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# EDITED TRANSCRIPT

TGNA - Q3 2017 Tegna Inc Earnings Call

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## OVERVIEW:

Co. reported 3Q17 results. Expects 2017 total Co. GAAP revenues to be approx. \$1.9b. Also expects 4Q17 reported total Co. revenues to decline in high-single to low-double digits YoverY.



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## CORPORATE PARTICIPANTS

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**Victoria Dux Harker** *TEGNA Inc. - Executive VP and CFO*

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**Barton Evans Crockett** *FBR Capital Markets & Co., Research Division - Analyst*

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## PRESENTATION

### Operator

Good day, and welcome to the TEGNA Third Quarter 2017 Earnings Conference Call. This call is being recorded. Our speaker for the day will be Dave Lougee, President and Chief Executive Officer; and Victoria Harker, Chief Financial Officer. At this time, I would like to turn the call over to Jeff Heinz, Vice President, Investor Relations. Please go ahead.

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**Jeffrey Heinz** - *TEGNA Inc. - VP of IR*

Thanks very much. Good morning, and welcome to our third quarter earnings call and webcast. Today, our President and CEO, Dave Lougee; and our CFO, Victoria Harker, will review TEGNA's third quarter results. After that, we'll open up the call for questions. Hopefully, you had the opportunity to review this morning's press release. If you have not yet seen a copy of the release, it's available at [teгна.com](http://teгна.com).

Before we get started, I'd like to remind you that this conference call and webcast include forward-looking statements and our actual results may differ. Factors that may cause them to differ are outlined in our SEC filings.

This presentation also includes certain non-GAAP financial measures. We have provided reconciliations of those measures to the most directly comparable GAAP measures in the press release and on the Investor Relations portion of our website.

With that, let me turn the call over to Dave.

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

Thank you, Jeff, and an early good morning, everyone. The third quarter marks TEGNA's first as a pure-play media company following the completion of the spinoff of Cars.com and the sale of CareerBuilder. Our third quarter performance demonstrated the strength of our operating model. Revenue for the quarter on a comparable basis grew 5%, in line with our guidance. Growth in subscription revenues, combined with execution against our strategic initiatives including substantial growth for our OTT ad network, Premion, drove this revenue performance.

First, I'd like to talk about the progress made this quarter and then turn to the future. In everything we do, we aim to bolster our relationship with our local consumers and clients by doing our part to bring communities together in every way and act locally. To serve these audiences, we're



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infusing digital in everything we do, ensuring we're not missing cord cutters and the next generation of always-on mobile consumers. We're focusing our efforts on three key pillars: our content transformation strategy; our advertising and marketing services transformation and initiatives and how we go to market; and the way we distribute our content now ubiquitously.

Our content transformation efforts have transformed from an initiative to a culture, and it's core to our future strategy. We're taking our future into our own hands by creating unique, live and original content, both in news and non-news time periods, to combat changing viewer habits. In an on-demand, OTT world, unique live, locally relevant and differentiated content is becoming far more important than it was in the past and we are acting on that trend.

In the third quarter, we continued to make wholesale non-incremental transformations of our local news operations. We're creating true digital-first newsrooms and using data to better serve audiences on air and in mobile and their social feeds.

For example, in Charlotte, we saw continued ratings growth in both the mornings and late news throughout the quarter. We've owned that station more than 2 years now and the content transformation of this previously underperforming station started 16 months ago. Since then, we have significantly grown our share of audience as well as revenue.

Another example is WFAA in Dallas, our largest revenue market, where we transformed every newscast. Ratings are up in the mornings and evenings and their data-driven decision-making off of social media and their own digital platforms is driving increased engagement on every screen.

Also in the quarter, we launched innovative multi-platform, non-news programs, replacing some traditional syndication programs in those time slots. Importantly, these shows are not capital-intensive. They are produced at our local stations, which reduces cost and increases our agility. And we own all of these shows and the associated advertising inventory.

In September, we premiered Daily Blast LIVE, our groundbreaking 30-minute news and entertainment show produced out of KUSA in Denver. We are very pleased at how the show is doing and believe it is one of the most innovative shows anywhere in daytime TV. DBL, as it is called, is a first-of-its-kind format that is live in every time zone across 35 TEGNA markets, live in every time zone that we needed, I should say, something unprecedented in TV syndication. The content on DBL is always live and crowdsourced in real time from viewers through social media. Truly an example of live interactive social TV.

The same week we launched DBL, we also debuted Sister Circle, another example of audience targeting and segmentation. This new, live daily talk show targets African-American women, a large and traditionally underserved audience and an audience that we over-index on in a number of our large markets. We're off to a strong start on our own stations as well as a national distribution deal with cable channel TV One.

And just yesterday, we announced that we are partnering with Cooper Media to launch Quest, a new ad-supported exploration and adventure multicast network that targets male viewers. From a programming perspective, think of the type of exploration program the Discovery Channel used to have a lot of. We know this programming will resonate well in the over-the-air homes where the multicast channels over-index. Quest will initially debut early next year across our portfolio. We also have an ownership stake in them and we'll share in the network's revenues.

This partnership with Cooper Media is similar to our existing relationship with them on the Justice channel, which is carried across our portfolio and continues to grow each quarter. This is a zero cost, 100% margin monetization of our spectrum that also further diversifies our content offerings.

Also in the quarter, we launched redesigned mobile platforms across our local media properties, resulting in a 71% sequential increase in mobile video plays. Our digital properties averaged 38 million unique visitors in the quarter, which is an increase of 16% over the prior quarter.

And this past quarter also proved how critical a robust digital presence is in times of need. Throughout hurricanes Harvey and Irma, we were able to provide people vital, often life-saving information on our mobile and digital platforms when the power was out. For example, the number of visitors to our Houston station's digital properties rose 166% and video plays were up almost 400%.



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In a moment, Victoria will give us more detail on the financial impact of the hurricanes in Florida and Texas, especially in Houston, where we specifically got hit hard. It's worth noting, though, that due to our scale and values as an organization, we were able to leverage our talented journalists from across TEGNA to support and enhance the coverage in all our affected hurricane markets, which were multiple, in addition to raising millions of dollars for relief efforts.

On the marketing and advertising sales transformation side, we continue to advance our efforts and strategy of expanding the markets we're taking share from by expanding the markets we're after with additional products.

As I've talked to you before, we've created a brand-new disruptive business, the industry's first OTT local advertising network. As I've talked to you and to many of you in person about over the past few months, Premion is a one-stop shop that allows local, regional and some national advertisers to place advertising on long-form programs across a broad array of OTT services such as streaming devices, smart TVs, and web browsers.

Premion is a first mover and is meeting a need many of our clients didn't even know they had. It continued to surge in the quarter, executing more than 6,500 campaigns, serving 800 clients in 195 geographic markets, to my point about expanding markets. It has quickly become a must-buy for our advertisers trying to reach cord cutters.

With Premion, we have a distinct advantage because of our large local sales force that is leveraging their relationships with local and regional advertisers. Premion's third quarter revenue was up 92% over the second quarter and is on track to achieve the high end of our full year guidance of \$25 million to \$30 million.

And we're building on this leadership in the OTT ad space by launching new business extensions. For example, in 2018, we will be launching a DMP or data management platform for OTT publishers, leveraging blockchain technology to enable them to better understand and target their audiences. We're also one of the founding partners, along with MadHive and IBM, in the AdLedger Consortium to advocate for blockchain as a standard in the industry, reducing cost and improving trust and transparency throughout the ad tech ecosystem.

Premion is just one of the many tools our sales force uses to provide our clients with a holistic approach to marketing, allowing them to optimize their spend, putting their ad dollars to work in the channels that make sense to move their products regardless of the platform.

That strategy of innovative multi-product solutions against a broader set of clients is producing results. For instance, third quarter revenue attributed to Hatch is up 49% over last year. Hatch is our internal sales solution agency based in Dallas, leveraging our scale once again. Of the Hatch campaigns running, there was 122% year-over-year increase in the number of clients attributed to Hatch. These are new accounts from advertisers who have not previously worked with us.

Now moving to the distribution side. We continued in the third quarter to make great progress in the OTT space. In the quarter, we closed now virtually all of our major OTT distribution deals with major network partners and major streaming services who will carry our stations and are now in many cases. Those services like YouTube TV and DirecTV now are just being rolled out and just now starting to be marketed, as you probably saw with YouTube being marketed during the World Series, and the TEGNA stations are on those platforms.

As we said before, we're generally agnostic whether a consumer views us on a traditional MVPD or so-called virtual MVPD or OTT service. That's because there are benefits of moving our content on to OTT platforms. Not only does it allow us to reach cord cutters, but as significantly, it gives us access to a new market of subscribers, specifically cord-never's, who may never sign up for a higher-priced cable. The net effect of these trends will be a widening of our distribution advantage over cable and others because only a few cable channels are carried on these skinny bundle services. This has very positive future implications for us in terms of audience, advertising and program distribution.

And to reiterate what we said all along, the per-subscriber economics of these deals are equal to, or slightly better than, the per-sub economics of our traditional MVPD deals. We've just gotten our first payments from one of these services, and although they won't provide any material revenue for the remainder of 2017, it will clearly grow throughout 2018.



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To recap on third quarter performance, this is the quarter where we face the challenge of Olympics and political advertising comparisons occurring in the same quarter, a comparison we have only once every 4 years. This quarter's revenues results are the strongest third quarter we've ever had against those specific prior year comps. In a moment, Victoria will give you details on our results and projections for the fourth quarter. But similarly, our fourth quarter revenues will also be our strongest fourth quarter ever coming off of a presidential election year.

Turning to next year, we will have significant tailwinds in 2018, both internally and externally. Internally, our many strategic growth initiatives, like Premion and others, will continue to ramp up. And in the first quarter, we'll have both the Winter Olympics and the Super Bowl on our strong NBC stations, the first time in 12 years we've had those events in the same quarter.

As always, our large group of NBC stations will over-index on audience and revenue with these events.

Turning to political advertising, the outlook for political advertising tied to the 2018 midterm elections continues to look very good for broadcasting overall next year and for us specifically. And I would point specifically to the elections in Virginia yesterday, which saw a record turnout for an off-year governor election. And clearly, the outcome, which went very much the Democrats' way, as it did in New Jersey, is only going to fuel record fundraising for the midterm elections.

Although it's too early to give a specific outlook because of the competitiveness of our footprint can change in either direction between now and then, I can say it's improved just since we last spoke. Specifically, the resignation of an incumbent Republican Senator in Arizona will all but certainly lead to one of the most expensive Senate races in the country, if not in history, and we have a strong presence throughout the state. Overall, across our portfolio, we've got 18 gubernatorial elections out of 36 nationwide. And of the 34 Senate races nationwide, we have 14 of those.

Finally, let me look beyond 2018 and talk for a moment about the implication of the pending FCC in-market ownership changes. The FCC is about to vote on updating those in-market ownership rules that have been carried over literally from the previous century. And we commend FCC Chairman Pai for aligning these rules with the reality of the modern video marketplace. TEGNA is uniquely positioned to take advantage of these long overdue changes over time, and here's why.

The ability to own and operate 2 Big Four stations in a market has tremendous financial and strategic synergies, as you all know. This type of consolidation has already taken place in the small markets, size 100-plus and smaller, through a variety of sidecar arrangements. But until now, the FCC has prohibited this in the medium and large markets that we operate in, and we are the largest owner of Big Four affiliates in the top 25 markets.

This portfolio optimization can be achieved through a variety of structures, traditional station group M&A as well as swaps, to deliver substantial mechanical synergies. Other affiliate owners in our markets are going to be motivated to optimize their portfolio as well and swap stations with us because of the inherent industrial logic. We have a proven ability to be a disciplined consolidator, creating significant shareholder value through accretive M&A. We know how to operate in these size markets and we have a track record of reaching and exceeding synergy targets ahead of schedule.

Our solid cash flow and disruptive initiatives put us in an ideal position to invest further both in organic growth as well as strategic M&A. Thanks to our financial discipline and operating excellence, we have the rock-solid balance sheet and free cash flow firepower that will allow us to play an opportunistic role in the consolidation of our industry to the benefit of our shareholders.

And with that, I'll pass the call over to Victoria.

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### **Victoria Dux Harker** - TEGNA Inc. - Executive VP and CFO

Thanks, Dave. Good morning, everyone, and thanks for joining us. As Dave had already noted, we are executing well on our content initiatives while enhancing our sales and marketing efforts to support our growth as a stand-alone media business in 2018 and beyond. As a result, our capital allocation strategy remains focused on reinvesting in these types of organic growth opportunities as well as continuing to de-lever, creating future firepower.



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Before I cover our consolidated financial results and capital allocation for the quarter, I'd like to review a few special items for you. As you're aware, during the quarter, two major hurricanes impacted much of the Southeast and Southwest. Hurricane Harvey, in particular, caused major damage to our Houston station, forcing us to permanently evacuate the facility. As a result, during the quarter, we incurred \$19 million in expenses including write-offs related to destroyed equipment and the value of the building as well as additional staffing and operational expenses required to keep the station running during this critical time.

Late in the quarter, we received a partial insurance recovery of \$11 million, which helped mitigate these costs. As a result, the combined impact of these hurricane-related expenses, net of insurance proceeds received, was a negative \$7.6 million or about \$0.02 per share. Beyond these items, the quarter also included transaction-related fees of about \$2 million or \$0.01 per share and an \$8 million or positive \$0.04 a share income tax true-up.

All in, special items for the quarter largely offset each other, providing for a slightly positive impact to EPS from continuing operations of about \$1.3 million or less than \$0.01 per share.

So moving now to the third quarter consolidated financial results. Keep in mind, all of my comments today are focused on performance from our continuing operations in order to clearly provide financial insight into the drivers and results of our business. As a reminder, you can find all our reported data and prior period comparatives in both the text and the tables contained in our press release.

As we discussed last quarter, we now report only one consolidated Media Segment, which also includes a small digital marketing services business that was previously reported in the Digital Segment prior to the Cars.com spin.

As we noted before, TEGNA's even- to odd-year results are disproportionately impacted by the cyclical drivers of Olympics and political spending, driven by our high concentration of NBC stations and traditionally favorable political advertising footprint.

Just to give this further context relative to this quarter, our NBC stations generated a record \$57 million of Olympics revenue and \$38 million in political revenue during the same quarter last year. Naturally, without these events this year, our financials reflect significant even- to odd-year swing for the quarter, later than all our broadcast peers. And while we only face the challenge of the Olympics and political advertising comparisons in the same quarter every 4 years, this quarter's revenue results are the strongest third quarter we've ever had against those specific year prior comps.

In addition, as discussed during our call last quarter, last year's financial results also included a digital marketing services TSA with Gannett, which was terminated during the second quarter of 2017. 2016 results also included Cofactor, a business which was sold in December of that year. Both of these items were previously reported in the Digital Segment.

As I also mentioned last quarter, as a result of these digital items, revenue comparisons were unfavorably impacted by \$16 million again this quarter. Early comparisons will be negatively impacted by nearly the same amount for the remainder of this year and into next until we lap these changes midyear.

So all in, excluding the impact of Olympics and political advertising, terminated digital marketing services and the sale of Cofactor, total company revenue for the quarter was up more than 5% year-over-year, well within the range we provided last quarter.

On a reported basis, total revenue was down 11%, also within the range we provided. Just as a reminder, all of these comparisons can also be found in a detailed table contained in our press release.

So now breaking down total revenue composition a bit further. Subscription revenue growth for the quarter was up 24%, reflecting newly negotiated agreements in 2016 and escalators. Advertising and marketing services revenue improved again this quarter on a comparable basis. Excluding Olympic advertising, terminated digital marketing services and lost revenue of more than \$3 million due to the impact of hurricanes Harvey and Irma, advertising and marketing services revenue was down just 2% for the quarter, and we've seen a sequential improvement in advertising and



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marketing services revenue each quarter this year. On a reported basis, advertising and marketing services revenue was 16% lower than the third quarter last year.

So now turning to expenses. Total company operating expenses on a non-GAAP basis were 8% higher compared to the third quarter year-over-year due primarily to substantially higher programming fees including first-time reverse compensation feeds paid to NBC for 11 of our stations which began earlier this year. Net of programming costs and accelerated depreciation due to the spectrum repacking-related disposals, which began this quarter, adjusted operating expenses were down 8%.

Excluding corporate expenses of \$12.9 million, adjusted EBITDA for the quarter was \$158 million producing a recurring margin from our business operations of 34%, despite the one-time step-up increase in programming fees.

Now as we look forward to the fourth quarter, keep in mind that total company comparisons will again be unfavorably impacted by substantially lower political advertising, which will decline approximately \$82 million from the fourth quarter of 2016.

In addition, the terminated digital businesses will once again impact the quarter's revenue by approximately \$16 million. Excluding these factors, on a comparable basis, total company revenue in the fourth quarter will be up in the high single to low double digits year-over-year. On a reported basis, total company revenue will be down in the range of high single to low double digits year-over-year. On a full year basis, we expect total company GAAP revenue to be approximately \$1.9 billion, which includes roughly \$17 million from the digital marketing services businesses terminated earlier this year.

So just to put this in perspective, on a year-over-year basis, excluding the \$17 million of terminated digital marketing services business revenue this year and \$64 million from last year, we project non-GAAP revenue will be down roughly \$50 million year-to-year, a little over 2%, despite the challenge of overcoming \$170 million loss of cyclical revenue from the Olympics, political and Super Bowl advertising. Excluding those specific factors, full year non-GAAP revenue is expected to be up 6% to 8% on a comparable basis.

As a result of these projections, we expect to have a very strong jump-off into 2018, which is setting up to be an unprecedented year for us. Next year, in addition to continued growth in innovative initiatives, we have material tailwinds which specifically benefit TEGNA in an outsized way, through our very large NBC portfolio of stations and our political advertising footprint. We look forward to telling you more as the year gets underway.

Now turning to liquidity and capital allocation during the quarter. Capital expenditures from continuing operations for the quarter totaled \$11 million, reflecting investments in our news content and infrastructure development as well as system efficiency enhancements and maintenance.

During the quarter, we further strengthened our balance sheet and enhanced our firepower with cash proceeds from the spin of Cars.com and the sale of CareerBuilder. As we discussed on our last earnings call in August, we completed the sale of CareerBuilder on July 31. As a reminder, we retained a 12% ownership stake on a fully diluted basis. Cash proceeds of \$244 million from the CareerBuilder sales net of taxes and other adjustments, combined with the remaining \$40 million Cars.com distribution, were used shortly after the end of the quarter to redeem \$280 million over 2019 fixed rate notes. This will reduce interest expense by approximately \$3 million per quarter through the end of the third quarter of 2019.

Subsequent to the disposition of Cars.com and CareerBuilder, free cash flow from continuing operations was strong at \$98 million. As a result, at quarter end, total debt was \$3.3 billion, producing net leverage of 3.9 times. In addition, as you've seen from our previous release, we expanded the scope of our capital investment opportunities during the quarter through a new \$300 million, 3-year share repurchase program.

As we said when we announced the program in September, we initiated the buyback because at current market prices, we believe TEGNA's stock represents a strong buying opportunity. It is significantly undervalued relative to both its recent and expected future performance. The new repurchase program will allow us to opportunistically deploy cash from time to time but has not changed our capital allocation priorities.

Now let me turn the call back to Dave for some final thoughts.



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**David T. Lougee** - TEGNA Inc. - CEO, President & Director

Thank you, Victoria. Our success in the third quarter shows the power of our model and our ability to execute ahead of a dynamic and changing market. Given our scale, content and culture of innovation, we're able to leverage all of those to meet changing consumer needs as well as our advertisers. And our focus on localism gives us a level of trust with our audiences to cost-effectively turn innovation into growth. The reputation capital and free cash flow generated will be the fuel for consolidation and organic growth.

As we said, we are looking forward to a great year in 2018 with substantial tailwinds, and that, coupled with our strategic initiatives, you can see we are poised to take full advantage of the opportunities in front of us. In a nutshell, we are proactively embracing change.

And with that, Leanne, I'd like to open it up to questions.

### QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) And we'll take our first question from John Janedis with Jefferies.

**John Janedis** - Jefferies LLC, Research Division - MD and Equity Analyst

Dave, maybe a couple for you. One is just, as you know, subscriber trends have been a focus this earnings season. So, can you talk about what you're seeing? Was the sequential decline more stepped down and retrans related to a true-up? And is there a delay -- I know you spoke a little bit about it, but is there a delay in the money or maybe a mismatch on VMVPD dollars coming in?

**David T. Lougee** - TEGNA Inc. - CEO, President & Director

Yes. So I'm going to take those in order, John. So when you talk about sequential decline, do you mean from second quarter to third quarter?

**John Janedis** - Jefferies LLC, Research Division - MD and Equity Analyst

Correct.

**David T. Lougee** - TEGNA Inc. - CEO, President & Director

Yes. That's just seasonal. I mean, it's exactly the same seasonal trend we have last year. We have a number of Sunbelt markets, and remember, we get paid in arrears. So with our high profile in Florida and Arizona as such, we have always seen a sequential decline in second and third quarter, and it's exactly the same ratio as last year.

And yes, your second question, you're exactly right on the delay because -- and we're going to be in a little bit of a black hole time period for a period of time because with the traditional MVPDs, we get paid basically 60 to 90 days in arrears from their subscriber actuals. But that's not -- it's not clear yet what the time line will be on the reimbursements and payments we'll get from our new OTT entrants. With DirecTV, it'll be the same as it is with the traditional side. But the new entrants like YouTube and Sony, it remains to be seen when we'll get that clarity.



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**John Janedis** - *Jefferies LLC, Research Division - MD and Equity Analyst*

Okay. That's helpful. And separately, just given all the ins and outs as we head into '18, can you help us with any kind of pro forma numbers to think about as it relates to the Super Bowl or the Olympics in '14? And with your comments on political, do you see an early ramp in dollars? Or are you looking more like a late spring or summer type of event for the money?

**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

Let me take the second question first while we pull up the -- your question for you on the numbers. I think like we saw in '16, I think spending is going to start earlier. I think the ratio of spending will be pretty close to the same as it's been in the past with that vast majority coming in those weeks between Labor Day and Election Day and specifically really the weeks of the fourth quarter leading up to Election Day.

But in the federal races, the Congressional, Senate and now the governor's races, we've seen it start earlier and earlier every year. Part of that is because there's more early voting in the states. So yes, I think we probably might see a little bit more -- the ratio changes a little bit next year between the quarters, but I wouldn't call it a material change.

I think everybody should realize that the vast majority of it's going to come in the third and fourth quarter, and even then, more than half in the fourth.

And your other question was about Olympics. So Olympics was \$41 million total, not incremental, back in '14. And the last time we had the Super Bowl on NBC, which was 2015, that was \$12 million, and that's basically all incremental, given that it's just displacing a night of prime.

**Operator**

And we'll take our next question from Barton Crockett with FBR Capital.

**Barton Evans Crockett** - *FBR Capital Markets & Co., Research Division - Analyst*

I wanted to ask a little bit more about the proposal from the FCC around top 4 station ownership. And you guys have highlighted, I think, that role at your May Investor Day as something that could contribute, I think, \$100 million to \$175 million of EBITDA.

Now that we see the proposal, which sounds maybe a little bit kind of half measure in that you have a case-by-case review as opposed to a complete elimination of the restriction on ownership, does that rule seem like something that could allow you to hit the target that you put out as a possibility in May? Or is it maybe a little bit less than you had hoped for?

**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

No. Thanks for the question, Barton. Actually, absolutely not. I think as I may have indicated in a call and I've talked to some people individually, the FCC had to write the rules very carefully, and the reason it took a while was they needed to write it in a way that was going to get through any kind of judicial review because there'll be likely lawsuits against it. The case-by-case language will give them the flexibility that makes it more penetrable on appeal.

In our situation, we think TEGNA will fare very well on any case-by-case review of our particular issues. And to go further on answer, Bart, I didn't talk about in the script, but obviously, when people talk about the DOJ piece, right, so I think the important part for us in the back of that number that I gave at Investor Day, we made that number based on the rules come out like they did and not assuming any relaxation of the DOJ guidelines. So conservatively, if you stay within the base, it's not a rule but sort of a tradition of a 40% market share, we still have enormous opportunities across our portfolio to execute 2 Big Four duopolies inside that 40% number.



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Now we have a new head of the antitrust division, who's in the Republican administration. And I think there's some optimism that that's a very antiquated rule, obviously, as well because it doesn't look at the broader marketplace, and there's some optimism that, that will be relaxed as well. But we're not banking on that. But the answer to your core question is no. It came out, frankly, as well as we could have hoped.

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**Barton Evans Crockett** - *FBR Capital Markets & Co., Research Division - Analyst*

Okay. That's helpful. And I wanted to switch gears a little bit, Dave. One other thing that you had been talking about over the past, in recent quarters I think, was the likelihood that you would receive some marketing push from YouTube TV, some advertising for their direct over-the-top service, and that ad revenue would be helpful to your ad trends and perhaps spark a competitive response from the traditional MVPDs and maybe some of the new skinny bundles to also advertise on your stations. Have you seen any of that? Has that kind of played out as you would've hoped, that category lift to the ad line?

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

Well, it's YouTube TV specifically. Their advertising has been national to date and I think it's because they rolled out nationally. They're the one company that has really gone full bore. A lot of the other services have not gone full bore and it's going to be a while before they get into smaller markets.

So local advertising is going to make more sense. So we haven't seen a lot of advertising from these new entrants yet, but I can tell you that, interestingly, in the quarter, to your question, our spending on media and telecom was up significantly. We don't know exactly the reasons, but it does make sense that the competitors may be starting -- the traditional MVPDs may be trying to lay down more markers.

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**Operator**

And we'll take our next question from Jim Goss with Barrington Research.

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**James Charles Goss** - *Barrington Research Associates, Inc., Research Division - MD*

Dave, you were talking about the relative indifferences to whether a subscriber is via MVPD or alternatively through OTT. I'm wondering if there are strategic implications as to how you will act in that regard. And to tie it into their retrans issue, we're looking at retrans versus reverse comp and the net trend. I'm wondering, to the extent that the networks, I think, are looking at programming fees that aren't tied to the number of subs, how does that tie into that OTT shift?

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

Let me take the first question. In terms of strategic, I would just say is sort of as I said in my script, I think it has implications for us as a distributor being a more powerful player in the live ecosystem. So if it was more to that question, let's come back to it. On the net retrans piece, you're absolutely right. The networks -- look, together, we expect to see more out of this ecosystem.

The move to OTT is actually from a broadcast asset perspective good for both of us because we now have far more competitors in the marketplace for our channels. And as I've said to many of you, it's clear that we have the most highly viewed channels, we and the networks together, and they are going to be a must-have for consumers on these services. So that puts us in a sweet spot relative to future negotiations on distribution. And having -- for us, it's not a national negotiation, right, because we're only in 30% of the country. So in the past, we may have been in negotiation with a cable operator that had 60% distribution of the market and maybe there wasn't even a telco competing against it, which gave us - them, a lot of leverage against us.



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So now we'll have more leverage in the negotiations. Where I'm going with that is the net pie is going to rise. And I've always said, right, let's focus on the size of the total pie before we talk about the split between us and our network partners. So the bottom line for us is despite whatever trends in the share of the split, et cetera, we will see net retrans continue to grow.

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**James Charles Goss** - *Barrington Research Associates, Inc., Research Division - MD*

Okay. And the only other thing related to the strategic implications were whether there's any incentive for you to even push the notion of greater OTT share of the mix and then...

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

No, I don't think. No, our MVPDs are good partners. And like I said, I'm calling out the benefits, but some of those benefits come more down the line as those OTT players get scale. But I think we'll let the system play itself out.

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**James Charles Goss** - *Barrington Research Associates, Inc., Research Division - MD*

Okay. And the other question I have are the profit calculations for Premion. I assume there are some start-up costs in creating it. But is there much of a net benefit at this stage? And how will that change as it grows in terms of fixed cost, variable cost or whatever else you'd have to say about it?

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

It will grow in margin as we get into next year. But right now, we've been running at almost zero margin intentionally, as I mentioned on the last call, to just go grab market share. This is a first-to-market opportunity for us. And then we don't intend for it ever to be a -- necessarily a 50% margin business, but I think as it grows, we will start to get into double digits quickly and then go up from there.

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**Operator**

And our next question comes from Kyle Evans with Stephens.

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**Kyle William Evans** - *Stephens Inc., Research Division - MD and Associate Director of Research*

You reported an adjusted OpEx reduction of 8% in the quarter. What were the main components of that reduction? And how lasting would you expect that to be?

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**Victoria Dux Harker** - *TEGNA Inc. - Executive VP and CFO*

In terms of the OpEx adjustment, we have the cost as we continue to talk about all year relative to our businesses on the terminated digital marketing side continue to decrease over time into next year. So each quarter, we've seen a decrease in those. I think the other piece we've also continued to see and you'll see into next year is we've got more efficiencies coming out of the consolidated business that's using more of a hub approach. So a lot of support functions continue to have lower cost, both at the corporate level as well as within the media operations themselves. So it's both pieces.

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**Kyle William Evans** - *Stephens Inc., Research Division - MD and Associate Director of Research*

Victoria, do you have a leverage target for year-end next year?



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**Victoria Dux Harker** - TEGNA Inc. - Executive VP and CFO

We really don't at this point, in part because there is, obviously, a number of different opportunities for us to use our free cash flow. So whether we'll end up using it to pay down further accelerated debt or just the amount that actually comes due during the year versus doing additional M&A or other investments, I think it's still TBD. Obviously, ending the year where we expect to be at a little bit less than 4, I think, is a very fine position to be in. So we're not aggressively driving for a reduction further to that. So we'll just let the year play out and see what the use of cash needs are.

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**Kyle William Evans** - Stephens Inc., Research Division - MD and Associate Director of Research

Okay. And I hate to be too laser focused on this, but kind of back to an earlier question on sub trends. If you x out the snowbird impact in your Sunbelt markets, what does your sub trend look like?

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**David T. Lougee** - TEGNA Inc. - CEO, President & Director

Yes, Kyle. This is Dave. I'll take that one. I think so we're just a little bit over 2% on the traditional MVPDs, down a little, just right around 2%, which is about where we had modeled it when we built our forecast for the year. But as I mentioned before, that actually continues to be disproportionately hit by the AT&T U-verse losses because we have a disproportionate footprint in that.

So they are 50% of our losses. About half of that is made back on subs that Direct picked up but you put the 2 together -- so Direct and AT&T together represents about 1/4 of that. So now -- and it does not include back in the OTT subs that are now only a handful. But we know they're out there, but we just don't have -- to the earlier question, we don't have our hands on them yet.

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**Kyle William Evans** - Stephens Inc., Research Division - MD and Associate Director of Research

So that down 2% is excluding what caused the sequential drop?

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**David T. Lougee** - TEGNA Inc. - CEO, President & Director

Yes, yes.

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**Operator**

And we'll take our next...

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**David T. Lougee** - TEGNA Inc. - CEO, President & Director

And excluding the increase in OTT subs that we're getting, but we just don't know how many. I'm sorry. Go ahead, Leanne.

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**Operator**

We'll take our next question from Alexia Quadrani with JPMorgan.

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**Alexia Skouras Quadrani** - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

Just if we can circle back to your earlier comments on the Olympic spending. Do you know, I guess, what was incremental in the last Winter Olympics? And I guess if you have any comments in terms of how you were thinking of what could be incremental coming ahead in 2018. And then I would just love -- you gave a lot of data, which is very helpful, on sort of trying to parse out what core underlying advertising is with the different pieces, which I appreciate.

But I would love to just hear your comments on what you think the sort of core -- how we should be thinking about core advertising, really just a very basic definition of core going forward, what the run rate might be sort of longer term, you think, from what you can see in this business when you think out to '18.

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

So the first question, back to '14, our Winter Olympics were about 50% incremental but we'll only know that after the fact, Alexia, because it really will depend on how the money comes in and what we call unwired money is or that isn't in the market. And there will be competition for those dollars from the Super Bowl too. So we'll have guidance after the fact on what that actually ends up being.

To core, again, we don't report on core and don't talk about on core. If you'll bear with me for a moment. Like I said before, because we are now taking our services to market agnostic to our products and so we're not pushing any product lines. So in some cases, we may actually be -- they may be proactively moving money out of core into other places just because that's what the advertiser wants relative to the suite of products we have.

But I would just talk about advertising trends overall. We've seen a sequential increased improvement quarter-to-quarter, and I think that we are -- our local growth is strong. The drag has been national and I think will continue to be and as we've always said that in the past. As we forecast moving forward in the growth strategy of the company, we are not modeling inherent market -- strong market growth in the way you define core, but we are modeling share increases through our initiatives as we know we will get them.

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**Alexia Skouras Quadrani** - *JP Morgan Chase & Co, Research Division - MD and Senior Analyst*

And then just I apologize if I missed this, but do you think you fully circled the U-verse transition head run that you were sort of struggling with the last few quarters?

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**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

No, no, we haven't. As long as there's any U-verse subscribers, we haven't circled them. And we've got quite a few left, to be honest with you. And again, they're not all total losses because they're moving either -- they're not -- those aren't people that are just becoming cord-nevers. They're either getting Direct service or another cable service or an OTT service. Again, there's going to be a lag in the timing on which we will see where they will go.

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**Operator**

And our next question comes from Michael Kupinski with NOBLE Capital Markets.

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**Michael A. Kupinski** - *NOBLE Capital Markets, Inc., Research Division - Director of Research*

I just have a couple of quick ones here. Since you are the largest NBC affiliate group, I was wondering if there are inherent benefits from being -- or having a large affiliate group like that. And the question is really related to, as you look at in-market consolidation, how do you plan to look to adding new markets? Particularly, do you plan to focus on a particular network or is there -- as you kind of grow out your network affiliations?

**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

I'll take the first one first. We have an incredibly great relationship with NBC and have for a long time. Gannett did before it bought Belo and Belo did as well. And we have some of their strongest stations but we also have, at many levels of the organization, a tremendous amount of good relationships and have great strategic conversations with them. So it is -- yes, there's a lot of value to having a large position in one of the networks and that particular relationship is very, very strong.

When we go out to do the in-market consolidation, yes, we will look -- affiliations will just be one of the many lenses we'll look at, Michael, but it's also going to be accretive, what the opportunity is. Some stations won't be actionable because their market share may be too high depending on the DOJ rules, et cetera. So we -- but more likely than not, just given our portfolio, when we do those -- as that plays itself out, we'll likely have an NBC station in many to most of those markets as it plays itself out.

**Michael A. Kupinski** - *NOBLE Capital Markets, Inc., Research Division - Director of Research*

But synergies outweigh the network affiliations, so to speak, it sounds like. So you're...

**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

You'll get the synergies regardless of the network affiliation, so I'll just put it that way. And so yes, the synergies will be the #1 criteria, obviously, for it. And then there'll be a subsection of other lenses we'll look at.

All right, we appreciate your time on the call today. As always, please follow up with Jeff Heinz at -- Jeff, your number is?

**Jeffrey Heinz** - *TEGNA Inc. - VP of IR*

873-6917.

**David T. Lougee** - *TEGNA Inc. - CEO, President & Director*

(703) 873-6917 for any follow-up questions. Again, thank you for your time this morning, everyone.

**Operator**

And that does conclude today's conference. Thank you for your participation. You may now disconnect.



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