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Quad/Graphics, Inc. (QUAD)

Q4 2019 Earnings Call

CORPORATE PARTICIPANTS

Kyle Egan
Director of Investor Relations and Assistant Treasurer, Quad/Graphics, Inc.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

OTHER PARTICIPANTS

James Clement
Analyst, The Buckingham Research Group, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen. Welcome to Quad's Fourth Quarter and Full Year 2019 Conference Call. During today's call, all participants will be in a listen-only mode. [Operator Instructions] A slide presentation accompanies today's webcast and participants are invited to follow along advancing the slides themselves.

To access the webcast, follow the instructions posted in this morning's earning release. Alternatively, you can access the slide presentation on the Investors section of Quad's website under the Events & Recent Presentations link. Following today's presentation, the conference call will be opened for questions. [Operator Instructions] Please also note today's event is being recorded.

And at this time, I'd like to turn the call over to Mr. Kyle Egan, Quad's Director of Investor Relations and Assistant Treasurer. Kyle, please go ahead.

Kyle Egan

Director of Investor Relations and Assistant Treasurer, Quad/Graphics, Inc.

Thank you, operator, and good morning, everyone. With me today are Joel Quadracci, Quad's Chairman, President and Chief Executive Officer; and Dave Honan, Quad's Executive Vice President and Chief Financial Officer.

In terms of our agenda today, Joel will lead off the call with an update of our fourth quarter and 2019 performance and a continued progress we're making the with Quad 3.0 transformation. Dave will follow with a summary of Quad's fourth quarter and full year 2019 financial results and a summary of our 2020 guidance followed by Q&A.

I would like to remind everyone that this call is being webcast, and forward-looking statements are subject to Safe Harbor provisions as outlined in our quarterly news release and in today's slide presentation on slide 2. Quad's financial results are prepared in accordance with generally accepted accounting principles. However, this presentation also contains non-GAAP financial measures, including adjusted EBITDA, adjusted EBITDA margin, free cash flow, and debt leverage ratio. We have included in the slide presentation reconciliations of these non-GAAP financial measures to GAAP financial measures.

Finally, a replay of the call and a slide presentation will be available on our Investors section of quad.com shortly after our call concludes today. I'll now hand over the call to Joel.

J. Joel Quadracci

Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

Thank you, Kyle, and welcome, everyone. I am pleased to report that our fourth quarter results exceeded expectations driven by continued execution against our strategic priorities, including aggressive cost management and increased manufacturing productivity as well as winning new work to offset organic sales decline. We had one of the best quarters in the past decade in terms of customer service performance achieving strong quality and on-time delivery performance for our clients in their busiest season. This strong performance is due in large part to our decision to invest $40 million to increase hourly production employees' wages as we saw significant productivity gains throughout the quarter.

Given this performance, we ended 2019 with net sales, adjusted EBITDA and free cash flow exceeding revised 2019 guidance and we've reduced our debt leverage ratio to 3.1 times. In 2020 we will continue to transform Quad as a marketing solutions partner through our consistent focus on our five key strategic priorities as shown on slide 3.

Our first priority is to grow our business profitably over the long-term by leveraging our data-driven print expertise as part of an integrated marketing solutions platform. This unique platform helps our clients not only plan and produce marketing programs but also deploy, manage and measure them across all traditional and digital channels. It creates greater value and growth opportunities for our clients by helping them to reduce the complexity of working with multiple agency partners and vendors, eliminating multiple handoffs that compromise both the strategy of the programs as well as the speed at which they are executed, increase efficiencies through workflow re-engineering, content production, and process optimization and improved marketing spend effectiveness across all channels through data-driven consumer insights, media planning and creative and campaign strategy.

Our second priority is to walk in the shoes of our clients by listening to their needs and developing solutions to help them grow their businesses. We have made it a priority to strengthen relationships at all levels within our clients' organization, so we can better understand and anticipate and solve their problems. We are advancing conversations beyond print execution to be more consultative and centered on enterprise wide marketing solutions. To facilitate these conversations, we continue to hire additional experienced marketing talent with client side or agency experience.

Our third priority is to strengthen our corporate manufacturing platform. In 2020, we will continue to optimize our platform and make the necessary long-term investments to streamline, automate and improve efficiencies in throughput and drive labor productivity so that we remain the industry's high quality low cost producer. We continue to adapt our platform for the realities of a changing print industry such as the need for quicker makereadies in shorter runs. We also offer our clients the ability to efficiently produce multiple different product lines under one roof. We continue to engage and power employees to find a better way every day. We foster an environment that encourages employees to embrace Quad's culture of continuous improvement in an effort to not only drive ongoing productivity improvements but also product, service and technology innovation, all of which helps our clients succeed in today's evolving marketing landscape.

And finally, we manage all aspects of our business to enhance financial strength and create shareholder value over the long term. In 2020 we will continue to prioritize de-leveraging the company's balance sheet through debt reduction. Our transformation as a marketing solutions partner is our strategy to counteract ongoing print industry volume declines and reposition our company toward growth.

During 2019 this strategy led to $225 million of organic incremental sales growth helping to significantly offset the decline in organic print sales. Our ultimate goal is to completely offset this decline through growth of our higher margin of marketing services, which also drive incremental print revenue across all our product categories.

As we turn to slide 4, I want to share a few examples of how we plan to accelerate our transformation as a marking solutions partner and continue to offset organic print sales decline. First we will continue to aggressively manage our product portfolio, evaluating our offering with a focus on long term value creation and strategic fit.

Last month we completed the divestiture of our Omaha packaging plant, which specializes in high volume, low cost converting for folding cartons and is a better fit with a vertically integrated supplier that operates both paperboard mills and converting facilities. However, we are committed to packaging for the long term and this sale allows us to focus our efforts on higher value packaging solutions that help clients create a cohesive brand experience across all channels from consumer packaging to print, broadcast and digital advertising and in-store signage and displays.

Last year we divested our industrial wood crating business Transpak and announced our decision to divest our book business, which is progressing as expected. As we've reviewed our product portfolio, we determined these businesses could not be leveraged as part of our greater integrated marketing solutions offering.

By shifting away from certain product lines, we're not only better allocating our capital but also better allocating our focus, allowing us to make significant gains in other product areas. Over the last few years, we have made bold decisions to strengthen our platform to ensure marketers and publishers have access to a stable supply chain.

We have used our economies of scale, strong balance sheet and access to capital markets to take advantage of consolidating acquisition opportunities using a very disciplined approach to remove our excess, inefficient and underutilized capacity. With our strong and stable platform, we continue to gain new volume.

For example, we recently gained significant segment share in long-run publications earning 100% of print volumes from two large national magazine publishers, representing more than $60 million in additional annual revenue. These titles, a mix of weeklies, monthlies and special editions are transitioning to our nationwide manufacturing network right now. These publishers will benefit from the strength and scale of our platform including the industry's largest co-mail, postal optimization program as well as access to our enterprise solutions that solve marketing and process challenges.

The second way we continue to accelerate our transformation is through expanding our partnerships with clients. For example, given the tremendous amount of pressure retailers are under to market to a changing consumer, our expanded offering creates an opportunity for us to help them in a unique way, specifically by optimizing their marketing spend across all media types to achieve improved return on investment. With printed newspaper inserts under pressure, we can help retailers identify and implement higher performing media mix strategy that includes direct mail, catalogs, online, broadcast, out of home, and in-store programs. Then with our data analytics expertise we can measure outcomes so retailers can further tailor campaigns for even greater effectiveness.

The result is we are able to help retailers lower their new customer acquisition costs, drive repeat purchases and most importantly, grow their businesses. For example, we've recently developed a robust technology solution that simplifies and streamlines the process a national home improvement retailer users to update its in-store signage weekly at its 1,700 plus locations. This solution has created in excess of $10 million of additional revenue with this 20-year retail insert print client. Because we are a trusted partner, the client asked for our assistance in creating a solution that would get in-store promotions and shelf price tags tailored to individual stores needs into local markets faster and make it easier for store employees to adjust the signage.

Our client-facing technology group innovated a solution that allows each store to verify its data for signage, all in one central location. We then access the data to print and ship the signage in kits packed according to each store's layout. As a result of our efforts, we help the retailer increase speed to market, allowing it to be more responsive to changes in consumer behavior, reduce in-store resources to install the signage, bring up employees to focus on customers and significantly reduce waste by producing and delivering signs that match each individual store's actual needs.

Another Quad innovation gaining momentum among our clients is Accelerated Insights, our proprietary virtual testing platform that allows clients to rapidly test print creative and formats and identify precisely what combination of format, offer, messaging and imagery will be most successful. Through our platform we are able to slash testing times to 60 days versus traditional methods, which can take from one year to two years. Accordingly, we are able to reduce testing costs by 90%, and helps clients avoid incremental loss in sales from underperforming test packages, while also driving enhanced personalization. Accelerated Insights was a catalyst behind 40% of our new customer engagements for our direct mail business in 2019.

A third example of how we continue to accelerate our transformation is by introducing the power print to direct-to-consumer brands. Many of these brands market exclusively in social media channels. However they are finding that social media alone is not enough to support their long-term growth.

This is one reason why we chose to partner with Tim Armstrong and his dtx company which is revolutionizing the way consumers discover new direct-to-consumer brands. As online customer acquisition costs increase and the effectiveness of those efforts decreases, print is prized for its ability to effectively create a connected experience drive traffic and increased frequency of engagement.

In fact just last week the Harvard Business Review published an article on why catalogs are important in the media mix. The article said many brands and retailers are investing in catalogs "even pure online retailers that prided themselves in creating efficient and digitized consumer experiences such as Wayfair, Bonobos, Birchbox, and Amazon". The article concluded with what we at Quad know to be true. It's as physical products catalogs stand apart from cluttered e-mail inboxes, and social media feeds and because they linger in a consumer's home, they also do a great job of increasing top-of-mind brand awareness and driving traffic to all channels.

We continue to expand our relationship with a large direct-to-consumer retailer, who is successfully using catalogs and direct mail to increase its household presence in certain market verticals. We printed tens of millions of catalogs towards 2019 holiday campaign. The print catalog performed exceptionally well establishing Quad as a strategic solutions provider. Now, we're expanding the print relationship to the retailers other market verticals. We're also putting employees onsite to assist with design and production, integrated agency services including creative development. Looking ahead, we will continue to make investments in established partnerships that support the continued evolution of our integrated marketing solutions offering and help accelerate our overall company transformation.

As I turn the call over to Dave, I want to take a moment to thank all of our employees for their dedication and hard work to make certain we delivered strong customer service performance in the fourth quarter. They were able to deliver top quality products with low waste, shift on time and it accomplishes all of this while hitting a historic record across all safety metrics. Congratulations, and thank you to all our employees.

With that, I'll turn the call over to Dave.

David J. Honan

Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

Thank you, Joel. And good morning, everyone. We ended 2019 performing well, both operationally and financially. Customer service performance was exceptionally strong with high quality and on-time delivery metrics and great safety performance in our facilities. The strong operational performance sets the stage to finish the year with adjusted EBITDA and free cash flow above our latest guidance ranges. We look to build on that performance in 2020 while continuously improving productivity and focusing on reducing debt levels.

Slide 5 shows our 2019 net sales breakdown as compared to 2018. These product types are classified into three marketing solutions categories, integrated solutions, targeted prints, and large scale prints. Integrated solutions represents 21% of our net sales and includes higher margin agency solutions such as marketing strategy, creative, management, production and media planning and buying as well as logistic services. Integrated solutions is a growing category for Quad with organic growth of just over 1% per year over the past five years. This growth is despite a significant change in the mix of our service sales from large scale print related services and into surrounding targeted prints and other media channels.

Targeted print represent 39% of our net sales and includes highly targeted and personalized print products such as catalogs, direct mail, in-store signage, packaging and special interest publications that clients use to create a connected, personalized, consumer experience. Targeted print organic sales have remained flat over the past five years as marketers continue to utilize more forms of targeted and personalized prints to realize higher returns on advertising to drive sales and brand exposure. The combination of integrated solutions and targeted print now represents 60% of our net sales and is growing as a result of our Quad 3.0 strategy.

Lastly large scale print accounts for 30% of our net sales includes retail inserts, magazines and directories that are primarily mass produced and marketed. This area of print still represents great value for our clients who wish to reach mass audiences. Over the past five years organic volume decline in this category has averaged 10% per year and has migrated to other media channels, including more targeted and personalized forms of print.

We continue to aggressively manage costs in this category to offset organic decline. However it remains critically important to our Quad 3.0 strategy as it provides both the scale and cash flow necessary to support future value creating products and services and also provides further Quad 3.0 opportunities as we work with our clients' needs to flexibly adjust their media mix to more forms of targeted media.

Slide 6 provides a snapshot of our fourth quarter and full year 2019 financial results as compared to 2018. We're pleased to report that each of our key financial metrics, net sales, adjusted EBITDA and free cash flow exceeded our revised financial guidance. Net sales were $1.1 billion in the fourth quarter, down 4.9% from 2018. Organic sales which exclude acquisitions declined 5.9% during the quarter and benefited from new revenue generated from the Quad 3.0 strategy offset by ongoing print industry volume and pricing pressures, primarily in the large scale print category and a negative 0.3% impact from foreign exchange.

Full year 2000 (sic) [2019] (00:18:16) net sales were $3.9 billion as compared to $4 billion in 2018, down 1.6%. Excluding acquisitions, organic sales declined 3.5%. The organic sales results reflect new revenues generated from the Quad 3.0 strategy offset by ongoing print, industry volume and pricing pressures primarily in the large scale print category and a negative 0.6% impact from foreign exchange.

Our Quad 3.0 strategy drove $225 million of organic net sales growth in 2019. This help to offset over 5 percentage points of annual print sales decline. Adjusted EBITDA was $96 million in the fourth quarter of 2019 as compared to $118 million in 2018 and the adjusted EBITDA margin was 9% as compared to 10.5%, respectively. The variance in the prior year primarily reflects the impact from the organic sales decline of 5.9%, a $13 million decrease in print process profits from the reduction in market prices for paper byproduct recoveries, the impact of a $6 million non-recurring gain in 2018 in Peru and $5 million of strategic investments made to increase hourly production wages partially offset by cost reduction activities.

Full year 2019 adjusted EBITDA was $335 million as compared to $428 million in 2018 and the adjusted EBITDA margin was 8.5% as compared to 10.7%, respectively. The variance to prior year primarily reflects the impact from organic sales decline of 3.5%, $33 million in non-recurring benefits in 2018 that did not repeat at the same level in 2019, a $29 billion impact from strategic investments made to increase hourly production wages and a $27 million decrease in print profits from the reduction in market prices for paper byproduct recoveries. All this was partially offset by cost reduction activities.

Full year 2019 free cash flow was $106 million and excludes $61 million in payments from a terminated acquisition during the year, this compares to $164 million in 2018. The reduction in free cash flow is primarily due to lower net earnings and increased capital expenditures on long term investments in automation and productivity improvements in the manufacturing platform. In addition free cash flow includes the impact of the discontinued operations of our book business, which negatively impacted our consolidated free cash flow in 2019 by $25 million.

Slide 7 includes the summary of our debt capital structure as of December 31st. We finished 2019 with a debt leverage ratio of 3.12 times, which decreased from 3.24 times as of September 30. Our year-end 2019 debt leverage ratio is above our long term targeted leverage range of 2 times to 2.5 times. And while we may operate outside of this range due to the timing of compelling strategic investment opportunities such as the Periscope acquisition in 2019, we'll continue to target this long term range.

In the near term our priorities for capital allocation will continue to be debt reduction. Our debt capital structure is 65% fixed and 35% floating with a blended interest rate of 5.2% as of December 31, 2019. Available liquidity under our $800 million revolver was $764 million, and we have no significant maturities until May of 2022. We have the financial resources to pursue future growth opportunities and return capital to our shareholders through our quarterly dividend. Our next quarterly dividend of $0.15 per share will be payable on March 9, 2020 to shareholders of record as of February 28, 2020.

On slide 8, we've included a summary of our 2020 financial guidance, which excludes the discontinued operations of the book business in all metrics with the exception of cash flow. We anticipate 2020 net sales to be in a range of $3.5 billion to $3.7 billion. This includes a 2% decrease from 2019 related to the divestiture of our Omaha packaging plant in January of 2020. In addition we expect organic net sales to decrease by 6% at the midpoint of our guidance, primarily due to anticipated declines in sales, in our large-scale print category.

Full year 2020 adjusted EBITDA is expected to be in the range of $285 million to $315 million representing a 10% decline versus 2019 at the midpoint of our guidance. The primary factors impacting the decline between years are related to lower net sales primarily in our large-scale print category, lower print profits due to lower market prices on paper byproduct recoveries, which significantly weakened in the back half of 2019, and are expected to negatively impact the front-half of 2020 by approximately $20 million, and continued impact from the long-term investments made to increase hourly production wages in the front-half of 2020 by approximately $10 million.

We are encouraged by the strong labor productivity improvement seen in 2019 from these investments and expect to realize more savings over the long-term. Offsetting these impacts, we've doubled our previously announced cost reduction program to $100 million. These savings will sequentially build throughout the year and we expect all of the $100 million in savings to be realized in 2020. Given the pressures in our industry, we will continue to proactively work on additional cost savings projects, including EBITDA enhancing sales growth through our Quad 3.0 strategy. The impacts of the decline in paper byproduct rates and the long term investments in hourly production wages combined with the seasonal nature of our revenues will result in the majority of our expected decline in year-over-year adjusted EBITDA to be realized in the front-half of the year.

We expect to see sequential improvement in the year-over-year comparisons and adjusted EBITDA as the year progresses. We also expect 2020 free cash flow to be in the range of $100 million to $130 million representing an 8% increase from 2019 at the midpoint of our guidance. As a reminder we realized our strongest volumes in the back half of the year due to seasonality and as a result, the majority of our free cash flow will be generated in the fourth quarter of the year.

The remainder of our guidance includes interest expense in the range of $70 million to $80 million; depreciation and amortization in the range of $185 million to $190 million; cash restructuring charges in the range of $40 million to $50 million; capital expenditures in the range of $70 million to $80 million; pension contributions of approximately $20 million; and less than $10 million of cash taxes.

As we continue to accelerate our Quad 3.0 transformation, we will remain focused on reducing debt and delivering long term sustainable value to all stakeholders. We believe that our integrated marketing solutions offering, which comes at a time of continued media disruption makes Quad a compelling long-term investment for our shareholders. As we move forward into 2020, we'll continue to serve our clients well and drive productivity improvements and sustainable cost reductions to remain a high quality, low cost producer all while continuing to generate significant free cash flow. This focus will allow us to maintain a healthy balance sheet to help us adjust to changing industry conditions, invest in our business and return capital to our shareholders among other priorities.

And now I'd like to turn the call back to our operator, who will facilitate taking your questions. Jamie?

QUESTION AND ANSWER SECTION

Operator: Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions] And our first question comes from James Clement from Buckingham. Please go ahead with your question.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Hey, gentlemen.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.
A

Hey, Jamie.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Good morning.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.
A

Good morning.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

Good morning, Jamie.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Dave, if I could go to you real quick, I was just trying to jot some of the stuff down. So in thinking about annual EBITDA guidance and kind of the cadence between first half and second half, do I have a – so paper byproducts, did you say an incremental $20 million hit in the first half, is that right?

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

Yeah. Yeah. So, we...

[indiscernible] (00:26:34)

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Sorry, go ahead.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

We experienced the decline rate towards the last half of last year. This will annualize through this year. So, we have built into our guidance $20 million of annualized impact, all hitting the front half of the year.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay. And then on the labor side, is that another $10 million and that would be in the first half also?

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

That's correct.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

So is the way to think about this just kind of at the midpoint, I think you said – did you say substantially all of the year-over-year decline in the first half and then things flatten out in the back half or am I putting words in your mouth there?

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

A little bit of words in my mouth, but directionally you're correct.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

You're correct.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

And then we expect sequential improvement. So on a year-over-year comparison basis, the first quarter will be the most decrease, followed by the second quarter with improving a decrease year-over-year and then on throughout the year.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

A moderating decrease Dave, a moderated, right. Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

Exactly. So definitely you're going to see front half pressure but back half of the year looking a lot better as we'd annualized a lot of the kind of headwinds coming at us with paper byproduct rates with our investments and labor rates to – which really, really benefited us this year in the fourth quarter as we just hit record levels of on-time delivery and performance for our customers. It was just outstanding performance by our manufacturing team and so that really led to what you saw with the strong financial performance in the fourth quarter as we exceeded guidance.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

So to think about the labor aspect of things. You still face – just as you annualize those increases, you still face the EBITDA headwinds, but you're already demonstrating productivity, so you no longer have that headwinds and then we should see margin improvement in the numbers. Is that all of being equal?

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

Yeah, I agree with all of that – really the doubling of our cost reduction initiative, which also includes EBITDA producing revenue wins in it. That ability – that grows throughout the year for a full $100 million of impact for 2020. That's really helping to offset the headwinds that we're seeing in just organic print declines.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Right.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

Especially in that large scale print category. We have retail inserts pressure, directories pressure and magazines pressure.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

And I think that would be a good point to segue to Joel, if I may. Obviously the organic decline as the year progressed got a little harsher with the most severe number being in the fourth quarter. And I guess how much of this in your opinion is – the demand side of the equation, the customers' side changing their mix with things that you're helping them with obviously Quad 3.0 versus and I have to ask a question – versus maybe other suppliers out there that are potentially running into trouble? And maybe that impacted pricing in one way or the other?

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Yeah, well – look, I think if you look at the different categories, I mean, we all know that retail inserts is probably one of the most heavily pressured – and if I look at like fourth quarter – you know as this industry retail inserts were down about 20%, our mix was actually down about 13%. So we outperformed and if you kind of converted that to a trailing 12 months, the industry was like 17%, we were at 10%. But in this space, it's retailers are probably the ones that we're probably having the most engagement with on Quad 3.0, because they're under a lot of pressure from lots of different angles. And so the retail insert decline, let's not forget also has to do with the decline of the carrier of the retail inserts to the market, which is...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Yeah.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

...newspaper circulation...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Sure.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

...along with people kind of trying to figure out different mixes. And so what we're finding is as you see some significant reductions there, we're actually increasing the use of things like direct mail, so heavily personalized direct mail like if you look at a Kroger direct mail piece, it's almost 100% variable where there's coupons of product that you actually bought last week imaged right on the piece with a one-time individual barcode for you across, and this is – every piece across millions of pieces every month being completely variable.

So some of that's – that's a good example of how some of this is being diverted to other print areas because our customers do know that print is important. And as they lose the ability to circulate retail inserts, they obviously look at the whole mix, but they do continue to look for other ways to use print in it. And the example of that we used in the script of doing retail inserts for that huge retailer that suddenly we ended up gaining $10 million of in-store signage from them just through helping them with the pressures was really important because it wasn't just about printing in-store signage, we actually built the technology that the store managers use across 1,700 stores to spec out the demand. And then we use our own analysis to make sure that each store is getting the right amount. But more importantly we're cutting the time it takes for them to do this, which gives them time to react to their competitive set in pricing and things like that.

So that's really important and if I look at the catalog industry, we have like a J. C. Penney went back to catalog, you have other big retailers who never did catalog, doing catalog right now. The industry – a number of books in Q4 were down almost 7%.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Right.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Quad in terms of catalogs mail was up 10% and that's up 10% in the fourth quarter, a good chunk of that was new entry into catalog and actually new entry into print. So again about rediscovering it, but you also see people who are kind of [ph] cutting (00:32:31) back on retail will also still focus on catalog as another print opportunity.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Joel, I just – oh sorry.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Yeah. Go ahead.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

I was just going to ask you like is this the comp, been a theme for a couple of years, what about traditional e-tailer only going to catalogs?

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Well, that's what we're talking about.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Right.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

I mean you know if you look at what's going on with Google, Facebook, even Amazon, it's – that the – and you specially hear it from the new upstarts because they're a little more honest about it. But the cost of using social media is going up and the effectiveness is going down. And I think that's only going to increase as you look at the cookies going away, as you look at, antitrust things going on and it's really going to benefit the publisher or put it this way, think about a big retailer advertising their own stuff direct-to-consumer as opposed to through these third parties, it only will enhance that.

So we believe that there is going to be a decent amount of new revenue coming into print that may not have existed before and again, we'll still deal with the natural decline in the industry. But for us, it's all data driven and that's why it's so important for us to have our services aspect of the business, which includes Workflow Solutions, which includes Data Analytics, which is Accelerated Insights combined with the ability to execute on the core print products. Because that's where we're giving not only our current customers an edge up on how their existing print works with the other channels. But then when you think about the people coming into print, they really don't have the experience or the know-how and how to even execute on it, and so we're able to give them the equivalent of a full staff to ramp up very quickly in using print campaigns and also to show them how to analyze it.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Right. I appreciate the time. Is there anybody else in queue? I don't want to hog up all the time.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Well, Jamie, let me just – there's another important aspect here...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Yeah.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

...when we talk about know shifting through print. I mean our direct mail volume, so in Q4 of 2019 the industry was according to USPS was down about 3.8%. Our direct mail volume was up 13% and almost all of that was very much data driven type of direct mail as opposed to commodity type of direct mail and as I said in the script -

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

So...

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Go ahead.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Oh, I'm sorry. I was just wondering are there certain like – you need to help people like me to help investors understand like the kind of customer verticals where you're seeing like the outsized growth like can you help us out there?

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Yeah. I mean it's anywhere from financial services to...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

...to satellite radio...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

...to even to traditional catalogers. And what's happening is with the Accelerated Insights program where we can show them a different way to target people and prove to them that the increase in response, that's been a real door opener and about 40% of the new sales volume in DM that we saw, came because we were engaged with them about how do they use data, and use content and align those to market to people in a more effective way.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Okay. Okay got it. All right. Anybody else in queue?

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.
A

No one else is queue? No, there's no one else in queue.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Can I – so back to Dave, if I could – hey Dave. I may have made a mistake in my head about something. Can you talk about – because I've heard some questions about this. The adjusted EBITDA that you will have report versus – the adjusted EBITDA that's used for leverage calculations, I think I may have in my head ignored the stock-based comp. Is there anything else, I need to think about in terms to add-back to EBITDA?

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

Well, I think your question is – those two calculations aren't identical. We've got – so what we always do is this simple Street leverage calculation...

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Yeah.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

...that this takes total debt divided by EBITDA. Our covenants are negotiated, those have more room than that of a simple Street leverage. You highlight one key difference is we're allowed to add-back to our EBITDA non-cash expense related to stock compensation.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.
A

But when you think about it in terms of a covenant versus the Street, the covenant has more room in it than that of a Street calculation.

James Clement
Analyst, The Buckingham Research Group, Inc.
Q

Okay. And then the other thing in terms of cash restructuring spending for the year, I know you have your guidance out there. Should we think about that as kind of even throughout the year, and then also are there any kind of working capital movements in first half versus second half that we need to be aware of other than the normal kind of usage of working capital in the first half of the year versus second half? Thank you.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

Yeah, yeah. It's a good question Jamie. On restructuring, we often make a lot of restructuring changes in the front half of the year because that's our seasonally low point.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

So that's when we have the need to reduce those fixed costs during that low point. So you won't see a straight line basis of that, you'll probably see a little bit more in first and second quarter.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

And then maybe kind of more smooth throughout the year. But nothing on working capital other than the typical seasonal movement of working capital, and just a reminder, we do generate the majority of that free cash flow in the fourth quarter because of the working capital decline in the fourth quarter...

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay.

David J. Honan
Chief Financial Officer & Executive Vice President, Quad/Graphics, Inc.

A

...has become out of our seasonal peak.

James Clement
Analyst, The Buckingham Research Group, Inc.

Q

Okay. Thank you very much. I appreciate that.

Operator: And ladies and gentlemen...

J. Joel Quadracci
Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

A

Jamie? Yeah, anybody else in the queue?

Operator: At this point I would like to turn it back over to management for any closing remarks.

J. Joel Quadracci

Chairman, President & Chief Executive Officer, Quad/Graphics, Inc.

Okay. Well. Thank you all for joining us. We look forward to our next update at the next quarterly call. Thank you.

Operator: Ladies and gentlemen, that does conclude today's conference call. We do thank you for joining today's presentation. You may now disconnect your lines.