Gray Television, Inc. (NYSE: GTN) – Levered Value with Growth Kicker Opportunity

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Trading Stats (as of 26-Mar-21)		Financials	FY19A	FY20A
Share Price	$18.16	Revenue	$2,122	$2,381
Market Cap.	$1,906	Growth %	96%	12%
Net Debt	$3,259	EBITDA	$618	$923
Preferred Equity	$650	Growth %	39%	49%
Enterprise Value	$5,815	Margin %	29%	39%
52W High	$21.22	EBIT	$481	$734
52W Low	$9.19	Growth %	22%	53%
% Free Float	93%	Margin %	23%	31%
Short % of Float	2%	UFCF	$182	$536
EV/LTM EBITDA	6.30x	Margin %	9%	23%
P/LTM Dil. Common Stock EPS	4.85x	*All data is in USD and Millions except per share data		

Price Target	
Bear Case	$19.16
% upside (downside)	6%
Base Case	$23.57
% upside (downside)	30%
Bull Case	$32.26
% upside (downside)	78%
Price Target	**$27.03**
% upside (downside)	**49%**

Investment Recommendation

This pitch presents a recommendation to LONG Gray Television, Inc. (NYSE: GTN) with a conservative price target of **$27.03**, reflecting a **~49% upside** and **significant margin of safety**. Gray Television offers a compelling "levered" value investment opportunity with a growth kicker due to (a) **sustainable competitive moat**, (b) **increased political revenue**, (c) an enticing opportunity to expand its footprint in the fast-growing e-sports and streaming sectors, (d) the potential for accretive **strategic acquisitions**, (e) **strong financials** and dividend policy, and (f) an **attractive valuation** in the current market.

Business Description

Gray Television, Inc. is a publicly-traded broadcasting and television company based in Atlanta, Georgia, and is a part of the Russell 2000 Index. In 1946, James Gray founded the business with the purchase of *The Albany Herald* and the launch of the company's first television station (WALB-TV) in 1954[1]. Over the past 75 years, the company has acquired over 100+ stations and operates in 94 markets with 160 affiliations with the Big 4 television networks (ABC, Fox, CBS, NBC). It is also involved in video program production, marketing, and digital business through its subsidiaries.

Raycom Media: Raycom is a sports television program producer based in Charlotte, North Carolina, and a subsidiary of Gray following a $3.5 billion deal in 2018[2]. The company owns and operates television and radio stations and focuses on providing sports-oriented programming. Raycom syndicates sports videos and events, hosts different football and basketball shows, and has produced preseason games for various NFL teams.

Quincy Media: Quincy is a media company based in Quincy, Illinois, and a future subsidiary of Gray following the confirmation of a $925 million acquisition in 2021[3]. The company is involved in different media segments such as newspapers, radio stations, and television stations. Following the acquisition, Gray aims to divest certain stations and assets of Quincy to comply with legal compliance terms and increase operating efficiency and profitability.

VUit: VUit is a local news OTT platform that allows users to stream local news for free from any device in a live or on-demand format. The app is available on devices such as Roku, Firestick, and iOS and Android devices. Gray, along with Syncbak, launched the venture to capture digital ad revenue and combat cord cutting.

Premion: Premion is an OTT advertising solution that allows advertisers to access advertising inventory across premium, branded OTT sources. The service has direct partnerships with over 125 OTT providers and networks. Premion places ads in prime-time live, live sports and news, network programming, and VOD content.

Other Subsidiaries: Other key assets Gray operates include journalism assets such as *Full Court Press*, a national weekly syndicated political news show, *Gray Washington News Bureau*, a local news-oriented channel reporting from Washington D.C., and *InVestigateTV*, a team of investigators committed to investigative journalism. The company also has marketing and production companies such as *RTM Studios*, a television marketing and media company focusing on automotive tech content, *Swirl Films*, an independent film and T.V. production company, and *Tupelo Honey*, a company developing programing and branded broadcast features for venue entertainment.

Investment Thesis

I. Sustainable Competitive Moat

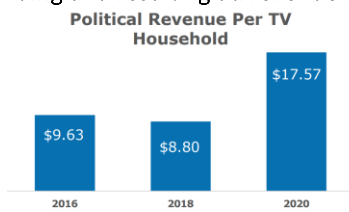
Gray Television boasts a strong competitive advantage and moat due to their long-standing customer loyalty in their 94 television markets. Their market dominance, evidenced by the fact that they reach over 25.4% of U.S. television households[4], leads to high brand awareness. More importantly, the company has consistently been ranked #1 in ratings between all local stations, local newscasts after 6 PM, and the #1 ABC, NBC, and CBS station. Furthermore, the strong connections Gray's channels have with the Big 4 television networks via their 160 affiliations offer future protection from the national players' market scalping. Following the COVID-19 pandemic, the country has seen a growth in independent local news sites and stations – an industry tailwind that can protect Gray's moat in its core markets. In the past, concerns of a dying local news market led to discussions of a shrinking market share, but with the rising demand for specialized and

[1] Gray TV – About, Our Story
[2] Gray Television January 2019 Merger News Release
[3] Gray Television March 2021 Investor Relations Presentation
[4] Gray.TV – About Us

region-specific news from the younger demographic, Gray Television and its stations have a strong backbone for the future[5]. During the COVID-19 pandemic, Nielsen conducted various studies since the outbreak and confirmed a spike in local news viewership from young adults as they find a significant lift in the interaction among younger persons aged 2-17 (~20% increase)[6,7]. The unreliable nature of the younger demographics' social media news sources offers local news channels an opportunity to sustain a part of this spike by converting a portion of the new COVID-19 viewers in the future.

II. Increased Political Advertisement Revenue

Local broadcasters such as Gray Television thrive with political elections with a large flow of money from campaigns and political action committees. Election years have been highly profitable for Gray, with 2020 revenues at $430 MM or $17.57/household. Gray has seen an increase in their advertisement revenue and penetration in the market with each successive election cycle. As such, in the upcoming 2022 election cycle, Gray will be well-positioned for large inflows of ad revenue and benefit from numerous elections. Specifically, in 2022, 28 Gubernatorial elections, 27 Senate races, and House races in all of Gray's markets will offer substantial revenues. Considering the country and the major political parties' rising politicization, it is highly likely Gray will continue to see an increase in their political revenue/household metric in the coming elections (shown below)[8]. The even split in Congress adds more reason for a heavily contested 2022 election with potential for unexpectedly high campaign spending and resulting ad revenue for companies like Gray Television.



The likelihood of increased political advertisement revenue is bolstered by the country's increasing politicization and the relevance of national elections. With an ever-divided country across political spheres, there have been historical increases in campaign spending conducive to increased ad revenues[9]. In the recent Georgia run-off election, campaign spending was not limited to just Georgia Democrats or the national parties; rather, stakeholders across the country spent money on ads in non-Georgia states and broadcasters. These secular trends greatly benefit a company like Gray, whose key markets are battleground states for the major political parties. In addition to ad revenue, the company's media assets in InVestigate TV, Full Court Press, and Washington News Bureau are poised for an increase in viewership and revenues with the growing focus on independent political news sources. Finally, the volatility and cyclicality in political spending revenue in non-election years can be combatted via sufficient revenues in election years and from off-schedule local elections.

III. Entry Into New Sectors: Streaming/OTT and E-Sports/Gaming

For the media and broadcasting world, streaming and OTT platforms and esports and gaming are the future with innovative companies entering the market. With its growth investments and partnerships, Gray Television is poised to be a part of this future growth. Gray saw record-breaking growth in 2020 with increases in sessions, video plays, users, and page views (10%+ in each category) on the digital and streaming front. The company's partnership with digital streaming providers and platforms such as YouTube T.V., Roku, and Apple T.V. is valuable in the future as it can leverage its (Gray's) 1.1 billion monthly aggregate users for greater ad revenue contracts. Furthermore, the company's investment into VUit and Premion alongside TEGNA and its in-house digital agency servicing (Gray Digital Media) poises itself for the digital transformation of advertisements and streaming. Through its investment in Premion (which can increase with the potential acquisition of TEGNA), Gray can combat secular headwinds in the traditional ad revenue segment. On the e-sports and gaming side, Gray's growth investment in Envy Gaming offers it exposure in the growing sector and a potential to develop a future revenue stream in the industry vertical. While the investment is on the smaller end, future investments in fundraising rounds can increase their market and company stake.

IV. Accretive Strategic Acquisitions to Expand Geographical Presence and Consolidate

Throughout its history, Gray Television has developed its business and culminated a large set of assets via transactions. The broader industry is in a consolidation phase, and Gray is poised for further acquisitions. The company has had two large transactions in its accretive acquisition of Raycom and Quincy Media. Considering the company's strong debt profile and sufficient cash balance, the company can continue to acquire targets to develop its asset base. Specifically, the company should look to penetrate the West Coast market (yellow in the map below) and continue garnering market share in its existing markets. The Northeast Region, where the company has existing stations, should be further pierced to increase its profitability. Mark R. Fratrik and BIA Advisory Services have researched and shown that when Gray purchases a second station in an existing market, they see reduced fixed costs, more news production, more support from the FCC, and greater profitability[10]. Considering the clear benefits of strategic acquisitions, it is intuitive Gray should transact. Furthermore, the

[5] Neiman Lab – COVID Sparks Growth of Independent Local News Sites
[6] Nielsen New Normal: Local TV News Medium of Choice
[7] Nielsen Local Watch Report
[8] Gray Annual Filings 2020
[9] 2020 – Record Campaign Spending Year (CNBC)
[10] BIA Advisory Services Report

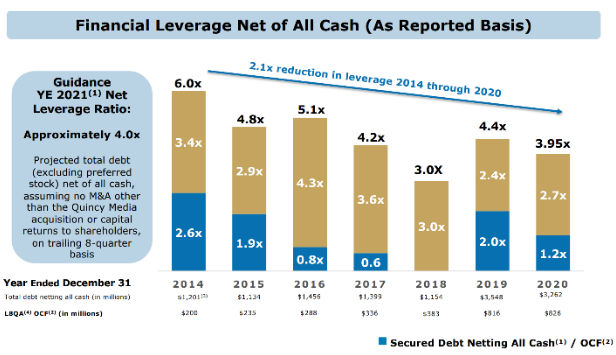
announcement of the company's previous acquisitions has led to stock price increases and multiple expansions as a result of an increase in combined earnings.

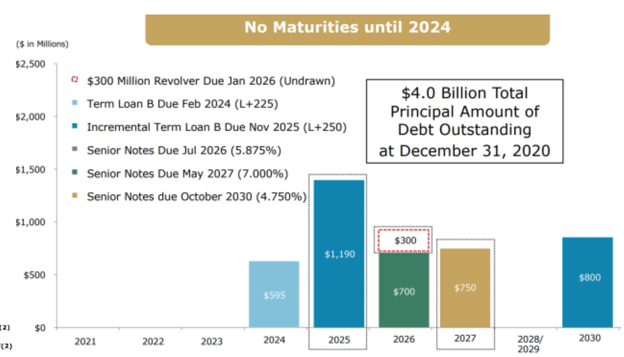
A potential transaction target for Gray is TEGNA Inc., a company they have attempted to acquire in the past with a now withdrawn $8.5 billion bid (due to COVID-19)[11]. Considering the local news industry's stability since the pandemic, Gray has a great opportunity to re-enter the market to acquire TEGNA, potentially for a lower price, and expand its market with 60+ stations[12]. Furthermore, this consolidation will push Gray to the top of the industry in regard to market share while trading at an attractive multiple. Finally, any future Gray transaction (including Quincy) should see no FCC issues given its T.V. ownership (<26%) is below the FCC 39% cap.

V. Strong Financials and New Dividend Policy

Since 2014, the company has seen strong, sustainable, and growing financials with consistent margins. This increase in profits corresponded with a healthy increase in the value of the company's equity and book value. The strong operating performance offers protection for investors during a market downturn or the market's current inflation-fear conditions. Furthermore, management has acknowledged this strong operating performance and implemented a highly attractive $0.08/share quarterly dividend policy for common equity shareholders[13]. The dividend payout indicates management's expectations for a consistent net income in the coming years as if it were not confident in its profitability, it would not re-introduce a dividend. Furthermore, the dividend, along with proposed share buybacks, send a positive signal to investors losing confidence in the industry and the rapid growth acquisitions undertaken in the past.

A key attractive feature of the investment is the stable, levered nature of the Gray and its operations. Unlike other levered companies, especially those in the industry, Gray is in good operating condition and, more importantly, has no major debt maturities until 2024. This gap of time for maturities enables Gray to increase their liquidity to de-leverage when required. Indications of de-leveraging activity have been seen in the past, and now the company is extremely undervalued considering it has $900 MM+ in EBITDA with no considerable leverage concerns. The large cash balance ($773 MM in 2020) and broadcast licenses (~$3,600 MM in face value and ~1,800 MM in market value if 50% discount is applied) on Gray's balance sheet are high-quality assets that can offset the maturity of debt in 2024 and beyond. The market is incorrectly undervaluing the company because of its high leverage – the company has healthy and stable credit ratings. Finally, the $650 MM in preferred equity issued in connection to the Raycom Media acquisition is of little worry, as well, considering the equity cannot be converted into dilutive common stock and is very pro-company.





VI. Attractive Valuation in the Competitor Sphere and Current Market Conditions

A value-oriented investment looks to offer significant upside and protection from rising bond yields and an inflation-high sentiment in the current market and macroeconomic environment. Market strategists at Bank of America support this assertion as they cite the esoteric increases in the 10-year yield[14]. The media and broadcasting industry is a value industry considering the lower average earnings multiples and the market not pricing in the local news revenue recovery post-COVID-19. While there has been a move to streaming and OTT platforms, traditional media platforms are sought after and companies like Gray, who are diversifying into the "growth" sectors, are attractive investment opportunities. Furthermore, with the above initiatives, Gray is a growth-like investment in a value sector, given it has fundamental reasons to see multiples expansion and the corresponding price appreciation. In the valuation section, there will be a discussion about the undervalued nature of Gray in relation to the competitor sphere.

[11] Gray Television and Apollo's Bid Withdrawals
[12] Gray Television Bid for TEGNA
[13] Gray Television Initiation of Quarterly Dividend Press Release
[14] Financial News London – March 12, 2021

Variant View and Catalysts

Underestimation of Sustainability of Political Revenue: Currently, the market is greatly underestimating the sustainability of political revenues in non-election years and when there are no significant elections in Gray's markets. However, with the increasing politicization of America, political campaign spending trends suggest linear increases in campaign spending in both national and local markets. Furthermore, the markets Gray holds market share in are where the two major parties aim to either hold their stronghold or increase their penetration. Qualitatively, the potential for continued political spending in local elections will lead to great ad revenues in non-election years than expected by the market. More importantly, the company's independent media assets have the potential to garner more traffic and amplify in value with the surge towards independent media sources.

Amnesic in Considering Streaming and OTT Exposure and COVID-19 Recovery: As the media and broadcasting industry moves toward digital streaming and OTT platforms, the market is forgetting about Gray's stake in the industry trend. The company's involvement with Premion and VUit is a strong future revenue source and will grow concurrently with the shift to digital and cushion decreases in traditional advertising revenue. Furthermore, the market is not considering the idiosyncratic revenue streams the company and its assets will garner following a recovery from COVID-19. For example, canceled events like the Olympics will increase advertisement revenues for their news stations, and the return of independent music and live event productions can offer seasonal sales.

Catalysts: For future price appreciation, there are several key catalysts to consider 1) the closing of the Quincy Media acquisition and the future disclosure of currently non-public accretion synergies, 2) state municipal, general, and special elections in Gray's market in 2021 that can lead to sustained political revenues; 2022 and 2024 general elections, 3) seasonal revenue from the Olympics, 4) press releases regarding new and unannounced acquisitions and earnings, and 5) the un-considered potential to partner with new streaming platforms like Paramount Plus and serve as the key local news provider.

Valuation

The adage valuation is an art, not a science is well known. To appropriately value Gray Television, it is important to look at the company compared to its comparables and a valuation of its assets. A discounted cash flow model is futile in this situation, given the changing dynamics of the industry and Gray's businesses. Hopefully, the valuation presented is closer to a science than art by focusing on the market and the asset valuation.

Comparables Price Target		
Multiple	**Median**	**Base P.T.**
EV/EBITDA	7.76x	$34.86
P/E	8.12x	$35.42

Asset Valuation Price Target	
Bear Case	$21.46
Base Case	$28.88
Bull Case	$36.30

Key Financials	
Net Debt	$3,259.00
Pref. Equity	$650.00
Shares Out.	97.00

Comparables Analysis: The company set includes Nexstar Media ($NXST), Sinclair Broadcast ($SBGI), E.W. Scripps ($SSP), TEGNA ($TGNA), Gannett Co. ($GCI), and others. Compared to its direct competitors, Gray trades considerably lower and is greatly undervalued on an earnings basis, and warrants substantial price appreciation considering its entry into new markets and accretive acquisitions, leading to strong future earnings potential. From a free cash flow and profitability standpoint, Gray is comfortably in the middle/top of the pack in regard to trading at an unwarranted discount. The lack of debt maturities till 2024 should allow the free cash flow and profitability metrics to be consistent and expand in the future. The company warrants price appreciation on a relative basis, given its above-average operating metrics and management of debt capacity.

Asset Valuation: Given the growing consolidation in the broadcasting industry and many saleable assets in Gray's treasure chest, it is appropriate to value the company's key assets. For this valuation, the assets valued include the Raycom Media and Quincy Media subsidiaries, the recent Envy Gaming investment, and the company's remaining broadcast stations. The remaining broadcast stations term incorporates the stations Gray purchased over time or built themselves.

Raycom Media Value: $3,547 MM – for simplicity and "science's" sake, the value of Raycom was assessed to the purchase price Gray paid in its 2018/19 acquisition.

Quincy Media Value: $925 MM – again, for simplicity and "science's" sake, the value of Quincy was assessed to the purchase price Gray paid recently in 2021. In the future, the value of this asset can increase, given unexpected cost synergies and transaction accretion related to unplanned divestitures with additional acquisitions[15].

Envy Gaming Investment Value: $28.5 MM – valuing Envy Gaming is significantly more art than science, considering Gray made a growth-like investment in the rising e-gaming stalwart. In the future, with the growth of the industry, there is strong potential for the investment to increase multi-fold after discounting the cash flow. However, there is a strong risk of no return. Overall, while the value of the investment can be seen as negligible in the composite, the lottery upside potential offers a reason to include the investment in the valuation.

[15] Gray Television March 2021 Investor Presentation

Remaining Stations Value: Valuing the remaining stations of Gray is dependent on the case an investor is interested in considering (bear, base, bull). Given that Gray has purchased and developed these stations over a long period and during different pricing cycles of the stations, a broad average was used for the cases. Subtracting stations acquired from Raycom and Quincy, the count set for the remaining stations was 144.

Bear Case Average Value/Station: $10 MM for an overall value of $1,440 MM – The average set equaled the lower of the prices paid by Gray in the past for its stations in more remote markets.

Base Case Average Value/Station: $15 MM for an overall value of $2,160 MM – The average value set is a calculated average of the different acquisitions Gray has been a part of over the past 10 years.

Bull Case Average Value/Station: $20 MM for an overall value of $2,880 MM – This average value is in the upper end of Gray's purchase prices and the industry standard.

Remaining Key Assets: $50 MM – given the lack of transparency from Gray's part and comparable valuations, a broad value was attached to the remaining key assets of Gray.

Risks and Mitigants

Losing Out in Ad Revenues in the Shift to Digital: While this is a risk that Gray has yet to fully address, the compression in ad revenue Gray is experiencing in its traditional channels is starting to be covered by and most likely outpaced by the revenue they have generated via their digital-centric platforms Premion and VUit.

Cord Cutting: The divergence from cable networks is frightening for broadcasters, but Gray's exposure to O.T.A. (over-the-air) T.V. (cheaper broadcasting of small set of local channels) via Circle T.V. and general exposure to digital and partnerships with growing mediums such as YouTube T.V. gives it exposure to the new market and ensure it's not "cut" from existence. Furthermore, the company is reducing its dependence on prime-time revenues (<20% of core revenues) and is protected from the headwind.

Overdependence on Political Revenues: This counter is of merit, but it has already been priced into the stock price during the recent market correction, and post-earnings share price decrease. Gray's key markets' upcoming political elections offer a steadier political revenue that the market has not considered. In a short timeline, Gray can see price appreciation via strong political revenue numbers as a result of elections in 2021, 2022, and 2024. Finally, in key election years, political revenues are <20% of total revenues and the decrease in political revenues in non-election, for the past ten years, have consistently been covered by increases in local news and retransmission consent revenues.