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TIVO - Q3 2017 TiVo Corp Earnings Call

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PRESENTATION

Operator

Good afternoon. My name is Erica, and I will be your conference operator today. At this time, I would like to welcome everyone to the TiVo Corporation 2017 Third Quarter Results Conference Call. (Operator Instructions) I would now like to turn the call over to Derrick Nueman, Vice President of Investor Relations.

Derrick L. Nueman - *TiVo Corporation - VP of IR*

Good afternoon, everyone, and thank you for joining our call. I am Derrick Nueman, Head of TiVo's Investor Relations. With me today are Tom Carson and Peter Halt as well as Samir Armaly for Q&A.

We just distributed a press release and filed an 8-K detailing our third quarter 2017 financial results. In addition, we posted a downloadable model on our IR website showing our historical financial results and non-GAAP to GAAP reconciliations. After this call, you will be able to access a recording of this call on our website at tivo.com.

Our prepared remarks will last about 15 to 20 minutes, followed by a question-and-answer session. For the purposes of this call, when we refer to TiVo Inc., we are referring to legacy TiVo Inc. entity and its business that was renamed TiVo Solutions after the acquisition by Rovi. Otherwise, references to TiVo mean the combined company operations of TiVo Corporation.

Our discussions include forward-looking statements about TiVo's future business, licensing, product and growth strategies. We caution you not to put undue reliance on these forward-looking statements as they involve risks and uncertainties that may cause actual results to vary materially from these forward-looking statements as described in our risk factors and our reports filed with the SEC. Any forward-looking statements made on this call reflect our analysis as of today, and we have no plans or duty to update them, except as required by law.

With that, I will now turn over the call to our CEO, Tom Carson. Tom?

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Thank you, Derrick, and good afternoon. TiVo continued its strong execution in the third quarter, delivering solid financial results and making progress in all areas of our business. We drove strong operating cash flows and declared a Q4 dividend of $0.18 per share, bringing our total expected dividend payments for 2017 to $0.72 a share or roughly $87 million.

Before getting into those specifics of the quarter, I wanted to take a couple of minutes to remind investors of what TiVo is today. TiVo has moved well beyond a hardware company, and is now an innovative, entertainment technology company. To that point, 95% of our revenues this quarter came from software, services, advertising and licensing. Today, our business falls into 3 categories: first, Platform Solutions, where we offer end-to-end user experience software solutions for pay-TV operators in both developed and emerging markets. These products focus on bringing OTT offerings into the pay-TV experience, and helping operators provide great multi-device experiences; the second area is Software and Services, where we offer components of the entertainment experience, ranging from metadata to advanced search and recommendations, including voice search, advertising and data solutions. In this area, our customers include pay-TV operators, CE Manufacturers, ad-tech companies, content providers and even streaming music providers; and finally, IP Licensing, aimed at those who wish to build their own solutions. They can license our world-class intellectual property in order to provide a robust entertainment discovery solution. Our customers include 9 of the top 10 U.S. pay-TV providers, some of the leading virtual pay-TV operators, the largest international pay-TV operator, mobile device manufacturers, OTT players and other CE providers. All of these businesses have been built on innovative and compelling entertainment technology. Over the last decade, TiVo, including both Rovi and TiVo Incorporated, has spent almost $2 billion in R&D, making the consumption of entertainment better. And we're continuing to put significant resources towards this goal.

Now getting into the specifics of our third quarter. Starting with our product efforts. We recently launched conversation in our next-generation retail product, which is important, as voice is becoming a critical element of the entertainment experience. TiVo strives to set itself apart from other voice solutions in 3 key ways: focusing solely on the entertainment domain, facilitating natural language interactions by leveraging our Knowledge Graph, and providing an increasingly personalized experience. Also, began deploying our new, visually-rich user experience, both in our retail channel and with operators, and officially launched our next-generation operator platform with Millicom in Columbia. This is a positive milestone as Millicom is one of the largest pay-TV and mobile operators in Latin America. And we believe success there can help us drive footprint expansion in Latin America and other international markets. Finally, we've made a significant amount of progress with several of our product-growth initiatives. And while not yet visible, we expect these efforts to start showing results next year and beyond. One example of this is IPTV, where there is a significant opportunity to accelerate upgrades from current customers and to meaningfully grow our footprint. Our IPTV product will enable pay-TV operators to deliver a great user experience with multiscreen and OTT functionality, but with much lower operational and deployment costs. We anticipate this product being available in the first half of 2018. Looking forward, we expect IPTV, upgrade to classic guides and international expansion to be important drivers of our Platform Solutions business.

Another area we're very excited about is data and advertising. Data is an important enabler for TiVo to bring many new capabilities, including advanced advertising and media personalization. Today, TiVo processes TV-viewership data for over 25 million U.S. households. We have obtained rights to millions of TV households for anonymous, de-identified third-party use, and we're seeing strong demand for our TV data platform offering. We expect this offering to continue to grow as we onboard more households.

We will also be rolling out an innovative, new interactive advertising service. This solution will be available to customers that use the TiVo user experience or our search and recommendation product, to allow more targeted and personalized promotions. Our continued advancements in data, advertising and search and recommendations are key areas of innovation, which we believe will drive future growth for our Software and Services business.

Shifting to our IP business. We had a very good quarter. We signed a 3-year extension with AT&T, extending the license through 2025. This extension with the largest pay-TV operator in the U.S. highlights the long-term value and relevance of our intellectual property to U.S. pay-TV providers. Together with previously announced long-term agreements with other leading U.S. pay-TV operators, this provides a strong foundation and corresponding annuity-like revenue stream well into the middle of the next decade.

We also renewed and expanded our IP-licensing relationship with Liberty Global, the largest pay-TV operator outside the U.S., bringing their entire footprint under license. And we announced a multiyear renewal with Sony, that licenses all of their relevant entertainment products, including OTT and virtual pay-TV. Looking forward, bringing Comcast under license remains one of our top priorities. While we are pleased with the success we have had bringing the rest of the U.S. pay-TV market under license, as we have cautioned before, litigation can be a long process. However, we are committed to taking the necessary steps and actions through the courts and other venues to ensure that our valuable intellectual property is properly respected by Comcast.

With respect to the pending ITC action, we expect the final determination will be issued on November 9. We remain hopeful that the ITC will affirm the key aspects from the initial determination, including the exclusion order barring Comcast from importing infringing products. Beyond the upside from a potential licensing agreement with Comcast, we believe there are multiple significant opportunities for our IP Licensing business where we can grow recurring revenue. This includes making further progress with international pay-TV operators, especially in Canada, signing additional deals in the mobile and OTT spaces and opening some new adjacent verticals. We will discuss these opportunities in more detail in future quarters as we continue to make progress in signing new licensees.

With that, I will turn it over to Peter to cover our Q3 financial results before returning for some brief closing remarks. Peter?

Peter C. Halt - *TiVo Corporation - CFO*

Thank you, Tom. To reiterate what Tom said, we delivered solid financial results in the third quarter.

Revenues were $197.9 million, up 29% from the third quarter of 2016. This increase was largely driven by the acquisition of TiVo Inc. Third quarter revenue include $23.6 million of legacy TiVo time warp-related IP revenue, $9.9 million of hardware revenue and $600,000 of other revenue, almost entirely ACP. Excluding these items, our core business generated $163.8 million in revenue. Product revenues were $103.6 million, up $33.6 million from Q3 2016. It is worth highlighting our advanced user experience products, including both higher-end and emerging-market offerings, continue to grow and are helping to offset headwinds from our legacy guide products. IP Licensing revenues were $94.3 million, up $11.2 million from Q3 2016. There was approximately $7 million of catch-up IP revenue in the quarter, bringing the year-to-date total to $28 million. On a sequential basis, our revenues include $9 million less in catch-up IP revenues when compared to the second quarter.

Turning to cost. We exited the third quarter taking synergy actions that will result in annualized savings of almost $90 million, well in excess of our 1-year target. Additionally, this puts us very close to our in-state target of $100 million in annualized synergy savings. Getting into the details, GAAP total operating costs were $199.5 million in Q3. Q3 GAAP operating costs include $41.7 million relating to the amortization of intangibles, $13 million related to stock-based compensation and $8.9 million of cost related to restructuring, transition and integration efforts and several smaller items.

On a non-GAAP basis, non-GAAP total COGS and operating expenses, including hardware and depreciation, were $135.8 million, up $2.9 million from last quarter. The increase was primarily driven by the timing of litigation spend, which can be lumpy. On a GAAP basis, we reduced our net loss before taxes to $12.6 million in the third quarter from a net loss before taxes of $29 million in the third quarter of 2016. On a non-GAAP basis, non-GAAP pretax income of $54.1 million was up from the $45.6 million in the third quarter of 2016. Estimated cash taxes for the quarter were approximately $5 million. GAAP and non-GAAP diluted weighted average shares outstanding for the quarter were 121 million and 122 million shares, respectively. For those interested in calculating our non-GAAP EPS, take our non-GAAP pretax income, subtract our cash taxes and divide by non-GAAP weighted average shares outstanding.

Finally, we generated strong operating cash flow in the quarter. That said, our cash position was basically flat sequentially due to our dividend payment, the timing of some IP Licensing collections and the final licensing payment to a third party.

Turning to our estimates for 2017. We provide estimates as to our revenues and pretax income. In addition, to allow investors who want to calculate certain non-GAAP metrics, such as non-GAAP net income and non-GAAP EPS, which we don't provide in accordance with the SEC's guidance from last year, we provide estimates of non-GAAP pretax income, expected cash taxes and non-GAAP diluted weighted average shares outstanding.

We continue to expect full year 2017 revenues of $810 million to $830 million. On the cost front, we are maintaining our 2017 non-GAAP pretax income expectations of $218 million to $232 million.

In terms of adjusted EBITDA, we're maintaining our expectation of $276 million to $290 million. Recall that we increased these ranges last quarter, as we are running ahead of our plan on cost reductions. Additionally, for those looking to calculate our non-GAAP EPS expectations, we expect to have cash taxes of $20 million to $22 million, and approximately 122 million non-GAAP diluted weighted average shares outstanding for 2017.

Our expectations at the midpoint continue to include approximately $35 million of hardware revenues and approximately $45 million of non-GAAP hardware COGS.

Finally, we can either expect to exit 2017 with annualized Q4 non-GAAP total COGS and OpEx cost of approximately $540 million. The one COG you have on the run rate, exiting the year remains the timing and extent of litigation spend.

To wrap up, we delivered another strong quarter. We remain intently focused on continuing our operational and financial execution as we end 2017 and look to next year.

With that, let me turn the call over to Tom for some closing remarks. Tom?

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Thank you, Peter. Before opening the call for questions, I wanted to comment on our CEO search. As we disclosed several weeks ago, we're making progress and expect to have the process wrapped up shortly.

In closing, we had a strong first 9 months of this year, where we've not only delivered solid financial results, but put ourselves in a great position to create both near- and long-term shareholder value through continued strong execution. I am proud to see several of our efforts poised to begin driving the results as we look to next year and beyond.

With that, let's take questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And you do have a question from the line of Sterling Auty from JPMorgan.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Couple of questions. Just to start, make sure my math is correct, based on the input, it looks like non-GAAP EPS would be about $0.40. Does that sound right?

Peter C. Halt - *TiVo Corporation - CFO*

That would be correct, Sterling.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

All right, great. Now moving on to the business. On the Sony agreement, just to make sure we're clear because the description of the services, does this incorporate all the products including things like Sony Vue?

Peter C. Halt - *TiVo Corporation - CFO*

Yes, it does. It includes the Sony PlayStation Vue.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

All right. Great. And last question. When we look at Latin America, you talked about the Millicom deal. I seem to recall, a year ago, there was negotiations that are, kind of, 3-way between set-top boxers, providers yourselves, which was kind of like the old days, I think in North American and Canada. Has that changed the resolve to go direct or what's happening in terms of how the contract structures look in that region?

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Probably need a little help on that one. Sterling, you were breaking up a little bit. So I was having a hard time in hearing the question.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

I was saying in Latin America, I think a year ago, you were talking about 3-way deals, including the set-top box manufacturer, kind of like the old days in North America. Has that changed? Or what's the structures looking like in these deals now?

Peter C. Halt - *TiVo Corporation - CFO*

Well, that was -- the discussion was centered around the IP deals, that we were trying to negotiate. And that they were taking longer to do because basically we wanted to locate -- we want to license directly with the service provider, and not through the box manufacturer in order to cover all of their households. Because not all the households are totally covered by one-box manufacturer. And in the past, we've done some deals going directly with box manufacturers. And that's what was elongating the deals. Millicom is really more of a product deal that we've been talking about in terms of getting our product deployed.

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Yes. So Sterling, this is Tom. The basic approach is still very much try to go to the operator and license them on a recurring-revenue basis, on a per-sub-for-month basis. So that's the game plan here in North American and also in Latin America.

Operator

And your next question comes from Michael Olson from Piper Jaffray.

Yung Rok Kim - *Piper Jaffray Companies, Research Division - Research Analyst*

This is Yung Kim on for Mike. Just a very quick question in terms of the Millicom deal. How should we think about Latin America as a region in terms of the market opportunities for TiVo? And also, is it more the product or would it be guides or what kind of products would be best for that region and how are you thinking about it?

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Yes, it's great question. And so we -- we actually have a variety of products to go down there. I think if you, kind of, go back to the legacy Rovi days our a Passport product, it is always been a pretty active product in Latin America and continues to be. We certainly think the full suite of the TiVo products are also our product down there. You'll also see some of our Cubiware product, depending on the particular country, going to the certain parts of Latin America. So for us, it's a bigger market. The ARPUs aren't as high as what you would get in North America, but certainly a good market for us historically, and we think going forward, too, particularly with the combination of the Passport Guide, the TiVo Guide and Cubiware.

Peter C. Halt - *TiVo Corporation - CFO*

And the territory there, over the past we've announced a couple of deals. So it is the area that where we're very favorably exposed to.

Operator

And there are no further questions at this time. I will turn the call back over to Mr. Tom Carson, President and CEO, for any closing remarks.

Thomas Carson - *TiVo Corporation - President, CEO & Director*

Okay, guys. Thank you very much. I appreciate you guys joining the call. I know it's a busy day with lots of earnings announcements going on, and we certainly look forward to talking to some of you in the call in the next 24 hours or so. So thanks very much for joining the call.

Operator

Thank you. And this does conclude today's conference call. You may now disconnect.