

## **FINAL TRANSCRIPT**

**Indigo Books & Music Inc.**

### **Third Quarter Investor Conference Call**

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Length: 16 minutes

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**CORPORATE PARTICIPANTS****Janet Eger***Indigo Books & Music Inc. — Vice President, Public Affairs***Heather Reisman***Indigo Books & Music Inc. — Chief Executive Officer***Laura Carr***Indigo Books & Music Inc. — Chief Financial Officer***CONFERENCE CALL PARTICIPANTS****Matthew Gan***Cormark Securities — Analyst***Bill Nasgo***Heartland — Analyst*

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**PRESENTATION****Operator**

Good morning, ladies and gentlemen, and welcome to Indigo Books & Music Inc.'s third quarter investor conference call. At this time, all lines are in listen-only mode.

Following the presentation, we will conduct a question-and-answer session.

If at any time during this call you require immediate assistance, please press \*, 0 for the Operator.

This call is being recorded on Wednesday, February 3, 2016.

I would now like to turn the conference over to your host, Janet Eger. Please go ahead.

**Janet Eger** — Vice President, Public Affairs, Indigo Books & Music Inc.

Good morning, and thank you for joining us to review Indigo's third quarter of fiscal 2016 results. My name is Janet Eger, and I'm the Vice President of Public Affairs.

Joining us from Indigo today are the Chief Executive Officer, Heather Reisman, and Chief Financial Officer, Laura Carr.

Regarding the materials for this conference call, we issued the press release after market close yesterday, which can be found at [indigo.ca](http://indigo.ca) and on SEDAR.

The conference call will be recorded and archived in the Investor Relations section of the Indigo website. A playback of the call will also be available by telephone until 10:00 a.m. on February 10, 2016.

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This conference call may contain forward-looking statements, and to the extent that it does we refer you to our cautionary statements regarding forward-looking statements in the press release and the MD&A related to this quarter and year.

I would like to now turn the call over to Heather Reisman.

**Heather Reisman** — Chief Executive Officer, Indigo Books & Music Inc.

Thanks, Janet. Good morning, everyone. Thank you for joining us. Laura Carr, our CFO, and I will make a few brief comments, and then we'll take any questions that you may have.

We are really delighted with the third quarter results that we announced yesterday. This is actually our ninth consecutive quarter of revenue growth. And I'm pleased to report that the growth numbers have been getting bigger during those nine quarters.

It's equally pleasing to announce a significant improvement in our earnings. This has been a record-breaking quarter for us with new daily highs set in both physical and digital channels. All of our key metrics showed meaningful growth. Traffic, units, conversion all increased. Same store sales exceeded 15 percent growth, and our digital channel grew by over 18 percent.

Of equal prominence our net promoter score, which for us is the key measure of how our customers feel, has increased to an impressive 68 percent. These are definitely great results, and we feel proud of the team for delivering such fantastic customer service during the all-important holiday quarter.

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We are feeling cautiously positive about the future. We recognize that with retail you're only as good as yesterday. That said, we do think that the investment in the business that we've made over the last number of years is showing real results and connection with our customer.

We're working on a number of key strategic initiatives, and we feel that Indigo is well positioned for continued growth.

I would now like to hand this over to our CFO, Laura Carr.

**Laura Carr** — Chief Financial Officer, Indigo Books & Music Inc.

Thanks, Heather, and good morning, everybody. The results that we're talking about today are for the 13 weeks ended December 26, 2015, and the comparative figures have been provided for the 13 weeks ended December 27, 2014.

So for the third quarter revenue was 383 million, which was \$44 million higher than last year despite operating one less superstore and four fewer small format stores. On a comparable store basis, the retail revenues were up 15.5 percent in our superstores and up 13.4 percent in our smaller format stores.

Our online business also continued to perform well, growing by 17.9 percent compared to last year.

This revenue growth was driven by double-digit growth across all general merchandise categories and by high-single digit growth in our core book business.

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I've been asked to sort of go into more detail on the categories, but it's fair to say that we had consistent strong growth across all categories, and the only two I'll call out is that we did have a strong change for our adult colouring books and related accessories, which generated strong sales across all channels.

And we opened two new specialty American Girl boutiques during the quarter in two of our stores in West Edmonton Mall and Chinook in Calgary, which helped to drive our IndigoKids business.

Our third quarter revenues in general merchandise categories grew to 39.5 percent of the total compared to 34.8 percent last year as we continued to extend our product assortment beyond our core book offering.

For the quarter, our margin rate improved by 0.6 percent, and margin dollars increased by 71 million. This margin rate improvement was achieved in spite of absorbing almost \$7 million of adverse effect headwinds due to the weakening Canadian dollar. The rate improvement was driven by a combination of more effective promotions, a higher sell through of full-priced products, and pricing adjustments to offset the impact of FX.

Our operating cost increased by \$5 million this quarter compared to the same period last year. The increase is the result of higher sales volumes in the retail and online channel.

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Selling and administration costs increased by 4 million compared to last year, driven by higher marketing and creative costs, increased expenditures for store renovations, and higher bonus accruals relating to improved business performance.

Overall, our EBITDA improved by \$12 million this quarter, driven by higher revenues and an improved margin rate; net earnings of \$53 million this quarter, which is an improvement of \$20 million compared to the same period last year. The improvement was driven by higher EBITDA and a lower tax expense.

On the fiscal year-to-date basis, our revenue has increased by \$65 million, or 9.1 percent to 774 million compared to 709 million for the same period last year.

Our year-to-date comparable store sales increased 12.3 percent for superstores and increased 9.7 for our small format stores.

On the year-to-date basis, our EBITDA has improved by 23 million to 54 million compared to the 31 million in the same period last year.

Just a quick mention of our balance sheet. Our cash position remains very strong, and we ended the quarter with 312 million in cash, which represents a 25 million increase from the quarter last year. The increase was driven by improved business performance and lower working capital.

At this point we'd like to open the call for any questions.

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## Q&A

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**Janet Eger**

Thank you, Laura. To ask a question, please press \*, 1. Operator?

**Operator**

Thank you. Ladies and gentlemen, as a reminder should you have a question, please press \*, followed by 1 on your touch-tone phone. If you are using a speakerphone, please lift the handset before pressing any keys.

Your first question comes from Matthew Gan, Cormark Securities. Matthew, please go ahead.

**Matthew Gan — Cormark Securities**

Hi. Good morning; calling on behalf of Dave McFadgen. Just want to ask on your same store sales growth. It was very strong, and I was wondering if you can kind of get into details of what's driving that same store sales growth? And whether you're seeing that same trend in Q4?

**Heather Reisman**

I just want to say your speaker's not very clear, but I think you're asking about same store sales.

**Matthew Gan**

Yeah.

**Heather Reisman**

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I think it's sort of everything. Our traffic increased a good couple of percentage points, so the customer was definitely indicating that they wanted to engage with us. And we had growth across every single category in the store.

So really this was just—it was literally we had wonderful growth in books, which is always the core of the business and which remains a very significant focus for us, and we had growth in every single main business, every single main category in the store. Our papery is a very strong business for us; our Kids business was very strong; our channel business was strong.

So we literally experienced growth across every aspect of the business. And also something which is important to us, and that is that our customers were shopping across categories.

**Matthew Gan**

Okay. Great. And I guess in terms of books did you guys have any hit titles in the quarter driving that result? Or was it again just broad category?

**Heather Reisman**

Yeah. For sure less the fiction titles. We had some good fiction titles, but this year the unicorn, so to speak, was the huge trend in colouring books. So we could consider that that was a hit.

Every year it's something. Some years it's sex, like Shades of Grey; some years it's colouring; and some years it's just amazingly written biography or story. But when we look at the sales for the books that would be considered unicorns it seems to even out year over year.

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So this year was different, but...

**Matthew Gan**

Okay. And then turn to the general merchandise...

**Heather Reisman**

It was a strong performance across all book categories, even when we removed the colouring books.

**Matthew Gan**

Okay. Great. And then I guess in terms of general merchandise, I was wondering if you can speak to what you saw in sales for American Girl in the quarter?

**Heather Reisman**

Well, we don't break out the sales for American Girl.

**Matthew Gan**

Okay.

**Heather Reisman**

We opened two new American Girls, one in Edmonton and one in Calgary. We can just continue to say that the market is responding wonderfully to it.

The books associated with American Girl also take a big hike, so you've got the books and the American Girl experience. And consumers are responding well to it.

**Matthew Gan**

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Okay. And then are you still kind of planning on opening four more—expanding four more store fronts in fiscal 2017?

**Heather Reisman**

We'll probably have another couple of opportunities, but we haven't announced anything as yet.

**Matthew Gan**

Okay. Okay. And then I guess...

**Heather Reisman**

Actually we'll—I guess the one that we sort of announced, I'm just being reminded, is we open a new store in Sherway in a couple of months. And there will be an American Girl at that store.

**Matthew Gan**

Okay. Great. And then in terms of your other general merchandise, the growth, was it a matter of growth in volume? Or growth in SKUs? Or is it again just a matter of both of them?

**Heather Reisman**

So we had unit growth. Obviously we had—I can't say number of SKUs; I don't know. But we had unit growth,

**Matthew Gan**

Okay.

**Heather Reisman**

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In every single one of our businesses, saw unit growth. So I would know—the question—we get a little bit of growth because we did some adjustment on the FX. We did not have to do all of it.

So we track whether we have actual unit growth, and we did indeed. There is unit growth in every single business.

**Matthew Gan**

Okay. And then I guess in terms of the cash balance in the past you've guided that you wouldn't kind of institute a dividend. Has that tone kind of changed? Or is it still...

**Heather Reisman**

No. We have no plans to issue a dividend. We see ourselves as having several opportunities to grow the business, and we'll be using the capital on the balance sheet as appropriate to grow the business.

**Matthew Gan**

Okay. I guess asked another way, is there a point where maybe when the Company reaches a point in cash or in free cash flow generation or a change in growth plans that that might be a consideration on the table?

**Heather Reisman**

There's absolutely no plan at all—

**Matthew Gan**

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Okay.

**Heather Reisman**

—at this moment to do that. We really feel that the big focus is on growing this business.

**Matthew Gan**

Okay. Sounds good. And then in terms of so this quarter we saw a bit of a hike in CapEx, and that was for new growth initiatives. I was wondering if you can speak to what those initiatives are?

**Laura Carr**

The increase is mainly just touching more stores this quarter compared to the prior year. So yeah, the capital—there's nothing exceptional in those numbers.

**Heather Reisman**

Yeah.

**Matthew Gan**

Okay. So going forward we should project what you guys tracked historically? Or...

**Heather Reisman**

I think as we do things we'll announce them.

**Matthew Gan**

Okay.

**Heather Reisman**

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Okay. Thank you.

**Matthew Gan**

Thank you.

**Operator**

Thank you. Ladies and gentlemen, as a reminder should you have a question, please press \*, followed by 1 on your touch-tone phone.

**Heather Reisman**

Okay. It looks like there are no more questions. No? Thank you for your time...

**Janet Eger**

Hang on.

**Operator**

We do have a question from Bill Nasgo, Heartland. Bill, please go ahead.

**Bill Nasgo — Heartland**

Yes. Good morning. I'm sorry. I came on late and missed part, but congratulations on an excellent quarter.

**Heather Reisman**

Thank you.

**Bill Nasgo**

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The retail environment certainly has been challenged for most. So what do you attribute this to? And what's your biggest worry in retail across your various lines?

**Heather Reisman**

So quite frankly, we attribute the performance to the investments we've been making in the business over the last four years to enrich the experience for our customer. I don't know if you were on when I said always at the core of the business and the strong focus is books, but we had a very deliberate strategy to expand the categories in line with what we felt our customers would really respond to; in fact, working with the customer.

So I have to say I think this is—I could say it's about the ninth straight quarter of growth and the biggest growth, and we attribute it to the connection between what we're doing and our customer. So we're always very respectful. The retail business is one where things can emerge, but we do feel that these are real results earned as a result of investment in the business and connection with the customer.

As far as what we worry about, right now the factors are more external than internal. The Canadian dollar obviously has an impact that we have to keep managing. We do buy some of our product, especially our proprietary products, in US dollars, and we don't pass all of the cost of exchange on to our customer. So we do have—we do watch that carefully, and we have some concern.

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We see it, though, as a temporal issue that's not—it's not structural to our business. It may be short-term structural or it may be medium-term structural to the Canadian economy, but it's just one of those external factors. So that's certainly a factor and the impact of that overall on the Canadian consumer.

But we focus a lot on being careful on pricing and value with the customer. So we only can control what we can control.

**Bill Nasgo**

Okay. Thank you.

**Operator**

Thank you. There are no further questions at this time. Please proceed.

**Janet Eger**

Okay. Thank you for your time and attention today. We appreciate you calling in, and look forward to reconnecting on a quarterly basis.

Our annual results will be announced on or around May 31, 2016.

Thanks again for your support, and have a good day.

**Operator**

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

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