Clarivate Analytics, plc

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Manav Patnaik: All right. Good morning, guys. Thank you for being here. For those of you who don't know me, my name is Manav Patnaik. I'm Barclays' business and information services analyst. And we're very glad to have with us here today Jerre Stead, who's the CEO of Clarivate Analytics now. Jerre, we've obviously known each other for a long time, as you worked at IHS. And maybe just to start off with, just a little bit of background on how you came to Clarivate Analytics.

Jerre Stead: Yeah, it's a really funny story. 2012 I had a handshake to acquire Clarivate from Thomson. At the time, they decided I hadn't offered them enough money. And so we walked away from it. They came back to me in 2015, when they were ready to sell it, and I then was deep with doing the merger with Markit. So we didn't do it.

So when I stepped down at the end of 2017 from 18 years at IHS, I was on a semi-sabbatical, because I knew I wouldn't retire. And Michael Klein, who had been on my board for years, called me and said, he wanted to do a SPAC. And I said, okay. He had to explain to me what a SPAC was, because I didn't know. We raised $690 million. It was CCC, took that public in September of last year. And I always had huge respect for Clarivate, but I didn't think -- Onex had acquired it less than two years before. So I didn't think we'd get a shot at that. I was actually in Europe looking at other platforms when they called and said they wanted to do the deal, they wanted to have discussions.

So that was October 15th of last year. We announced it on January 14th. And on May 13th of this year, we closed with the reverse merger and I've been CEO of them for just over six months. I wanted it back in the IHS days for three reasons. One, best business I've seen for having the inside value of the customers, best one asset-wise. Actually four reasons; the second one was in 2007, '08, and '09 it was flat but marginally up, which is, if you think about back when I had transportation at IHS and also gas and oil, if you will, the resources; we ran a great business. But we knew we were going to go up and down. This one didn't. The third one was it had great Asian assets. And then the fourth one was it was underinvested in and underused.

So we were able to get it. I would say two or three things. It's better than I hoped and it's got more work to do to get it to be the great company I want it to be. If you go back and read what I said when we did this SPAC, I said I wanted to find something that I could do twice as fast and as good or better from a shareholder return, as we did at IHS. So that's what I've got now.

Manav Patnaik: Got it. Well, maybe we can dig into those a little bit, because I think you offended a lot of your formal colleagues when you said this was the best asset you've seen. But just on those four key points, maybe, just go down them. Like, what -- and maybe a little bit of nuance in the business as well.

Jerre Stead: Just to be crystal clear, if those of you that don't remember 20 years ago, when I got to IHS, it was bankrupt. It was five little divisions that had never been merged on energy and 54% of the revenue was engineering standards with royalties of 50%. So that's what I was referring to, to be clear. That the assets I left with at IHS Markit were incredibly good.

These are really interesting. It's the most fun I've ever had. And one of the reasons we're able to attract great young people is they actually make a huge difference to the world. The mission that we have as a company is to help create innovation and provide great returns for people that are researchers and innovators. And two or three quick things, because these businesses are really four businesses that we put into two. There's life science and Web of science; and then the pieces that come together for intellectual property. What they do are things that are must-have for the world.

The patent business is the very best. It's the gold standard in the world. We actually have 105 years of patent information and data. We actually provide 40 of the largest patent offices, national patent offices in the world. We provide them with judgment to help them make decisions on what patents they should do. Last year you may know, over 50% of the patent business, new patents, came out of China. And over 70% of the trademark inquiries came out of China. So that's critical for us going forward.

Web of science is totally world-class and what it provides is the single-best source in the world, in fact there is nobody close to it, of recommending what journals need to be used, what the researchers need to be. It's an interesting statistic that we've predicted 90% of the Nobel Prize winners accurately 2 to 3 years ahead, just as an example for researchers. Like I said, the trademark business is incredible. And then life science spans the research that's done from the very beginning all the way through the businesses that -- we work with the 30 top researcher companies, the pharma companies in the world, and actually all the startups too. Each of those, as we now bring them together, and sell in packages which we will our solutions going forward, those things that nobody else can do. So it's fun to see.

Manav Patnaik: And can you just help us to understand the industry? Like, has Clarivate underperformed the industry? Is Clarivate the industry or is the whole industry under-managed?

Jerre Stead: Yeah, no. Great question. Underperformed, with the exception of Web of science. That one I think underperformed. Richard, my CFO and I, would agree today underperformed of what it could be, but comparatively performed relatively well for other peer groups. What you need to think about though is this business in 2 to 3 years will be a mid-40s adjusted EBITDA business, like most of the peer group we have are.

We've got a lot going on, six different things to reduce cost. The flip side is it's under-growing. Life science should be growing double digits, because life science in the world grows double digits. It has not, again, just because of underinvestment and not spending the time and money to get it where it should be. And then bringing -- the patent business actually was on a slope downward. Because two things we did right after we got there is we ran two customer delight surveys and two things came back out of that. One was highest scores I've ever seen. We've done this forever, highest scores I've ever seen in the way that customers value the product. That's great news. 87, we worked hard to get to 82 in other places I've been. But then the least satisfied from "easy to do business with" for two reasons. One, we didn't have good customer care. I'll come back to that in a second. And then the other reason was user interface was as good as it should have been with Derwent, which is the great trademark for patents.

I just a week ago today actually, used the new model when I got up early in the morning. I could make it work in five minutes. And that's me. So that says it's a good one now, so that's a huge job. What we've done to correct the "hard to do business with" is by the end of 2020 we'll have three customer care centers set up worldwide, one in each region, where we shift about 80% of the customer to inside sales. We have the classic -- I've never seen it this good -- 20% of the customers are just over 80% of the revenue. 80% of the customers are less than 20%. So we'll shift that. Then most importantly, put those three customer care centers in place to get the responsiveness up to what we need it to be. So that's when I think of underproviding, you should think of this business being at 6% to 7% or higher organic growth business in the years to come, and a mid-40s adjusted EBITDA. That will get us up to performing the way the rest of the industry does. And everybody says, so, what can go wrong? The only thing that can go wrong with it is whether we execute right or not. It's all there.

Manav Patnaik: Got it. And maybe just to frame those 6% to 7%, mid-40 targets, where are we today and what's kind of the building blocks, and how long before we get there?

Jerre Stead: Yeah, great question. So when Richard got here three years ago, you grew 0.7%. This year we'll exit, pick your number, but close to 4%. And next year we committed we'd grow 4% to 6% organic. And the following year I said we'd grow 7% to 8%. Let me give you the keys there. Price realization was negative, because there was really no control in pricing with the customer. Actually the field sales organization back then could get paid 100% commission and reduce price. So that discipline is now in place. This year we increased prices 2% and next year 3.2%. And in 2021 and '22, it will be 4-plus going forward. Because one of the things I saw, like I said when we did the customer delight survey; it's the least complaints I've ever seen in my life about pricing. We're way underpriced. So think of that as 4% for years to come.

Point two, we'll significantly increase the renewal level. We're running 92% today, 91.9%. We'll get that up well north of 95-96% with the customer care, the inside sales, and fixing the user interface. Point three is we start to bundle. You'll see us at least 2% a year, maybe 2.5% in selling solutions as compared to one-off sales. Point four, another 2% as we put in place in the next two years, the ability to do really true global account executives. If I can get to 11% quickly of what we can do, we won't because some of it won't go right. But it's a rock solid 7% to 8%.

Manav Patnaik: Got it. And maybe the pricing power that you think you have and the 4% explains why it grew a bit in the recession?

Jerre Stead: I think it did.

Manav Patnaik: But I think we all need to do more work on the assets. So maybe just a little bit more like, why is the customer so sticky?

Jerre Stead: Yeah, because two reasons, a great question. There is no alternative in most cases, period. And we are the gold standard in each of the businesses we're in. And it's actually built into the customers' interfaces inside in their work streams. That's the reason.

Manav Patnaik: Got it. And you know, a lot these strategies building blocks, the way you've been describing it; well, it's similar to what you did at IHS. And M&A war is an important part of that story as well. So are we looking for similar with Clarivate?

Jerre Stead: Great question. Let's say we get to 7% to 8% organic. If you look back at IHS, we did 19% a year for 15 years. That was about half and half. This one probably won't be quite like that. Let's say we get to 7% to 8% organic. You should think about us doing over time 3 to 4 of tuck-ins. We did a classic one last week with our trademark business. It fit all the criteria we hoped for. One, it was not for sale, which is critical for me. If you look back at the 82 acquisitions we did at IHS, 80% of those were not for sale, 90%. So that's critical.

Point two is it's got to be accretive at the end of year one, accretive in revenue, organic growth, accretive in EBITDA and accretive in free cash flow. And this one we did last week, absolutely happened that way. Most importantly to me with this one was, its proprietary data worldwide that was not being sold worldwide. So those are the kind we're looking at. There's quite a few like that as we go forward. There are larger ones that when we get everything humming the way we want it to, we would look seriously at. Again, those are basically divisions of other large public companies, or they're privately owned. And there's some of those that will be interesting.

Manav Patnaik: Got it. And obviously you're not going to give us the name of those. But just in terms of you said there's no competition, but yet there's a lot of these, I guess, complementary assets out there. How would you describe that immediate comp in terms of the businesses that you guys have?

Jerre Stead: Yeah. So big B. If you think about us doing x, these would be doing y and z in the same industry. So they're side-by-side and then in some cases where we partner today, we would end up acquiring. But they're not head-to-head.

Manav Patnaik: Okay. And then in terms of -- I mean clearly acquiring proprietary data makes complete sense. Where are you in your technology and do you need to acquire capabilities or some of that--?

Jerre Stead: Oh, great question. One of the beauties of doing the carve-out that Richard and others did, that Clarivate from having been underinvested for years at Thomson, we went to 100% cloud-enabled. We went to an entirely new back room. It's not perfect yet. But as we optimize that, if you think what we did at IHS actually seeing Jane Okun Bomba who's here, who was my Chief Administrative Officer, did the -- and you'll remember. And we had to start at zero with our back room. It took five years and six years and we had to do it inside. We got that today, so big difference.

And the other piece on technology that was really interesting, Thomson had a model which I've not seen before, where they used over 50% of the developers were on contract. So we'll be done with that by this time next year. And what that does is increase productivity and cost savings a lot, and lets us speed up the new development we've got. And I feel really good about that from a technology standpoint. We will, as you would expect, make sure that we've got the best pricing going forward from all of the technology users we were with. I mean we were 100% AWM. We'll make sure that we get a legit price going forward with that. But in general, I feel good.

The other critical one that was amazing to Richard and myself is we have a project called Singularity, which will put all of the product data on a common platform. Because none of it was. There is 80 different data sets that we'll put on. But equally or more important is we had no artificial intelligence, no machine learning period. And by June of next year, we'll be 80-90% there. We'll free those people up to do what I would call insight, which we've not been able to do with our customers going forward. But when we exit 2020, we'll have world-class development in place and we'll have the very best back room in place. So a lot of work to do get done, but it's going to happen.

Manav Patnaik: Got it. And can you just talk a little bit about your team, your bench strength. I know you've made a lot of changes. There are two parts. One, at the different levels, your senior executives, sales, tech, whatever; what is the magnitude of change you've already made and what's coming?

Jerre Stead: Yeah. So let's just start with salesforce first. From the time that the carve-out was done to now, we've turned over probably 60% of the salesforce. And I would say as we get through during the conversion to inside sales and outside sales, especially with account execs, we've probably got another 10% to 15% to go there. Because these folks were caught being administrators and order takers, and what we're moving to is really account execs. So the first three levels, so if I'm level one, my team, level two; I have 13 that I support. I feel really good about those. We made the moves I believe we need to make that happen for years to come. Then the next level, which would be level three in the company, we actually interviewed every one of them 80-some of them and ended up picking about 45 of them. So I feel really good about that.

The rule I've always had is surround myself with great people, spend my time helping them be successful, point one. And point two, I want everybody in those first two levels below me to be able to grow the business at least three times. And I feel like we've got that today. The other thing it's so interesting is; 70% of our people are three out of five years, have been there 3 to 5 years. And it makes sense if you think about it. It was on the carve-out time and I think they're very excited people today of what we're doing. Interestingly enough, when we ran colleague engagement, which I do each year, because that's the way you really run companies is if you don't have your people excited, it's not going to work. And we scored better than I expected with all the change going on. Interestingly enough, the new ones scored very high and the long-term 30-years-plus scored very high. It was the ones that have been there, pick your number, but 5 to 15 years that scored lower. That's probably a place we've got more work to do.

Manav Patnaik: Got it. You know, you touched on it earlier. But the number of incremental patents coming primarily from China and Asia and I think you mentioned every one of your pillars as well in terms of Asia being the opportunity. Can you just talk about that and you know, is it -- are there any roadblocks with the tension?

Jerre Stead: Yeah, no. Great question. We're blessed, for those of you that don't know me, I actually worked in Japan in 1967-68. I was in China in 1980. I opened the Hong Kong office and Singapore office for Honeywell in '74 and '75. So we've been there forever. I have the best team I've ever seen. David Liu, who runs Asia for us out of China, he was the first Thomson employee in China. He's still -- he's not 50 yet, been there 26 years I believe it is, incredibly competent, totally underinvested though historically. And so we're pulling the coals to that area. You should think about that business right now about 25% of total revenue. It will be 30% in 2 to 3 years. And the only roadblock frankly is us being able to pick the right people and build the right systems quick enough for them.

We've got to do some localization. We will do partnerships again in China. We announced one this year. It's interesting, White Rabbit. There's a couple more we're working on that. And we will do acquisitions in Asia that have not been done before. So as we move forward, those are the only roadblocks I see. And you're right. If you look at -- there is no place else in the world for Chinese companies to get like the patent information. One, assuming there is eventually some sort of a trade agreement, they've talked -- everybody's talked about two steps, first step being some control over IP, the second step being more control. They have to come to us when that happens.

Manav Patnaik: And maybe just a quick to round up a quick snapshot of North America, Europe, otherwise just steady, or is there opportunity there as well?

Jerre Stead: Yeah, no, no. That's a great question. The Americas still has my belief, the potential not to grow 3.5% but 10-plus percent, with the kind of things we're doing with the organic growth. But there's acquisitions to be made there. I think Europe is solid at where we're at today. But if you think about growth, they'll probably grow 4% to 5% and be passed in two years by the Asia seg, but great businesses in total.

Manav Patnaik: Got it, and then maybe a last question in the two minutes we have left, just like you said, you've done a lot of the initial changes, but there's still a lot of work to be done. So you know, where's the confidence? How do we get comfortable just like you are in terms of writing the story?

Jerre Stead: Yeah. No, no, no. It's the only way it should be. We said we'd exit 2020 at 4% to 6% organic. Think of us being in the north end of that. We said we'd exit 2020 with 35% to 38% adjusted EBITDA. We'll be at the north end of that. We said we'd do 60-plus percent of free cash flow of EBITDA. We'll be north of that. So that's a good intermediate measure. And then think of us in '21-22 doing the kind of numbers I talked about, so that by the time we get into '23, you'll see us in the 40s, a question of how high, with adjusted EBITDA. You'll see us in the 70s in free cash flow and you should see us all in, including acquisitions, in 9% to 10%. So really very transparent of where we're going to be.

Manav Patnaik: Got it, and then last question and I should have brought this up earlier, but a majority of your business is subscription. And so that visibility obviously helps. But can you just talk about the characteristics, is it multiyear or just --?

Jerre Stead: Yeah, 2-3 things. The ideal mix we're at 83% annual or longer subscription base today, 85/15 is perfect. The 15 is a bit unique with transactions, because providing that kind of insight I talked about has not been done. And that will be a significant margin enhancer for us. Then we actually sell slices of data for those that subscribe to us now, which I could never get done at IHS, which is historical slices. So that makes the -- those are very high margins. So that's the 15%. The 85% though, you should think of us running at least 95% to 96% of renewals in the next 2 to 3 years.

Manav Patnaik: Got it. All right, well I think we'll end it there. But it's kind of like a lot of work to be done, but it's getting done.

Jerre Stead: It's a great one. It's a lot of fun. Thank you.

Manav Patnaik: All right. Thank you for being here, Jerre.

Jerre Stead: Yeah.