let's now turn to capital expenditures on slide 12. Our maintenance CapEx is higher than last year as we catch up on some operations and IT spending that was postponed last year, and we spent on tech upgrades in various facilities. Growth CapEx was ahead of 2020, but far behind 2019 level, as the uncertain supply chain has held up our digital screen deliveries. We did add 34 new digital billboards this quarter through conversions, management agreements and acquisitions, and our pipeline of conversion locations remains robust. So we believe the supply chain delay is only a timing issue, and we will catch up to our multi-year target once the shipping backlog dissipates. We expect to spend more on capital projects in the fourth quarter, but because of the uncertainty in the supply chain and timing of deliveries, we now think our full year capital expenditure number will be in the range of $70 million to $75 million lower than our previously estimated $85 million.

Slide 13 shows $79 million in AFFO, which is up 185% from last year. Continued sequential recovery in billboard and transit revenues are flowing through to OIBDA and AFFO. Our revenue outperformance and the passage of another three months to evaluate any business impact from COVID variants in certain parts of the country has provided us enhanced visibility and confidence to again increase our AFFO guidance. We now expect our AFFO growth for the full year will be around 80%. Slide 14 has our quarterly MTA deployment update. Subject to any supply chain delays, we have returned to our normalized pace of activity. Over the last 12 months we prioritize the

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installation of digital urban panels, the screens of the top of steps heading into the subway to take advantage of active pedestrian traffic when other audience segments may have been less crowded.

Now and into next year, we are finishing various stations and ramping up rolling stock efforts. Subway ridership has been steadily increasing since Labor Day marked by back-to-school, and the recent average daily ridership is above 3 million, which is about 55% of 2019 levels. This steadily rising number has become polite cocktail conversation among advertising buyers and busy commuters, and we are excited to be seeing the expansion of revenue that is accompanying these eyeballs. Looking on our balance sheet on slide 15, one can see our committed liquidity is still around $1 billion. We'll use a small amount of our cash this quarter as we resumed MTA deployment, restarted a quarterly common dividend and spent $12 million on global tuck-in acquisitions. This brings our year-to-date acquisition total to $55 million with an active pipeline of interesting local opportunities we are still working on.

Our revolver remains undrawn, and our overall weighted average cost of debt is 4.3%. Our leverage peaked earlier this year and is continuing its descent as OIBDA steadily recovers with net total leverage at 6.6 times at the end of the third quarter, down from 7.9 times three months earlier. And I'm sure you noticed last week that our board of directors approved the $0.10 common dividend for the fourth quarter. We believe this amount for the third and fourth quarters, combined with the preferred dividend for our full quarters will effectively cover our full year REIT requirement, and we look forward to growing our quarterly dividend as business performance continues to improve. Our financial outlook is very strong and the business performing better than we had hoped. We look forward to finishing the year on a high note into an exciting 2022.

Let me now turn the call back over to Jeremy.

Jeremy J. Male

Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

Thanks, Matt. And now let's turn to our third quarter outlook on slide 16. As I said at the start of the call, we're very excited about our industry these days and the prospects for our business going forward. Advertiser demand for out-of-home, traffic, subway ridership and revenue are all moving in the right direction. Therefore, as we sit here today, we expect our total revenues to be up in the low 30%s range in the fourth quarter. Within this, we expect to further improve our relative outperformance for US billboard versus 2019, and the continued strong growth in transit.

Our notable performance in the past two quarters and our outlook for this quarter are driven by the return of certain categories that reduce their activities and their advertising during the last 18 months, such as movies and entertainment. It was good to see the Bond movie open in theaters and performed so well after moving the release date a number of times. We're also enjoying the benefit of some newer categories that are still small overall, but growing nicely like cannabis and online gaming. And importantly, many of our steadier categories driven by local advertisers such as professional services, retail and healthcare, continue to be important for our business and are showing solid growth.

While, it's a little early to speak about 2022, for a quick preview we are seeing similar category performances into next year as we all look forward to more movies and other forms of recreation returning. The reopening of Broadway, increased tourism and travel are lifting the spirit of the population and increasing consumer confidence. This confidence is enabling businesses to spend more to entice new and returning customers to their doorstep. From my office here in Midtown, I can see increasing numbers of commuters, pedestrians, office workers and diners, and know that they will drive the continued growth of our industry. This is equally true for cities right across the country. This is a great time for out-of-home and indeed for OUTFRONT.

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So with that operator, let's now open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from Alexia Quadrani with JPMorgan. Please go ahead.

Alexia S. Quadrani
Analyst, JPMorgan Securities LLC

Q

Thank you. My first question really is on the improvement you're seeing in the transit business. I guess, do you have any sense of when maybe approximate timeframe, and I know you don't have a crystal ball, but you probably have more knowledge than we do, well we might see it kind of get back to closer to 2019 levels, and is the 80% to 85% I think ridership, I think in the past [indiscernible] (17:00) you only need to be there to sort of get back to sort of normalized advertising run rate. Is that still sort of a good gauge in terms of where you think you need to get in order to see advertisers sort of really return to the medium the way they did in 2019?

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

A

Yeah. Thanks for the question, Alexia. We're obviously seeing some strong increases right now in our transit business, albeit off that low base. And as we look forward, we expect that 2022 will be a sort of continued year of recovery. And while as you rightly say we don't have a crystal ball, we would expect that in 2023 we will likely be back to our sort of 2019 levels. And in terms of that ridership versus revenue, we've never quite been here before, but it is certainly our expectation that we will be able to achieve the revenues that we saw in 2019 without 100% of audience. And yes, we think it's likely to be in that 80% to 85% range.

Alexia S. Quadrani
Analyst, JPMorgan Securities LLC

Q

Okay. Great. And if I could just have one follow up on the – I think you mentioned maybe some supply chain issues potentially impinging just slightly on your conversions to digital boards going forward. I think one of your peers also commented into that vein. Do you have any sense of how much behind it maybe, like how much of the backlog you may have, or do you sort of think that it might be a slow start to the year, but you have to kind of get back to a normalized rate maybe by the back half of next year?

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

A

Alexia, it's Matt. I think it's going to be a slow finish to fourth quarter, and we think most of our screens are somewhere in the ocean. So we think when they do come in, we can get them installed quickly, by mid-year we should be caught up and we would expect a bigger year next year than normal just for an over-indexed 12 months. But it really depends on supply chain. I'm guessing all competitor screens might be in the same boats in the same oceans.

Alexia S. Quadrani
Analyst, JPMorgan Securities LLC

Q

Okay. Thank you very much.

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Operator: Thank you. And our next question comes from Jim Goss with Barrington Research. Please go ahead.

James Charles Goss
Analyst, Barrington Research Associates, Inc.

Q

Thanks. I was wondering, in terms of the return of traffic into the transit systems, do you benefit basically ratably in terms of increase in ridership, or with return of traffic, do you get any pricing uplift from greater capacity utilization?

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

A

Thanks for the question, Jim. I guess, the first thing to say about our business in transit is that, actually compared to 2019 as we move forward and continue to digitize we're actually going to have a really fabulous product that we think will be increasingly appealing to advertisers. So I think the fact that we're going to have this sort of differentiated digital product will allow growth beyond that which we're all at the level that we saw in 2019 as we go forward. Now, that is to do also based on ridership returning back towards something like the levels that we saw before, and we talked earlier about that 80% to 85% range. And then getting back to those revenues will be dependent on two things, it will be dependent on pricing in terms of sort of cost per 1,000, and also there is opportunities in utilization. So it will be both of those things that drive us back to those 2019 levels.

James Charles Goss
Analyst, Barrington Research Associates, Inc.

Q

[audio gap] (20:56-21:03) contracts that were up for bid, and certainly that's ancient history now it seems. But I'm wondering, as you move forward, are there some that will come back that you'll have an interest in and be capable of taking a look at? And you might also relate it in terms of any appetite you'll have and at what point for billboard market acquisitions and maybe further digital installations.

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

A

Yeah. Thanks Jim. The first part of your question went a little bit quiet, but I think it was regarding sort of the opportunities for further transit franchise wins. So as we look forward, most of the key franchises have actually been put to bed for quite a long time. So we don't anticipate that there will be significant change in significant franchises over the sort of, over the coming months, that's for sure. With regards to billboard acquisitions, as Matt said, we've spent $55 million so far this year. We've got a very active pipeline and we're keen to add weight in a number of our markets around the country. So we're pursuing those with positivity to put it like that.

James Charles Goss
Analyst, Barrington Research Associates, Inc.

Q

Okay. And one last one. It was encouraging to see you have a common dividend. I think that's long been a reason to own the stock. And I know there are requirements REIT-based, and then also the preferred that account for some of the requirements. I was wondering if you might frame up the rationale to the extent you can that the board might look at in terms of how valuable that common dividend component is going to be, and I know it's been under pressure recently, but how we might look forward with that as an investment component?

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

A

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Jim, it's Matt. Thanks for the question. The board looks at it a number of different ways. Obviously first and foremost is the REIT requirement, and we think this year two quarters of $0.10 plus the preferred coverage that requirement as our business is recovering and growing, and we've said we expect to be a grower, an aggressive grower of the common dividend. Also very importantly and I think just what we thought about in the summer, the signal and the communication benefit that dividend that we saw mid-year, the growth and recovery of primarily our billboard business and more recently our transit business. So we wanted to make sure people knew that, we felt confident of bringing the dividend out before we did any year-end calculations on the REIT. So we feel really good about where we are, and the board is very comfortable and starting and looking at growing that dividend over the next few periods.

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.
A

And just adding to Matt's comment, Jim, briefly, you remember in the past that as a company we tended to pay a dividend in excess of the absolute REIT requirement, and we're looking forward to getting back into that kind of range as we look forward. But from where we are now and as Matt just said, there's the opportunity for us quite aggressively to grow that dividend as we move on from here.

James Charles Goss
Analyst, Barrington Research Associates, Inc.
Q

Okay. Thanks. Good to hear. Thanks so much.

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.
A

Thanks, Jim.

Operator: Thank you. And our next question comes from Ian Zaffino with Oppenheimer. Please go ahead.

Ian Zaffino
Analyst, Oppenheimer & Co., Inc.
Q

Hi. Good quarter. Great outlook. Just sort of one question, maybe a follow-up on the last one would be use of capital. What does the M&A market look like right now? Things are recovering pretty rapidly. So just curious what the bid ask right might be and how many sellers there are now versus the way it was maybe pre-COVID ? Thanks.

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.
A

Hi, and thanks for the comments, and thanks for the question. Look I think it's fair to say that at the moment there seems to be a lot of activity in out-of-home. There's a number of other private equity institutions chasing assets in out-of-home right now. I think that is driving some sellers to come forward. So our competitor acknowledged in a reasonable pipeline when they commented just yesterday, we have a good pipeline. And yeah, we feel good right now that the pricing out there in the market is likely to be pricing at which sellers may wish to move their assets on.

Ian Zaffino
Analyst, Oppenheimer & Co., Inc.
Q

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Okay. And then on the digital board side with the supply chain issues, will you be able to make [indiscernible] (26:44) that you'll miss out on this year into next year, or is this something that you're going to continue to do what you plan to do in 2022 and no more, meaning, you're not going to make up the backlog that you might have from this year?

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.
A

Yeah. I think it's really the pipelines in place, our real estate team is still developing getting permits. It is waiting for screens. So if we annually target 150 to 200, and we fall short this year, I think we would target a little more next year to make up for that, obviously the development, the permitting will be there. And assuming we can get the screens, we'll have a little more growth CapEx than usual, and catch up. As far as revenue, it takes three to six months to ramp up the revenue on those digital billboards. And we have an install base of 1300 or 1400. So I don't think the few that we're not going to install this year are going to materially impact the revenue in the longer term, it won't be missed.

Ian Zaffino
Analyst, Oppenheimer & Co., Inc.
Q

All right. Perfect. Thank you very much. Good quarter again.

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.
A

Thanks.

Operator: Thank you. [Operator Instructions] Next, we'll go to Ben Swinburne with Morgan Stanley. Please go ahead.

Benjamin Swinburne
Analyst, Morgan Stanley & Co. LLC
Q

Thanks, good afternoon. I have two questions, both on kind of margins. Matt, it looked like billboard margins, and it were a couple of hundred basis points higher this quarter than even the third quarter of 2019. You mentioned geographic mix. I just was curious if there were any other drivers you'd highlight, and whether you think the billboard business, as we look out over the next few years is any different than it was from a margin point of view once everything sort of recovers? That's my first one. And then I have one to ask about transit.

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.
A

Great question. And I appreciate you noticing. We really, you look over a couple of year comparisons from 2019 to 2021. The digitization that we've been doing over the couple of years has an impact. So you see almost every market, the higher percentage of digital inventory and digital revenue is helping margins. On the mix issue, this isn't the plan, but the weight of non-New York, non-LA, very high growth has helped margin overall as well. So we think portfolio and operating businesses all work in our favor.

Benjamin Swinburne
Analyst, Morgan Stanley & Co. LLC
Q

Okay. So it sounds like with digital growing that there might be margin growth in billboard kind of all else equal over time? Don't want to put words in your mouth, but...

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Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

A

Yeah. We think directionally billboard margin is moving higher, both the operating leverage of the business and the digitization. I think, one of the beauties of the digital inventory if we increase revenue higher than we increase cost, eventually you see the difference in the numbers.

Benjamin Swinburne
Analyst, Morgan Stanley & Co. LLC

Q

And then kind of a same line of questioning on transit. So as we think about 2022, we can't see the MTA per se inside of your transit business, although obviously we have a rough sense of how big it is. But is it one way to think about the incremental leverage you're going to get as you go from the MG back to a rev share that maybe by the time we exit 2022 we're back at kind of the transit margins of pre-COVID because you've sort of scaled the thing? I don't know if there's any way if you can help us think about what will be sort of an unusually profitable recovery for a period of time and then back to kind of standard transit economics.

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

A

Yeah. This is probably the silver lining of the MTA being under the MAG. So as we get back to that line, every dollar of revenue 90%, 95% of that goes to OIBDA, is the fact that we're repaying a fixed cost and no more, and we're just paying commission. So it's in our best interest and everyone's best interest to drive New York transit revenue back up to its formal level. So we're excited by the return, and we're excited about the future once it gets there.

Benjamin Swinburne
Analyst, Morgan Stanley & Co. LLC

Q

Thank you.

Matthew Siegel
Executive Vice President & Chief Financial Officer, OUTFRONT Media, Inc.

A

Thanks, Ben.

Operator: Thank you. And that concludes today's question-and-answer session. At this time, I'll turn the conference back to Jeremy Male for any additional or closing remarks.

Jeremy J. Male
Chairman & Chief Executive Officer, OUTFRONT Media, Inc.

Thanks, operator, and thanks to everyone for attending this call. We look forward to speaking to you next quarter about the further positive developments in our business. And in the meantime I'm speaking with many of you at investor events in the coming weeks. Thanks very much and have a good day.

Operator: And this concludes today's call. Thank you all for your participation. You may now disconnect.

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