General Cinema talks with New York Security Analysts

October 18, 1978

GENERAL CINEMA CORPORATION

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Remarks by

Richard A. Smith

PRESIDENT AND CHAIRMAN

J. Atwood Ives

SENIOR VICE PRESIDENT—FINANCE

New York City, N.Y., October 18, 1978

Turning now very briefly to our Communications Group, it is again a happy story. Coral TV, Channel 6, Miami, continues to do well in a fast-growing market. Revenues grew over 20% this year. It has achieved an Arbitron rating of about 11% for total audience and it is getting about 15% of the total TV advertising dollars in the market.

We have now received all the necessary permits to raise the master antenna height from 1,000 feet to 1,500 feet and we are in the process of having that tower raised and also adding a circular, polarized antenna—all of which should make a vast difference in the signal quality. This improvement ought to lead to continuing sales and profit gains for Coral TV.

WIFI, our FM station in Philadelphia, is continuing to make strong progress, staying on its growth pattern. WEFM, our FM station in Chicago, which you may recall became a popular music station just last January after four or five years of litigation, is now just about breaking even and we are looking forward to profits for the first time in 1979.

The Communications Group, as a whole, will contribute about **$3** million pretax to General Cinema's operating earnings in 1978 and we do expect a good gain in 1979.

I would also like to comment that we are continuing to look at opportunities within the communications area and we will be acting from time to time when these opportunities present themselves.

Let's talk about Sunkist®. I guess you all know by now that a year ago, in August, 1977, we signed an agreement with Sunkist Growers, licensing General Cinema to use their trademark for carbonated soft drinks in the United States. In the fall of 1977, we assembled a management team to undertake this venture. I want to give you a few facts about them.

Mark Stevens has been with General Cinema for five years. He was VP—Marketing of our Beverage Division. I emphasize that because he did a terrific job in that position and we continue to benefit from many of the programs and policies that Mark put into place. Prior to joining General Cinema, Mark had an extensive career in new product development and brand management at General Mills, R. J. Reynolds and International Playtex.

Peter Murphy is Vice President in charge of national sales and franchising and he has had 16 years experience in the beverage industry. Previously he was responsible for all sales and franchising activities for the Dr Pepper Company in the eastern half of the United States. Those of you who follow the industry have some idea of what Peter accomplished in those years with Dr Pepper.

Jack Leffingwell. who is Vice President in charge of research and development, came to Sunkist Soft Drinks after 13 years at R. J. Reynolds, most recently as Vice President of research and development in their flavoring subsidiary. He is numbered among the top flavor experts in the world.

The advertising agency associated with Sunkist is Foote, Cone and Belding, headquartered in Chicago. They are the sixth largest U.S. agency and have a strong record of success with new products. They have among their clients: Sears, Armour, Dial Soap, Levi's, Kraft, and Ralston Purina.

The packaging agency for Sunkist was selected following interviews with the top graphics firms. Alvin Schechter, President of the Schechter Group, personally handled the project team at his firm to assure the superiority of Sunkist graphics.

In addition, several respected consulting organizations were also utilized for specific assignments.

 Having put together this team, there was an extensive amount of market research to be done. The first thing that research disclosed was that there is a billion-dollar consumer market in the orange category, a much larger number than previously published estimates indicated. It also disclosed that there is strong potential consumer interest in a Sunkist orange soda. The Sunkist name *does* stand for excellence and quality and we were pleased to make a substantial investment in talent, research and market testing to deliver a superior product worthy of that name.

Starting in May, we entered six test markets in different geographical areas representing high soft-drink consumption and low soft-drink consumption, urban areas and rural areas, high orange consumption and low orange consumption. Also, in these test markets, we utilized both high and low levels of advertising support. Our objective is to establish Sunkist as the No. 1 orange soda. So we tested to find out essentially two factors: first, the level of solid repeat usage; and second, the sales responsiveness to advertising at various levels.

Today, I am very pleased to report that Sunkist exceeded all objectives in all markets without exception. It was tested in ten states and consumer tracking shows a remarkable 75% repeat purchase rate, one of the highest ever achieved in the introduction of any package goods product of all types in the United States.

The product, the packaging, and the advertising, have delivered on the promise that the consumer expected from the Sunkist name.

We feel that we have been vindicated in undertaking this high-risk venture for General Cinema.

Today I am pleased to announce that we will begin rolling out Sunkist Orange to obtain full national distribution.

The Sunkist story is not only a story of professionalism and absolute dedication to quality in every respect but it is a team effort involving outstanding franchise bottlers in our test areas, one of which I want to mention just briefly. That is the very prestigious Coca-Cola of New York organization which has done a terrific job with this product. We are very pleased to have them as our franchisee.

Our policy is to franchise Sunkist, if possible, to the strongest array of Pepsi-Cola, Coca-Cola and independent bottlers. One of the reasons that Sunkist Growers selected General Cinema to carry out this venture was our willingness and flexibility to implement this policy.

In summary, a decision had been made that Sunkist will be a business. not a venture. The objective is to make Sunkist the number one orange drink in America, and to have it add to General Cinema's earnings in the 1980's.

Now, if I may, I would like to introduce Woody Ives, Senior Vice President—Finance, who will cover some financial aspects of the Company,

J. Atwood Ives: Let me briefly comment on our third quarter and nine-month operating results.

Quarterly net earnings exceeded $10 million for the first time and were up 23.8% on a revenue gain of 23.1%. For the nine months, net earnings were up 26.9% on an increase in revenues of 30.3%.

More importantly, however, operating earnings increased 43.9% for the quarter and **41.9%** for the nine months, as both major divisions made significant gains. Net earnings advanced at a lower rate as corporate charges increased significantly during the period, primarily due to the expense of the Sunkist development program. We are pleased with these results as they reflect the continuing strength of our two basic businesses—soft drink bottling and movie exhibition.

Following the presentation there was an informal discussion. We have included certain questions and answers which we felt would be of general interest to our Shareholders and the investment community.

Participating were:

Richard A. Smith, PRESIDENT AND CHAIRMAN

Melvin R. Wintman, EXECUTIVE VICE PRESIDENT

J. Atwood Ives, SENIOR VICE PRESIDENT—FINANCE

Herbert J. Hurwitz, SENIOR VICE PRESIDENT

Mark L. Stevens, PRESIDENT—SUNKIST SOFT DRINKS INC.

Mr. Smith: In those films that General Cinema is financing, either in part or in full, we have not permitted blind bidding.

Question: You were involved in some litigation concerning your right to get first crack at the films you were involved in financing. How did that turn out?

Mr. Smith That is still ongoing. It is a very interesting test case.

Question: Could you quantify what Sunkist cost you this year?

Mr. Ives: About 55 cents a share, net. However, it is important to remember that there will be significant expenses involved in rolling out and promoting this new product nationally, next year.

Question: What are your policies going to be on capitalizing the advertising and roll-out expenses next year?

Mr. Smith: We haven't determined that yet but we have made the basic decision that it is a business and our accountants will advise us as to our alternatives. Up to now, we have expensed all development costs because we didn't know whether, in fact, the project would be aborted or continued. Now that the basic decision has been made, our accounting treatment of some of these expenses will differ.

Question: How soon do you think Sunkist will be national and what do you think the earnings contribution will be next year?

Mr. Stevens: I'm afraid that is a very difficult area to speculate on because we are dealing with franchises and literally hundreds of independent decisions. That is why we talk about the roll-out phase, because it **is** going to take place over time.

Mr. Smith: You must understand that the soft drink business, especially for new products, is highly competitive. We are trying to be as open and complete as we can, but there are some things that we just can't discuss for competitive reasons.

Question: What percent of the country have you already signed up for Sunkist at this point?

Mr. Stevens: We are currently in population areas which total over 13% of the United States. This includes additional test markets we have added within the last several weeks.

Question: You indicate Coke of New York was successful with Sunkist. Would you characterize that their market is a high orange market or a low orange market and would you characterize it additionally as one of the areas that got a lot of advertising support or a little advertising support?

Mr. Stevens: New York is a low total per capita soft drink market. It is a relatively high orange incidence market. It was obviously paired up with several other test markets and was one of the high advertising test markets.

Question: From your income statement it looks as though last year your theatre write-offs were around $2.5 million pretax. You mentioned it's a lot less this year. Could you give us some idea as to how much less?

Mr. Ives: I think the $2.5 million is the simple answer for '77. There were also some theatres that were closed in our inactive real estate group that brought that number up somewhat. This year the number presumably will be, and we haven't finished the year yet, under $2 million.

Question: Would you be willing to tell us the test market areas for Sunkist?

Mr. Stevens: The initial six were the New York Coke franchises in New York and Connecticut; Rapid City, South Dakota; Winston Salem; Shreveport and

Texarkana. More recently we added five General Cinema markets including: Savannah, Georgia; Jacksonville, Gainesville and Miami, Florida; and Sacramento, California.

Question: What is the current national orange drink market, and did you find in your test markets that you expanded the market significantly in any of those test markets?

Mr. Stevens: Beyond the information that Mr. Smith outlined, orange soft drinks are about a $1 billion business, at retail, which is approximately 7.5% of total industry sales. I think it is probably a little early to judge what the total impact has been in terms of market expansion versus share within an existing category.

Question: How far down the road is a diet Sunkist?

Mr. Stevens: We are looking at the possibilities of testing a diet companion product. We are going to go through the same kind of very rigid disciplines as we did with the regular product and those things don't happen overnight.

Question: In a period when soft drink concentrate producers—in this case, Pepsi—are putting a tremendous increase in their own marketing effort behind their secondary brands, which they never did before, General Cinema and other bottlers are putting a substantial increase in their marketing effort behind names like Country Time Lemonade, Hawaiian Punch and your own soft drink. What are the implications?

Mr. Smith: I think the implications are that soft drinks are an expanding product category, that the market is responsive to new products and new packages and new strength in distribution. There is plenty of business out there and the public is responsive. Conceivably, I suppose, some of the market shares might shift over a long period of time, but Pepsi and Coke are growing very nicely.

Question: What does a $1 billion dollar consumer market for orange drinks translate into at the syrup level?

Mr. Stevens: That is really a very difficult question to answer. One of the things that our early research turned up was how incredibly fragmented the orange category is. I think we had one fellow who started counting and quit when he got up to 600 items that he had been able to isolate.

Unlike, say, the colas that have three major factors accounting for the bulk of the volume, you have literally hundreds of sources of supplies, and it's very difficult to obtain reliable information.

Question: Is the Sunkist franchise strictly limited to orange? Could you conceivably some time in the future have a grape soda?

Mr. Smith: Conceivably; however, our license agreement covers citrus flavored soft drinks.

Question: The implication of one question before was that, after you expand Sunkist and make the capital commitments that are required, it may jeopardize the participation arrangements that you have with Pepsi-Cola, or perhaps your other franchisors. You become a competing franchise company for a piece of the pie that other bottlers might be spending on market development. Have you considered that possibility and what effect that might have?

Mr. Smith: We consider that possibility to be quite remote. One of the most intelligent and successful things that the Pepsi-Cola Company ever did was to try to encourage the concentration of some of its franchises in stronger hands, in fact, leading public companies. This has been a very fine program for them and they have prospered mightily as we and others have grown in this business.

No, we really don't anticipate that as a major problem.