

# Best Ideas 2020,

Hosted By MOI Global

CLEAR MEDIA

白馬戶外媒體

(100:HK)



LAUGHING  
WATER  
CAPITAL

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## About Laughing Water Capital

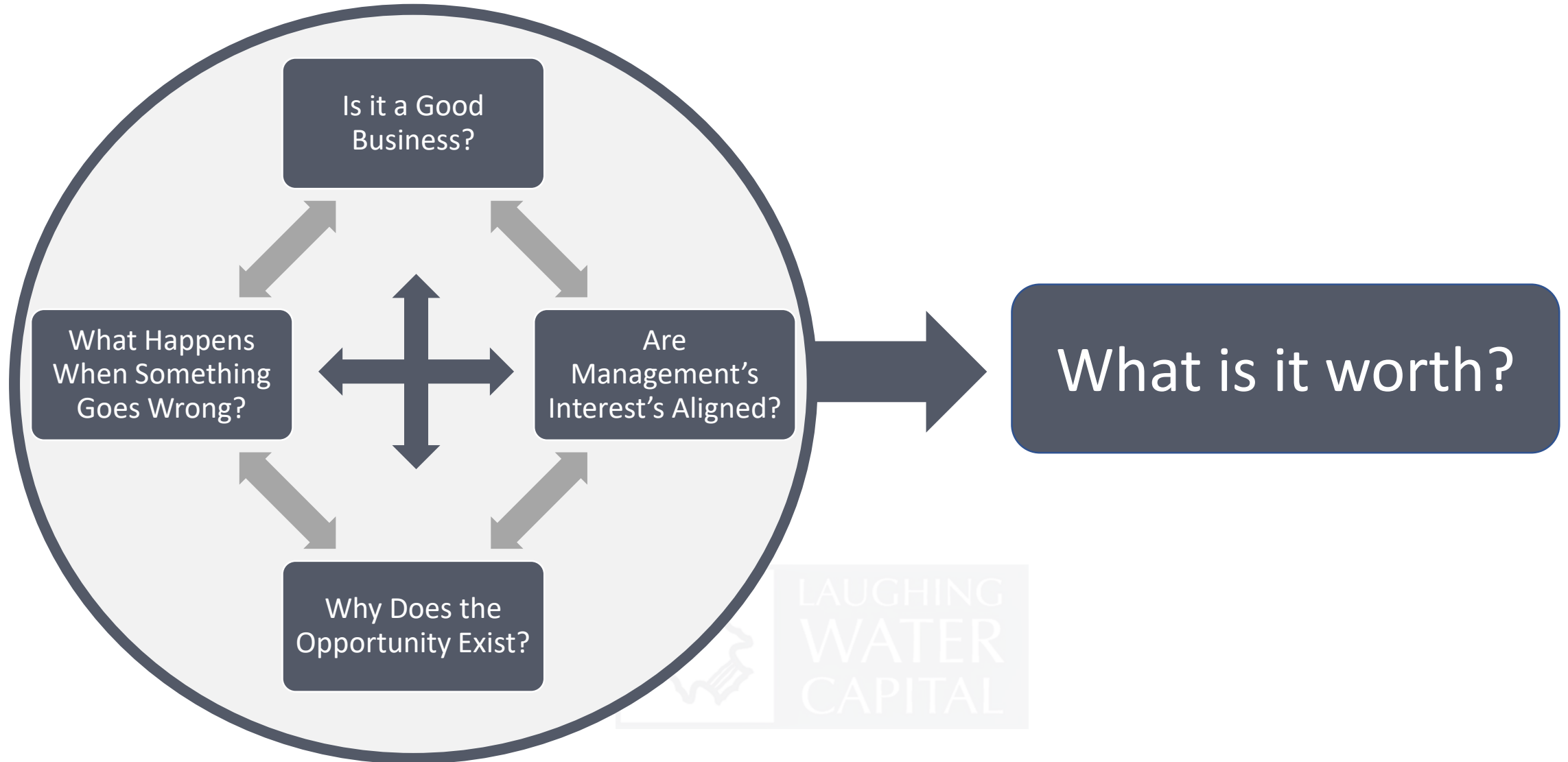
- Private partnership formed in 2016
- Concentrated value strategy: typically own 10-20 stocks
- Common sense approach to investing: seek out good businesses that are dealing with structural and/or operational problems that are likely easily solved by an incentivized management team given enough time
- Patience is essential: typically invest with a 3-5+ year view
  - Volatility is not risk

## About Matt Sweeney

- 18 years in sales, trading, banking and research roles on the buy and sell side
  - Sales experience covering hedge funds and mutual funds focused on small/mid cap names
  - Learned what not to do: focus on short term, trade frequently, over-diversify
- Additional experience in change management consulting
  - Learned the importance of people and culture, and that turn arounds often don't turn
- Almost my entire net worth is invested in the strategy
- Former Vice Chair, New York Society of Security Analysts (NYSSA) Value Investing Committee
- CFA charter holder

# LWC's 5 Part Framework

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# Elevator Pitch

Clear Media (100:HK) is a disruption proof business with tremendous secular tailwinds available at a cheap price due to temporary cyclical factors. While patient investors stand to benefit from a simple reversion to the mean over time and we would be happy to own this business for 10+ years, the high probability of hard catalysts in the near and mid term will likely crystalize returns in the not too distant future, while simultaneously providing downside protection.

## Valuation Summary (HKD)

	Target Price	Upside	1Y CAGR	3Y CAGR	5Y CAGR
"Normal" Value	\$14.23	126%	-	31%	18%
Olympic Value	\$20.17	220%	-	47%	-
Draconian M&A Value	\$9.31	48%	48%	-	-

# Context



“Back in January 1992 I read the Barron’s Roundtable and Felix Zulauf recommended Potash of Saskatchewan (POT) as a unique way to play the China growth story... It all made sense to me so I took a modest position. The stock did quite well, I recall I bought it for \$2/ share. I held onto it for 3 years and got a 4-5 bagger out of it. I was pretty impressed with myself at my market acumen. It stalled out eventually and I sold it around 1996 as I got tired of it treading water. Now mind you the original premise never changed, it was always intact, yet I craved new action.

If I had held on until the blow off in 2007 I would have had my 100-bagger. If one had bought even earlier it was a 200+ bagger.”

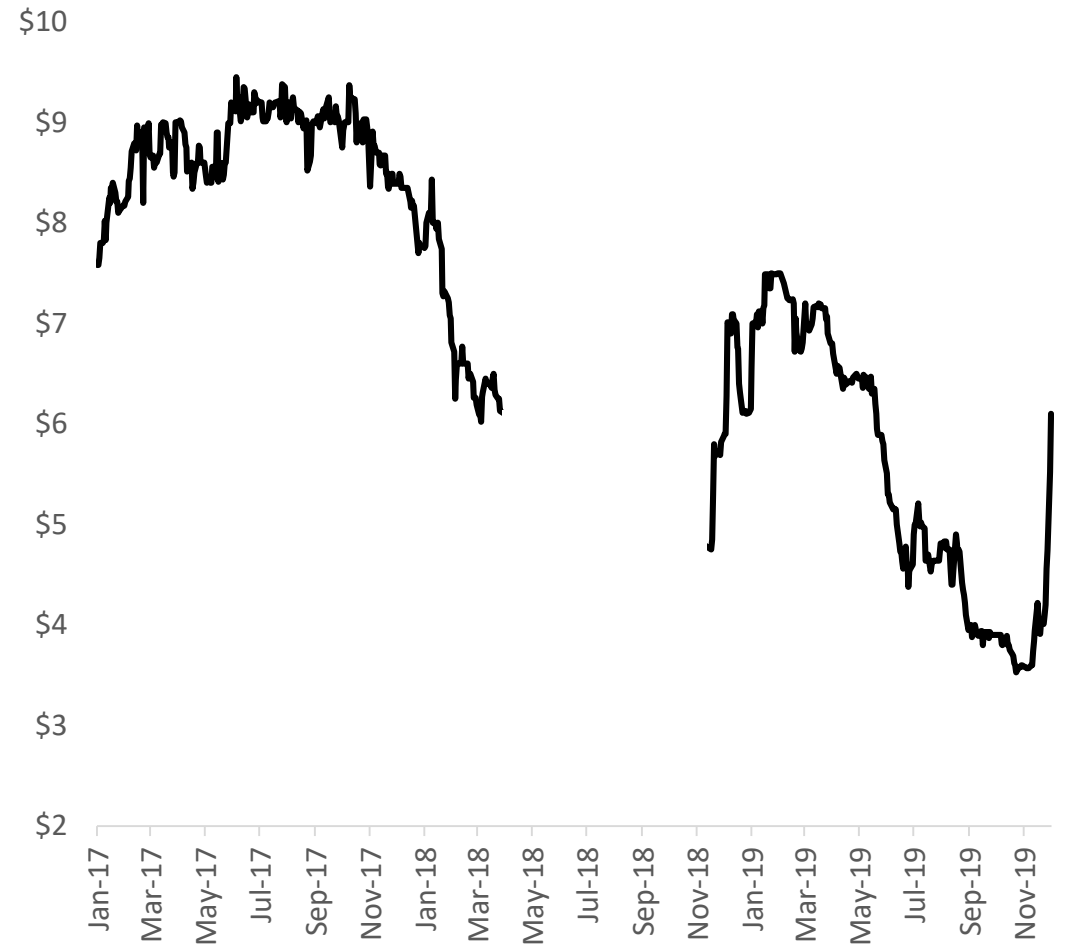
# Investment Basics

- ✓ Easy To Understand
- ✓ High Insider Ownership
- ✓ Rock solid balance sheet
- ✓ Dominant competitive position in niche vertical
- ✓ Tremendous secular tail winds
- ✓ Large Margin of Safety
- ✓ Potential near term catalyst
- ✓ Definite medium term catalyst
- ✓ Multiple ways to win



# Stock Basics

Stock Symbol	100:HK
Stock Price*	HKD 6.30
Shares Out (000)	~540,642
Market Cap	RMB 3,052,839
Cash	RMB 536,345
Debt	RMB 0
Enterprise Value	RMB 2,516,494
% Owned By Insiders	~52%
Current Yield	2.6%*
52 Week Range	\$3.50 - \$7.50

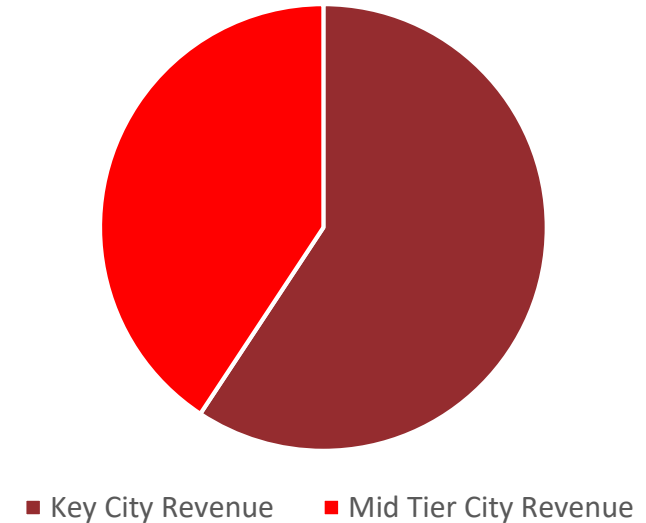


\*Share price as of EOD 6/14/2019 Dividend represents 2018 distribution

# Company Basics

- Largest operator of street furniture (bus shelter) advertising in China
  - 54,000+ panels
  - 24 cities
  - 70+% market share in “key cities”
    - Beijing, Shanghai, Guangzhou
- ~50% owned by Clear Channel Outdoor (CCO)
- Local partner: Hainan White Horse

## Key cities vs other



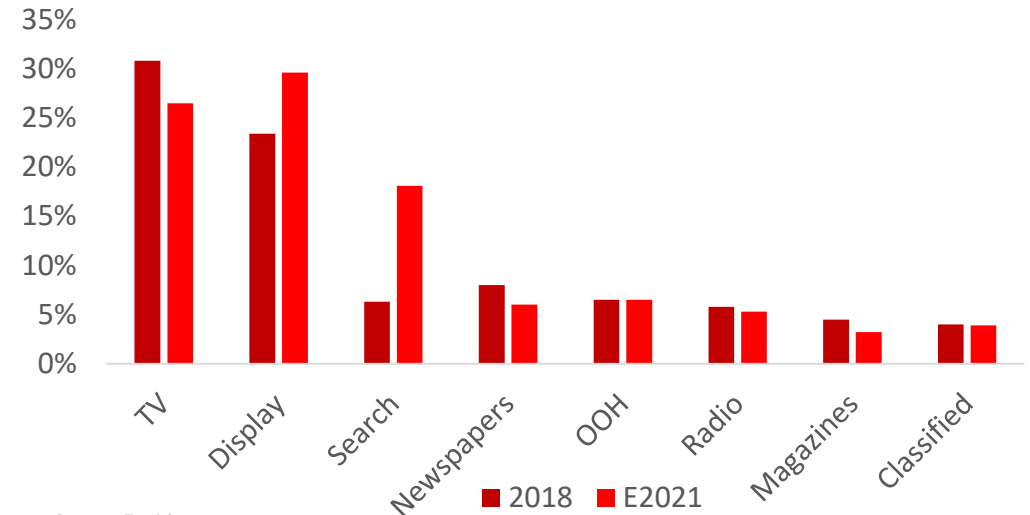
## Client Industry

	1H'18	1H'19
E-commerce	36%	30%
IT Digital Products	26%	17%
Food	5%	9%
Entertainment	5%	7%
Business/Consumer services	4%	7%
Beverages	6%	6%
Realty	3%	5%
Telecommunications	3%	3%
Educational Institutions	2%	2%

# Industry Basics

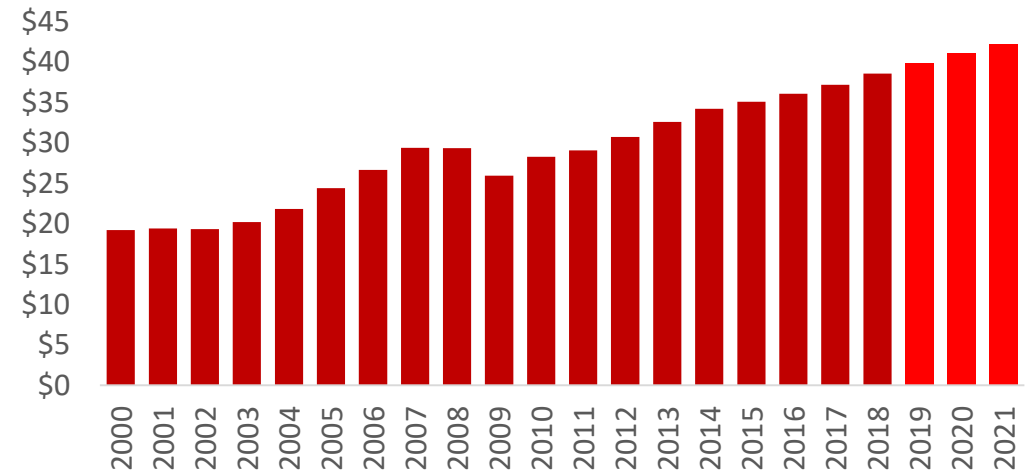
- Clear Media operates in an attractive subset of the Out of Home (OOH) advertising market
- OOH is an attractive niche for advertisers:
  - It is the only medium consumers can't opt out of:
    - DVR and skip television ads
    - X out of and ignore pop up ads
  - Less likely to appear near objectionable content
- While the shift toward mobile has upended the ad world in recent years, studies have shown OOH leads to a ~15% improvement in mobile ad effectiveness
- APAC is an attractive market for OOH
  - the largest OOH region, with ~\$13B USD in 2018 sales
  - the region with the highest percentage of OOH market share (7.8% vs 5.6% globally)
  - China is the 3<sup>rd</sup> largest OOH market (USD \$4B – 13% of global spend)

## Share of Global Ad Spend



Source: Zenith

## Global OOH Ad Spend (\$B)



# Is It A Good Business

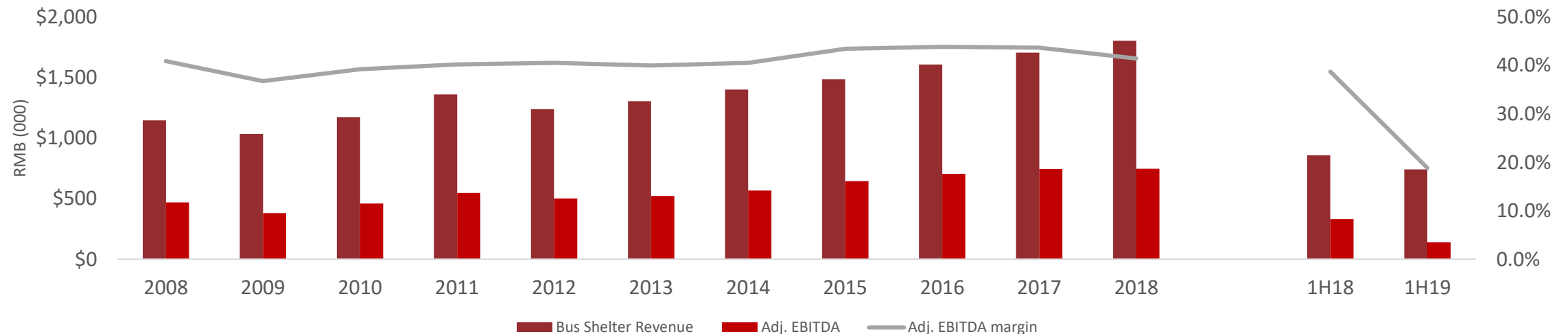
## Positives

- Advertising is never going away, and OOH is an especially attractive niche that is unlikely to be disrupted
- Examining competitors who operate in multiple channels reveals that Street Furniture has significantly higher margins than other areas of OOH
- With the exception of the last ~12 months, this business has been remarkably consistent, and has generated significant cash
- Rock solid balance sheet
- Long runway for growth attached to Chinese urbanization and growth of consumer spending

## Negatives

- Fixed costs are high and there is a duration mismatch between long term leases (~10 years) and short term ad campaigns
- Ad spending tends to track economic health, which is cyclical
- Street furniture tends toward more of a local business than OOH in airports etc., which can attract recession resistant global luxury brands

## Key Metrics



\*not adjusted for IFRS 16

# Competitive Advantages

With ~70% market share in major cities, Clear Media is the largest player in a competitive market

- Revenue advantages
  - Network breadth
- Cost advantages
  - Sales efficiency
  - Route density
  - CapEx purchasing power

Combined with long term (~10 year) contracts, these advantages make it difficult for an upstart to take share

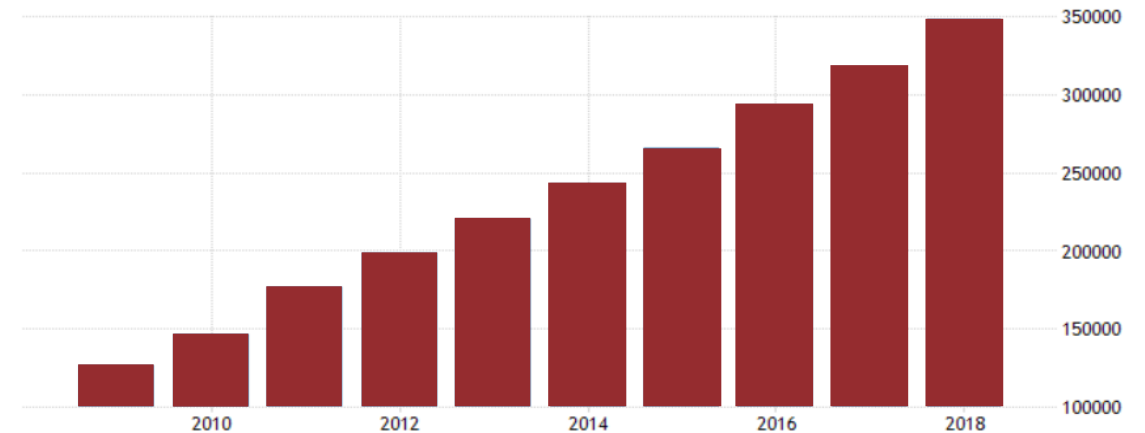
# Secular Tailwinds

## Chinese Consumer Spending is Still Far Below Developed Nations

Consumer spending is a key driver of ad spending

- Chinese consumer spending has been growing rapidly, but remains well below developed country levels
  - Beijing / Shanghai per capita GDP is less than 1/3<sup>rd</sup> of NYC
- It is a stated goal of the Chinese government to increase consumer spending

### Chinese Consumer Spending



SOURCE: TRADINGECONOMICS.COM | NATIONAL BUREAU OF STATISTICS OF CHINA

### Per Capita GDP



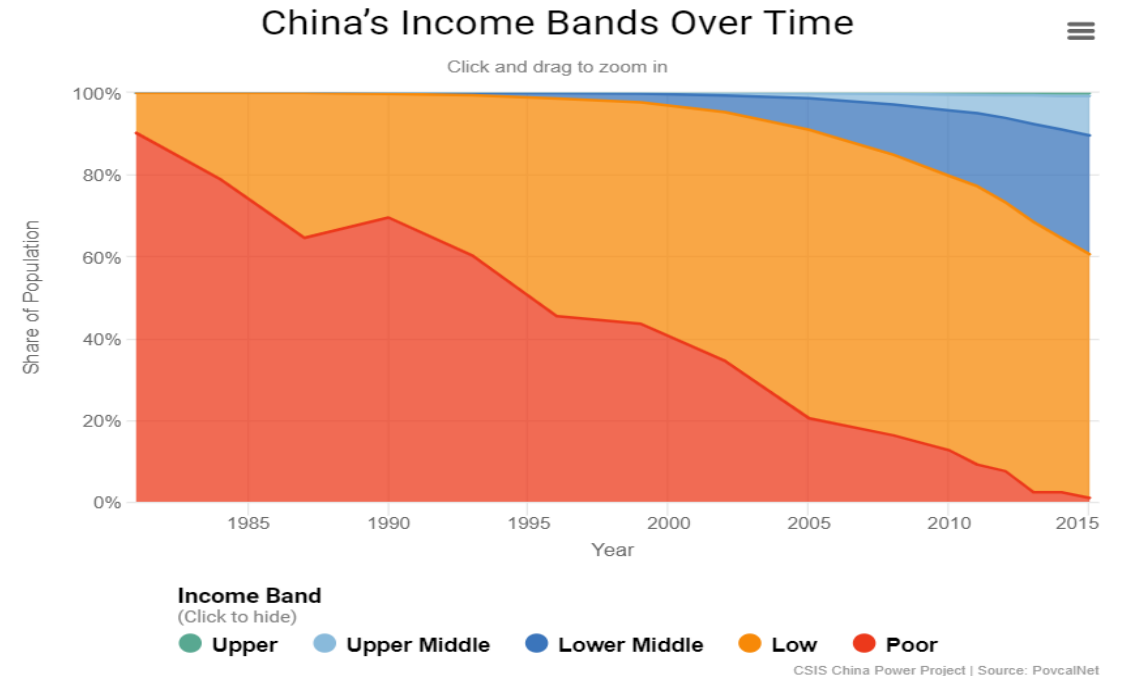
# Secular Tailwinds

Chinese Consumer Spending is Primed to Accelerate in the Years to Come

China's middle class only began to develop in earnest ~20 years ago

- The first wave of Chinese people that grew up middle class is about to enter the work force and enjoy guilt free spending power for the first time

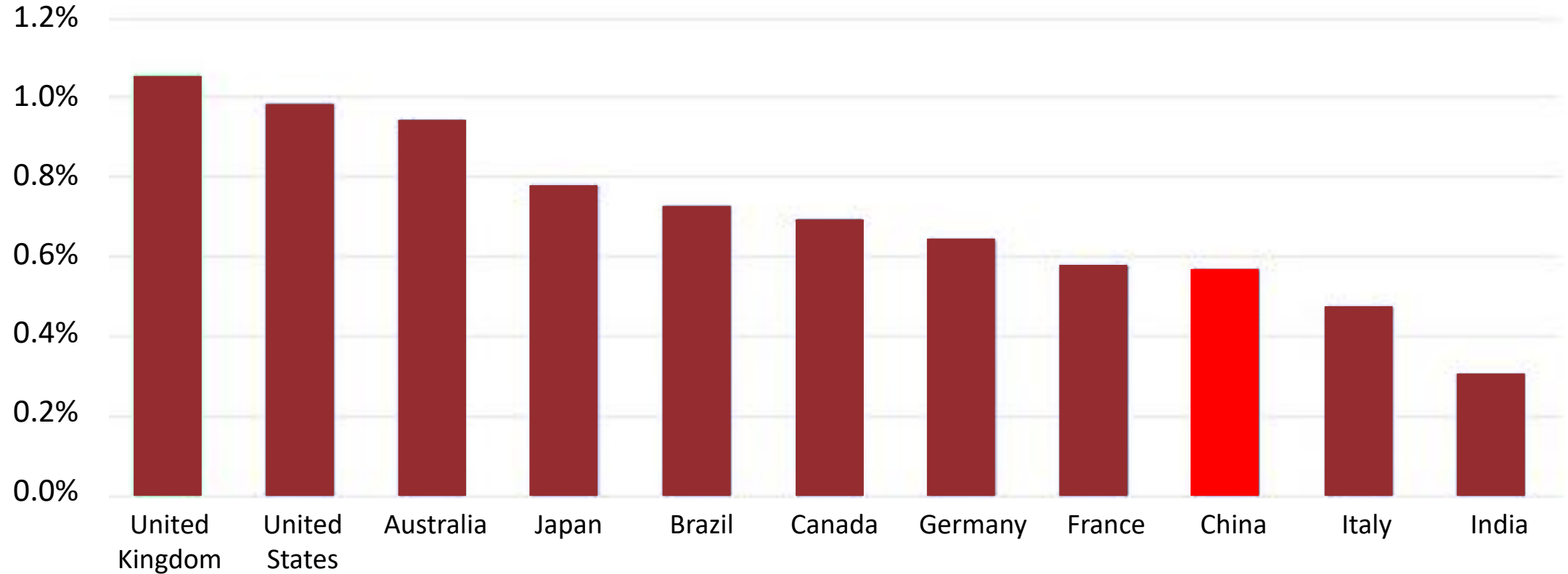
## Chinese Middle Class



# Secular Tailwinds

As Consumer Spending Accelerates, Ad Spending Will Accelerate

Advertising Expenditure % of GDP (2016)





# Secular Tailwinds

## Chinese Urbanization

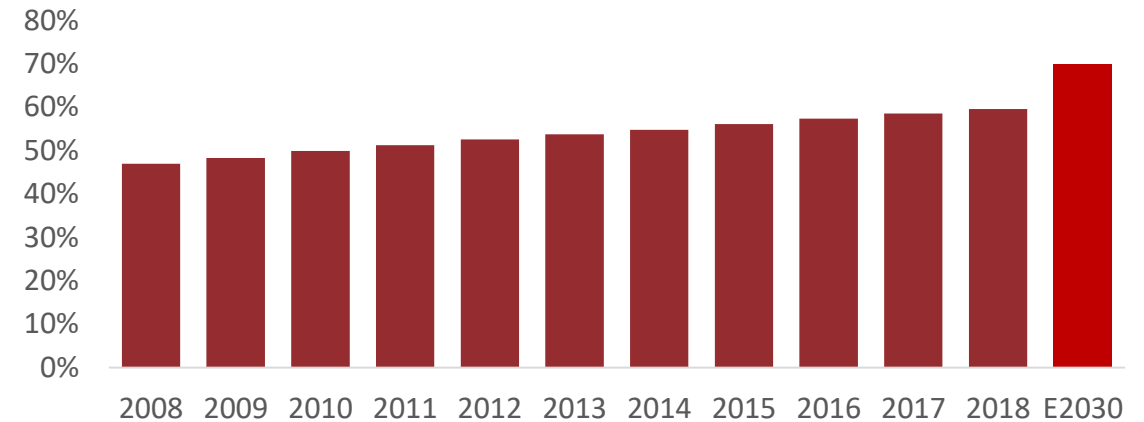
China is becoming increasingly urban

- As population density increases, average selling price for OOH panels goes up

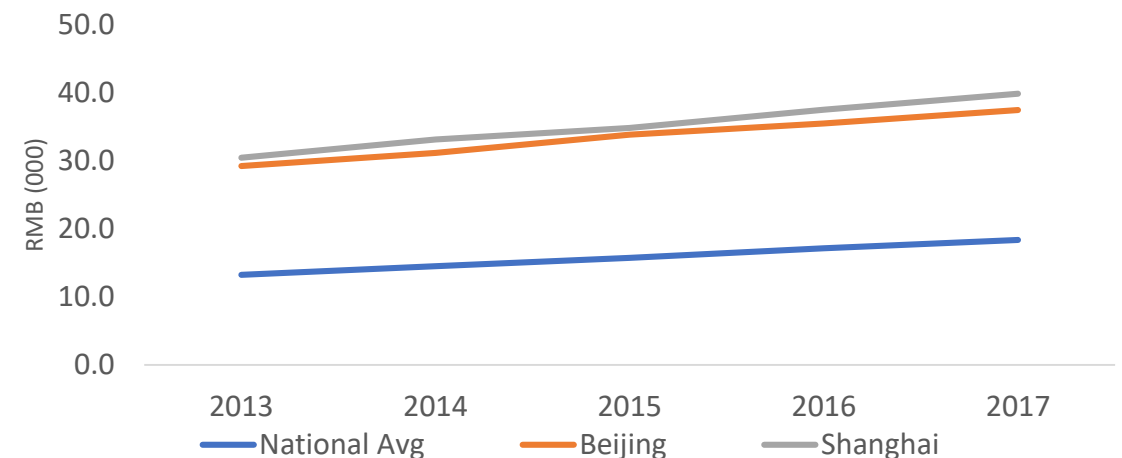
Growth of mega cities

- At present, only Beijing, Shanghai, and Guangzhou rival western cities in terms of economic power
- More than 20 Chinese cities are expected to have more than 5M inhabitants by 2030
- 2/3rds of the growth in 2030 consumption is expected to come in 2<sup>nd</sup> tier cities, benefiting Clear Media's 21 "other" cities

## Chinese Degree of Urbanization



## Regional Per Capita GDP



# Secular Tailwinds

## Street Furniture Utilization Rates

The company no longer discloses occupancy rates, but historically +/- 60% had been typical

In developed economies ~80% occupancy rates are more typical

As tier 2 cities and the outer rings of tier 1 cities continue to gentrify, occupancy rates will improve, leading to a substantial revenue uptick and margin improvement

# Secular Tailwinds

## Digitalization

Adoption of digital panels has driven significant revenue and margin improvement across other OOH verticals

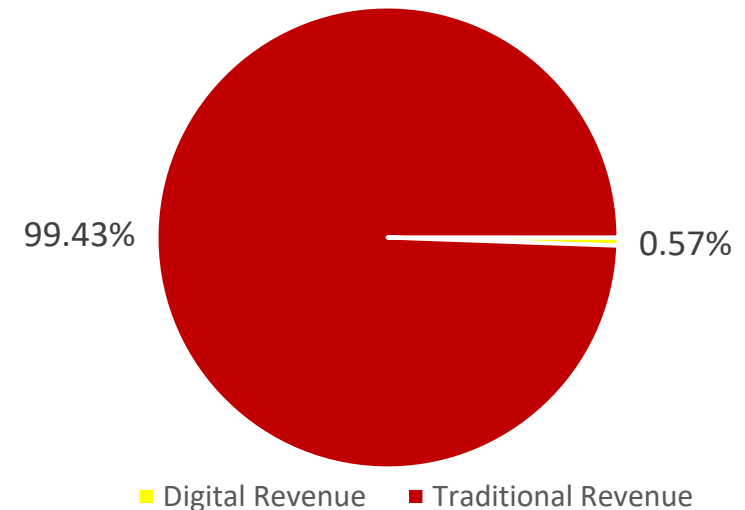
Thus far, governments have been slow to permit digital street furniture for fear of distracting drivers

- Chicago only allowed digital street furniture in 2017
- Finland only allowed digital street furniture in 2017

Clear Media is currently experimenting with digital in one Chinese market, and we believe eventually this format will be widely embraced

- Revenue growth
- Margin improvement

## 1H'19 Revenue Mix

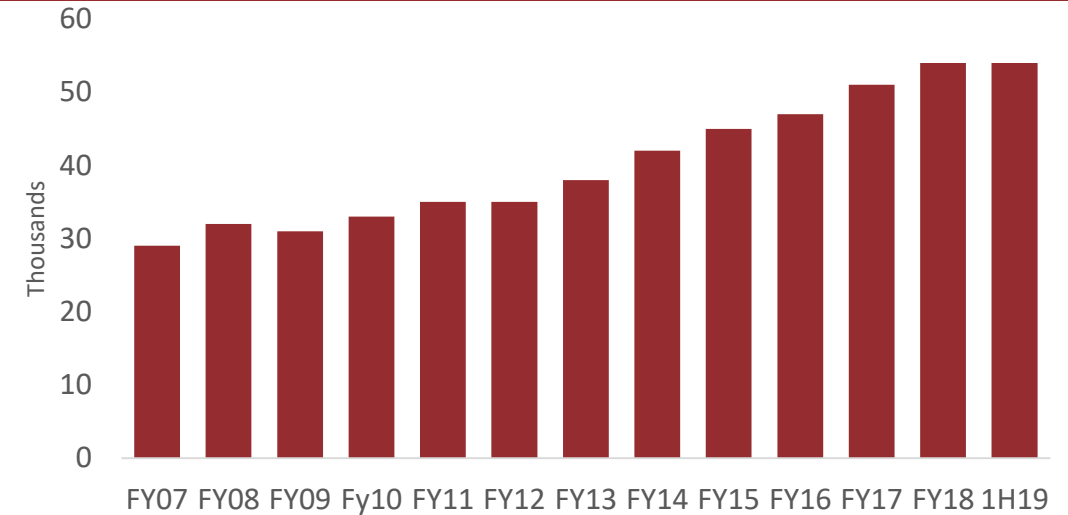


# Capital Allocation

## Growth in Footprint (YE Bus Panels)

Historically the company has expanded their network through bidding on new locations and/or M&A

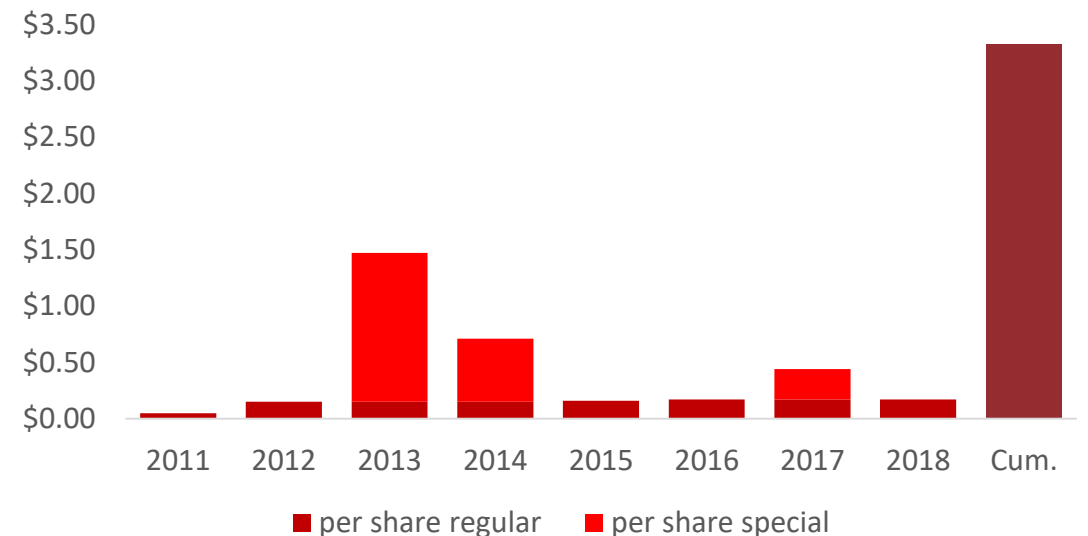
- Target 15% IRR



## Cumulative Dividends

In addition to funding growth, the company has returned cash to shareholders via dividends

- Target payout ratio 20-40%



\*Litigation and recovery pending

# Why Does the Opportunity Exist?

Big Picture



A slowing economy has caused Chinese advertisers to be cautious

- Street furniture is over indexed to domestic/local ad spending vs. Transportation OOH that enjoys a more international / luxury clientele

# Why Does the Opportunity Exist?

## Big Picture

While Clear Media navigated the 2009 downturn well, we believe they were poorly positioned to face the current downturn

JC Decaux has indicated that when new shelter networks come online, it can take a year to fill them out. This is in more developed markets.

We suspect that ramping up new networks takes even longer in China, and thus estimate that Clear Media had as many as ~6,500 pre revenue panels incurring fixed costs as the market fell off a cliff in Q4'18

- Q3'18 revenue +9.5% YoY
- October '18 revenue -25% YoY

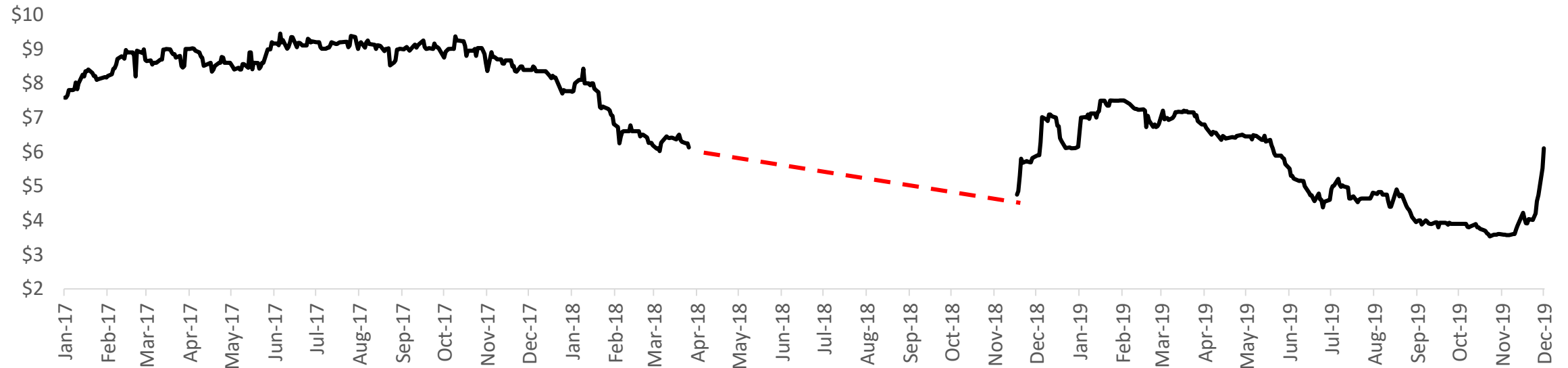
## Empty Capacity?

	Period End Panels	Period Delta
1H'17	48,000+	
2H'17	51,000+	~3,000
1H'18	54,000+	~3,000
Pre Revenue Panels?		~6,500

# Why Does the Opportunity Exist?

## Idiosyncratic Factors

- Early January 2018 the company announced they had uncovered an 8 year old fraud involving the theft of ~\$10M USD.
- Late March 2018 the HK stock exchange halted trading while an investigation into internal control failings was conducted.
- Shares did not re-open until mid November 2018



# Why Does the Opportunity Exist?

Non-economic Factors

Trading Characteristics

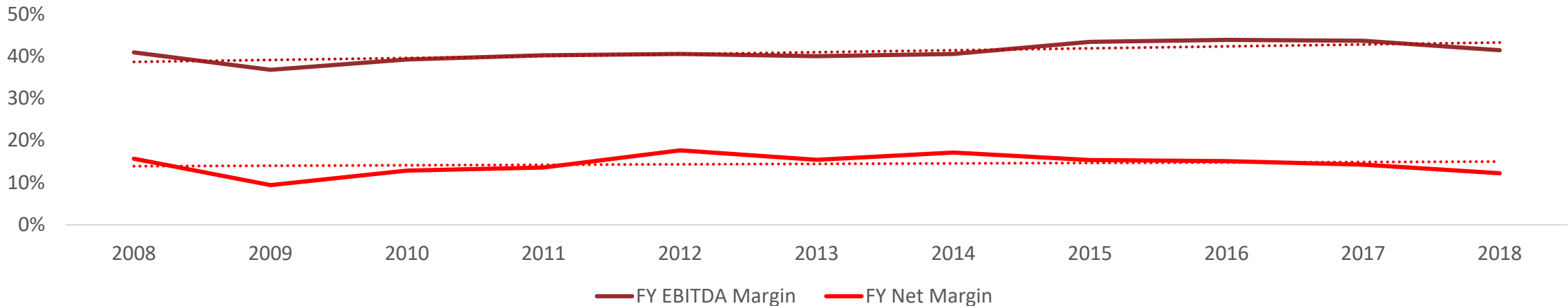
- Microcap stock
- Low float
- Limited liquidity
- No sell side analyst coverage
- No forward earnings guidance
- China corporate governance risk



# Bear Arguments

**Bear Argument 1:** Clear Media will be forced to grow into less attractive markets, hurting margins:

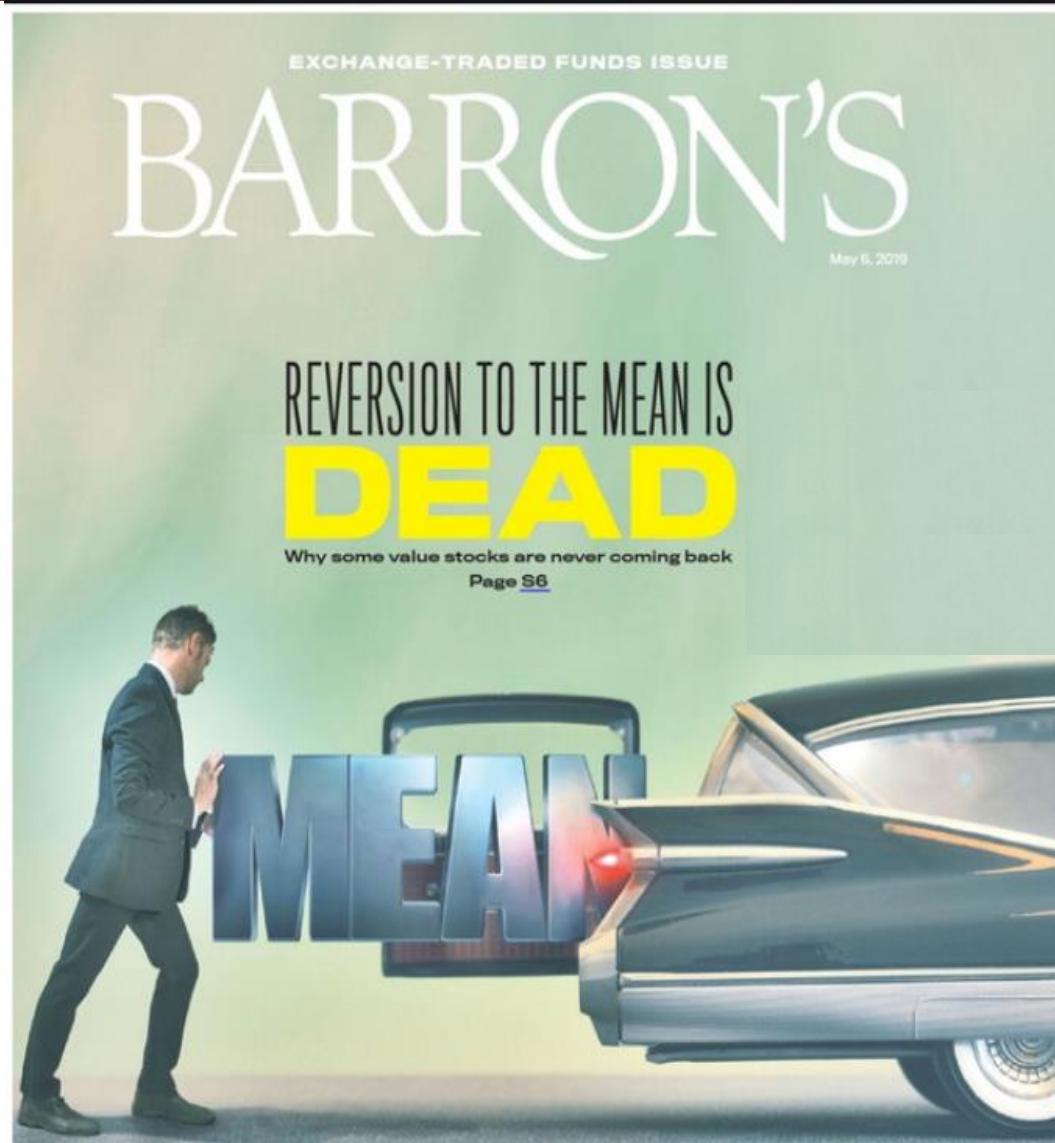
- Outer rings of larger cities
- Tier 2 cities
- Counter: This has been true for a long time, and margins have remained stable



**Bear Argument 2:** The Chinese government may prevent Clear Media from winning new business in retaliation for the accounting scandal

- Counter: Clear Media has grown panels by ~7% since the announcement of the scandal

# Valuation: Context



# Valuation: Reversion to the Mean

Key Assumption #1: Clear Media is a disruption proof business with strong secular tailwinds presently operating in a cyclical downturn

Key Assumption #2: At some point in the next 3-5 years, OOH ad spending in China will return to “Normal”

## Defining “Normal”

(RMB, 000)	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Avg. # of Bus Panels	29.3	30.1	29.4	34.0	35.0	36.5	40.0	43.5	46.0	47.0	52.5
Bus Panel Revenue	1,147,000	1,034,000	1,173,000	1,361,000	1,238,800	1,303,880	1,400,509	1,486,462	1,607,778	1,706,000	1,803,700
Avg. Revenue/Panel	39,152	34,303	39,840	40,029	35,394	35,723	35,013	34,172	34,952	36,298	34,356
FY EBITDA Margin	40.9%	36.8%	39.2%	40.2%	40.5%	40.0%	40.5%	43.4%	43.8%	43.6%	41.4%
FY Net Margin	15.7%	9.4%	12.9%	13.6%	17.7%	15.4%	17.2%	15.4%	15.1%	14.2%	12.2%

“Normal” is defined as mean Revenue/Panel and mean Margins from 2012 – 2017

- 2008: Beijing Olympics
- 2009: Financial Crisis
- 2010: Shanghai Expo
- 2011: Record high occupancy rates
- 2018: Severe drop off starting in October

\*not adjusted for IFRS 16

Source: Sentieo, Company Filings. Note: adjustments made for the discontinued bus body business and one time charges. Avg. # of bus panels = wtd. avg. when disclosed, and YE avg. when wtd avg. not disclosed.

# Valuation: Reversion to the Mean

Key Assumption #1: Clear Media is a disruption proof business with strong secular tailwinds presently operating in a cyclical downturn

Key Assumption #2: At some point in the next 3-5 years, OOH ad spending in China will return to “normal”

## “Normal” EBITDA

Avg. 2012-2017 Revenue Per Panel:	\$35,258
Avg. 2012-2017 EBITDA Margin:	42.0%
Bus Panels (000):	54

“Normal”

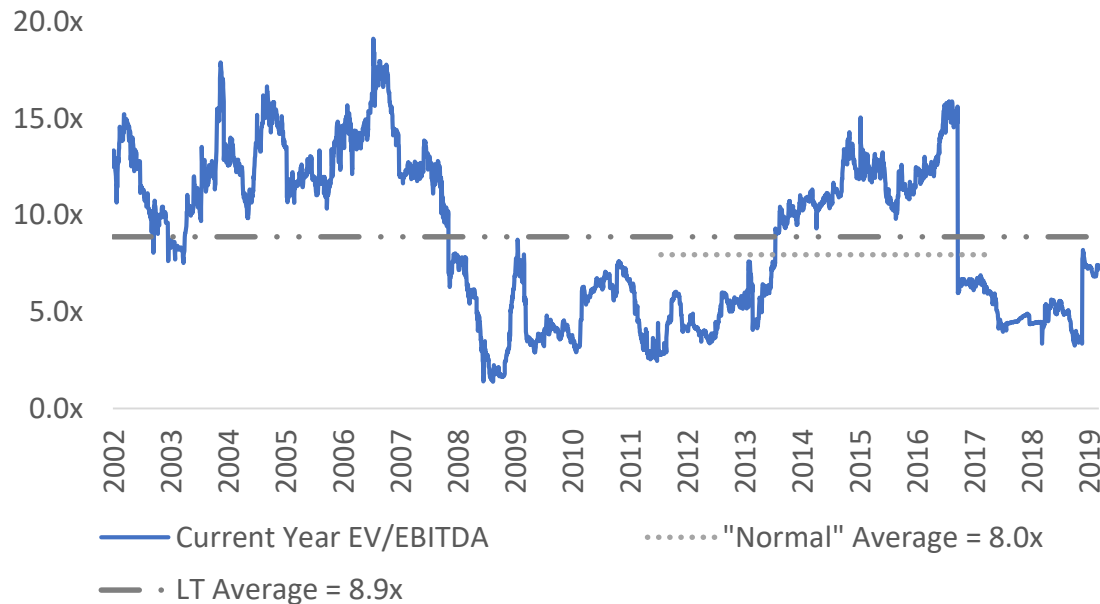
		Revenue Per Panel (RMB)				
		29,947	31,194	32,494	33,848	35,258
EBITDA Margin	EBITDA	549,821	572,730	596,594	621,452	647,346
	34.0%	582,138	606,393	631,660	657,979	685,395
	36.0%	614,454	640,057	666,726	694,506	723,444
	40.0%	646,771	673,720	701,792	731,033	761,493
	42.0%	679,088	707,383	736,858	767,560	799,542

# Valuation: Reversion to the Mean

Key Assumption #1: Clear Media is a disruption proof business with strong secular tailwinds presently operating in a cyclical downturn

Key Assumption #2: At some point in the next 3-5 years, OOH ad spending in China will return to “normal”

## Historic EV/EBITDA (current year)



## Per Share Value

“Normal”

		"Normal" EBITDA (RMB)					
		HKD/Share	549,821	606,393	666,726	731,033	799,542
Multiple	4.0x	\$5.62	\$6.08	\$6.58	\$7.10	\$7.67	
	5.0x	\$6.75	\$7.33	\$7.95	\$8.61	\$9.31	
	6.0x	\$7.87	\$8.57	\$9.31	\$10.11	\$10.95	
	7.0x	\$9.00	\$9.82	\$10.68	\$11.61	\$12.59	
	8.0x	\$10.13	\$11.06	\$12.05	\$13.11	\$14.23	
	9.0x	\$11.26	\$12.31	\$13.42	\$14.61	\$15.88	
	10.0x	\$12.39	\$13.55	\$14.79	\$16.11	\$17.52	

# Valuation: Upside Potential

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FY Net Margin	15.7%	9.4%	12.9%	13.6%	17.7%	15.4%	17.2%	15.4%	15.1%	14.2%	12.2%

## Mid Term Catalyst: 2022 Beijing Winter Olympics

Historically, global mega events have led to a significant uptick in Revenue/Panel

- 2008: Beijing Summer Olympics
- 2010: Shanghai World Expo

In 2022, Beijing will host the Winter Olympics, which should lead to above "Normal" Revenue/Panel



"Normal"

Olympic

# Valuation: Upside Potential

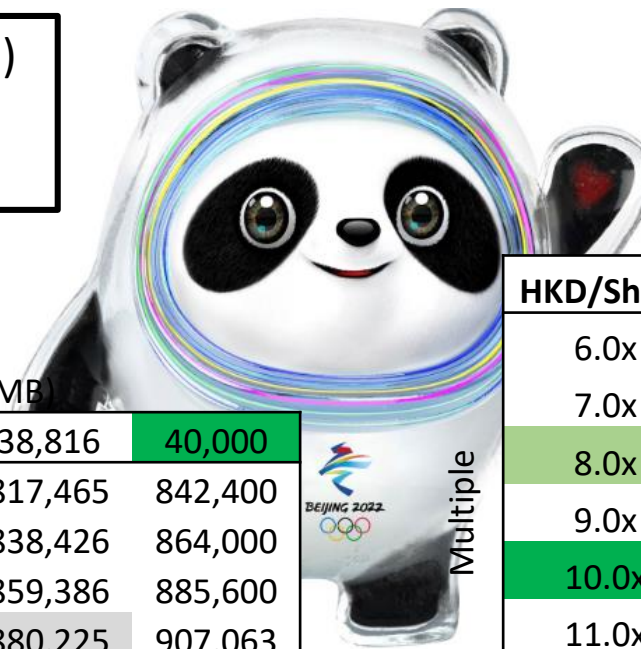
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## Mid Term Catalyst: 2022 Beijing Winter Olympics

Bus Panels: 54,000 (assumes no growth)  
No growth = higher utilization  
Higher Utilization = higher margin

"Normal"

Olympic



### Olympic EBITDA?

		Revenue / Panel (RMB)				
EBITDA		35,258	36,444	37,630	38,816	40,000
EBITDA Margin	39%	742,544	767,511	792,488	817,465	842,400
	40%	761,583	787,190	812,808	838,426	864,000
	41%	780,623	806,870	833,128	859,386	885,600
	42%	799,542	826,436	853,330	880,225	907,063
	43%	818,702	846,230	873,769	901,308	928,800

### Olympic EBITDA (RMB)

HKD/Share	742,544	787,201	833,139	880,225	928,800
6.0x	\$10.25	\$10.80	\$11.36	\$11.94	\$12.54
7.0x	\$11.77	\$12.41	\$13.07	\$13.75	\$14.45
8.0x	\$13.30	\$14.03	\$14.79	\$15.56	\$16.36
9.0x	\$14.82	\$15.65	\$16.50	\$17.37	\$18.26
10.0x	\$16.35	\$17.26	\$18.21	\$19.17	\$20.17
11.0x	\$17.87	\$18.88	\$19.92	\$20.98	\$22.08
12.0x	\$19.40	\$20.50	\$21.63	\$22.79	\$23.98

# Valuation: M&A Target

## Potential Near Term Catalyst

~51% owner Clear Channel Outdoors (CCO) has announced that it is conducting a preliminary strategic review of its investment in Clear Media

- Sector M&A has taken place at attractive multiples historically (10-18x EBITDA)
- CCO is heavily indebted and thus a (potentially) motivated seller. Combined with currently depressed EBITDA it is difficult to pinpoint where a sale may take place, but we would expect some combination of a discounted multiple on normalized EBITDA or a healthier multiple on depressed EBITDA. Both scenarios lead to attractive upside.
  - Draconian scenario: 5.0x “Normal” EBITDA = HKD 9.31 per share
- If a sale is delayed a few years and completed at an average transaction multiple of normalized EBITDA, multi bagger returns are possible
  - *“if there are better owners of some of those assets that we have around the world, who will pay more for those assets than they are worth to us, then we will entertain those conversations. But I believe that there is an organic path that we can go down that will enable us [de-leverage].”*

CCO @ Morgan Stanley European TMT conference, 11/13/19



# What Could Go Wrong?

## Risk

- Chinese hard landing
- Continued rough patch – next quarter likely ugly
- Government interference
- Digital transformation in other OOH sectors is happening first, which represents new supply in those verticals

## Mitigant

- A real risk, but ad spending rebounds quickly
- A real risk, but M&A speculation likely insulates shares
- A real risk that applies to all businesses in China
- A real risk that may lead to pricing pressure in street furniture, but street furniture caters to a different clientele than Transportation

# Summary

An investment in Clear Media represents an opportunity to purchase a resilient business during a period of temporary weakness. With tremendous long term tailwinds and a solid competitive position, we believe Clear Media could provide outsized returns for years to come.

However, potential near and mid term catalysts will likely crystalize returns in the not too distant future.

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If you are a patient, open minded, accredited investor that is not afraid to stand away from the crowd, we should talk. Please join our mailing list at:

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