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IMAX Corp. (IMAX)

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CORPORATE PARTICIPANTS

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

OTHER PARTICIPANTS

Drew Borst

Analyst, Goldman Sachs & Co. LLC

MANAGEMENT DISCUSSION SECTION

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Great. We'll get started with our next session. I'm pleased to welcome to the stage IMAX. We have Rich Gelfond, the CEO; and Patrick McClymont, the CFO. Very pleased to have them here again.

Rich has been with IMAX since mid-90s, 1994 I think, is when you made your original investment. He's really helped transform IMAX at that time. Kind of focused on nature and science and space documentaries and museums and he's really pivoted the company. More than a pivot, so dramatic shift and made it into one of the leading networks for commercial tentpole action films around the world. You're up to over 1,200 theaters in 75 countries, so it's a pretty amazing run.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

1,600 in 82 countries.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Oh, pardon me. Wow, even better yet.

QUESTION AND ANSWER SECTION

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Let's start off with some big picture questions. On that point, the network continues to grow. You're on track to add 140 to 145 new screens this year. A little bit slower than last year, but not dramatically so. Where you see the biggest opportunities over the next few years to drive network growth?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

The big markets for us, which have been exploding in recent years have been the Middle East, Japan, Western Europe and China still continues at a very fast pace. So, the really good news about some of these markets is, the theaters there are extremely successful. So on the Middle East, we have about 30 theaters in that market. Saudi Arabia, as you all know, recently opened up to cinema and we have some very successful theaters in that market. Japan has – not surprising to many of you, Japan is usually not the first one to go into a business. But when it works and they go in, they go in in a big way, so we have about 35 theaters in Japan right now and probably another 10 in backlog, but a lot of activity there that's going extremely well.

Western Europe, surprisingly, we're still somewhat underpenetrated. In the UK, we have about 50 theaters, so that's done very well. And France has also done very well. But countries like Germany, Spain, Italy, are very under penetrated.

China, because we've been so successful there, true as you know we have 650 theaters opened. I keep waiting for it to slowdown, but it doesn't. And, we just signed a 40-theater deal with CGV this year, the Korean company, and there's a lot of activity in the pipeline, so that keeps going very well.

And then, India has also become strong. India was slow for us for a number of years, because of, I think the lack of transparency and the lack of construction. But in the last year or two, India has started to provide us with about 10 signings a year. So, we're up to 20-ish theatres in India and another 10 to 20 in backlog. So, our global growth pattern continues to advance nicely.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Yeah. There's plenty – some of those "emerging markets or developing markets" seem like fantastic opportunities, a lot of runway for you guys to grow. But I did want to pick up on one thing that you mentioned and ask a follow up, which was just about some of the European countries like Germany, Spain, Italy, I mean those are pretty big box office markets. When you look at it globally, U.S. films play pretty well there. There's also heavy local content. Is there something structural that makes it more difficult to get better penetration in those markets?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

I think it just takes time. So, there are two elements for us to build out a market. One is successful reference theaters. So people go, look at and said, oh, IMAX works in this territory. And the second one is competitive theater chains.

So, it's like in England for example, for years, our only client was ODEON, and they had theaters that did well, but they took their time. And then, when other companies like Cineworld got into the business more rapidly and Nordic Cinema, which is now part of AMC, the existence of the competition really generated the growth. So, that's been very much our strategy in the countries where we're underpenetrated.

So, in Germany, our per screen averages are extremely strong. We opened three or four theaters over the last 12 months and they're all doing quite well. So, I think what – you need those two dynamics and they're starting to happen.

I think Spain and Italy are a little bit different. Ticket prices have been low. They went through a relatively slow phase in the last couple of years. Another market I didn't mention, which is high potential for us and a big way to go, but hasn't taken off is LatAm.

And I think in Mexico, we have a fairly strong presence. But in South America, we've started to get some good reference theaters in Brazil and Argentina. But I think those places were traditionally held down by tariffs and high tax rates, but that's starting to turn around particularly in Brazil right now. So, that's a little way off, but that has potential.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

And in South America – I mean, Cinemark has a big presence down there. Are you going through them or is it from some of the competitors, local competitors?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

[indiscernible] (00:05:32) that we have more significant presence with UCI down there. Also, I think Cinemark has the same issues about taxes and importing things. Their network was there a long time ago, so they had a lot in place, but there were more structural issues in that market.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. I want to ask, you had a pretty significant backlog of – I wanted to – given what's going on with the economy, what's the risk that the backlog doesn't come through? Is that something that you've seen historically? Does it correlate with economic cycles? Is it not really an issue? How should we think about it?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

Well, in 25 years that I've been here, I'd say at most, we've written off a handful of theaters in the backlog. And the reason for that is, before we put it into backlog, we either get a significant upfront deposit or if somebody who's quite credit-worthy.

In 2000 and 2001, when cinema went through a lot of consolidation and issues, that's when the limited trouble with the backlog happened, but that really hasn't happened in almost 20 years, and I don't really see a significant risk there.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. That's pretty good. I wanted to ask about the laser projector system. I think you're approaching about 10% of your global network. You know, talk about the outlook for the rollout for laser and how the economics compare to the traditional xenon system.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

One thing about our philosophy at IMAX is, we're constantly innovating. We think, if we don't innovate, we're going to lose ground. And for us, that means expanding the difference between regular cinema and IMAX to justify the price premium. So, we recently introduced laser, which is a much, a much bigger leap than traditional digital IMAX. We introduced the new sound system. We introduced different kind of seating, and we're always trying to justify the price premium that we charge and make sure audiences are happy to pay it. And in fact, some consumer surveys we've done and we need to do more, because it just started the rollout show that people are very satisfied with laser. I don't remember the exact number, but like 70%, our top-two boxes, where they really like it. Patrick, maybe you want to talk a little bit about the economics.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

Yeah. The economics, I think the proof is in the pudding, which is we announced it about a year-and-a-half ago now with two large customers and 143 systems. Since that time, we've added additional signings and we're up to about 230 now. The value proposition for our exhibitor partners, we went to them and said, we've now created something that is clearly the best-in-class consumer product. And we want to partner with you. And the basic proposition was, we want to maintain constant value to IMAX.

Our cost of goods sold on the system is a bit higher than the xenon system as you'd expect. And so we are charging our customers more either more in upfront purchase price or more in terms of the economics we're taking from box office over time, but we're solving for the same deal value for IMAX. And our customers agreed to that, because they see this as a game changing platform. They know that being in the IMAX business drives, not just higher ticket price, but also incremental foot traffic and demand at their multiplex. And so, that strategy has worked really well. The rollout is going very smoothly.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Okay. This year Avengers: Endgame was filmed entirely with IMAX cameras. I think you have films for next year that will also be similar, James Bond, I believe, Christopher Nolan's Tenet, Wonder Woman. Can you talk about the importance of filming it with the IMAX cameras? I mean, what does that mean to the studios, the directors? What does it mean for you guys?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

Well, when you look at traditional indexing of IMAX films, there are two ways to release films. One is they've been filmed with regular cameras and we use algorithms to oppress them, to make them look really good on that giant screen. The other way is to use IMAX cameras. And when we've used IMAX cameras, the indexing is traditionally higher. For some of the films like Chris Nolan's Dunkirk, we did 23% of the U.S. box office on less than 1% of the screens. So it really can make a significant difference in the movies. We have – in the performance, we have a conscious strategy going on to try and get more films using IMAX cameras and it's working empirically.

So, last year – well, this year, for Endgame, the whole movie was filmed by the Russo brothers with IMAX digital cameras and we recently have put together a program where we made it easier for filmmakers to use their favorite digital cameras through a suite of lenses that were putting together and create a film in IMAX Experience. So Endgame was the only movie this year that was filmed with IMAX cameras. In 2020, at the moment, we have five films being released filmed with IMAX cameras.

So, as you mentioned, Wonder Woman, Tenet, which is a Chris Nolan movie, and Bond have all been filmed with IMAX film cameras. And then Top Gun, and Dune are scheduled to be filmed with IMAX digital cameras. So I think that will make a tremendous difference having, we call it, IMAX DNA, having that much IMAX DNA.

And we have a new Head of Entertainment, who came in this year. Her name is Megan Colligan, and she has visited every studio, and she has visited with filmmakers with a whole package of why using the cameras makes sense, and I think that's one reason next year is better. And I think that's one reason other years will be better.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

Yeah. Rich, if I could just add, we're also employing the same strategy in China with film makers there. We have cameras in China now that filmmakers can use. We're going through the process of developing relationships, educating the filmmakers on how to use those cameras and there are a few films that will come out in the next little while that use IMAX cameras for local language films in China.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Wanted to ask about the subscription plans that the US exhibitors have been rolling out, the AMC A-List program, consumers can see any movie in any format including IMAX for their \$20 to \$24 monthly price. But with Regal and Cinemark, they're applying surcharges if you want to see the IMAX format or large screen. I wonder if you could just share with us what you're seeing from the behavior of customers and their willingness to maybe upgrade when they have that Regal or Cinemark plan to.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

So the Regal plan was launched in the last month, so it's hard to give meaningful data at this point. However, there's nothing new about those plans. There is in North America, but they've existed in Europe in some cases for decades the path they won in the Cineworld plan I think are over 15 years old. And they've been very successful, because what happened is I think when people pay their \$20 a month, they see that as a sunk cost. So when they can see Tenet by Chris Nolan or they could see a Marvel film for the \$5 surcharge it seems like a bargain, it's only \$5 to see it. In this way that's so special.

The AMC plan arose partly because of movie pass at that time. And I think AMC was concerned about the impact of movie pass on the theater going experience, so that's why they devised it a little bit differently and they gave people the chance to go to IMAX for the no additional surcharge.

From our point of view, the AMC plan has been very successful and our results with AMC have been very strong. We made significantly more money than we made the year before when they didn't have the plan. How this all shakes out though, Drew, I'm not sure. I think we'll see what the data is from the Regal plan. We'll see what the return is to Regal. I'm not completely sure what the return is to AMC from that plan. And in time, we'll see which one works best, but I think it's only a net positive for us.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. I wanted to ask about what's going on with direct-to-consumer, and how that may potentially have impacts on your business. When you look at the major studios, Disney, Warner Brothers, all of these companies are going to either will launch or have launched a direct-to-consumer service. And when you talk to investors, I think many of them are concerned that, as those services start to scale that some of these companies will start to shift theatrical product into those services rather than going a traditional release. What's your view on that? Do you think that that's likely or that's a risk or – and how would it impact your business if it did play out?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

For IMAX, I don't think it's a risk. As a matter of fact, I think it's an opportunity. And the reason for that is IMAX eventizes content. So now we're in the movie business. That's what we're eventizing. But we even did a small piece with Netflix called anime where we eventize before they released it in streaming a few days later.

So I think they all know that with all the content being created that somebody has to curate for the consumers, which content they want to see and IMAX has definitely served that function in the feature film business. And I think one reason studios like IMAX so much is, when consumers wake up on a weekend and they don't know what to see, I think IMAX becomes a shorthand for that's an important thing to see.

I think it's clear, the streaming services know that also, because you look at what went around, around the Irishman and you know the streaming services really wanting a theatrical release badly. And as a matter of fact, with Amazon, we're doing a theatrical release in the UK of Aeronauts (sic) [The Aeronauts] (00:16:08), which comes out in a couple of months. And we've talked to all of them, because they know in order to create a want-to-see, they just can't put it up online and believe people will come.

With that said, the other part of your question is, what happens to the traditional studios? And I'll use Disney as an example, and I was just there last week with a lot of the senior executives, and they get it that way they can maximize the return on a property is to release that over different windows. So, I don't think, I don't know what you'd think that Avengers would be nearly the success it was by releasing it online in different places. We create these worldwide events around it.

And from the studio's point of view, it's different, because the streaming services, their economics for now are based on selling subscriptions, right? So for them, trying to package it and sell subscriptions is their economics. But for the studios, it's really about creating franchises and long-term value and Disney wants to create sequels, they want to create theme park rides. They want to create games, they want to create T-shirts and I think I mean, they said it, I think they know that the way to create that isn't to launch it on a weekend and you know with no disrespect at all for either Scorsese or Netflix, I do think launching a three-and-a-half-hour film online is not going to create the same kind of worldwide excitement and worldwide buzz that releasing a blockbuster through a traditional means do.

And without belaboring the point, I think the industry has faced greater challenges like the invention of TV and the invention of DVD, but I think the consumers' desire to congregate in social experiences and particularly when it comes to IMAX eventize things isn't going away, because a new delivery system is in place.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. How do you – like The Irishman, which got a lot of attention, is there a role for you to play. And it does seem like even Netflix – Scorsese certainly wanted it theatrically released, but – and it will be in some theaters, but the big three are – still seem pretty resistant and are very sensitive to the windowing and having exclusivity.

Netflix is obviously – wants to do kind of a day-and-date release and that remains a big tension point. And look, your network, you guys control what gets displayed, but you also have these deep relationships with the big three. Like, how do you sort of balance that? I mean, is there an opportunity for you to be more aggressive and helping Netflix or maybe Apple down the line as they do? And some of the films are starting to do – become action movies. That would typically play well in your circuit for your network rather. I mean, how do you think about that that delicate balancing act of your traditional exhibitor partners, but an opportunity on these sort of newish studios?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

So, we would love to have the opportunity to play some of the blockbusters streaming movies in IMAX. But our partners, as you say, were housed in multiplexes even though we have nothing to do with being an exhibitor, we're a technology licensing company. But as long as we're housed in those places, we're going to respect the window that they agreed to. Period. End of story.

On the other hand, going forward, we would love if there was a compromise of some sort reached that worked for the exhibitors and allowed us to play some of that content. And behind the scenes, we're hoping to facilitate that. And again, because we eventsize things, we could be helpful to the people at least in that content and we think we could drive the box office for exhibitors. I mean, it's just unequivocal for us. The exhibitors have to agree on what that is and then we'll go along with that.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. I was wondering if you could give us an update on some of your key commercial relationships. Meaning, you've got long-term arrangements with the various film studios on kind of the supply side. You also have generally long-term relationships with various exhibitors. I recognize you probably don't want to get into any sort of one company or one relationship, but is there any way to sort of describe the status of where you are in terms of when contracts expire with the studios and the same question, I guess, on the exhibitor side?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

The contracts are one thing, the relationships are another thing. And I think with all the studios, people want to do more IMAX releases than we have the capability to do. So we're already talking to all the studios about next year, the year after, the year after, and those relationships, they're not my relationships, they're not Megan's relationships. They're organization-wide relationships. And Disney would be one great example because, obviously, they're an important supplier to us, but we're embedded with them in the marketing department, and I'm sure you haven't seen it. But if you looked at the direction of the marketing, we're much more integrated with Disney than we were. We're integrated in the distribution department. We're integrated and maybe most importantly with the filmmakers. So, we're talking to them about what we might do with IMAX cameras years out. So, the contracts have different expiration dates. But from my point of view, they're a rounding error because they need us and we need them, and it's a relationship that works very well.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. And I guess, it's sort of a similar view on with the exhibitors sort of symbiotic relationship, I guess.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

Yeah, it is. And we have great relationships on a worldwide basis. And I think consolidation in the exhibitor space has been a very good thing for us. Because as Wanda bought AMC, both were our clients, but AMC became a bigger client. And when Cineworld bought Regal, Regal became a bigger client. So, the winners in the consolidation game are generally the bigger chains that have a longer history with IMAX. So, our relationships are excellent.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Let's talk a little bit more about international. Just under 50% of your screen footprint is in China now. The China IMAX network grew by 97 screens this year and is poised to continue to grow. Can you talk a little bit about sort of the multiyear outlook for China and driving more screen growth? What is your view?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

I mean, I think the IMAX bet is a bet on the Chinese consumer in China. And I think there's a lot of noise in China, which we all know well. We turn on our TV every day and hear about it. But our box office in China this year is up 30% year-over-year and it's been up eight quarters in a row. So, I think our same-store sales are up almost double-digits in China. So I think the real performance – we're not a manufacturer, we're not an exporter, we're a play on the retail consumer there, and it's going extremely well. Patrick has been spending more time over there. He goes over there once a month now, so maybe you want to talk a little bit about growth prospects?

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

Sure. The way we look at China, we've talked about the addressable market there being about 1,100 screens. We're at 650 now plus a little bit short of 300 in backlog. So, from an installed base, we're kind of around halfway there. If you include the backlog, we're three-quarters of the way there. We're in active dialogue with our clients in China about additional signings. We signed a 40-theater deal with CGV, other smaller deals with partners there.

It's interesting. When I go to China and I'm meeting with our exhibitor partners, we're the best part of their business right now. Our strategy in China of picking multiple films, local language films, and having those available for our partners gives them tremendous flexibility so that they can ramp up the showings of the film that's working best in IMAX. That's been hugely successful for us and for them.

This year, we did Wandering Earth. We did a film called Ne Zha, both of which ended up being now in sort of top – in one case, top 5; another case, top 10 all-time box office performers for IMAX in China. So, our business model is extremely flexible, very focused on delivering value for the customer – the exhibitor customer and we see further opportunities to grow with them. And that's against the backdrop in China that's a little bit unsettled right now. Box office overall is flat to a little bit down. So, we're really punching way above our weight in that market.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

But it doesn't sound like all the trade tension that's going on presently at a macro level hasn't had a discernible impact on your business?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

I haven't sensed any impact on our business. I mean, I think the noise impacts investors more than it impacts consumers. And literally, I mean, the last couple of years we've done a number of changes, such as, Patrick alluded to, we're playing more films at the same time. We did a joint venture with a company called Maoyan which has 55% of every ticket in the country is sold through Maoyan. So we have much more intelligence, much more data to make better decisions. But no, it hasn't really had any impact on us.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

The shift to more locally produced content versus the Hollywood, I mean, what sort of impact does that have on your economics, on your margins. Is that a positive trend for you?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

It's a positive trend for us. Because the studios get a smaller take rate in China, they only get 25% rather than an average of 50% worldwide. Our take rate is lower in China. In North America, generally it's around 12.5% on Hollywood films. And in China, it's 9% on Hollywood films because of the take rate difference. But on Chinese local content, we get 12.5% of the box office. And as Patrick was talking about, the local language films that did very well this year were in different genres. One was a sci-fi film and the other was an animation film. And as their box office approaches \$10 billion, they can create better local content because they have the ability to recruit more expensive movies through the bigger theater network. So that's a good trend for us.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. And are the play periods for the local language pretty similar to Hollywood? Like, I'm wondering if you're doing more DMR volume than maybe in the US or is it not really that different.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

The play periods are pretty similar. What typically happens is there'll either be a formal blackout period where there is no Hollywood content and so then we're releasing local content or it could be a holiday period where so many Chinese films are coming out. That will be the winning strategy to focus on those. But, yeah, it's typical, we make most of our money in the first couple of weeks similar to a Hollywood title. We've got flexibility to change show times or showings to optimize the outcome.

And then from a DMR perspective, our team has worked really hard to make sure that we've taken a lot of cost from a process standpoint out of DMR. We're able to do things that are overwhelmingly the technology now as opposed to human intervention value-add. And so, we can do it in a pretty streamlined fashion. If we're releasing three or four movies on a weekend, we have to do it in a very efficient way.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

One thing about China is the operator is much more flexible on playing multiple films. So, in the US, that's starting to happen. But the studios, historically, have resisted that. They've said, if we're releasing this film on day one, we want you to only play that for two weeks. In China, they're much more open about mixing and matching films. So, although it's the same play time, if a movie is really working, you can have a longer tail to it. So, Wandering Earth, for example, would have played for four or five weeks over there and we were able – we had \$50 million in IMAX box office over there. The film did about \$700 million. So, that flexibility really helped us.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Are you doing more, I guess, what I would call day-parting or where you might show certain film in the afternoon, a different one in the evening, or is that not really an effective strategy?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

You mean, in China or...?

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

I meant in China. I'll probably ask a follow-up on the US, but first on China.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

We do, yeah, absolutely. So, as Rich said, the exhibitor partners there are very nimble and they'll make changes very quickly. And so, what they'll typically do for one of these weekends is within one multiplex, they may try offering movies we release at different times, and then typically by Saturday and Sunday, they're starting to shift it already to try to sort of draft behind the most successful title. So, it's definitely a part of the strategy in China. And then, yes, we experimented with it more broadly as well. There can be times where we have two movies that are available. Maybe one skews younger or family and we'll do daytime showings of that, the other one may skew more adult, and we'll do the evenings with that. So we've got that flexibility.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

It sounds like they're driving that decision or is that in concert with you guys or how does that work?

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

It's a partnership discussion.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Because I always thought in the US, it was more sort of you guys program the network and that's sort of the way it goes and the exhibitors, they could have input, but [indiscernible] (00:30:27)

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

We have a lot of rights to program. Again, like the answer I gave you, the contracts before, I mean, you work with these people every week over 20-plus years. I mean, the way to have a good relationship is really to work with them rather than to say, well, the contractual provision says this or that. So we usually consult with them about it.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. I wanted to ask you one of the exhibitors, AMC has been talking about experimenting, I think they're running a beta where they're kind of doing, I guess, blockbuster surcharges for films or in peak periods. How would that impact your decision to price IMAX? Would you kind of price up IMAX on the back of that? It could get complicated because maybe AMC is the only one doing it while the other exhibitors aren't. But what are sort of your initial thoughts on that? I know it's very early and sort of in test phase, but what are your early thoughts?

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

So, first of all, we don't have the right to price in the theaters. They set the pricing. But with that said, China has dynamic pricing and it's been an incredible success for us. So, the last Avengers, I don't remember what the name of it was, the second one in the series, the price point in China for IMAX was around \$9. And Avengers: Endgame, the price point was \$20 and that was set by exhibitors. And if you looked at total attendance, it was similar for us between the two, but our box office was double the first one because of dynamic pricing.

So I think when you're in the blockbuster business, which we are, and in the early days, there's so much demand for a lot of these movies. That would be a good thing for us. It could be interesting with AMC, though, because obviously the studios have an interest and you're probably aware of this, but one of the pushbacks the studios have had on dynamic pricing is that they're afraid that it signals which film is better and which is worse. So when you come out with a movie that people aren't anxious to see, do you price it down and is that a signal to people not to see it. So I really respect them trying it, but I think it's complicated.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. It's probably a little less controversial to do like peak time periods, right, like weekend is more expensive than weekday or that type of thing. And I guess, as you said, it's a partnership. So I assume they kind of consult you on how they're going to approach that. And I guess, they probably just keep their pricing up on a Friday night. They probably just price you up by the same increment there.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

A

Again, I don't think we've yet gotten into those discussions, but you would hope there'd be two-way discussions.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Yeah. I want to ask a few questions about costs. You've been managing your R&D and SG&A pretty tightly. It's down 10% in the first half of the year. Can you elaborate on IMAX's cost savings program and whether there are incremental opportunities to manage down the cost base over time?

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

Yeah. I think over the last handful of years, we've done a very good job keeping total operating expenses flat. That started in 2017 when we did a restructuring focused really up and down the P&L and we also use this as an opportunity to try to change the culture and the approach. We've been able to maintain that flat operating costs.

The way we've done it is really we want to be in a position where there are certain areas where we can either keep grinding away at costs or we've made strategic decisions to deemphasize. And R&D is the best example. We did develop a best-in-class, extremely successful commercial laser platform. And once that was launched, we looked at it and said, we don't need to have these R&D resources kind of hanging around for the next project. Let's reduce our investment in R&D for some period of time. We'll keep a team that's focused on cost curve issues, taking down our costs in our systems and available to think about what could be next. But we took that down to a more base level and then we took that money and we reinvested in areas where we want to drive growth, primarily marketing and also some innovation ideas. And so that's been the approach more recently.

Let's look at our value chain. I talked about DMR. We've taken a ton of cost out of the DMR process. Post-production, we're actually finishing the films and distributing to our customers. We've taken a lot of cost out there. We're at the point now what we're going to do is when we find those is let's reinvest those and things that will drive the top line. And that's the philosophy, we're diving into the budget right now for next year and that's the approach for next year as well. Let's be very disciplined, but also where we've got win behind our sales, let's further invest.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

I think if I do this correct, while you're down in the first half, like when you look at the full-year guidance of flat, it looks like there's a little bit more cost growth in the second half of the year. Can you just briefly remind us sort of what's going on with that dynamic?

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

It's mostly timing. A lot of it's actually just timing of head count positions being open when they get filled, marketing expenditures when they flow through the P&L, there's nothing structural there.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Q

Okay. We have a few more minutes. I want to give the audience an opportunity to ask questions. So, if you have a question, please raise your hand and we'll get a mic to you. I want to ask about your balance sheet. You guys are in a net cash position. Your model is different than the exhibitors, but they historically have had a couple of turns of leverage. Can you just talk about how you think about the balance sheet and where there's maybe an opportunity to put some debt on the balance sheet?

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

A

Sure. I think, just to clarify, we are in a net cash position. The way that our business works, most of that cash is actually within the China entity. When you look at IMAX core, ex-China, we've got a little bit drawn on our revolver, we have a little bit of cash, but there's not a meaningful cash position right now outside of China and we

can get the money out of China. We do. China pays dividends. Most of those go back to Corp. And over time that will increase, but the face of the balance sheet shows a bit more cash than what I could actually deploy right now without paying a little bit of a tax to get it out of China.

The way we think about it is the first thing we want to do with our capital is invest in growing the network. We still see opportunities to invest in our JV partnerships with our exhibitors where we're keeping the assets on our balance sheet and sharing in the box office. Anytime we've got an opportunity to deploy that capital, where we see a good return on the invested capital, we're going to do that. And you'll see that we spend \$35 million, \$40 million, \$45 million in a given year on those types of investments. That makes the network bigger, that creates more enterprise value, that's the first best use of our cash.

After that, we've concluded that when we have excess cash, it makes sense to buy back stock. We had a \$200 million program that wrapped up in 2017. We put another program in place. We spent about \$75 million against that. We're opportunistic about it, the price at which we're comfortable buying stocks. So, that's what we'll be doing. And at some point, as the network continues to grow then we'll think about things like dividends. But right now, we want to have the flexibility to invest in driving growth in the network.

Drew Borst

Analyst, Goldman Sachs & Co. LLC

Okay. Well, thank you, guys. We're out of time. I really appreciate you being here.

Richard Lewis Gelfond

Chief Executive Officer & Director, IMAX Corp.

Thank you, Drew.

Patrick S. McClymont

Executive Vice President & Chief Financial Officer, IMAX Corp.

Thanks, Drew.

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