Corus Entertainment Inc.

Q4 and Year-End 2023 Analyst and Investor Conference Call

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PRESENTATION

Operator

Good morning. My name is Lara, and I will be your conference Operator today. At this time, I would like to welcome everyone to the Corus Entertainment Q4 and year-end 2023 Analyst and Investor Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, please press *, then the number 2. Thank you.

As a reminder, this call is being recorded.

I will now turn the call over to Mr. Doug Murphy, President and CEO of Corus Entertainment. Mr. Murphy, you may begin your conference.

Doug Murphy — President and Chief Executive Officer, Corus Entertainment Inc.

Thank you, Operator, and good morning, everyone. Welcome to Corus Entertainment's fiscal 2023 fourth quarter and year-end earnings call.

I'm Doug Murphy, and joining me this morning is John Gossling, Executive Vice President and Chief Financial Officer.

Before I read the cautionary statement, I'd like to remind everyone that we have slides to accompany today's call. You can find them on our website at www.corusent.com under the Investor Relations - Events and Presentations section.

Now let's move to the standard cautionary statement found on Slide 2. We note that forward-looking statements may be made during this call. Actual results could differ materially from forecasts, projections, or conclusions in these statements.

We'd like to remind those on our call today, in addition to disclosing results in accordance with IFRS, Corus also provides supplementary non-IFRS or non-GAAP measures as a method of evaluating the Company's performance and to provide a better understanding of how management views the Company's performance.

Today, we will be referring to certain non-GAAP measures in our remarks. Additional information on these non-GAAP financial measures accompany the quarter results, and factors and assumptions related to forward-looking information can be found in Corus' fourth quarter 2023 report to shareholders and the 2022 Annual Report, which can be found on SEDAR+ or in the Investor Relations - Financial Reports section of our website.

I will now start on Slide 3 with a look at our year-end results and then provide an update on the current environment and what we're seeing in the media marketplace.

I've been using the term double whammy to describe the twofold blow that we've been dealt in fiscal 2023.

The first blow has been the meaningful decline in advertising revenues. The second has been a significant increase in required spending on Canadian programming. This one-two combination has resulted in a very challenging year for our company.

Our focus remains on what we can control and influence. We are undeterred in our pursuit of our premium digital video growth initiatives.

Our strategic plan and its priorities reimagines our business beyond broadcast television towards our evolution into a multiplatform aggregator of premium video with cross-platform monetization capabilities. This is what we call our Video First strategy.

In service of this Video First ambition, we are concurrently demonstrating a disciplined approach to streamline our operations and rationalize our asset base. This enterprise-wide cost review, which we call Fit for the Future, has revealed meaningful opportunities to change the way we work and to better position Corus for the future.

We are taking prudent actions now to ensure the resiliency of our company. We have proactively secured amendments to our credit agreement and further redirected our use of free cash flow to debt repayment, which will provide additional financial flexibility while we position Corus for the expected eventual recovery in advertising and program-supply conditions.

Against this backdrop, our results for the year are as follows:

Our consolidated revenues were $1.5 billion for the year.

Total consolidated segment profit was $334 million for the year with free cash flow of $107 million.

We reduced bank debt by $172 million this year, resulting in pro forma leverage of 3.62 times.

John will take you through the results for the fourth quarter and year in more detail in his remarks.

Moving to Slide 4. The word distortion fittingly describes this very unusual post-pandemic environment we find ourselves in. The definition of distortion is the “act of twisting or altering something out of its true, natural, or original state.” Let me explain.

Supply chain disruptions have affected and still affect companies producing goods and services. Labour shortages persist throughout the economy, impacting industries everywhere as wage inflation challenges business models. Economists still debate the likelihood that we will avoid a hard landing and move from today’s slow-motion rolling recession to a soft landing.

Geopolitical tensions remain an unknowable risk to the markets and the economy. And now consumers themselves, once purchasers of durable goods such as furniture, electronics, home renovations during the pandemic, are now favouring the service economy by dining out, travelling, and going to concerts. These same consumers are contending with high prices at the pump, increasing mortgage expenses, and food inflation.

Last summer, we began to see the effect of these distortions impact our clients' businesses, with chief marketing officers cutting top-of-the-funnel marketing investments to protect their margins. That's the macroeconomic backdrop.

Now turning the dial to the entertainment and media industry, where we've been dealing with a distortion field of our own. Let's briefly review what's happened in our industry.

In recent years, and certainly during the pandemic, all of the US media and entertainment studios launched subscription video-on-demand products to offset declines in people viewing linear television.

As interest rates increased, the challenging economics of the streaming industry became apparent, and we witnessed a pivot from a subscriber growth at all costs mentality to more of a disciplined pursuit of a path to profitability.

On that path to profitability, these very same SVOD services now embraced advertising-supported video, launching advertising layers to grow their revenues and ARPU.

In parallel, we witnessed the launch of free advertising-supported streaming television, FAST channels, that successfully leveraged quality library programming cost-effectively to grow online advertising revenues with no charge to audiences.

So as the demand from the macroeconomic distortions weakened, the industry was creating a whole new supply of premium digital video impressions to monetize.

Then, midway through the broadcast year, the entertainment industry was distorted once again when the Writers Guild of America walked out on May 2nd, followed by the actors on July 14th. The last time writers and actors were both on strike at the same time was in 1960. At that time, business models were changing and the unions wanted to get better residuals from movies that were now being broadcast on the television networks, a new technology at the time.

The actors strike, now over 100 days in length, persists, although both sides have returned to the table this week. There remains uncertainty as to the duration of the strike, but across the industry there is optimism about achieving a resolution by US Thanksgiving. Writers' rooms are open. If that timeline is realized, we could then expect a full schedule by March, just in time for our second-largest advertising revenue quarter, Q3.

In our first quarter, however, these strikes have caused all deliveries of scripted, simulcast content to stop. This significantly reduced our audience delivery during prime time, impacting advertising demand and revenues during what is our largest quarter typically.

Over to Slide 5. The Fit for the Future initiatives demonstrate the hard work we are doing to streamline our operating model and rationalize our asset base.

We have tenaciously implemented cost cuts and ongoing workforce structural reviews throughout the Company to deliver reductions quarter by quarter, as we find ways to work differently and improve productivity across all aspects of our business to lower our cost base. Let me give you a few examples.

In the fourth quarter, we successfully completed the sale of Toon Boom, with net proceeds of $141 million used to pay down bank debt and rationalize our asset base.

We have reorganized our sales team to deepen expertise in cross-platform selling. As we transform into an aggregator of premium video, our goal is to provide a seamless buying experience for our advertisers.

We have streamlined our approach to content, introducing the expanded role of Executive Vice President Networks and Content and eliminating the role of Executive Vice President Content and Strategy. This consolidated role is accountable for the oversight of all programming investments for both Canadian and foreign programming as we streamline our programming operating model and maximize our audience delivery across all platforms.

We have made tough decisions to discontinue certain Canadian productions to reduce costs. Let me provide two examples.

After 18 amazing seasons as our flagship entertainment news program, the difficult decision was made to wind down Canadian Screen Award-winning entertainment news program ET Canada.

Equally difficult was shuttering the Global News production, The New Reality, a news program launched during the COVID-19 pandemic. The New Reality answered the public's most pressing questions of the day during an uncertain time, while looking forward to the future. Corus invested more in news at that time than other broadcasters were, but not anymore.

When we last spoke in June, we mentioned that our cost-reduction efforts were translating into an almost 8 percent reduction in our workforce. Based on our current work, that number is now approaching 15 percent, and we continue to look at all other opportunities to reduce costs.

Moving to Slide 6. Our rapidly expanding scale in digital video is creating exciting new opportunities for advertisers. With our investments in cross-platform monetization, we now deliver dynamic ad insertion across all streaming platforms, offering more targeted and effective solutions to clients.

With last year's launch of Pluto TV alongside the Global TV App, STACK TV, and our Global News FAST channels, we're delivering more than seven times the digital video ad impressions than just two short years ago. This gives us confidence that the new platform revenue remains a significant opportunity for us as adoption by audiences and advertisers grows and is evidence of our Video First strategy in motion.

In Q4, 13 percent, or $33 million of total TV advertising and subscriber revenue was attributable to new platform revenues, while representing 11 percent or $146 million for the year.

Corus remains steadfast in our efforts to offer more targeted ways for advertisers to better reach their desired audience. We are extending our industry segments across all platforms, linear and digital alike, to improve our cross-monetization capabilities.

In Q4, 55 percent or $75 million of advertising revenue was optimized, and 54 percent or $411 million for the year, which is an important step towards breaking out of the legacy TV trading model.

And with that, I'll turn it over to John.

John Gossling — Executive Vice President and Chief Financial Officer, Corus Entertainment Inc.

Great. Thanks, Doug. Good morning, everyone. I'm starting on Slide 7.

Given the prolonged advertising market distortions and unexpected labour disruptions in our industry, as Doug has mentioned, this morning we announced certain prudent actions to support our

approach to capital allocation. This includes the suspension of our dividend and an amendment to our bank credit facility.

We announced the suspension of our dividend to enable free cash flow to be redirected from dividends to debt repayment.

We also announced a further amendment to our credit facility, which we proactively secured given the uncertain duration of the current macroeconomic conditions and the ongoing actors strike, which is impeding our program supply and impacting audience levels and advertising demand, as mentioned earlier and also as pointed out in our outlook.

In February 2023, we had renegotiated the covenants under our bank credit facility to address the persistent headwinds in the economic environment and provide us with additional financial flexibility. But at that time of the February amendment, the writers and actors strikes were not in view.

Today's amendments increase the maximum total debt to cash flow ratio permitted, up to and including the end of the fiscal year, August 31, 2024; reintroduce mandatory quarterly repayments of the term facility totalling 5 percent per annum; change certain conditions related to the use of net proceeds on asset disposals; and introduce additional restrictions on distributions to shareholders.

Our intense focus on deleveraging is appropriate and necessary, given the low revenue visibility and the uncertain outlook at this time. We continue to expect improvement in macroeconomic conditions and a resolution of the actors strike, both of which should have a positive impact on our TV advertising revenue in the coming quarters.

Over the past five years, we have reduced our debt by $912 million and diversified our sources of financing, improving our debt profile to maintain financial flexibility.

At the end of the fourth quarter, we were in compliance with all covenants and had $56 million of cash and cash equivalents and $286 million available to be drawn under our revolving credit facility.

Our pro forma leverage at August 31, 2023, of 3.62 times net debt to segment profit reflects a significant repayment of bank debt of $172 million for the year, and that includes the net proceeds of $141 million from the sale of Toon Boom in the fourth quarter that were used to pay down the debt.

As Doug noted, our Fit for the Future initiatives will continue to result in aggressive cost-reduction measures, which are increasingly reflected in our financial results, while maintaining focus on our long-term strategic objectives.

All right. Now over to Slide 8, a review of the consolidated results.

Advertising revenue in our fourth quarter was impacted by the ongoing challenges in the economic landscape, compounded by the writers and actors strike.

This was largely offset by positive results from our content business, contributing to a relatively consistent Q4 consolidated revenue of $339 million. For the year, we delivered $1,511 million in consolidated revenue, an increase—sorry, a decrease of 5 percent from the prior year.

Consolidated segment profit for the fourth quarter was $46 million and $334 million for the year, and that reflects the lower advertising and subscriber revenue, together with the increased programming costs that we saw.

This included higher Canadian programming expenditures, or what we call CPE, of $5 million for the quarter and $11 million for the year. And that was partially offset by G&A cost saves that were identified as a result of our enterprise cost review.

Consolidated segment profit margins were 14 percent for the quarter and 22 percent for the year.

Net income attributable to shareholders for the quarter was $0.25 per share, and that includes the gain on sale of Toon Boom of $142 million, partially offset by non-cash impairment charges of $100 million in the Television segment, and that's as a result of the continued contraction in advertising demand and the lower share price since May 31, 2023.

The net loss per share for the year was $2.15, which includes the gain on the sale of Toon Boom and non-cash impairment charges totalling $690 million in the Television segment.

We delivered free cash flow of $32 million in the quarter and $107 million for the year, and that reflects the impact of lower segment profit in both periods.

All right. Let's turn to our TV results for the fourth quarter and the year, and that's on Slide 9.

Overall, TV segment revenues of $314 million in the fourth quarter were consistent with the prior year, and for the year, revenues of $1.4 billion were down 6 percent. TV advertising was 10 percent lower in the fourth quarter and it was down 11 percent for the year.

The persistent challenges in the macroeconomic conditions contributed to significant contraction in advertising demand for both the quarter and the year.

Subscriber revenue was down 1 percent in the quarter and declined 3 percent for the full year.

Distribution, production, and other revenue grew a significant 46 percent for the quarter and 21 percent for the year, and that was driven by increased content delivery from all of our content businesses, Nelvana, Aircraft Pictures, and Corus Studios.

Direct cost of sales was up 10 percent for the quarter and 7 percent for the year and that's as a result of the increased amortization of programming costs, and that was driven mainly by a ramp-up in the Canadian spend, as well as investment in US studio output deals in the year and the increase in

amortization of film investments, and that's driven by the higher production deliveries at Nelvana and Aircraft Pictures that we saw.

Our effective CPE rate for the year was more than 35 percent. And that was driven by higher regulated revenue in the prior year and further exacerbated by the required CPE catchup spending from COVID-related production shutdowns in 2020.

This level of spending for the year was required under the terms of our broadcast licences and came at a time where we experienced significant pressure due to many factors.

Total general and administrative costs in TV declined 6 percent in the quarter and 3 percent for the year. Employee costs were down 6 percent and 4 percent for the quarter and the year respectively. And other G&A expenses declined 5 percent and 1 percent respectively.

Overall, TV segment profit was down in the fourth quarter and year, primarily as a result of the situation with advertising, reduced subscriber revenue, and higher amortization of program rights and film investments, partially offset by the aggressive cost controls.

TV segment profit margins were 16 percent in the quarter and 24 percent for the year. And that compares to 19 percent and 31 percent in the respective prior periods.

Looking ahead to the first quarter of fiscal 2024, we expect continuing macroeconomic uncertainty. Coupled with the impact of the extended writers and actors strikes, we expect television advertising revenue to decline in the range of 15 percent to 20 percent compared to the prior year.

Amortization of program rights is expected to decline by a similar range due to lower programming deliveries. We continue to aggressively pursue a number of cost-management initiatives in response to these factors.

While we expect improvement in the economic environment in the medium term, our visibility remains extremely limited at this time.

All right. Let's turn to our Radio results now on Slide 10.

Fourth quarter results reflect revenue softness, particularly in the entertainment, professional services, restaurant, and telecommunications categories. And that was partially offset by growth in categories such as retail and automotive.

The full year results reflect the impact of the broader environment on national advertising across all categories.

Radio segment revenue decreased $0.8 million for the quarter and $3.1 million for the year as a result of lower advertising sales, partially offset by higher podcasting revenue.

Radio segment profit increased $1.2 million and $0.2 million in the quarter and year respectively, as a result of cost-control measures. Q4 segment profit margins for radio were 12 percent and that was up from 7 percent last year, while full year segment profit margin was 13 percent, consistent with the prior year.

It is a new fiscal year, and we are hopeful for improved visibility in the coming months. In the meantime, we are taking prudent actions as we navigate unfavourable market conditions.

We are reducing costs, putting appropriate measures in place to maintain our financial flexibility, repaying debt, and strengthening our balance sheet. This is all part of how we maintain a disciplined focus on the long-term health and stability of our company.

We have tremendous operating leverage, which we stand to benefit from when these cyclical pressures eventually dissipate.

And with that, back to Doug.

Doug Murphy

Thank you, John. Finally, over to Slide 11.

Last week, the CRTC indicated that it is inclined to issue an order granting Corus the interim relief we first requested in November of 2022. This relief would come after years of structural changes that have meaningfully impacted the whole broadcasting industry.

The regulators' statement last week was the most substantive move toward regulatory change that our company has seen in years, and we are encouraged by it.

I won't get into the specifics of costs or timing right now, as we will be working through this once the decision becomes final. However, PNI relief and a CPE underspend extension acknowledges the challenges and opportunities of the moment. It would provide the much-needed flexibility in our content planning and spending for the coming years by letting us focus more on producing the best content that drives our linear and digital businesses.

Bill C-11 gets the big things right in its stated objective to level the playing field. We remain supportive of its implementation, but also note that more comprehensive regulatory reforms are still urgently needed.

Additional contributions from foreign-owned streaming platforms must result in permanent reductions in Canadian broadcaster's overall Canadian programming expenditure requirements.

Our focus is on navigating this unusual environment while delivering strong execution of our strategic plan and its priorities. We will continue our work on our Fit for the Future initiatives focusing on improving productivity across all aspects of our business to lower costs.

Our programming and sales teams are ready to quickly pivot with a great lineup of returning hits and new shows on our spring schedule once the actors strike is resolved.

In the meantime, our work continues as we move beyond being a television broadcaster to becoming an aggregator of premium digital video and building cross monetization capabilities as we embrace the Video First business model of the future.

With that, I'll turn it back to you, Operator, for questions.

Q&A

Operator

Thank you, sir. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press *, followed by the number 1 on your touch-tone phone. You will hear a three-toned prompt acknowledging your request, and your questions will be polled in the order they are received.

Should you wish to decline from the polling process, please press *, followed by the number 2.

If you are using a speakerphone, please lift your handset before pressing any key.

Your first question comes from the line of Adam Shine from National Bank Financial. Please go ahead.

Adam Shine — National Bank Financial

Thanks a lot. Good morning. So, Doug, I won't push you, obviously, on the CRTC relief. We'll hear more about that, I guess, in due course. But can we pivot to the size of the cost cuts? As you alluded to, I think it was about 250 positions that had been eliminated in the context of the near 8 percent.

Can you just speak a little bit more to the nearly 15 percent restructuring about a savings that this could involve? And when most of that might start to hit in F2024?

And then perhaps we could pivot next to John on any details around the amendments, but I can elaborate after.

Doug Murphy

So I'll make a qualitative comment. John can touch on the quantitative.

So this is sort of an ongoing quarter-to-quarter analysis we're doing across all aspects of our business. We announced a number of quarters ago our enterprise-wide cost review, which we've now named our Fit for the Future work. And so you're seeing the numbers showing up now in our G&A and salaries and benefits line. And I'll just underscore the fact that we're not done this work yet.

It's critically important as a counter measure to the uncertainty on the revenue outlook that we manage what we can control and influence, and that's specifically our expense lines.

John Gossling

Adam, back to my remarks, employee costs in TV were down 6 percent in the quarter and that's been accelerating through the year.

I'd say going forward, Doug mentioned a couple of shows that we had to take down. Some of those costs are going to show up in program amortization as well. So we'll try to bundle that going forward so we get a complete picture of it because it'll be across different lines in our reporting starting in Q1.

Adam Shine

Just on the amendments, I think you were stepping down on the covenant to 4.5 times in Q1.

John Gossling

Yeah.

Adam Shine

Obviously there might be some related adjustments over the next couple of quarters. Are you able to give us any sense of how the covenant metric has been updated?

John Gossling

Yeah. Look, the pattern that we've amended to as of today is very similar to what we did back in earlier in the year. It's just extending that, really.

So the pattern has us staying at the higher level through Q3 and then it starts to step down in Q4. So it's really, I guess, effectively an extension of another three quarters with the first one—sorry, with Q1 this year being slightly higher than it was going to be.

Adam Shine

Got it. Okay. I know where you're heading with that. Understood.

Maybe just one last one for you, Doug. Just as we kick into the new year, and the scramble that all broadcasters need to pursue in regards to some new products, some repeats, some international product, can you speak to how the Frankenstein schedule has come together? And how advertisers are effectively reacting to this? Is it a wait and see? Is it any particular commitment in pockets of the schedule?

Doug Murphy

First off, I'm impressed with your seasonal Halloween Frankenstein comment. You sound like a programmer, Adam.

So a couple things. First off, as I mentioned in my comments, the writers rooms are all open now. So all the studios are just cranking on getting the scripts completed for the episodes of comedies and for the dramas. So that's super encouraging.

As I said also, the consensus, generally speaking, or at least the opinions of our friends south of the boarder, is that we should get resolution effectively before the US Thanksgiving. And once that begins

then we understand that the comedies will be quicker to be completed and then the dramas. The returning shows will come a lot faster than the pilots and the new shows. That's pretty logical. Luckily for us in our schedule we have a lot of returning shows.

So we're cautiously optimistic that the third quarter we should have a full schedule. And we'll move beyond the Frankenstein schedule to a very strong showing in our second-highest quarter.

As for the advertisers' demand, you're right. At the moment, people are waiting to see what's going to happen out there with the audience delivery. We've seen these strikes in the past. The return to a full schedule usually brings with it a very significant reinvestment in marketing dollars once the schedule's locked.

So we are, again, expecting the same outcome once we can get closure and resolution on the actors strike.

Adam Shine

Okay. Thank you very much. I'll leave it there.

Doug Murphy

Yeah. Thanks, Adam.

Operator

Your next question comes from the line of Vince Valentini from TD Cowen. Please go ahead.

Vince Valentini — TD Cowen

Thanks very much. First I'm going to go back to the debt covenants, John. First on the mandatory repayment, 5 percent of the principal per year? That's like $17 million, if I'm correct.

John Gossling

Yeah. Yeah.

Vince Valentini

It's almost like why even bother? You're paying down way more than that anyways. Is there any reason why it wouldn't be much higher than that?

John Gossling

Well, you're right. The plan is to repay more than that. So that takes us back to where we had been a few renewals ago. And look, I think it's part of a total package that we took to the bank syndicate and that was a piece of it, so.

But you're right, I don't feel like that's going to be particularly onerous on us because we were planning to do that anyway.

Vince Valentini

Okay. Well, I just want to make sure, I mean, it's not like—

John Gossling

Yeah.

Vince Valentini

—5 percent of what the original principal was three or four years ago.

John Gossling

No.

Vince Valentini

It's 5 percent—

John Gossling

No, no, no. No. And if you look at, we've actually pro forma'd the debt maturity ladder on Slide 7 of the presentation. So you can see where that $17 million number pops in between '24, '25, and '26 before we get to the maturity in '27.

Vince Valentini

And not that you're not going to generate $17 million in free cash flow anyway, plus you've got cash, but just for technical purposes—there's a lot of people following the bonds now, as well as the equity—what is the ability to use the revolver to pay down bank debt? It seems a bit strange to me that you'd take from one bank pocket and put it in another bank pocket, and they would characterize that as being adequate.

Are you allowed to do that? Or is the revolver untouchable until the bank lines are paid down?

John Gossling

No, no. The revolver is subject to availability based on the leverage. So we quote every quarter what the available amount of the $300 million revolver is. I believe it's $285 million or $286 million this quarter, so the revolver has that cap on it. But that's just a leverage cap.

You're right. That's not something that we would want to do. But the revolver availability and what it can be used for is sort of a separate thing. So yeah, the revolver's still there.

Vince Valentini

And any update on—I'll tie these two together—other asset sales processes and then the ability to use those asset sales to buy back your bonds that are now at even lower levels than the last time we talked about it? You can't use all of the proceeds it sounds like, given the new bank covenants. But can you use some of it if you're able to sell any of your noncore assets?

John Gossling

There's an availability that's quite de minimis under the revised package that we can use assets disposal proceeds. We don't need to apply them to repay the term loan. But that's more designed for things like smaller asset sales and surplus pieces of land, or vehicles, or things like that.

So at this point, anything that's material would be swept into the term loan.

Vince Valentini

So you basically have to get the term loan to zero before you can take advantage of where the bond price is now?

John Gossling

I don't think that's quite the way the timing works. But we can get a little more specific on that if you'd like.

Vince Valentini

Okay.

John Gossling

I just don't have the full amendment in front of me.

Vince Valentini

And just, I mean, Adam asked, but I mean, we haven't seen the filing yet. I don't think it's there yet. It's going to be there, though, and we'll—

John Gossling

Yeah.

Vince Valentini

—be able to see the exact ratios every quarter. Can you not just lay out the next four quarters? Is it 4.5 times maximum Q1, Q2, and Q3, and then drops to 4.25?

John Gossling

No. Where we had taken them to back earlier in the year it was 4.75 each quarter, then—well it ramped up to 4.75, then it came down to 4.50 in Q1. And then it went back to 4.25, which is the sort of back to normal, if you want to call it that.

So what we've done is we've pushed it back to 4.75 through Q1, Q2, Q3, and then it starts to ramp down to 4.50 in Q4 and then back to 4.25 for the start of what would be our fiscal '25.

Vince Valentini

Okay. Separate topic; probably still for you, though, John. I'm not quite sure I can reconcile the amount of money spent on programming in the fourth quarter. The cash spend was $180 million versus $161 million in Q4 last year and the amortization was only $140 million. So the cash spend was way above the amort.

How did you spend so much money when everybody was on strike and there wasn't—plus it's a seasonal slow period in Q4 for deliveries anyway?

John Gossling

So—

Vince Valentini

Is this just a lot of the CRTC catchup stuff that disappears as soon as we get into fiscal '24? Or is there something else unusual in that?

John Gossling

No. I'd say it's more—it's absolutely not just a bit more. It's absolutely a case of what was happening last year. So this year I'd say was a bit more normal. And last year, if you look at how the whole

year played quarter by quarter in ’22, it was actually quite a bit lower in Q4 than it should have been. And you saw that come through in Q1, actually, of ’23.

So the increase—we’re just talking about the cash here, not the net—is primarily timing related to some of our big output deals. Those are US. That’s a big chunk of it. Canadian cash was actually down a little bit in Q4, so it’s not due to the catchup. We’ve built that largely. Some of that was earlier in the year, but the output timing is what’s doing it to us.

And again, I mean, we’ve talked about this before. The way that we are invoiced for some of these deals is very erratic. And we’ll get no invoices for two quarters and then we’ll get three quarters all at once. And that’s completely beyond our control. But of course, we’re going to pay our bills.

So that’s our frustration. I know it creates frustration for you trying to understand what’s going on and forecast this. But unfortunately, for whatever reason, it’s just not a steady stream.

Vince Valentini

Okay. So but based on what you just said, Q1 of ’23 had jumped back to more normal levels. So you now have an easier comp in Q1 of ’24? So if amortization is down 15 percent to 20 percent, so—

John Gossling

For sure. Right? Because—

Vince Valentini

—cash outflow would be that same amount in Q1?

John Gossling

Well, especially since that most of the programming reductions we’re seeing are Global prime time and those are on pay-per-play pricing. So that means that if we don’t get delivery we don’t pay for them. And that’s on a relatively short fuse in terms of the cash.

So absolutely, that will get us relief on cash in Q1 that's similar, I would say, to what's happening with the amortization, again, subject to the variability on the way the outputs get invoiced and paid. But I think your main point is bang on, which is that amort reduction will result in a cash reduction.

Vince Valentini

Cool. Last one, which will allow Doug to speak. The 15 percent to 20 percent down on TV ad revenue in the first quarter, is there any way to roughly break that down as to how much of it is just not having an inventory of impressions because you're not getting the programming, versus how much of it is just the lack of advertising demand for impressions that you do have?

Doug Murphy

That's a good question. And feel free to keep asking John questions too if you want, Vince.

I would say it's kind of sort of 50/50, if you want me to kind of pick a lane. Clearly not having a full schedule for the highest quarter of demand is going to give you a pretty significant inventory issue.

On the flip side, and as I tried to explain with my many kind of distortions theme, there's just so much noise out there in terms of the advertising marketplace and uncertainty. So even within categories there's massive variability.

Some CPG players are heavying up and others are—they're long gone and waiting. And some of that's a function of trying to establish brand positioning; when others aren't advertising, strategically investing when your competitors aren't.

But some of the reasons why the competitors aren't advertising is because they're having inventory and packaging issues getting goods on shelves, over-the-counter medicines, et cetera.

Every single category has similar-type issues. Even autos, for example, which is a growth category at the moment, is growing more significantly south of the border than it is in Canada. Why? Well, because

most of the inventory that's coming out of the plants is going to the States and not coming up to Canada. So days of supply in lots in Canada are still significantly lower than what dealers would like to have. And of course, with the walkouts, the UAW, that's further complicating it.

So I could speak for hours on a category-by-category basis as to what the noise is happening here. And so it's all those factors that are on the top line as well.

Vince Valentini

So let me ask one final one then, Doug.

If schedules are back to normal by your fiscal third quarter, as you've aspired to—I know you don't have perfect certainty on the actors strike and nobody does—but if you had a full schedule in Q3, and assuming there's some stabilization in the economy and some of these disrupted ad categories come back even close to normal, it's not going to be anybody's forecast on the Street, to be clear.

But just in terms of a blue-sky scenario, is there any reason you can't get double-digit advertising revenue growth in the third quarter off of a minus 12 percent comp in the prior year and all the shows coming back? If things all worked out is that even remotely possible? Or has there been some structural change in the business that you'll never get back what's been lost in the past year?

Doug Murphy

I don't know if I'd go down the path of double digits. I think there's reason to expect a stronger quarter, relatively speaking, in Q3 versus last year, should we have a full schedule

But even today what we're doing is we're being conservative in our outlook and not assuming meaningful year-over-year growth. I think it's important for us at this stage to be conservative in our outlook and really focus on what we can control, which is the expense part of the equation.

Vince Valentini

Cool. Thank you.

Doug Murphy

Thank you.

Operator

Your next question comes from the line of Drew McReynolds from RBC. Please go ahead.

Drew McReynolds — RBC

Yeah. Thanks very much. Good morning. Just some random follow-ups here. Hopefully I'll take a little less time than Vince on it, but—

Doug Murphy

Drew?

Operator

His line got disconnected. We will move forward to the next question.

Your next question comes from the line of Aravinda Galappatthige from Canaccord. Please go ahead.

Aravinda Galappatthige — Canaccord

Good morning. Thanks for taking my questions. I wanted to sort of come back to programming costs for a second. Given sort of obviously the writers strike is resolved and the comments you've made, Doug, about the SAG, the possible resolution there, how should we think about the prospect of programming costs potentially coming back in the second half? How much room do you have to control that, given there's uncertainty around the longevity of the advertising weakness? That's sort of the more shorter-term question, I guess, number one.

And then longer term, I guess similarly when you look further out, given sort of the terms of your output agreements with US studios, is there any room to if you need reduce your programming costs by 10 percent, or 15 percent, or whatever the number is, when do you get that flexibility? Do the terms kind of give you very limited flexibility in the near term? And then is there a point at which you can potentially renegotiate that given sort of the uncertainties of the business and, I guess, the macro as well?

Doug Murphy

So I'll take both those questions, and John will probably have some more detail.

Our content supply agreements are kind of they're bespoke to each partner and they're staggered in terms of their timing. And so generally speaking, there's a renewal every year of one sort of the other and it's a conversation that we have mutual with our partners to try to grow both of our businesses. And there's always things we're trying to reduce in the cost side of the equation. And where available, there's opportunities to have increased investments to get more premium digital video rights. And so that's a continuous exercise.

And if part of your question is, do we see potential cost savings in foreign; quite frankly, that's where the audiences are really delivered. And so we're more of the view that we need to find cost savings in other line items than necessarily in the foreign programming side of the equation. But we spend a lot of time on our ROI analysis of all of these deals to make sure that they're economically sensible for our company.

And I think I've spoken in the past about the four-corners model that we have confidence that we'll be able to continuously secure renewals in the years ahead because of the value of the content licensing business for the US studios.

As for the inventory coming back, the fact of the matter is the scheduling of our prime-time simulcast shows by our US network partners will, in some ways, follow the macroeconomic backdrop regardless. Right? So everybody's down roughly 10 percent. If you're sports, you're down maybe high single-digits.

But blend it all together and everybody's down around 10 percent, roughly speaking. So they're not going to put a lot of inventory out there on their schedule if they can't monetize it. So in some ways we're going to track that up here on our simulcast side.

I don't know, John, if you want to add anything on how to think about the back half on programming?

John Gossling

Yeah. I mean, Doug covered off the what we call foreign. That's basically Hollywood programming. There's definitely, Aravinda, a bigger opportunity on the Canadian side because it self-adjusts with revenue.

So between what we've seen happening, really, since Q4 of '22 and getting the COVID catchup relief behind us and some likely positive things coming from the CRTC, but it's too soon to talk about that, and part of that is mix of where we spend, but we still spend, I think there's definitely opportunity.

But on the foreign side there's a bunch of different models how we buy the programming. The benefit of what we call what I talked about just before with Vince on the pay-per-play model is if we don't get the shows—and they tend to be simulcast shows, which are very valuable—we don't pay for them.

If we buy other shows on an output deal with a price card on it, then that depends completely on episode delivery, and that's partly up to us when those shows start on our networks.

And then other output deals are time based and they're bulk and once they start they run. Those ones are hard to control the expense, obviously, because it's a straight-line situation on those ones. So there's a mix of things going on in there.

The one thing we're not really doing is we're not going out and buying shows a la carte because that's where we have the most control is to not spend any of our programming dollars on additional shows that are above and beyond our output.

Aravinda Galappatthige

Thanks, John. And just a quick follow-up on I think on your conversation on Vince's questions about the cash programming spend. I mean, the quarter aside, when you sort of look at the full year, the cash programming cost was up over 20 percent versus the amortization of 8 percent. I mean, that's a fair, I mean, substantial delta when you consider this is an annual number.

Even on a full year basis, I mean, is it reasonable to think that there would be kind of a reversal of that in fiscal '24? I wasn't 100 percent clear on that.

John Gossling

So it's a subject of many, many hours of debate and analysis on my team here at Corus. I'd say the starting point is that the amort and the cash should be similar. So just take all the timing issues and invoicing issues and building of CPE to make up for COVID underspend, take all of that out of the equation, the numbers should be similar, but there's always going to be some pre-spend on Canadian. And there's other elements of the way the cash works in the output deals versus the way the amortization works.

So I think structurally long term, you're going to see the cash higher than the amort, but it should only be to the tune of $20 million to $30 million a year. It shouldn't be what we've seen. Because we've

been going through this prolonged catchup—we had a catchup in Q1 last year—that was then distorting things if you look at the number from ’21, or ’22, so. And COVID screwed everything up completely.

So I get your frustration. It does drive our team crazy too trying to forecast this. But I think we’re getting to a much more stable place. But there’s always things that happen that are just, as I said, beyond our control. And frankly, we’re not going to pay bills that we don’t have. Not—

Aravinda Galappatthige

Okay. Thank you. I’ll pass the line.

Operator

Your next question comes from the line of Drew McReynolds from RBC. Please go ahead.

Drew McReynolds

(unintelligible)

Doug Murphy

Drew?

Drew McReynolds

Can you hear me?

Doug Murphy

Yeah. Yeah. There you are. Got you.

Drew McReynolds

Yeah. Okay. Perfect. Sorry about that. Not sure what’s going on. Just a couple of random follow-ups from my perspective. I think just first with respect to Q1 here on the flow-through of costs—and maybe a question for John here—obviously a Frankenstein schedule, all of the dynamics, are you able to

just kind of give us some kind of range for TV margin here in Q1 just to kind of help us kind of set up the rest of the year?

Secondly, John, just the 0.25 percent roughly differential between reported leverage and covenants, I'm assuming that hasn't changed?

And then just the final one here. In terms of restarting the TV schedule—thanks for all that commentary, Doug, and helpful time frame here—is that three-month lag between resolving something like this and a return of kind of a normalized schedule, is that fairly typical? So if we kind of tidy up before Thanksgiving in the US, or maybe go beyond, is that something that typically we should assume is the lag here? Thank you.

Doug Murphy

Why don't I take that first then, John, you can answer the other one.

So just to give a little more detail. Yeah. All the studios and the streamers, too—I mean, let's be clear—this strike isn't helping anybody. I mean, the streamers are now running out of their new big shows as well, so there's a lot of alignment around getting going. And so once we were able to get the writers strike resolved, the studios have been just cranking on the writing rooms right now, which is great. And now they're trying to get ready to roll on the scripted products.

So on the returning shows, for example comedy shows, six to eight weeks to shoot an episode and they'll stagger those episodes. Right? So they'll shoot them every week and then they go into the edit room and et cetera. So those could roll pretty quickly in December and through Christmas into January.

The dramas are a little bit longer, but I'm now talking about returning dramas—again, not pilots or new series—returning dramas, of which we have a lot like NCIS, FBIs. Those are eight to ten weeks in terms of their process to get in the can.

So you can see where they're going to move really quickly once they get resolution—if they get resolution on the actors strikes to get those shows back, produced, and ready to roll.

So that's why we're thinking Q3 is a reasonable target.

John Gossling

Drew, I'll start with kind of what you said at the end of your question about TV margins. I would not take Q1 to be any indication of what the rest of the year might look like because it's such a weird quarter just in terms of program costs and obviously top line.

But look, there's a world where with the savings on the programming costs that we mentioned in the outlook that we could have a relatively flat margin in TV in Q1. But it's not really designed that way. It's totally an outcome of all the different pieces that are moving around here.

So it's obviously hard to predict, but that's kind of what we see right now is that we could be flattish on margin percentage.

Drew McReynolds

Okay. No, that's great, John. And then appreciate that and fully understood it's just an absolute wonky quarter, but helpful just for modelling here.

And then the 0.25 percent differential, just no change there?

John Gossling

Oh, yeah. Yes. That's still a very valid—that's why we gave the pro forma number because, of course, the LTM segment profit from Toon Boom was still in the number and the debt's been reduced from the proceeds. So we'll give you that pro forma number now quarterly going forward until it rolls out.

So yeah, the 0.25 percent bump is still the right way to look at it.

Drew McReynolds

Super. Thanks very much.

Operator

Your next question comes from the line of Maher Yaghi from Scotiabank. Please go ahead.

Maher Yaghi — Scotiabank

Yes. Good morning. Thanks for taking my call. I wanted to ask you when I look at the CRTC, I mean, my understanding in terms of policy and regulation is that it's supposed to be fair and reasonable for all the players in a specific industry. And regulation is not supposed to bring one of the parties down to the ground in terms of because of regulation.

Is there any legal avenues that you can utilize to extricate yourself from some of the regulation that you're facing on the CRTC side? Because evidently you're doing everything you can to bring down your cost structure, reorganize, restructure your debt, cut your dividend, and that regulation is just bearing down on you significantly. So is there any legal ways that you can deploy to stop having to deal with that regulation for a certain period of time until the CRTC might review the regulation themselves because it takes forever?

Second question I had is what's happening with Eastlink. Can you give us some of the takeaways you have had from that exercise? Is there any discussions with other BDUs in Canada that can have a similar outcome like you had with Eastlink recently?

And third question is, Doug, when you look at the visibility that you have on the advertising, you talked about Q1 being difficult. Without talking about … without quantifying, just I want to ask you about the visibility, the margin. Is it getting better, same, or worse than you had when you came into Q4? Thank you.

Doug Murphy

Okay. I'll go back to (unintelligible). Visibility, I would say, is the same, which is limited, so nothing's changed. And I don't expect it to change until and we see the resolution to the actors strike. That should be kind of the beginning of some, I hope, better visibility.

On the Eastlink file, we obviously won't talk about commercial negotiations on this call. But I can tell you that it's playing out. We're quite happy with what's happening now. We're getting growth with other BDUs in that territory and STACKTV as well. So we're pleased with the outcome.

And subscribers have options to access our channels through a number of different means, either through other BDUs or through STACKTV. So that's my answer to that question.

Just as regards to the CRTC and the regulatory, I guess the comment I would make there is that decision, or that opinion, or that outcome on the 11th of October, as I said in my comments, it's the most substantive move towards regulatory change our company has seen in years. And in that, there was an acknowledgement that we're Canada's largest non-vertically integrated broadcaster and that is a very important distinction and it's one that we have been trying to make for years.

And so providing more flexibility for our spending on CPE, on PNI, is very helpful for our content planning. It helps us conceptually to make the kind of shows that really work for our networks because we want to produce content for our networks that drive audiences.

And so we're going to wait until we get the final answer from the Commission and then work accordingly to iterate our strategies, given this new decision.

Maher Yaghi

Great. Thank you for that. Maybe just to go back on Eastlink. Yeah, I mean, the understanding is that BCE has probably picked up some of those subs that were disgruntled by the decision.

But I was more asking a question relating to other BDUs in other parts of the country who are facing a decline in subscribers. And on the TV side, have you had any issues renegotiating BDU distribution contracts with the likes of Telus or Cogeco or, I mean, the other guys that are seeing the same pressure that Eastlink is having?

Doug Murphy

Short answer would be no. We work hard to stay very close to all of our BDU partners. Obviously, Corus has always been an innovative partner with our BDUs, and we get across the table, again, when the timing is such that we'd have a renewal. And we've always been able to successfully find an outcome from both parties that work for us.

So again, are there going to be new and different ways of coming to conclusions on carriage agreements in the quarters and years ahead, given the circumstances of the industry and consolidation and such? Likely.

But again, we're trying to be a good partner and trying to make sure that everybody realizes that our entertainment channels punch above their weight from a share of subscription revenue perspective. When you look at audiences over the pie of revenues, sports disproportionately consumes those dollars. And while sports is an important part of the bundle, more than half of Canadians don't watch sports and many of them watch our services.

So it's a thoughtful and purposeful conversation, but at the moment Eastlink is kind of like sort of the only situation like that at this time.

Maher Yaghi

Okay. Thank you.

Operator

Your next question comes from the line of David McFadgen from Cormark. Please go ahead.

David McFadgen — Cormark

Hi. Yeah. Most of my questions have been answered, but just on the sub revenue, it was down 1 percent in the quarter. I thought it might've been down more than that. Were there any abnormal adjustments in the quarter that would cause that?

John Gossling

Yeah. There were several renewals, actually, in the quarter that bring with them some retro revenue. The normalized number, David, is minus 4 percent for the quarter.

David McFadgen

Okay. Okay. And then can you comment on the outlook for the distribution and merchandising business for '24? Do you think you would have another—or a double-digit year of growth?

John Gossling

Look, it's going to—a couple things going on there. One is there's just less demand generally for third-party content from some of the platforms and that's a worldwide effect.

I think the other practical consideration for us is with our CPE bubble starting to come down, and also that effect of lower regulated revenue rolling through, we're just not going to need to spend as much on Canadian and that's going to affect our own properties as well. So I guess the short answer is no, we're not expecting that.

It's going to be a tougher go now. Obviously, the contribution from the content business is lower than what we would ever see from TV advertising.

So yeah, it's going to have an impact, but I wouldn't say it's going to be that material.

David McFadgen

So maybe if I can just take that one step further, do you think you'd see a flat year? A modestly up year? Any comment there?

John Gossling

So based on the current slate, no, it won't be.

David McFadgen

It'll be down a bit?

John Gossling

Yeah.

David McFadgen

Okay. All right. Thank you.

John Gossling

Thanks.

Doug Murphy

Thanks, David.

Operator

Your next question comes from the line of Scott Fletcher from CIBC. Please go ahead.

Scott Fletcher — CIBC

Yeah. Good morning. Most of mine also answered as well. So I'll just ask a quick question on STACKTV. Last quarter, there was some discussion around new marketing strategies and feeling more confident about how to approach the market.

Any update on how that shift in strategy might have gone? And understanding that it's obviously a tough climate with the lack of new deliveries.

Doug Murphy

Yeah. It's interesting. I mean, we're very—we still remain very optimistic about our STACKTV target of getting to 1 million paying subs. Yeah. Obviously, the writers strike and actors strike has not helped. But actually, the service has been extremely resilient in the face of that, which is interesting.

We've purposefully kind of dialled back some of the marketing investments, given the lack of new content, which is sensible. But we're also learning that there's nothing like a hit show to help drive audiences and acquisitions. So Rick and Morty, once again, is proving to be an important acquisition driver on STACK.

And then from a time spent perspective, we're seeing a lot of our hit shows continuing to perform extremely well. One of our based on a true story is one that you might've heard about, the serial killer on the podcast, which is performing great. And then some of our other shows that help to drive longer viewing, such as the lifestyle or entertainment shows—Below Deck, for example—are performing extremely well also.

So it's a great product, and we still remain optimistic that there's an exciting future business there as part of our Video First strategy.

John Gossling

The other thing, Scott, is—and we haven't talked about it at all today or been asked about it—but another important part of both STACK/Amazon Prime Video and our kind of stream, of course, generally is Global News and it's performed incredibly well, both from an audience perspective and the revenue as well.

So a shout-out to our news team because they've been working really hard to get their product and their coverage into as many places as we possibly can.

Doug Murphy

Yep. I second that. And also just a public service announcement, the Hallmark Countdown to Christmas coming soon, once we get through Halloween. So that'll be another big audience driver, as is our custom here at Corus Entertainment.

Scott Fletcher

Okay. Thanks. And then maybe just a quick follow-up there. You mentioned, there was sort of passing comment earlier that you're willing to still invest in the digital distribution rights. Is the ROI conversation, does that still make sense given what the subscriber growth has looked like? Is that still—are you still looking at those investments?

Doug Murphy

Yeah. Well, the digital video growth is still happening in the market at the moment. The challenge we have right at this point in time is that there's a ton of inventory. That was kind of what I was alluding to in my comments. Right? So everybody was a purist in their subscription video on demand only, no ads a few years ago. Now everybody's dropping an ad layer in and they're all raising their prices on the ad-free sub so they can try to get more inventory and scale on the ad layers.

So what we have just at this moment is a lot of premium digital inventory in the marketplace, both because supply's increased significantly, but also because demand has been diminished, given the macroeconomic distortions as I described.

So we expect that to change and have the supply/demand disequilibrium kind of tighten up in the coming quarters. But no, we're very optimistic that the premium digital video opportunities are meaningful.

And you're right. It's about trying to just do the right math on the incremental cost of the acquisition. But because we have such a meaningful established linear-channels pay TV business with our partners and, increasingly, they value our partnership in the market and they value, quite frankly, our revenues that they get from licensing content to us, provided that they don't need their content for some other purpose in the marketplace, we'll look at those opportunities.

Scott Fletcher

Okay. Thanks.

Doug Murphy

Scott.

Operator

There are no further questions at this time. I'd now like to turn the call back over to Mr. Doug Murphy, President and CEO, for closing remarks.

Doug Murphy

Well, thank you, Operator, and thank you, everybody. We look forward to speaking to you next quarter.

Take care now. Bye-bye.

Operator

Thank you, sir. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a lovely day.