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# Quad/Graphics, Inc. (QUAD)

Q1 2020 Earnings Call

## CORPORATE PARTICIPANTS

### Kyle Egan

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

### David J. Honan

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

### J. Joel Quadracci

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

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good morning, ladies and gentlemen, and welcome to Quad's First Quarter 2020 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 note, this event is being recorded.

I will now turn the conference over to Kyle Egan, Quad's Director of Investor Relations and Assistant Treasurer. Kyle, please, go ahead.

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### 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. Joel will lead off today's call with a business update related to COVID-19, and Dave will follow with a summary of Quad's first quarter 2020 financial results, 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 the 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.

The year 2020 will go down in history as unprecedented for our company, our nation, and our world. We started the year with a strong first quarter, building on the momentum of our solid fourth quarter performance. However, we started seeing the initial signs of disruption from the COVID-19 pandemic during the last few weeks of the quarter which required swift, decisive action to fortify the business. Since then, we have seen a meaningful impact to our business in certain end markets, particularly in retail. As we continue to manage through the pandemic, Quad's main priority is protecting our employees' health and wellbeing while also protecting the company's financial health, thereby protecting our ability to perform well for our clients on into the future.

Early in the quarter, our crisis management team, together with company leadership, began executing on our business continuity plans with a strong sense of urgency. We followed guidance from the CDC and local health authorities as well as federal and state governments, and best practices and recommendations from our healthcare subsidiary, QuadMed, which has proved to be a tremendous asset during this critical time.

Early on, we shifted approximately 2,000 administrative employees to work from home within a very short timeframe to support social distancing while also testing our IT infrastructure. We then quickly ramped up our work-at-home staff and, today, we have well over 3,000 employees who work remotely on a consistent basis.

In our manufacturing facilities, we launched our Safe-at-Work Program to protect the health and safety of our production employees. Our program, outlined on slide 3, includes regular communication and education on how employees can stay healthy; protocols for cleaning and disinfecting equipment, tools and common areas; daily temperature checks, which we are in the process of rolling out company-wide; and guidelines for social distancing. Given the scale of our equipment and our extensive use of automation, our production platform naturally lends itself to social distancing. However, our continuous improvement team modified processes and adapted workspaces were necessary. To complement these efforts, our in-store marketing group produced signage and floor graphics to remind employees how to work safely apart.

Our Safe-at-Work Program also includes a well-defined process for assessing each potential COVID-19 case using a rapid response team comprised of our Quad HR professionals. This team helps transition impacted employees to self-quarantine, and performs rigorous contact tracing. The rapid response team also reports out daily metrics to our executive team, so we understand the real-time impact of COVID-19 on our workforce. To-date, the number of confirmed and suspected cases of COVID-19 remains relatively low among our employee base.

As this pandemic evolves, we will continue to take care of our employees to the best of our ability while also taking swift action to mitigate risk and implement cost reductions that protect our balance sheet and preserve cash flow and liquidity. Our leadership team has a deep experience managing through industry and economic disruptions. Our disciplined approach includes treating almost all costs as variable to help offset the impact from volume fluctuations over both the short and long-term. We made a number of tough cost reduction decisions that Dave will detail in his section, and we communicated those decisions to our employees and other stakeholders quickly and transparently.

Now more than ever, communications are important during this disruptive time, and we are using technology to strengthen inter-connectivity with each other, our culture, and our values. I post regular updates from my home office to make sure all employees hear directly from me on my perspectives and insights into why we are making

tough decisions; to remind everyone of the good news stories that are happening every day at Quad during this crisis; to encourage employees to use Quad's abundant resources for their physical, emotional, financial and social wellbeing; and to provide the vision forward in a post-COVID-19 environment where we will be stronger than before the pandemic.

Throughout all this, I continue to be impressed with our employees' unwavering spirit of innovation, not only to help our clients solve problems but also to help each other at this time of crisis. For example, as shown on slide 4, employees in our CRT ink manufacturing division began formulating hand sanitizer for use in our facilities across the country. Employees in our Direct Marketing group designed a disposable, non-medical facemask that has been mass-produced on our existing printing press equipment. We were able to outfit every employee throughout our nationwide network with a mask in our initial production run. Since then, we have continued to refine the design for easier production, self-assembly and wearability, and are now in our third version which is starting up production today and will be distributed throughout our network of facilities immediately.

COVID-19 has impacted our clients in a variety of different ways, depending on vertical market and product type. For example, department stores are having a particularly tough time right now given closure orders, and subsequently have pulled back in media spend. Nevertheless, the pandemic has also provided new opportunities to leverage our platform and innovate new solutions to help clients maintain business continuity and consumer engagement during this period of uncertainty.

This is where our Quad 3.0 strategy really differentiates us from other printers and marketing agencies. As a marketing solution partner, we are focused on solving clients' marketing and process challenges. Our strategy is informed by listening to our clients' needs and developing solutions to help reduce complexity and costs to improve marketing spend effectiveness and profitability. Because we have always made it a priority to build relationships at all levels within the clients' organization, we can better understand, anticipate and solve their problems.

On slide 5, we show a prime example of our Quad 3.0 innovation and action. We created our COVID-19 in-store marketing tool kit to help brick-and-mortar retailers provide visual cues on social distancing to keep shoppers safe. The tool kit features standalone signage and displays, floor graphics, checkout protection shields and cart ramps among other products, and is packaged by our experts to be install-ready. The tool kit has been an overwhelming success and is in use by retailers at thousands of locations throughout the country, including grocery, home improvement, convenience and drugstores. I'm pleased to share that this effort alone has created in excess of \$5 million of incremental revenue for our company.

Through our Quad 3.0 strategy, we've also been able to help our clients be more efficient and effective at content creation and production at a time when they have had challenges staffing those critical functions. We're recently engaged by a major clothing and accessory retailer to help with studio photography for its multiple brands. This retailer was experiencing labor shortages due to the pandemic. We're immediately able to step in and start photographing 500 samples per week for the retailer's e-commerce sites.

When the pandemic subsides and clients begin to rethink their operations in the new normal, including what functions should and should not remain staffed in-house, we will be ready in position to help offer them quicker path to success through the use of our content creation and production services.

During the first quarter, we are pleased to be selected by the White House and CDC to print a direct mail piece promoting coronavirus guidelines for America. We printed 42 million postcards for US households in record time.

As we continue to manage day-to-day operations, we are also planning for the reopening of the economy under multiple scenarios based on our clients' evolving advertising and marketing plans. Our Quad 3.0 strategy will serve us well, especially as our clients rethink how to operate in the new normal post-COVID-19. However, between now and then and as the economy begins its gradual recovery, we will continue to live in a new abnormal where economic activity may still be heavily and unpredictably impacted by virus hotspots. In this new abnormal, forward-thinking agile companies like Quad will have the advantage. Our Quad 3.0 strategy, which is focused on solving client challenges, combined with our ability to move quickly and decisively, will help clients successfully adjust to a new changing media consumption patterns and consumer buying habits.

Until then, uncertainty continues. We will closely monitor the COVID-19 pandemic and its impact on our clients in the worldwide economy while protecting our employees' health and the company's financial strengths, thereby serving our clients with high quality on-time delivery.

Before I turn the call over to Dave, I want to recognize and thank employees for going above and beyond during this challenging time, when every aspect of their personal and professional lives has been disrupted. I regularly receive client letters and emails praising our employees, and even received a video thank you from David Remnick, the Editor of The New Yorker magazine, who said, I just want to thank all our friends at Quad who have done an amazing, amazing job at this very strange and difficult time. The idea that we can put out The New Yorker week-after-week in print moves me beyond measure, and I know that's the case with everybody at the staff. It means the world to us. All the issues of The New Yorker that have come out in the last several weeks are some of the best work we've ever done, but that would be only possible with you.

I, too, thank our employees who continue to show our clients why we are a true partner in their business, and how that they are Quad proud and dedicated to the success of our company.

With that, I will now turn the call over to you, Dave.

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## David J. Honan

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

Thank you, Joel. Good morning, everyone.

As Joel mentioned, our first quarter performance was strong and better than expected, up until mid-March when we began to feel the economic impacts of the pandemic. We were performing ahead of plan, both operationally and financially, and we're recognizing more and more incremental benefits of our Quad 3.0 strategy, helping to offset organic print decline.

Our cost reduction program and productivity improvement trend from the fourth quarter continued to favorably impact our first quarter results. The investments we made in 2019 to increase hourly production wages and increase investments in automation continue to drive productivity throughout our entire platform. Additionally, customer service performance was exceptionally strong, with high-quality and on-time delivery metrics and great safety performance in our facilities. This operational performance was setting the stage to finish the quarter strong.

In mid-March, customer demand substantially weakened due to the economic impacts of the pandemic. We estimate that certain print product lines decreased by approximately 30% on average over the back-half of March. Almost our entire customer base has been impacted, but none more severely than brick-and-mortar retailers who've closed stores in response to safe shelter-at-home orders.

Given the sudden decline in print and print-related demand, the lack of visibility about future demand as well as the speed of reopening of the economy, we withdrew all financial guidance on April 2. We will evaluate providing guidance when we have more visibility into the economic recovery.

As Joel shared, we acted with great care and agility to keep our employees safe during the pandemic, and make tough decisions associated with protecting our financial flexibility through preserving cash and liquidity. We acted swiftly to align our cost structure to match lower demand for print. Slide 6 details the actions we took to control costs, conserve cash and protect liquidity. We suspended all domestic and international travel. We delayed most capital expenditure projects and expect capital expenditures to be approximately \$60 million now in 2020. This is a decrease of 45% from 2019. We implemented a hiring freeze, and established a COVID-19 temporary furlough program through which employees take an unpaid leave of absence. Eligible furloughed employees receive company paid medical benefits, so no employees without medical coverage at this critical time.

We also implemented temporary salary reductions for more than 750 of our leaders, including a 50% salary reduction for our CEO and a 35% salary reduction for named executive officers. We temporarily reduced director fees by 50% at the recommendation of our Board of Directors.

We suspended the use of vacation and vacation payouts. We suspended production at several manufacturing facilities where the effects of the pandemic impacted our ability to operate.

We increased borrowings by \$100 million to increase cash on hand to \$208 million at the end of the quarter, and provide sufficient liquidity to the business over the near-term. This action, combined with up to \$636 million of maximum available borrowings under our revolving credit agreement, allowed us to finish the quarter with significant financial flexibility.

And lastly, the Board of Directors made the proactive decision to temporarily suspend the company's quarterly dividend. This action conserves approximately \$8 million of cash each quarter. We remain committed to paying a dividend over the long-term and will seek to resume a dividend following the stabilization of our operating environment.

All told, we temporarily reduced costs by approximately \$250 million on an annualized basis, including reducing our largest variable cost category, wages and benefits, by over one-third of pre-pandemic levels to help partially offset the significant reduction in net sales.

I'm extremely proud of the Quad team for the speed and agility of their reaction to this pandemic. Most of these actions were implemented in advance of our clients notifying of their intentions to reduce those volumes. This agility was key to conserving cash and liquidity at an unprecedented time of uncertainty. It helped ensure a stronger financial position as of March 31.

Slide 7 provides a snapshot of our first quarter 2020 results. Net sales were \$823 million in the first quarter, down 14.4% from 2019. Organic sales, which exclude acquisitions and divestitures, declined 13.3% during the quarter after excluding the impacts of the sale of the Omaha packaging plant. The organic sales results reflect ongoing print industry volumes and pricing pressure, including the initial impact from the COVID-19 pandemic and a negative 0.4% impact from foreign exchange.

Adjusted EBITDA was \$75 million in the first quarter as compared to \$78 million in 2019, and adjusted EBITDA margin improved to 9.2% as compared to 8.2% a year ago. The variance to prior year primarily reflects the impact from the organic sales decline of 13.3%, a \$9 million decrease in print profits from the reduction in market prices



for paper byproduct recoveries, and a \$4 million increase in hourly production wages due to strategic investments made last year to increase starting wages. These impacts were partially offset by a favorable \$9 million net noncash benefit from a change of vacation policy; a favorable \$8 million reduction in worker's compensation reserve from improved production safety trend; and savings from cost reductions, many of which I outlined earlier.

Free cash flow increased by \$116 million in the first quarter. The increase in free cash flow is primarily due to improvements in working capital and a \$16 million decrease in capital expenditures. As a reminder, the company generates a majority of its free cash flow in the fourth quarter of the year.

Slide 8 includes a summary of our debt capital structure as of March 31. During the quarter, we reduced debt net of excess cash by \$49 million due to strong free cash flow and \$41 million in cash provided by the sale of our Omaha packaging facility. We also took two specific actions to further reduce our interest expense and net debt. First, we completed a \$38 million tender of our private placement notes at par value. We estimate the tender will save just over \$1 million in annual interest costs. As of March 31, \$31 million of the private placement notes remain outstanding. Second, we repurchased \$5 million of our 7% senior unsecured notes at an 18% discount, helping to reduce outstanding debt. As of March 31, \$239 million of the unsecured notes remain outstanding.

At the end of the quarter, our debt capital structure was 57% fixed and 43% floating, with a blended interest rate of 4.8%. We ended the first quarter with a debt leverage ratio of 3.0 times, which improved from 3.12 times as of December 31. While this leverage range is above our long-term targeted leverage range of 2 to 2.5 times, we are pleased with the progress we made to reduce our net debt levels and overall leverage since the end of the year. Our primary use of cash will continue to be debt reduction. We maintain significant liquidity as of March 31, including \$208 million of cash on hand and up to \$636 million in unused capacity under our revolving credit agreement, which is subject to certain covenants.

We have strong and trusted banking relationships that extend to the highest executive levels of our banks. Our top six banks in the credit agreement represent approximately two-thirds of our committed capital. And I'm proud to say that our relationships with these institutions average more than a quarter of a century.

We believe our available liquidity combined with the strength of our banking relationships, our agile cost to – our agile approach to cost management, as well as the success of our Quad 3.0 strategy will help provide substantial financial flexibility to adjust to current uncertainty in the operating environment. We'll continue to make necessary actions to respond effectively to the impacts of the rapidly evolving pandemic. Our Quad 3.0 strategy and integrated marketing offering can help our clients in new ways as we all learn to do things differently during these times.

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

## QUESTION AND ANSWER SECTION

**Operator:** Thank you. We will now begin the question-and-answer session. [Operator Instructions] Our first question today will come from [ph] Jamie Clement (00:22:49) [indiscernible] (00:22:50). Please, go ahead.

Q

Hey, gentlemen, good morning. Can you hear me okay?

**J. Joel Quadracci**

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

Yeah, Jamie. How are you?

A

Q

Yeah. I'm doing okay. Thanks for asking. So, Joel, first question for you. I think I looked this up, I think it was Winston Churchill who said – and I'm paraphrasing a little bit – never let a crisis go to waste. And obviously, you discussed adjustments to the capital spend and that kind of thing. But can you take us kind of through, with that said, some of the things strategically where you might have said, you know what, maybe now is the right – not the right time, versus some other kind of strategic directions where you said, you know what, now we got to redouble our efforts?

**J. Joel Quadracci**

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

Yeah.

A

Q

This is extra important right now. We're going to come out of this stronger than ever.

**J. Joel Quadracci**

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

Yeah. Well, I think first of all, whenever we see a crisis coming, we've learned. I've been in this job since 2006, and you think about the first two years are fun and then you had the great recession kick in, and then you had all the stuff that's going on with the print environment.

A

But I'll kind of answer that in two ways, both internally and externally. But I think what happens in normal times is lots of good ideas get formulated and implemented, but it tends to be more incremental. And I'd say that, in the past year, we've made some significant investments in our IT infrastructure because I wanted to kind of make use of more video conferencing, being able to do video blogs without taking down the network. And we finished that, probably perfect timing, last fall. So that now, as we pushed literally with a three-day notice 2,000 people to work from home to really test it further, it's worked out remarkably well. And I think most of the world is figuring out that



this all the video technology has changed so much, that you don't need two IT people standing over your shoulder to get a videoconference going. So, internally, we're pushing that very hard.

I'd also say that we end up making tough calls on cost reduction and capacity planning when the crisis is here, and we tend to find out that while it worked better than we thought or we can do more than we thought we could before. And so, that will go into, as we see the economy open up, not being bashful about in terms of how we manage that capacity on a go-forward basis.

On the external side, what I'll tell you is the 3.0 strategy – I've been saying this for years now – first of all, its working is really about Quad transitioning from selling people print products to really get involved in helping people solve problems when it comes to media planning and placement, campaign design, and then execution across all channels in media, which has been very fragmented during the past decade with the advent of the big holding company model and all the new sort of places you could spend your money. And so, while we've made huge headway in normal times with our client base on how we participate with them – I've talked about the 80-plus locations we now have where we have over 1,200 people working within people's marketing departments – some of the conversation tends to also get kind of [indiscernible] (00:26:04) incrementalism.

And I think that now that people send so many people home to work from home, every business is reevaluating. When the economy opens up, it's not about when we bring things back; it's what do we bring back and, almost more importantly, what do we decide not to bring back. And so, we see opportunity in terms of being that partner to take over execution and planning and media planning for many different customers so that they don't have to do it anymore and focus on merchandising and overall strategy. So, I see this really as a time where we can leap forward and speed up the transformation in Quad 3.0.

Q

Okay. Joel, I appreciate that. And just can you help us just understand a little bit more the seasonality of the business lines that you provide and solutions that you provide brick-and-mortar retailers? And really, what I am getting at is the first half versus second half seasonality. And I'm just trying to get a sense of, if we make an assumption on when the economy starts to reopen up again and people can go back to stores and that kind of thing, I mean sort of how much business was at stake in the first half of the year versus why I've always perceived as more of a stronger second half of the year?

**J. Joel Quadracci**

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

Yeah, yeah. Let me start and say that, clearly, the most impacted has been retail.

A

Q

Yeah.

**J. Joel Quadracci**

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

I mean, one day, you get a phone call from a huge retailer who says, the next day, every store in the country will be closed.

A

Q

Yeah.

**J. Joel Quadracci**

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

Surely, there's – it creates a rapid pullback. And so, the first half – as you know, we're a second half seasonal company...

A

Q

Yeah.

**J. Joel Quadracci**

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

...for retailers, for catalogers, magazines tend to be a little bit more spread out through the year. But the reason I kind of refer – everyone over uses the new normal. That's why through in sort of the descriptor I'm using with people, which is until you get to the new normal, we're in this new abnormal where the economy is trying to open up, things are going to happen in fits and starts. We are already seeing some of the big box companies, such as Kohl's and DICK'S Sporting Goods – this is public information – starting to open up their stores. But what we hear from our clients is kind of running the gamut of a little bit gun shy because there's concern about boy as this opens up, does a spike happened, therefore did we aggressively market too much? Then, we accuse buyer consumers of causing that spike. So, I'd say there's trepidation. And again, it just feels like this new abnormal.

A

And once – as we sort of people get comfort with how all the new safety procedures are being followed throughout the country, then you'll start to feel like, okay, now, we can get more visibility. But until then, it's really tough to get visibility. We can't just say, well, this store is opening all their stores, this company is opening all their stores; therefore, marketing comes back right away. That may be true with one, but not the other. It's kind of all over the board.

Q

Okay. Let me ask you a question on the inserts business. I have noticed here in New York that most of the grocery stores, while still open and lines' out the door and that kind of thing, have largely suspended their circulars. And I have asked the managers and they said, the reason we're doing this is because we don't want to promote products that we don't necessarily know we can keep on our shelves. So, that's an area of the economy that's seemingly healthy, if not...

**J. Joel Quadracci**

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

Yeah.

A

Q

...even stronger; yet, they can't buy circulars because they don't have confidence they can keep stuff on their shelves. So, any sense – first of all, do you think that's an accurate statement? And second of all...

**J. Joel Quadracci**

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

Yeah. It's...

A

Q

...any signs of improvement there?

**J. Joel Quadracci**

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

Yeah. I mean, I think like I said, it's kind of all over the board. When you talk about the grocery sector, they really have had a hard time predicting what they can have on the shelves. I mean, only now do you see the shelves full of toilet paper. The last month or so, it's been empty and we have had a lot of that. Now, the next phase is what we're hearing through multiple partners is the shortage of meat products. So, there's certainly been a bunch of that.

On the other hand, some of the big grocers who carry a lot of other goods like hard goods...

A

Q

Yeah.

**J. Joel Quadracci**

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

...a couple of weeks ago when the \$600 checks started hitting people's bank accounts, they told us that they started seeing flat panel screens flying off the shelves. So, there's some of the impacts of the financial incentives here or relief might be also helping things, but that will sort of play out over the long-term.

So, again, I think it's everyone's just trying to navigate a very blurry future. It's very hard to see, for the next month I would say, how people can predict what products they can count on, how fast their stores come back; but it will start happening. And my big concern on retail inserts is just that the pressure of the newspaper industry is under as a result of all this.

A

Q

Yeah.

**J. Joel Quadracci**

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

And so, you worry about decreased circulation, which is the carrier for the retail insert. But as we've said before, we've been dealing with that decline anyway and we've been adjusting our platform, but also growing our direct mail product for those people because ink on paper does matter to them. And oftentimes, we hear from them that

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we need to find more print replacement because we can't do circulars in this certain market because the newspaper closed. And so, the marketers still have a strong sense that there's offline and online have to come together. And yes, there's going to be shifts for different structural reasons, but we know how to manage that. And we continue to, where we can, pivot to wherever value add can help our clients market very effectively and efficiently to grow their business. That's what our whole Quad 3.0 model is based on, is how do we help you grow. We happen to just be founded in print where we have a lot of capability to execute, but we built out a whole platform here to help you on your spend elsewhere as well.

Q

Okay. So, just delving into that a little bit more, Joel. So, as part of the Quad 3.0 strategy, let's say, a grocery store chain in a city where a newspaper is closed. Can you give us a little bit more specific details in terms of what does that session with that customer – that strategy session sound like? I mean, is it direct mail that you're – what are the kinds of things you discussed? Could you just go into a little bit more detail [indiscernible] (00:32:50)?

**J. Joel Quadracci**

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

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Yeah. I mean, yeah, it's a combination of things. As you know, with our Ivie acquisition, they do a lot of media buying Vertis acquisition, we had those capabilities, too. We've only strengthened them. And it really comes down to what's the right mix of things. So, if you have a fall-off in one place – because it's not a nationwide situation, it happens in pockets.

Q

Right.

**J. Joel Quadracci**

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

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...we're able to shift and say, hey, let's try and make up for this. It may not be the perfect mix of what you wanted, but at least we're making up and still driving traffic. So, it's a combination of direct mail shifting to other paper, shifting to things like our partnership then with Valassis, who does a lot of couponing through the mailbox.

Q

Yeah.

**J. Joel Quadracci**

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

A

We print a lot of that for them and place a lot of it through them.

And so, it's – and then obviously, digital. And so, we work with them on, okay, well, how do we also then shift to some digital spend or radio TV to kind of make up for that? Because ultimately, it's about one ROI. When I spend a dollar on marketing in a region, does it produce \$5 or \$6 of revenue? What's the trajectory? And if it's going the wrong way, how do we adjust to make up for it? So, it's sort of a whole portfolio of things you have to work on with the client, and it's always evolving.

Q

Okay. And then lastly, Joel, if I may. And, Dave, I don't know if you want to chime in here at all. What do you all need to see to think about reinstating the dividend?

**J. Joel Quadracci**

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

A

Well, since Dave really wants to chime in here, I'll turn it to Dave.

**David J. Honan**

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

A

Thanks, Joel. We mentioned in our comments, just above stabilization in the operating environment. And as we currently see our operating environment, there's a lot of uncertainty, and I walk through this...

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Sure.

**David J. Honan**

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

A

...my prepared comments. But when you look at volume, and the comment I made about volume in the back-half of March being down approximately 30%, we've seen a similar trend in the April. We're closing our April...

Q

Sure.

**David J. Honan**

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

A

...booked on April that we saw a similar trend there. And really, what's the most impacted of our customer base as we've mentioned is the brick-and-mortar retailers, who had to take stores offline. As those stores start to reopen, we believe the near-term impact on our demand should lessen. In the meantime, we'll just keep adjusting our cost structure, but that only partially offsets the impact of volume. And I think what you'll see from us is just an acute awareness of how of how to manage cash flow and how to manage liquidity, so we can stabilize that operating environment quicker.

And on free cash, I think there's a few points that investors should be aware of. Number one, you mentioned seasonality in our business. So, when you think about seasonality of our cash flow, most of that comes in in the fourth quarter. So, with the volume decline that's currently hitting us, it's a bit of a mixed blessing that is during our low seasonal point. So, hopefully, as the economy reopens and stores reopen, gradually, we get to see that pressure come off of our cash flows. But in the meantime, we'll still be after those cost reductions. I mentioned on a run rate basis – on an annualized run basis, we've taken \$250 million out of our cost structure, so that the great work our operational and administrative leaders have done to reduce cost has been tremendous also in offsetting this decline.

And then, I think finally, just from a free cash flow perspective, our government did a pretty good thing for business in the CARES Act. And where we feel that most is in the cash flow relief that comes with some of the associated tax relief provisions, such as deferring social security payroll tax into 2021 and 2022. And for us, even more impactful, the ability to carry back some net operating losses into prior years. You couldn't carry back net operating losses prior to this act; you had to bring them forward. And what also helps in that, if you can take those net operating losses back in the year with a 35% statutory rate instead of the current 21% statutory rate we're at.

So, all told, we're suffering some cash decline from the volume. We're partially offsetting that from cash conservation and cost reduction. And then, we believe we'll see over a \$40 million impact just on those tax provisions I walked through to help cash flow in 2020. Many of which are timing, but still it's the ability to have that cash flow at this point in time has a tremendous impact for our business because our primary use of cash flow is going to continue to be debt reduction, and we think we can continue to reduce debt this year.

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**J. Joel Quadracci**

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

A

Hey, [ph] Jamie (00:37:52). Also, one thing to add in these fits and starts, when we say that we're making most cost variable, we really mean it. We've actually furloughed entire plants here during this COVID-19 problem.

On the book side, we closed three book plants temporarily because of COVID-19-related issues that were going on in those states. We're since opening those back up again. We've done it on the retail side. And having the relief for employees being furloughed as a result of that is helpful because we know that they're being taken care of with those weekly checks.

So, we'll continue to manage the platform aggressively. And the ability – I think, one of the things that we've really learned is how can you furlough a plant in a crisis situation as opposed to just people within it.

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Q

Okay. And Joel, last thing. You obviously – through QuadMed, do you all have any kind of insight you'd like to share in terms of observations on the spread of the virus? And it certainly seems, at least here in New York, that I think there's some reason to be little bit more optimistic over the last couple of weeks, particularly over the last week or two. Is that consistent with what your doctors are kind of telling you?

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**J. Joel Quadracci**

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

A

Yeah. Look, my brother-in-law is the head of thoracic surgery at Mt. Sinai in New York. So, he is front and center with all this. And my sister is a trained physician as well. Plus QuadMed. What's really important here and what we've seen – and I can't tell you this enough – is our team and how we're managing our own cases. We have 20,000 employees with big plants. We manage it right down to how we're tracking and tracing. We have four different categories of quarantine. We have confirmed positive, suspected positive, symptomatic, close contact. Then, we have sick but non-COVID. We have people categories of interviewed, needs to be interviewed, in progress, return to work, deceased. We've had one deceased employee, unfortunately, due to COVID; but less than 20 positive and not in any one place.

So, I think the message is that companies are taking it upon themselves to track and trace. We've shared our whole plan with the Greater Milwaukee business community, with the Governor of Wisconsin as well. And what it

shows you is that you can manage it if you take the time to do it. If we look at what's happened in some of the meat packing plants where they're working closely...

Q

Right.

**J. Joel Quadracci**

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

A

...if you had a tracking and tracing program in there and you're acting quickly, you might get ahead of it.

And so, I'd say that what we're hearing from QuadMed, from other people in the medical community is it's a multi-layered approach to managing this. Take it all seriously. It's hand sanitizer, it's masks, it's distancing – not one of them is going to make it work; all of them together is what's going to make it work. And I believe, much of the country is embracing that and we've got to get this economy going again.

Q

Okay. As always, guys, thanks so much for your time.

**J. Joel Quadracci**

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

A

Thanks, [ph] Jamie (00:41:08).

**David J. Honan**

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

A

Thanks, [ph] Jamie (00:41:09).

**J. Joel Quadracci**

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

A

Operator?

**Operator:** This will conclude today's question-and-answer session. I would now like to turn the call back over to management for any closing remarks.

**J. Joel Quadracci**

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

All right. Thank you, Sean.

Well, Quad has successfully faced this adversity before, and at this time is no different. We have a team and a time-tested disciplined approach to navigate change and make certain we transition into a post COVID-19 environment as a stronger company. As the economy starts to turn back on, marketing and advertising investments will be reprioritized. As it happens, Quad stand to benefit whether it's a gradual or fast recovery due to our impactful client relationships, leadership expertise, Quad 3.0 strategy which is our unique integrated marketing platform, and financial strength.



In the meantime, we live in continued uncertainty and, therefore, we will continue to create a better way every day for our employees and our clients.

So, thank you, all, for joining us. We'll see you next quarter.

**Operator:** The conference has now concluded. Thank you for attending today's presentation, and you may now disconnect.

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