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CNK - Q2 2018 Cinemark Holdings Inc Earnings Call

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PRESENTATION

Operator

Good morning. My name is Natalia, and I will be your conference operator today. At this time, I would like to welcome everyone to the Cinemark's Second Quarter Earnings Call. (Operator Instructions) I would now turn the call over to Chanda Brashears, VP of Investor Relations. You may begin.

Chanda E. Brashears - *Cinemark Holdings, Inc. - VP of IR & Corporate Communications*

Thank you, Natalia, and good morning, everyone. At this time, I would like to welcome you to Cinemark Holdings, Inc. Second Quarter 2018 Earnings Release Conference Call, hosted by Mark Zoradi, Chief Executive Officer; and Sean Gamble, Chief Financial Officer and Chief Operating Officer.

I would like to remind our listeners that certain matters that are discussed by members of management during this conference call may constitute forward-looking statements within the meaning of the safe harbor provisions of the United States Private Securities Litigation Reform Act of 1995. Forward-looking statements are subject to risks and uncertainties that may cause Cinemark's actual results to differ materially from the expectations indicated or implied by such statements. Such risk factors are set forth and expressly qualified in their entirety in the company's filings with the SEC, including the most recently filed annual report on Form 10-K. The company undertakes no obligation to publicly update or revise any forward-looking statements.

Today's call and webcast may include certain non-GAAP financial measures. A reconciliation of these non-GAAP measures to the most directly comparable financial measures calculated and presented in accordance with GAAP can be found in today's press release, within the company's most recently filed quarterly report on Form 10-Q and on the company's website, investors.cinemark.com.

I would now like to turn the call over to Mark Zoradi.

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Thank you, Chanda, and good morning, everyone. We appreciate you joining us to discuss our 2018 second quarter results. Let me begin by saying what a stellar quarter it was for the North America industry, exceeding even the most optimistic expectations. Second quarter industry box office



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established a new all-time quarterly high of \$3.3 billion that was propelled by attendance growth in the high teens. Furthermore, with \$6.2 billion of box office generated year-to-date, the first half of the year also broke records exceeding 2016's previous all-time high by a significant 10%.

I'm incredibly pleased to report that alongside North America's outstanding 2Q industry results, Cinemark achieved several all-time quarterly highs as well, across the range of our key global metrics, including admissions revenue, concessions revenue, total revenue and adjusted EBITDA. Furthermore, we set numerous second quarter records, including net income, earnings per share and adjusted EBITDA margin, which was just shy of 25%.

It's worth noting that these global records were achieved despite a more challenging second quarter industry environment in Latin America that put pressure on our international results. Much like the U.S., the top 5 titles in the quarter delivered outstanding growth across the region, including attendance figures that were up 20% compared to the top 5 films of last year. That said, overall industry box office in constant currency declined slightly as a result of shortage of family titles, adverse impact from the World Cup, a truckers' strike that shut down transportation in Brazil and had significant impact on commerce for several weeks, and a tougher year-over-year comp relative to the U.S.

Yet despite these pressures during 2Q, our global team still managed to deliver another quarter of record performance by capitalizing on the strength of the North American film content, effectively navigating a series of challenges in Latin America, and continuing to further advance our strategic initiatives. And for that, I'd like to commend our entire Cinemark team.

Let me now provide you with an update on several of those strategic initiatives that continue to enhance our guest experience and bolster our results, starting with Luxury Loungers. As of the end of the second quarter, we crossed the 50% mark with over 2,300 auditoriums featuring Luxury Lounger recliner seats. Consumers continue to express their strong preference for the reclined seat experience. Financial returns also remain lucrative, exceeding our 20% threshold, driven by significant attendance growth, favorable pricing power, and incremental food and beverage consumption. We remain opportunistic and prudent in our ongoing Luxury Lounger conversions, and expect to end the year with approximately 55% of our domestic circuit reclined. We also continue to realize robust concession growth, as we test and roll out a wider variety of offerings. We're providing our consumers greater choices that appeal to the very taste of our audiences.

Our consistent and dedicated focus on our food and beverage initiative helped us reach a global milestone this quarter of a \$4 per cap for the first time. Furthermore, we extended our streak to 46 consecutive quarters of domestic food and beverage per cap growth. I'd like to congratulate our food and beverage and field operations team on these outstanding achievements. While providing solid financial benefits, our food and beverage initiatives also helped us supplement and enhance the collective Cinemark guest experience, as do our 248 XD premium large-format screens. Our XD auditoriums provide a best-in-class premium movie-watching environment with their heightened sight and sound presentation that immerse patrons in the on-screen action.

We continue to work on further advancing the XD experience, which now has been 100% THX certified and features Luxury Loungers in approximately 70% of our domestic XD auditoriums.

As discussed on some previous earning calls, we enacted a strategic XD brand marketing campaign about a year ago to amplify the consumer awareness around all that XD has to offer. Most recently, we rolled out a series of new trailer on-screen at across social media that emphasize various attributes of the superior quality of XD sight, sound and screen brilliance. All of these initiatives, coupled with the phenomenal film slate, drove our XD percentage of worldwide box office to a historic high of 9.7% in the second quarter, which is a 70 basis point expansion over the previous record and was achieved on only 4% of our worldwide screens. 2 groups of Cinemark moviegoers that are particular fans of our XD experience are our loyalty and subscription members, who upgrade to XD twice as often as nonmembers. With that, let's shift our attention to our Movie Club subscription program.

We are thrilled to report that more than 350,000 active members in Movie Club. The first exhibitor-sponsored subscription program. For perspective, that translates to more than 1,000 members per Cinemark theater. We've maintained our sign-up cadence and doubled our Movie Club membership from the first to the second quarter. Our subscription program differentiates itself from other offering, as it targets the moderate to frequent moviegoer. Economically, the features of our program provide the best value for those individuals attending movies up to twice a month, which encompasses the majority of moviegoers across the country. Our value proposition includes the features for which our target audience express



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the most interest in, particularly ticket rollover, which allows consumers that do not use their movie credit in a particular month, the ability to roll over their ticket credit and accumulate them. These rollover credits never expire as long as the consumer is a member of Movie Club. To be clear, our offering is not a use it or lose it model. Consumer reaction has been very enthusiastic regarding this unique benefit.

In addition, Movie Club members pay no online fees. They can add companion passes at member pricing. And very importantly, they receive a 20% discount on concession during every visit. 8 months in, we're thrilled with our results, already between 5% to 6% of our box office is derived from Movie Club members, and 75% of all ticket credits have been redeemed, demonstrating that our members are highly engaged. Furthermore, as we survey our members, more than half our reporting that they are purchasing concessions more often than before and intend to see 4 to 6 additional movies per year compared to their prior behavior as a result of this program.

Also noteworthy, our percentage of membership base that was not previously part of our loyalty program has grown to 45%. The incremental data we're gathering on moviegoing habits and preferences is advantageous in our quest to personalize our marketing messages and drive more frequent moviegoing and loyalty to Cinemark. In that vein, we now have 8.5 million members in our worldwide loyalty programs to segment, analyze and identify trends and preferences for targeted marketing campaigns.

We remain laser focused on capitalizing on the opportunities associated with subscription and loyalty, and remain enthusiastic on our unique and financially viable Movie Club offering.

Another significant and long-term opportunity for Cinemark is our International business. We have operated in Latin America for more than 25 years through various economic cycles, high and low. Based on our tenure and experience in the region, we've seen that box office results are more closely tied to film content than economic cycles. While the timing of films released and the consumer appeal of Hollywood content ebbs and flows in our Latin markets, the long-term prospect for international box office remains robust. This is demonstrated by the record-shattering performance of Avengers in the region in addition to Incredibles 2, which is in contention to become the highest grossing animated film of all time.

Additionally, the long-term screen growth prospects remains strong, particularly considering that Brazil has approximately twice the population of Mexico, yet half the number of movie screens. That said, our screen growth is contingent upon mall development, which has been delayed during the economic challenges in a few of our key territories. With our diverse footprint in 15 countries throughout South and Central America, we continue to deliver screen growth and remain on track to deliver 50 to 75 incremental screens during 2018, representing approximately 5% annual screen growth.

And we consistently seek accretive acquisition opportunities that exceed our balanced and disciplined investment threshold of a 20% ROI and a 20% margin as evidenced by our tuck-in acquisition during the quarter of 3 theaters and 19 screens in Brazil. We remain diligent in the endeavor and optimistic on the long-term growth potential of Latin America.

Before turning the call over to Sean, I'd like to briefly address our financially accretive transaction with CineWorld to purchase the remaining shares of National CineMedia, which were held by AMC. As a reminder, AMC was required to sell its interest in NCM under the consent decree with the DOJ in connection with their acquisition of Carmike. Cinemark's half of the transaction equaled 10.7 million shares at a purchase price of \$7.30 per share, totaling \$78.4 million investment. Following the transaction, Cinemark now owns 28 million shares, representing a 25% ownership of NCM LLC. Screen advertising is a meaningful aspect of our core business model, and we have an ongoing confidence in the long-term opportunity associated with NCM. We believe that strategic ownership by founding members is incredibly valuable. And this transaction allows the founding members the opportunity for greater input on strategies and business plans, further securing our alignment and collaborative efforts. We look forward to working more closely with NCM and CineWorld to further enhance the domestic on-screen advertising potential.

In closing, on the heels of a record breaking first half of the year, we continue to encourage a long-term perspective when analyzing box office results. While the second half of the year may not appear quite as robust as the first half, the potential remains for the full year 2018 box office to set another record. And our enthusiasm for the 2019 film slate continues to grow on the large franchise titles and high-profile sequels across a variety of genres, ranging from family, entertainment, live action, adventure and superhero temples. Our studio and distribution partners have staked their ground with their most commercial movies nearly every key weekend in 2019, solidifying an outstanding line of a content that appeals



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to all audiences. Cinemark remains well positioned to capitalize on the upcoming strength of the content with our focus and execution of our in-theater and marketing initiatives.

That concludes my prepared remarks. I'll now turn the call over to Sean to address a more detailed discussion of our financial performance. Sean?

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

Thank you, Mark, and good morning, everyone. Before delving into the details of our second quarter's financial results, I'd like to remind you that beginning January 1, 2018, we adopted accounting pronouncement ASC 606, which affects how we recognize revenue for certain items.

Associated with this pronouncement, other revenues increased due to the inclusion of a significant financing component related to our NCM deferred revenue as well as a change in the amortization method used for such deferred revenue. In addition, transaction fees are now recorded on a gross versus net basis.

Finally, admissions and concessions revenues have been slightly impacted by deferring a portion of those revenues associated with the issuance of points to our connections loyalty members. Additional information about these changes can be found in the footnotes of our 10-Q. And as mentioned on prior calls, we do not believe the adoption of this new pronouncement materially affects our overall financials.

Shifting now to those financials. As Mark previously stated, our global company generated record-breaking results in the second quarter with total revenues of \$889 million, adjusted EBITDA of \$221.6 million and an adjusted EBITDA margin of 24.9%. In the U.S., total domestic admission revenues were \$408.9 million, which grew 22.1% versus prior year on an as-reported basis and were up 22.6%, excluding the impact of the new revenue recognition accounting adjustments.

This growth was driven predominantly by attendance gains in the quarter, which again outpaced the North American industry and grew 17.7% to our highest quarterly attendance on record with 50.6 million patrons served. Our average ticket price also increased 3.7% to \$8.08, largely as a result of inflation, incremental pricing opportunities associated with recliner conversions, and favorable adult versus child ticket type mix. Our varied food and beverage initiatives generated a U.S. concessions for patron increase of 7.4% to an all-time high of \$4.93. This per cap increase combined with this quarter's strong attendance drove total concession revenues up 26.5% to \$249.6 million. Domestic other revenues increased 167.2%, driven primarily by the revenue recognition accounting changes that I previously described. Additionally, this line item benefited from attendance-related growth in screen ad revenues, transaction fees and promotional income during the quarter.

Overall, our U.S. operations delivered all-time highs, in total revenues of \$709 million and adjusted EBITDA of \$188.4 million. Our adjusted EBITDA margin also set a second quarter record of 26.6%. Internationally, attendance declined 2.3% in 2Q to 25.8 million patrons. This decline was largely due to weaker volume in consumer appeal of family content that was down 50% compared to last year as well as the one-off impacts of the World Cup and the Brazilian truckers' strike that Mark previously mentioned.

Furthermore, while industry attendance meaningfully benefited from the sizable local title, *Nada a Perder*, that generated over 20% of second quarter tickets sold in Brazil. Because this title carried a lower-than-normal ticket price and yielded minimal concession sales, it had a significant distorting effect on many of our financial metrics. Second quarter international admissions revenues were \$100 million, which declined 13% versus last year as reported and were down 2.8% in constant currency.

Our average -- our reported average ticket price of \$3.88 translated to a constant currency decline of 0.5%, that was driven by the aforementioned impact of *Nada a Perder*. Excluding the effect of this title, our constant currency ATP would have grown by 5.5%. Similarly, our as reported international concessions per patron of \$2.16 declined by 3.3% in constant currency. However, it would've been up approximately 7% on a normalized basis. The limited consumption of food and beverage associated with *Nada a Perder* along with this quarter's overall attendance decline, led to total concessions revenues of \$55.7 million, that were down 14.3% as reported and down 5.4% in constant currency.

International other revenues were \$24.3 million, which increased 20.9% as reported and 37.8% in constant currency. This increase was predominantly driven by the previously described revenue recognition accounting changes. Overall, total international revenues were \$180 million as reported



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with an adjusted EBITDA of \$33.2 million and an adjusted EBITDA margin of 18.4%. During the second quarter, the strength of the U.S. dollar intensified and caused an approximate 10% foreign currency translation drag on our reported international results. And to the extent exchange rates continue to hold at current levels, we would expect a sustained percentage headwind in the low teens throughout the remainder of 2018.

As a reminder, the vast majority of our international operating expenses are transacted in local currency, including film rental and facility lease expenses. So the impact of currency exchange is predominately translation based and not transaction oriented.

Shifting back to our worldwide consolidated results. Second quarter film rental and advertising costs as a percentage of admissions revenues increased by 160 basis points year-over-year to 56.4%. This increase was driven by a higher concentration of larger films as a percentage of total box office. Concession cost as a percentage of total concessions revenues were up 80 basis points in comparison to the prior year, as a result of expanding food and beverage product mix across our global circuit. And while this increased variety of offerings may create a slight drag on our concessions margin rate, it continues to drive sizable growth in overall concessions revenues and income. Salaries and wages were 11.3% of total revenues, and declined 70 basis points compared to the second quarter of 2017. This decline was driven by improved leverage over our base level of fixed labor that resulted from this quarter's increase in attendance and that more than offset growth in wage rates, benefit costs, and staffing and new and recently remodeled theaters.

Facility lease expenses as a percentage of total revenues were 9.1% and declined by 190 basis points. Conversely, utilities and other costs as a percentage of total revenues increased by 90 basis points, driven by the impact of recording transaction fees on a gross versus net basis, associated with the new revenue recognition accounting standards.

And G&A for the quarter declined by 20 basis points as a percentage of total revenues. This decline also resulted from improved leverage of our fixed cost, even though total G&A spend was up year-over-year due to inflation, benefits costs, and additional headcount and professional fee investments to support our varied strategic growth and productivity initiatives.

Collectively, second quarter pretax income was \$100.8 million. Our second quarter's effective tax rate was 18.2% and net income attributable to Cinemark Holdings, Inc. was \$82.1 million, or \$0.70 per diluted share. With respect to our balance sheet, we ended the quarter with a cash balance of \$504.7 million and a net debt position of \$1.5 billion.

Shifting attention to our U.S. footprint. We operated 339 theaters and 4,566 screens in 41 states and 102 DMAs at quarter-end.

We've signed commitments to open 3 theaters and 30 screens during the remainder of 2018, and 9 theaters representing 95 screens subsequent to 2018. We expect to spend approximately \$99 million in CapEx for these 125 screens. We also anticipate closing 1 or 2 theaters before year-end.

Internationally, we operated 200 theaters and 1,432 screens in 15 countries across Latin America. As of quarter-end, we'd signed commitments to open 5 new theaters and 29 screens during the remainder of 2018, and 7 theaters representing 51 screens subsequent to 2018. We anticipate spending approximately \$46 million in CapEx for these 80 screens.

Regarding overall CapEx, we spent \$82.4 million in the second quarter, including \$13.6 million on new builds and \$68.8 million on existing theaters that were predominantly associated with recliner conversions. We continue to anticipate spending approximately \$350 million of CapEx during full year 2018, of which \$120 million is designated for new builds both domestically and internationally, \$80 million is for core maintenance of existing screens and in line with our historical run rate, approximately \$10 million is associated with completing the renovation of our headquarters building and the residual \$140 million is for cash flow generating projects that include additional Luxury Lounger theater conversions and varied food and beverage initiatives.

We continue to expect that our annual depreciation and amortization will increase to approximately \$260 million to \$270 million in 2018, as a result of these capital expenditures.

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I'd like to close by highlighting, again, that it was a tremendous quarter for the North American industry and for Cinemark. We're extremely pleased with the continued progress of our strategic initiatives, the sustained consistency of our financial and operating results, and the enduring strength of our balance sheet. And as Mark commented, we remain enthusiastic about long-term prospects for film content and our company.

Natalia, that concludes our prepared remarks. And we would now like to open up the lines for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question is from the line of Eric Handler with MKM Partners.

Eric Owen Handler - *MKM Partners LLC, Research Division - MD, Sector Head & Senior Analyst*

Couple of questions for you. First, I'm curious, where you think a critical mass is for your movie pass subscribers or where you could get in the next 1 to 2 years? And then secondly, as you make all these strategic investments, just curious what you're doing to sort of manage the cost so that they don't get out of control and where you can find areas to cut expenses?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Thank you, Eric. We appreciate your support and questions. I'm going to take the first question regarding Movie Club, and Sean maybe you take the second one on the cost side. Let me just say this, Eric, Movie Club, as you know, we launched on December 5, 2017. And I'll tell you, our going in first year projections, we have blown by those. And so we've had to raise our expectations because there's been such a positive response of the consumer and to be sitting at 350,000 active members today, we're incredibly pleased. That's -- as I noted, that's representing between 5% and 6% of our box office. We think the growth will continue throughout this year. And I think, it's certainly within reason to be looking for 0.5 million subscribers somewhere at the end of this year or into early part of next year. Where it goes from there, we're just going to have to see. Obviously, there's new competitors in the marketplace with competing programs. But the uniqueness of our program, especially the rollover component where consumers cannot go for a month and still have the benefit roll up and accumulate for them, has been particularly attractive as well as the 20% discount on concessions for each and every visit.

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

And on the cost side, I would say, we're very careful with the amount of spend we're deploying to these initiatives. We basically put them through the same type of analytical rigor that we would, our other CapEx related investments. Some of them, which is what we're kind of seeing, is putting a little bit pressure on our near-term G&A. Some of them require a little bit of upfront G&A investment in professional fees and consulting, and even headcount to a degree. Some will be revenue generating, but many of them will be also be focused on driving improved efficiencies and productivity both in our head office as well as in the field.

So the hope is that, in time, what we'll see is overall costs coming down as a result of some of this upfront investment. But the short answer is, all of them are being put through a very close analysis and rigor around how much we're spending in the associated returns we expect to derive from them.



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Eric Owen Handler - MKM Partners LLC, Research Division - MD, Sector Head & Senior Analyst

Great. And just one other quick question. When you look at the Latin American slate for the back half of this year, how do you think it compares to what we might see in North America in terms of, does the content play well there or are there any puts and takes that we might expect to cause it to be materially different?

Mark Zoradi - Cinemark Holdings, Inc. - CEO & Director

Sure. I'll take that one, Eric. I'd say, we're perhaps a little more measured in our expectations for Latin American box office in the second half of the year. Well, there are several films that we expect will do well in the region, like The Nun, we're seeing it with Hotel Transylvania and Incredibles 2, and even Fantastic Beasts to a degree. There is also several Hollywood films that we don't expect will convert too well, such as Crazy Rich Asians, Christopher Robin, Night School and The Grinch. Additionally, there are some tougher comps in the second half of last year, including a stronger volume of third quarter animated content, which is tough for the region. So while we're hopeful that we'll see a breakout film and some of these other titles will connect, maybe there will be a local film that will kind of surprise us, which is always possible in the region. Again, we're little bit more measured in our expectations for the second half. That said, when we look beyond 2018, we're very enthusiastic about what we see for the 2019 slate, not just how it'll do in the U.S. but the lineup of titles, especially with the family appeal and the type of content that it is. We think it'll translate really well to Latin audiences.

Operator

The next question is from the line of Robert Fishman with MoffettNathanson.

Robert S. Fishman - MoffettNathanson LLC - Analyst

I have one for Mark and one for Sean. Mark, now that some of the Hollywood M&A dust is starting to settle and even Bob Iger reaffirmed the importance of the theatrical window to Disney last night. Can you share any updated thoughts on how Disney owning Fox and AT&T owning Warner Bros. will either positively or negatively impact Cinemark's relationship with each studio, including the potential for a fewer number of releases?

Mark Zoradi - Cinemark Holdings, Inc. - CEO & Director

Well, let's start with the Fox and Disney combination. We actually see that there is some potential upside here. We're very pleased that Bob continues, and this wasn't the first time, this is just consistent with what he's done on multiple occasions, be very supportive of the theatrical window. And Fox is bringing some great assets to Disney, whether it's the Avatar series, X-Men, Deadpool, what they're bringing with Fox Searchlight, which is very incremental to Disney. So we think what Fox is bringing from an intellectual property standpoint, Disney will value very much and will be incremental to the Disney lineup. What Disney is bringing is probably the strongest ability to leverage synergistic marketing opportunities of any company in the entertainment business because of their strength in theme parks and consumer products, sports networks, ABC. So we think, the Disney marketing machine, given that Fox we think did a great job, we just think Disney has some potentially additional assets that can even -- either -- even further enhance that. So we're pretty positive about that. Regarding Warner Bros and AT&T. Again, AT&T has been very supportive both publicly and privately with what they think about the Warner Bros, and they're excited about having content. And we think that Warner Bros being within the AT&T family gives them the ability to have a significant additional access to data to again help them in their whole marketing and promotion area on the movies they have. So we think there also that is positive for our business.



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Robert S. Fishman - *MoffettNathanson LLC - Analyst*

Okay. And for Sean, now that you've upgraded more than half of our U.S. screens, just wondering if you can share any additional detail on how much recliners are contributing to U.S. revenues or profits? And if you've seen any slowdown from the earliest upgraded theaters or if the most recent recliner screens returns are below the initial level? Just any further color there would be helpful?

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

Sure. I would say, the more recent recliners that we're doing, they continue to drive healthy returns in excess of our 20% EBITDA threshold and ROI thresholds. The overall returns have certainly come down a bit from the early recliners, which were somewhat of the low-hanging fruit, and some of them just had kind of explosive results. So we've kind of mentioned in the past, we go at this on a case-by-case basis. So we're consistently looking at the changing dynamics in the marketplace and looking at what makes sense in making sure that we have a clear path to delivering those returns that will meet our hurdle rates. So just bringing that home, again, while the returns have come down a bit from their early levels. They're still in excess of our targets and we're still very pleased with what we're seeing in terms of consumer response and just overall attendance list and returns on those new recliners.

Operator

Your next question is from the line of Michael Ng with Goldman Sachs.

Michael Ng - *Goldman Sachs Group Inc., Research Division - Research Analyst*

I just have one on concessions and one on the U.S. box office. First, on the concessions. U.S. F&B

for patrons was really good, up 7.5% in the quarter. I'd just like to better understand whether there was something with film mix that may have helped F&B growth during the quarter or if there are any new initiatives or programs that Cinemark had just started to roll out this quarter, which we might be able to expect to help F&B growth in future periods?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Michael, relative to F&B, let me just do a little bit of a call out. We just have an outstanding team. And I think, it's a combination of a lot of things. Probably first and foremost is, they continue to innovate with new products and new layouts within the theater, probably the most significant new product that we've rolled out during the first half of the year has been our partnership with Pizza Hut, where we're in the process of installing by the time next year rolls around, 110 Pizza Hut installations throughout the country, and each one of those has been highly accretive because they're fresh Pizza, it's branded, they're cooked just the way they would in a Pizza Hut store. So there's been great response to that. In addition, we've got merchandising rolling out throughout all of our theaters, and we're looking very much at unique and individual offerings in various parts of the country beyond what is standard in every theater we're also looking for unique food and beverage offerings, which are -- which can further enhance that per cap. But the per cap just continues to be driven. And I would say, it's not one particular thing, maybe if there's one thing to call out, it was the Pizza Hut.

Michael Ng - *Goldman Sachs Group Inc., Research Division - Research Analyst*

Okay, great. And maybe just as a follow-up to that question for Sean. In the cash flow statement, there was a \$20 million investment and I think a joint venture. Was that Pizza Hut related or was that something else?



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Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Let me take that really good. That was not Pizza Hut related. That is the -- I think, you're referring to the \$20 million joint venture that we're doing to open an entertainment center attached to a theater here in Dallas. This is an R&D effort. We're extremely excited about it. It's in connection with the group that already does family entertainment, and that includes everything from bowling to laser tag, to video games, to climbing walls. They're highly successful here in Texas. And we're going to do a joint venture with them and test combining that with a movie theater in Dallas and see how that works.

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

And just to confirm, Michael, if you're talking about the \$20 million in the investment in joint ventures and other line, that's exactly what Mark was describing.

Michael Ng - *Goldman Sachs Group Inc., Research Division - Research Analyst*

Yes, that's exactly what I was referring to. And then on the box office, you mentioned that there was a potential for 2018 to set another record. I think that would imply about 3% box office growth year-on-year. Appreciating that the second half is tough, and you did say could, not would. Where do you see the areas of upside -- of potential upside, rather, whether that's from film basis or a month or a quarter basis?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

As I mentioned, we are very optimistic about the second half of the year. But we're also a little measured. We try and set expectation at a reasonable level. The first half was so significant. And now we're looking at Q3 and 4, and we think that potentially they're going to be slightly down or equal with last year. But when you do that and you add this all up, we're going to be north of \$11 billion and likely north of what 2017 was. And we see, obviously, in this quarter, the biggest picture was fall out. But we're also looking into the fourth quarter with things like *Venom* and *Bohemian Rhapsody* and, of course, *Dr. Seuss*, *Fantastic Beasts*, *Wreck-It Ralph*, a sequel from Disney, *Aquaman* from Warner Bros. So we're positive about what the third and fourth quarter can bring. And when we look at the full year, we think that on the strength of the first half and a good solid third and fourth quarter, it will all add up to be slightly above what we saw last year.

Operator

Your next question is from the line of David Miller with Imperial Capital.

David Walter Miller - *Imperial Capital, LLC, Research Division - Research Analyst*

I have one for Mark, one for Sean. Mark, on *Movie Club*, congratulations on the early success. What did you learn with regard to how often folks are accumulating credits and then using those credits on a delayed basis? In other words, are folks like waiting 3 months and then using the 3 tickets after 3 months or are they waiting 6 months or 2 months. Any kind of data you're willing to share there, I would appreciate that? And then Sean, on the income statement, it looks like you took a \$16.9 million loss on disposal, that's unusually high. It looks like that costs you about \$0.10 a share. Just wondering what was in that? Appreciate the feedback.

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

David, regarding *Movie Club*. Yes, we are incredibly happy about the 350,000 subscribers. And one thing that I pointed out too, that I think it's an important metric for us, is that relates to an average of over 1,000 members per Cinemark location, because we have 339 theaters. So we're seeing it across the board. It's not just concentrated in our large cities as well. Regards to utilization, I think the best metric for that is, of all the credits that are earned and every subscriber earns 1 credit per month, we've utilized 75% of those, which means that people are using the program. So if there



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is a movie, if they're not interested in going in a particular month, many times the next month they'll go twice. So that 75% utilization is a key statistic for us, it's telling us that people are really using them. In addition, we find that people are also purchasing additional credits during the month. In other words, they get 1 credit for their \$8.99. But if they want to come a second time during the month, they can do that at the \$8.99 price. And one of the other benefits is they can bring a companion with them for \$8.99. So all of these unique benefits are some of the reasons why I think we've seen the tremendous success of Movie Club.

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

And just to answer your question on the gains and losses line item. One of the big drivers of that line item is we continue to have a series of fixed asset retirements associated with our recliner remodel. So a big part of that is just kind of the timing and magnitude of those retirements based on the particular theaters that we're working on. There was also an accrual that was booked for a reserve associated with an outstanding litigation in that line item this quarter. But when you look year-over-year, I say the big driver of the variance with last year being almost flat -- almost zero. Last year, we had a fairly sizable onetime landlord buyout of a theater lease, which gave us credit in that line item and brought that to 0. If you were to take that out, it would be much more in line with what we're seeing this year.

David Walter Miller - *Imperial Capital, LLC, Research Division - Research Analyst*

Sean, if I could just follow up on Movie Club. Are you seeing the volume of concessions move higher as per the discount -- the 20% discount? And is that allowing you yet to kind of lower your overall cost of goods sold on concessions yet or you're not there yet with the 350,000?

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

We're seeing improvements in the consumption levels. And as Mark mentioned in his script, our consumers are even reporting that. Half of them are increasing their consumption versus their behavior before. In terms of the overall ability to take that volume and negotiate improvements in our cost of goods sold, I'd say it's still early for that. That's something that we'll just continue to work on it on a day-to-day basis with our vendors of how can we get better pricing on the actual cost of goods. But it's certainly something we're going to continue to look to as we have more data and continue to increase subscribership and have the ability to use that volume to improve our negotiating ability.

Operator

Your next question is from the line of Chad Beynon with Macquarie.

Chad C. Beynon - *Macquarie Research - Head of US Consumer, SVP and Senior Analyst*

First, just wanted to start with regards to your increased investment in the National CineMedia advertising business. Does this investment give you more access or maybe further knowledge into that business? And then, on a related note, could this help you further monetize or run your Flix Media business down in Latin America, which I believe is now over 2,500 screens?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Yes. Thank you, Chad. Relative to NCM, let me answer this second question first. We have a very good Flix Media business. We're the largest seller of advertising throughout Central and South America. So it's very established, it's well run. There's norms for doing things there. Clearly, we will look to share best practices, both North and South with each other. But that business is already running very well. I don't think, necessarily, we're going to see any great improvement because of the NCM. But if we find one thing that's working particularly well in the South, we'll certainly bring it up North and vice versa. And your first question, remind me, again, if you would, please?



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Chad C. Beynon - *Macquarie Research - Head of US Consumer, SVP and Senior Analyst*

With respect to your increased ownership, does this give you any ability to kind of see behind the curtain on that business or just understand the overall business more?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Yes. Well, I would say, slightly. Not materially more only and that we obviously had ownership. We were one of the 3 founding members to begin with. But I think the fact of CineWorld and Cinemark purchasing the remaining AMC shares and each of us now owning approximately 25% of the LLC, gives us maybe a little bit bigger seat at the table and we have a big investment in the company, as does CineWorld. So we're highly motivated to help and support them. We believe in the business tremendously. I mean, that's the first and foremost reason why we did it. We think it's core and a meaningful aspect to our business. And the fact that we can have some greater amount of input and influence on NCM, we think all those things are very positive as well as the idea sharing that you mentioned.

Chad C. Beynon - *Macquarie Research - Head of US Consumer, SVP and Senior Analyst*

Okay, Mark. And then my follow-up is just with respect to average ticket price and any surge or variable pricing. I know, you and your competitors are doing more of this in given how top heavy the quarter was. Could you just elaborate a little bit on if this was a strategy in the quarter? And if this could potentially help back half pricing, as you kind of figure out surge and variable pricing in a better measure?

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

Sure. I'd say, overall pricing strategy is something that we continue to actively work on. We've had a range of different pricing. So I wouldn't quite call it dynamic per se, but we've had highly varied pricing throughout the day, throughout the week, throughout the year to try to tailor that to wide range of access for all consumers as well as to properly meet demand. So we haven't implemented surge pricing per se for any unique titles, but we do have titles at different pricing at peak periods and things of that sort. So I would say, it's something that we're continuing to look at and experiment with. We do a lot of work in analyzing our elasticities on a theater by theater in day-part basis. Furthermore, as we've continued to roll out recliners, our general tactic has been to go forward with limited pricing upfront. And then when we see the demand opportunity, increase there, and I'd say there's still -- we still believe there is further opportunity as we look to the back half of this year and forward in that regard. So short answer, it's -- we think there is still a lot of opportunity with sophistication of data to increase that as well as with our recliner opportunities and something we're going to continue to test, and we believe there will be opportunity to benefit from the future.

Operator

(Operator Instructions) Your next question is from the line of Jim Goss with Barrington Research.

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

I was wondering about the M&A environment and any appetite you might have to consider any purchases traditionally as Cinemark has been very selective in making acquisitions. And if you were to be able to get properties, would you prefer to buy at a discount and renovate in your own fashion or buy something ready-to-go?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Jim, I'll take that. In regards to M&A, I would say our strategy is consistent and we're staying in the course. It's proved to be very, very successful for us. We are picky buyers. And I think that's proved to be a good strategy. We're looking to buy things that will be accretive from day 1. It doesn't



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really matter whether or not the cinema needs additional work and needs ability to be fixed up. It's just a matter of what are we going to buy it for. If we're going to put in a lot of capital, we're going -- want to buy it for less. If it's already reclined and has enhanced food, then we'll put that into the calculation of what we pay for it because we don't have the CapEx associated with it. We're going to continue to look at deals around the world, but we're especially aggressive at looking at markets in which we're already operating. We like the idea of gaining additional market share in our 15 Latin American countries and in the United States. But as you pointed out, we are picky buyers. I mean, as I noted in my comments, we completed a deal in Brazil this quarter, 3 theaters and 19 screens, and we're very happy with that price. And we think that it will -- like I said, will be accretive from the get-go.

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

Okay. And one other thing that sort of relates to NCM. There used to be something called Fathom that I think still does exist. I believe, I still see it in your own theaters and alternative content, in general, hasn't come up a lot lately. Is this sort of a just site issue these days or is there some active involvement in that as an additive process?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Fathom is jointly owned by AMC, Regal -- AMC, CineWorld and Cinemark, and it's still very much active and we're very supportive of Fathom. They provide alternative content to us. And that's everything from the most successful Met opera series they have to classic movies, to stage plays, to sporting events, to eSports. So we're very supportive of Fathom. It's not a significant driver of our income, but it's one that we're still very interested in. We have representation on the board and want to support them in any way possible to continue to provide alternative content, and additional and new avenues for alternative content into the future.

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

Okay. But the relative impact has remained very, very small?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

The impact has been relatively consistent. That's correct.

Operator

Your final question is from the line of Eric Wold with B. Riley.

Eric Christian Wold - *B. Riley FBR, Inc., Research Division - Senior Equity Analyst*

Just a couple of questions, most are kind of follow ons to ones have been asked so far. I guess, one on Latin America. Do the kind of headwinds you're seeing around mall construction, which I know has been an issue for a little bit of time. Does that kind of push the need for Cinemark to look more towards the acquisitions to kind of stay within that 50 to 75 screen range? If that going to be the range kind of at least for the near term? And if so, are there enough targets down there like the one in Brazil to -- (inaudible) evaluations?

Sean Gamble - *Cinemark Holdings, Inc. - CFO & COO*

Thanks for the question, Eric. I would say, yes, certainly, some of the economic environment influence has played through to mall development. We're seeing that, in particular, in Brazil right now. Does that increase our push for M&A? I wouldn't necessarily say that. I'd say, we're as active at kind of looking for those opportunities as we've ever been. If anything, perhaps some more opportunities are starting to shake out as a result of



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that economic environment. So we're may be seeing a little bit more activity on that front as a byproduct of that and that we're able to capitalize on, like we just saw recently. But specific to the new builds in the malls, what we've tended to see historically is, one country may be down for the time being, like Brazil is now, we've seen opportunities elsewhere. So we had that more recently in Colombia with a bunch of new builds that opened last year in Colombia and we're certainly seeing that this year in Central America, where we've got many opportunities, most of our new builds that are in the region this year are going to be coming out of Central America. So it's part of the benefit of having a diversified portfolio across the 15 countries we're in, when one country is down, somebody else may be up and we've got that benefit.

Eric Christian Wold - *B. Riley FBR, Inc., Research Division - Senior Equity Analyst*

Got it. And then the last question, kind of circling back on NCM. Obviously, you've been involved in that since the get-go. This increased investment does demonstrate your belief in the segment along with CineWorld (inaudible) their position. You talked about kind of best practices (inaudible) improve both. You've obviously had a greater incentive (inaudible) boost performance of this investment versus we had before. What are some of the things you can do internally at Cinemark to kind of help performance of the screens? Obviously, you can do best practices behind the curtain, as you kind of talked about already you can do at your locations, and is one of those things potentially integrating ads within the trailers as opposed to kind of keeping them separate or is that something you think moviegoers in the U.S. would not be okay with?

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

It's probably too early to make a comment on that. At this point, the management team at NCM is putting together a go-forward strategy. They'll be presenting that to the overall board and, of course, to CineWorld and to us, for us to look at and evaluate. CineWorld will be looking at some of their best practices and how they sell their ads and maximize their ads, and tie in a digital component to the screen advertising. We're doing the same thing with what we're doing in Latin America. At this point, many advertisers are looking for more and more accountability. They're looking for a digital component to the screen advertising time. They're looking for ways to co-promote greater within the theater. It might be outside of, again, just the screen, it might be into the lobby. So all these kinds of things are going to be looked at. And considering that we've got a long-term agreement with National CineMedia, both CineWorld does, we do and AMC does, we think the future is very, very bright for National CineMedia because there are new opportunities for us to look at and consider. It's probably a little early for us to be talking about those. And when we do in fact talk about them, I think it's probably appropriate for NCM to make that specific announcement.

Operator

There are no further questions. I will turn the call back over for closing remarks.

Mark Zoradi - *Cinemark Holdings, Inc. - CEO & Director*

Thank you all very much for joining us this morning, and we look forward to speaking with you again following our third quarter.

Operator

This concludes today's earnings call. You may now disconnect.



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