Askeladden Research Document:
Emerald Expositions (EEX)

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Why am I looking at this? / Executive Summary

I'm always excited to expand my knowledge of the professional services space by analyzing new niches, and I may have found a particularly interesting one: the tradeshow space. While I have been dismissive of in person events before, based on my somewhat skewed perspective as an investment analyst (given that investment conferences are largely webcast, there is laughably little value to attending unless you have a full day slate of one-on-one's with management teams), it turns out that tradeshows are actually a seemingly valuable way for the marketplace to meet – recently highlighted to me, anecdotally, by self-proclaimed Internet-based disruptor IronDirect (LQDT subsidiary) making a big splash at CONEXPO, a major construction industry tradeshow. (my logic being - if the internet disruptor thinks trade shows are effective marketing, then they probably are.)

Despite the cannibalization of many forms of advertising by the Internet, tradeshow attendance continues to be stable, and the industry seems to be having a fairly good go of things, with ridiculously high margins, great cash flow dynamics, and pricing power/revenue growth in excess of volume growth. Given the fragmented nature of the space, along with its financial characteristics, it has started to attract what seems like a meaningful amount of M&A attention, from both private equity groups and strategic players.

Within this backdrop, Emerald Expositions (EEX), a business that long languished under the ownership of Nielsen, was bought out by Canadian private equity firm ONEX in 2013 for just about $1 billion; ONEX subsequently spent over $500 million adding on bits and pieces, and recently brought the company public, although it retains a controlling stake. Emerald operates many industry-leading tradeshows, and appears to have metrics (such as extremely strong margins and a high renewal rate) that suggest it is well operated.

Before I get carried away, let me point out some of the negatives about the company: the long-term organic growth here is not as high as I would expect, at least based on napkin math from various disclosures under its previous owner; meanwhile, the business does display meaningful cyclicality combined with operational leverage, which would be problematic given that it is currently levered above 3.5 times debt to EBITDA on a net basis. While the cash flow characteristics and strong margins are definitely attractive, even at what I consider to be fairly robust 11.5 times EBITDA and 19 times NOPAT multiples, fair value looks to be about $16 per share, vs. a trading price of around $20 per share. Some of the delta is explainable to me docking the company for stock-based compensation as well as incremental public company expenses, while the rest is probably explainable by my sensitivity to leverage and preference for full capital structure valuations vs. valuations on free cash flow.

At the end of the day, this is a business that I'm unlikely to buy soon, but I look forward to further analyzing it and its peers, and adding this niche to my repertoire over the next 6 to 12 months.

The Business

Emerald Expositions is the largest operator of B2B trade shows in the United States by net square footage, with 500,000 global attendees and exhibitors in 2016, utilizing 6.5 million net square feet of exhibition space. Emerald operates more than 50 tradeshows, including 31 of the top 250, and all of its franchises are profitable, typically holding market-leading positions within their respective industry verticals, according to the company. Shows are held at least annually, with some held on a biannual basis. While the company does not have any customer concentration, it does have meaningful event concentration – its top 50 shows represent over 90% of its revenues, while its top-five shows (ASD Market Week in March and August, NY NOW in summer and winter, and the summer version of Outdoor Retailer) represent 35% of total revenues.

While I will momentarily get into the economics of the business and its past, present, and future, I think it's first worth dwelling on the context in which tradeshows operate. Although the Internet has disintermediated and devalued many legacy forms of advertising and even some kinds of face-to-face interaction, the value proposition seems to remain fairly strong for tradeshows. Below is a chart from Emerald's offering documents demonstrating the long-term stability of attendance:

Source: CEIR 2017 Analysis for number of attendees; Exhibit Surveys Trade Show Benchmarks and Trends for percentage of attendees planning to make purchases and percentage of attendees with authority to make purchases

Value Proposition to Attendees and Exhibitors

The value of tradeshows appear to be multifold: first and foremost, they serve as a marketplace/forum with network effects, connecting attendees and exhibitors. At a single tradeshow, vendors can meet with buyers from literally hundreds of organizations, and vice versa – it seems that the cost of exhibiting at a tradeshow is typically roughly a third of the company's total cost (including travel and so on) – so there are clear scale/aggregation benefits; imagine how long it would take and how much time and money it would cost to send a salesperson to 100 different organizations for a 20 minute conversation or demo, vs. meeting them all in one centralized location. While I do think that e-commerce will become increasingly prevalent for even B2B transactions over time, there will likely always be some significant role for tangible touch and feel, as well as in person discovery – and I think tradeshows fill that role pretty well.

As one brief, illustrative example on ROI – orders placed at the company's ASD market week show are just shy of $3 billion annually ($8.25K per buyer, with 44,000 buyers and 45,000 total attendees). While the company does not exactly specify how big this show is as a percentage of their revenues, given that the top five shows comprise 35% of revenue and market week is actually two shows, we can assume that it is no more than 20% of total revenue. At 20%, this would equate to Emerald earning 66 million of revenue for this show – if you multiply that by three to get attendees total costs, you get to around $200 million – that is 7.5% or less of "marketing cost" for orders placed in the show, which seems totally reasonable, especially given that the orders placed at the show are only part of the value proposition. This is obviously merely one anecdotal example and should not be weighted too heavily, but I do think that it illustrates to some degree the ROI of attending a tradeshow. Below are links to videos giving a better view of NY NOW and ASD market week:

- https://www.youtube.com/watch?v=p88bWtZlr_g
- https://www.youtube.com/watch?v=Qk9PD_6BWqI (also - https://www.youtube.com/watch?v=-eBgGmUIgcc#t=130.495445)

There is also a horizontal value – that is to say, competitive intelligence, along with keeping up with developments in the market. For what it's worth, it's not something that I've actively thought about a lot, but many of my portfolio companies tend to structure their new product introductions around major industry events, underscoring their value.

Business Model and Economics

From a business model perspective, trade shows are extremely compelling. First of all, tradeshow operators have little to no physical infrastructure; they rent space on a temporary basis from venues and sell it to exhibitors and attendees at a markup – resulting in very strong margins – Emerald Expositions, prior to its IPO, did mid 40s adjusted EBITDA margins, and with incremental public company costs, will likely do low 40s adjusted EBITDA margins. Meanwhile, capex runs sub $5 million a year on a business with roughly $340 million in revenue and over 150 million in adjusted EBITDA – and the company collects cash well in advance of events actually happening, creating a negative working capital cycle. The company also has extremely strong visibility, with exhibitors booking well in advance, in some cases even years in advance; the company noted that it had 98% visibility into booth space sales (representing 74% of total revenue) 2016 revenue by the end of Q2.

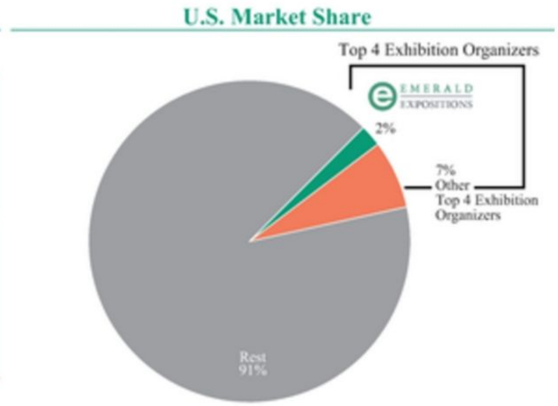
Before I get carried away with how awesome of a business model this is, it is worth noting that there are some concerns here. I'm skipping ahead a little bit in discussing the company's past, but briefly, Emerald Expositions spent quite a while under the Nielsen umbrella prior to being acquired by ONEX. This was a very small business for Nielsen, representing a low single-digit percentage of its revenues, so the company provided little to no commentary on it during conference calls, and only very basic disclosure on it and it's 10-K and other filings.

What I can ascertain for certain is that the business did 248 million in revenue in 2007, 240 million in revenue in 2008, dropping 25% to $180 million in revenue in 2009, dropping a further 7% or so to $168 million in 2010, before growing 7% the next year and 2% in 2012. Organic growth gets trickier to track after that – in 2013, the business is acquired by ONEX and promptly combined with George Little; we do know that revenue jumped to 273 million in 2014, 306 million in 2015, and 323.7 million in 2016, with acquisitions and organic growth combined – 2015 saw five and half percent organic growth, while 2016 saw 3 ½% organic growth.

To bridge the gap, ONEX paid $335 million for George Little, and presumably did not pay much more than the 10X EBITDA are so that it paid for Emerald (the company's 10-K does not disclose the specific EBITDA contribution, but states that most of the acquisitions excluding George Little have been completed at a mid to high single digit EBITDA multiple). For the sake of argument, let's assume that the 13 acquisitions consummated since 2014 for $530 million were done at an average multiple of 10 X EBITDA.

"Acquisition adjusted EBITDA" (i.e., pro forma EBITDA including acquisitions made in the year) increased to 158.5 million in 2016, up from about $94 million in 2012 when Nielsen last reported on the business. The gap is $62 million – and we know, from the above information, that at least $53 million of the contribution was inorganic. That leaves less than $10 million for organic growth, or less than 10% of 2012 EBITDA – suggesting, at best, something like 3% CAGR from 2012 onward.

Trying to bridge the gap to the revenue side, if you assume that the acquired businesses had an adjusted EBITDA margin of say 40%, then ONEX probably contributed an additional $120 million to $130 million or so of inorganic revenue. While the numbers are hard to pin down exactly, the most charitable I can come up with is a 15% or so total revenue growth from 2012 for the legacy Nielsen expositions business (LSD CAGR), getting it back to about $210 million – or, a full decade later, still lower than the 248 million that was booked in 2007. This contrasts with data presented in the 10-K that showed 4% historical and forecast 5% industry growth, as well as a comment in the panel discussion that I will link to later by competitor Diversified, which alleges that it saw a 30% decline in EBITDA during the crisis, but it bounced back right after. However, the EEX filings do note $7MM of "discontinued" revenue in 2014, which may bridge the gap (getting you to say 4% - 5% top-line CAGR for the Nielsen business), although it still doesn't excuse the performance through the crisis, nor the low CAGR in EBITDA.

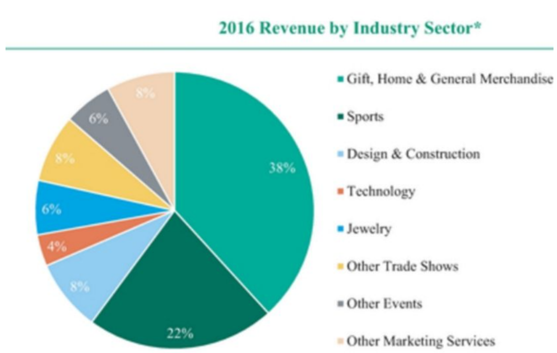


Nielsen documents do note that a restructuring was conducted immediately following the crisis, such that segment EBITDA dropped from 93 million in 2008 to 63 million in 2009, but bounced back to 78 million in 2010 despite the revenue decline, and reached $94 million (or, rough parity with the prior peak) by 2012, despite revenues still languishing a full 25% below 2007 and 2008 levels. It is worth noting that the business displayed 50% decremental margins during the financial crisis – i.e., EBITDA dropped 33% on a revenue decline of 25% – and of course, the restructuring helped restore profitability, but given robust existing margins, that completed restructuring, and the years of private equity ownership, I don't think there are more rabbits to pull out of the hat here, and you do have to make the assumption that the business would see meaningful revenue declines, coupled with operating the leverage, in an economic pullback.

From a cost perspective, roughly 6 to 7% of revenue is spent on decorating booths, 5% is spent on sponsorships from industry associations (which appear to be pretty important), 4 to 5% is spent on the venue, 2% spent on marketing, with miscellaneous expenses, labor costs, and other event related expenses comprising 40%.

<u>Business Mix, Strategy</u>

According to the company, roughly 92% of revenues are attributed to its shows; as I previously noted, the vast majority this revenue is attributable to booth space sales, with the balance attributable to attendees and perhaps some ancillary services. Roughly 8% of their revenue is attributable to a dozen regular frequency magazines aligned with their trade shows. The mix is below



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Clearly there is a major emphasis on retail here (at least in so far as the majority of the company's business appears to be with companies making consumer products that are selling them on a wholesale basis to retailers). I did notice Amazon among their clients, and it seems that the purchaser-buyer interaction will be fairly durable regardless of whether these products are being sold in stores or via e-commerce. However, to the extent that e-commerce may drive more winner take all dynamics, consolidating buying power in the hands of a few bigger chains vs. a number of fragmented, small chains, this would be negative for their business.

As demonstrated by the chart earlier, there's not a lot of volume growth in tradeshow attendance – I think GDP is about the best you can expect, and possibly lower for some of the shows. However, it seems like there remains pricing power in the industry, and the rate of inflation in booth costs seems to be less than the rate of inflation in travel and other costs. The company's organic growth strategy is to use pricing (on a disciplined basis), while also occasionally trying to introduce new shows and/or add on events to additional shows. This dynamic was discussed in a very interesting one hour panel discussion with the CEO of Emerald, the CEO of competitor Diversified, and the founder of a small website about programmatic advertising.

One of my major takeaways is that it is hard to start new shows – although the barrier to entry is somewhat smaller for existing operators. It sounded like fewer than one in five new events actually "take", and the goal is usually not to be free cash flow positive in the first year, but rather to just get the event to the second year and see if you can scale from there. As you might into it, there is a strong bellwether effect, wherein to get a new show started, what you really need is to get referenceable clients on board – i.e., for construction conference, if you get Caterpillar and AECOM, things will start to fall into place from there. Clearly, being the existing host of a strong industry event, and having relationships with industry associations and so on, makes it easier for a company like Emerald to start a new show than someone else – but it's still very difficult, and this should not be expected to contribute a time of organic growth. In some areas, the company may have the opportunity to expand existing shows with new features or components, but this also seems like fairly limited scope.

Therefore, the bigger component of the company's growth strategy will be inorganic – i.e., M&A to consolidate a fragmented industry. The company notes that the top four or five vendors only comprise about 10% of the market, leaving plenty of white space. The panel discussion I referenced above notes that both private equity and strategic firms (for example, Informa/UBM/Emerald) have demonstrated an increased attraction to the events business over the past half a decade, leading to an environment that was characterized by the panel on multiple occasions as extremely friendly to sellers/"robust" valuations. While Emerald alleges that it has been able to acquire companies for a mid to high single digit EBITDA multiple, and I expect it to be able to source acquisitions going forward, I don't think these will be ridiculously cheap or accretive – clearly there is interest in the space, and Emerald is not the only natural acquirer.

Meanwhile, I question whether synergies are really all that meaningful – I don't think there's a tremendous amount of scale in things like purchasing decoration, given that these are likely to be local vendors; there may be some room for G&A savings and venue savings and so on, but I don't view this as hugely meaningful – the capital light nature of this business also means that you don't have the sort of synergies you would in manufacturing deals. That said, the company did just implement a new ERP, and I don't believe that the smaller vendors they pick off (for example, a recently launched drone conference) will have the same level of infrastructure.

From a quality standpoint, however, I do believe that Emerald is a very well-run business. The company cites its renewal rate as an example of its management strength – their weighted average renewal rate of 81% over the period from 2014 to 2016 (83% including winbacks of exhibitors to did not exhibit in the prior show) is ranked at the 95^{th} percentile for the industry, according to industry sources. As previously discussed, the company's events also tend to be very large and consequently probably very profitable and "must attend" vs. smaller events.

All in all, there are indications that this is a well-run business, but I have not been following the industry long enough to understand the nuances and/or the KPIs that I should be following. Therefore, I will reserve further judgment until I have had a chance to work on the competitive group, and am able to effectively compare and contrast this company strengths with that of its peers.

Management / Valuation/Due Diligence

CEO David Loechner appears to be well-respected in the industry, although that's about all I can say so far.

The company's filings state that there are 72.2 million shares outstanding pro forma for the offering. However, reading through the registration filing, this number seems to exclude 7.2 million options that were issued a while back that have a weighted average exercise price of just under $11. Therefore, if all these options were exercised, the net impact would be to increase the share count by – roughly – 3 ½ million shares. Therefore, I am using a share count of 75.8 million for the purposes of my analysis, and will update this in future periods.

The company reports a metric called "acquisition adjusted EBITDA", which is essentially adjusted EBITDA plus the pro forma impact of acquisitions completed during the year whose financial results were not fully captured in reported earnings due to event timing. For 2016, "acquisition adjusted EBITDA" was $158.5 million; assuming 3% organic growth year on year, that puts us at $163 million or so for FY 2017. However, I am assuming that the company will incur roughly $10 million of public company costs that were not captured in adjusted EBITDA in 2016. Furthermore, I am assuming $10 million of unacceptable adjustments, including stock-based compensation as well as ongoing expenses to source deals. While I am willing to view restructuring and integration costs as part of the acquisition cost of a company, I am not willing to view deal sourcing as a special / one-time cost, since it seems to be part of their business model going forward.

That leaves us with about $142 million of estimated 2017 "true" EBITDA, on revenue of roughly $340 million (representing 4% year on year growth; I could be underestimating a little bit depending on acquisitions). As discussed, this is a very capital light business model; backing out about $4 million or so of assumed run rate, and applying a 37% tax rate, I get to NOPAT of $87 million. I'm pegging fair value at about 19 times EV/NOPAT (11.5 times EBITDA), which gets me to a fair enterprise value of roughly 1.65 billion, or a fair share price of 16, contrasted with the current share price around $20, and the current enterprise value of 1.9 billion.

In terms of the balance sheet, the company's debt load should be reduced to about 540 million pro forma for the offering, less a little bit of cash. Leverage, therefore, is still meaningful; with $150 million of "cash" EBITDA, net leverage is somewhere in the 3 ½ to 4 times range (closer to the lower end). While the cash flow characteristics of this business are good, there certainly is the potential for meaningfully reduced revenues in an economic down cycle, and I wouldn't be comfortable with owning this business at this leverage level – I would want to see something in the two and half times range. The good news is that they should generate just shy of $70 million of free cash flow I year; therefore, they should be able to drive leverage down by just under half a turn per year, assuming no further acquisitions – and assuming that acquisitions were completed at a lower multiple than they are currently trading at, these would be delevering as well.

Finally, I am also giving the company credit for roughly $96 million in deferred tax assets – they have about $20 million related to NOLs that will be utilized in 2017; they also have long-term, tax-deductible amortization, the present value of which I very roughly estimated at $75 million (and probably on the conservative side here). I count these as a favorable offset to enterprise value, just like cash or long-term investment. Some of this value will accrete every year, so need to make sure to subtract from this row in my model as time goes on.

Risks/Red Flags

ONEX continues to own a controlling stake in the company, so there's takeunder risk here.

The retail focus could also be a risk if more and more bricks and mortar retailers are put out of business and bigger players take share (reducing the fragmentation of the industry and therefore the value proposition of trade shows). This wouldn't blow up the value prop by any means, but could lead to pricing pressure and slower growth…

Expectations/Action Items/Summary

Ultimately, I think this one is a little away from actionable for me, both due to my unfamiliarity with the industry/business, the aforementioned questions around true organic growth, and the cyclical downside potential combined with the balance sheet. However, this was a very interesting introduction to a new niche within the professional services space that I had never previously looked at; my next step is to analyze businesses like United Business Media, Informa, and RELX Group.

I also want to spend some time browsing around here - http://www.tsnn.com/

Ongoing Monitoring/Journal

/// TBD ///