

## **FINAL TRANSCRIPT**

**Indigo Books & Music Inc.**

**First Quarter Results Conference Call**

**Event Date/Time: August 8, 2018 — 9:00 a.m. E.T.**

**Length: 12 minutes**

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## **CORPORATE PARTICIPANTS**

### **Hugues Simard**

*Indigo Books & Music Inc. — Chief Financial Officer*

## **CONFERENCE CALL PARTICIPANTS**

### **David McFadgen**

*Cormark — Analyst*

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## PRESENTATION

### Operator

Good morning, ladies and gentlemen, and welcome to the Indigo Books & Music Inc. First Quarter Results 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, August 8, 2018.

I would now like to turn the conference over to Hugues Simard. Please go ahead.

### Hugues Simard — Chief Financial Officer, Indigo Books & Music Inc.

Good morning, everyone, and thank you for joining us to review Indigo's first quarter fiscal 2019 results.

My name is Hugues Simard, and I'm the CFO of Indigo. Our Chief Executive Officer, Heather Reisman, is unfortunately unable to join us, but she may join us for the question period at the end.

Regarding the materials for this conference call, we issued the press release yesterday. It 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.

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A playback of the call will also be available by telephone until 11:59 p.m. Eastern Time on August the 15th, 2018.

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

I will make a few comments, as usual, and then open up the lines to answer your questions.

The results we are discussing today are for the 13 weeks ended June 30, 2018. Comparative figures have been provided for the 13 weeks ended July 1, 2017.

First and foremost, let me start by saying that we have embarked upon the largest and most aggressive investment program of our history to position ourselves for long-term growth, both in our retail network and online.

Throughout the quarter, we've worked to transform 16 large-format stores on our journey to become a cultural department store for book lovers, completing two of these renovations, and with 12 more coming onstream before the crucial holiday season, including two flagships in Toronto at Bay and Bloor and downtown Vancouver on Robson Street, and our first store in the US.

In addition, we invested heavily in supply chain, both in our Brampton facilities and opening up our new Calgary distribution centre, and finally online, with several new functionalities being launched over the next few months.

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This massive undertaking has temporarily hit our top line and bottom line, of course, but on the basis of the excellent results of our renovated stores, the expected productivity gains and service improvements from our Calgary DC, as well as the continued enhancement of our online experience, we strongly believe that the short-term pain is more than worth it to position ourselves for long-term sustainable growth in both of our channels.

Revenue at 205.4 million for the quarter was \$1 million less than the first quarter last year, impacted by the expected downward pressure of ongoing renovations and the closure of a few low-performing stores as part of our transformation strategy. We also comped over a onetime gift card breakage revenue adjustment of \$3.8 million last year.

That being said, excluding the noise from our investment program and onetime adjustments, total comparable sales, including online, were up 2.4 percent in the quarter, with growth in retail and continued double-digit growth online with an increase of comparable sales of 12.7 percent.

Online sales grew in both print and general merchandise, with highly successful promotional campaigns resulting in a lift across key performance metrics.

Our vast investment program also impacted our bottom line, of course. Adjusted EBITDA for the quarter decreased by 13.4 million year over year, as the top-line impacts and the onetime breakage adjustment flowed down to margin and due to the significant strategic operating expenses

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associated with our store renovations, with the new distribution centres as they—and especially the one in Calgary as it ramps up, and our online development.

Operating cost also increased due to the sales volumes on the online channel, and as well as the impact of legislated minimum wage increases in Ontario, Alberta, and BC.

Even as we are investing heavily, though, our balance sheet continues to be very strong. We ended the quarter with \$155 million in cash and short-term investments while having no debt.

At this point, that's all I'll say on the results, but be happy to answer your questions. So let's open up the call for any questions from our analysts.

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## Q&A

### Operator

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

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

If you are using a speakerphone, please lift the handset before pressing any keys. One moment, please, for your first question.

Your first question comes from David McFadgen, Cormark. David, please go ahead.

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**David McFadgen** — Cormark

Oh, hi. Thank you. A couple of questions. So first of all, can you just go over exactly what happened in the quarter again? I wasn't totally understanding it. So you said there were 16 large-format stores that were in renovation in Q1, is that correct?

**Hugues Simard**

Yeah. We've worked—exactly. The total number of stores that we've worked on during the quarter is 16. We've already opened two of them. We're going to open another 12 of them between now and November, and there's going to be a couple of others that will be opening in Q4 that we've started to work on.

**David McFadgen**

Okay. So the balance is two. So two will be opening in Q4 and you won't—they won't be ... well, I guess they won't be completed for the December quarter, correct?

**Hugues Simard**

Yeah. Only 2 out of the 16. So out of the 16 I've—

**David McFadgen**

Yeah.

**Hugues Simard**

—talked about, 2 are already open; another 12 will be—so 14 total will be open for the crucial holiday season, yes.

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**David McFadgen**

Yeah. But for those remaining two, they would still be open. It's just that the renovation wouldn't be completed, right, for the December quarter?

**Hugues Simard**

Correct. Yeah. That's correct. Yeah.

**David McFadgen**

Yeah? Okay. So on that 3.8 million in breakage, is the margin on that 100 percent?

**Hugues Simard**

Yup.

**David McFadgen**

Yeah? Okay. That's what I thought. And then on the new distribution centre, the costs for that, I thought that that would actually make you more efficient; results in a margin improvement? Or should it really be looked at as additional costs, then we have to ramp the revenue, and then we will be more efficient?

**Hugues Simard**

Yeah. It's the second case. I mean, we're opening at the end of the summer, and basically, we're doing this in steps. So we're opening gradually starting in the fall. So right now and throughout the quarter as we're ramping up and as we're hiring people and as we're putting in the equipment and all of that, so right now it's more of a cost drain. But as we open it up in the fall and

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certainly for next year this will be ... this is where the improvement, the significant margin improvement will come over time for this one.

**David McFadgen**

So when do you think we would actually see this being a net benefit? The new distribution centre? Is it six months away? Twelve months away? Or—

**Hugues Simard**

Well, we'll start to see benefits in our Q3 and then some in Q4 as well. And after that, it will be fully onstream, and we should have full efficiencies from then on.

**David McFadgen**

And then it would be a net positive to the—

**Hugues Simard**

Oh, correct.

**David McFadgen**

—to the business?

**Hugues Simard**

Oh, absolutely. Absolutely.

**David McFadgen**

Okay. Okay.

**Hugues Simard**

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I mean, having a new distribution centre in Calgary, both for our retail network and for the end customer, is going to be a big plus.

**David McFadgen**

Mm-hmm. Mm-hmm. Mm-hmm. Okay. And can you give us an update on the New Jersey store?

**Hugues Simard**

Yeah. That's ... it's on track. It's opening at the end of the summer/early fall. It'll be most probably a late-September opening. So we are working feverishly.

It's starting to look very, very good and everything's in place, and we're very excited by it. So wait and see. But it's coming. You'll get your invitation for the opening.

**David McFadgen**

But is it going to be a—I thought it was going to be a soft opening in, say, August and then a full-fledged opening, I guess, in September. Is that the case? Or is it going to be a soft opening in September?

**Hugues Simard**

Yeah. We're ... right now, we're looking at a soft opening first, some time in September, and then the full opening after that.

**David McFadgen**

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Okay. Okay. So I think in the past the goal long term has been to get or achieve, say, an EBITDA margin of, say, 8 percent or higher.

**Hugues Simard**

Mm-hmm.

**David McFadgen**

Is that still the goal of the Company? And when do you think that might actually be achieved?

**Hugues Simard**

It is still the goal of the Company, for sure. And we knew that as we were going to invest in the three main sectors—retail, supply chain, and online—that this would ... that we would take a hit doing it. But we fully believe in our long-term plan, and we fully believe that once these crucial investments are all done and the efficiencies and all the gains come from it that we'll be on our track to our original goal of EBITDA margin.

**David McFadgen**

Mm-hmm. And is there going to be in your, say, fiscal 2020 year—because you're in fiscal 2019 right now—is there going to be another large CapEx investment program heading into that year as well? Or is this the main year?

**Hugues Simard**

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Well, this certainly is an important year. We'll see how this comes along. I mean, as we've said both for our US market tests for the retail transformation, I mean we are proceeding on all of these fronts. And next year surely if we follow up with more renovations there'll be further noise on the line.

But that being said, don't forget that we will get the positive from all these new stores coming onstream in this first wave of good performance. So I think that'll help us, and that'll give us momentum going forward.

**David McFadgen**

Mm-hmm. Okay. All right. All right. Thank you. That's it for me.

**Hugues Simard**

Thanks, David.

**Operator**

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

There are no questions at this time. Please proceed.

**Hugues Simard**

Okay. Thank you very much, everybody, for your time this morning and for your attention and for being with us early in the morning. We appreciate you calling in, and look forward to reconnecting on a quarterly basis.

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Our second quarter results will be announced on or around November the 6th.

And thank you again, and have a good day. Thank you. Bye-bye.

**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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