Q4 2019 HC2 Holdings Inc Earnings Call

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TEXT version of Transcript

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Corporate Participants

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* Michael J. Sena

HC2 Holdings, Inc. - CFO

* Philip Alan Falcone

HC2 Holdings, Inc. - Chairman, President & CEO

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Conference Call Participants

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* Nicholas Brown

Zazove Associates, LLC - Partner, Convertible Bond Analyst & Senior Research Analyst

* Sarkis Sherbetchyan

B. Riley FBR, Inc., Research Division - Associate Analyst

* Garrett Edson

ICR, LLC - SVP

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Presentation

Operator [1]

Good day, everyone, and welcome to the HC2 Holdings Fourth Quarter and Full Year 2019 Conference Call. (Operator Instructions)

Please note this event is being recorded. I would now like to turn the conference over to Garrett Edson of ICR. Please go ahead.

Garrett Edson, ICR, LLC - SVP [2]

Thank you, and good afternoon. We'd like to thank you for joining us to review HC2's fourth quarter 2019 earnings results. With me today are Phil Falcone, Chairman, President and CEO of HC2; and Mike Sena, HC2's Chief Financial Officer. This afternoon's call is being webcast on our website at HC2.com in the Investor Relations section. We also invite you to follow-on with our webcast presentation, which can be accessed on HC2's website, again, in the IR section.

A replay of this call will be available approximately 1 hour after the call. The dial-in for the replay is 1 (844) 512-2921 with a confirmation code of 13700114.

Before I turn the call over to Phil, I'd like to remind everyone that certain statements and assumptions in this earnings call, which are not historical facts, will be forward-looking and are being made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to certain assumptions and risk factors that could cause HC2's actual results to differ materially from these forward-looking statements.

The risk factors that could cause these differences are more thoroughly discussed in our filings with the SEC. In addition, the forward-looking statements are included in this conference call are only made as of the date of this call and as stated in our SEC reports. HC2 disclaims any intent or obligation to update or revise these forward-looking statements, except as expressly required by law.

During the call, management will provide certain information that will constitute non-GAAP financial measures under the SEC rules, such as, but not limited to, adjusted EBITDA, insurance adjusted operating income and insurance pretax adjusted operating income. Certain information required to be disclosed about these non-GAAP measures, including reconciliations with the most comparable GAAP measures, is available in the most recent earnings press release, which is also available on our website. And finally, as a reminder, this call cannot be taped or otherwise duplicated without the company's prior consent.

Now I'd like to turn the call over to HC2's Chairman, CEO and President, Phil Falcone. Phil?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [3]

Thank you, Garrett, and good afternoon, everyone. Thank you for joining us.

On today's call, I'm going to review our accomplishments, including our progress on our top priority of debt reduction and overhead, and then I'm going to discuss our longer-term vision and strategy for HC2. Our CFO, Mike Sena, will then provide more details on our fourth quarter and full year performance, and then we'll take some questions.

Let me start by saying that our thoughts and good wishes are with all of you, our employees at HC2 and our subsidiaries and their families to stay healthy. These are certainly challenging times in the United States and the world, so thank you to all of our investors and analysts that are taking the time to join us today. It is appreciated.

2019 was a very successful year operationally for HC2 on several fronts. Our accomplishments over 2019 have positioned us well for further success in 2020, including notable progress towards significantly improving our capital structure and overhead reduction. I believe we are firmly moving in the right direction to transform HC2, and we are all confident in our strategic direction moving forward.

For 2019, our adjusted EBITDA for our core operating subsidiaries of $127 million was the highest it has been since HC2's inception and was $22 million higher than 2018.

Our Construction segment hit its adjusted EBITDA target for the year, while our Energy segment had a record year of adjusted EBITDA of $17 million, aided by the acquisition of 20 new CNG stations and the retroactive tax credit that was signed into legislation toward the end of 2019.

When we first invested in energy in 2014, it was doing $2.5 million in revenue on a pro forma basis. It is now becoming a material contributor to our plan as expected.

Total adjusted EBITDA for HC2 more than doubled to a record $91 million. In addition to our strong core performance, we saw an $8 million reduction in our corporate holdco overhead from $26 million to $18 million and significant improvement year-over-year at broadcasting. We also had strong contributions in pretax AOI from our insurance segment. Beyond our operational performance, we made considerable progress during the year on the sale of our marine businesses, culminating in the completion of the sale of Global Marine Group on February 28.

We also want to highlight that the sale of 51% of HMN from Huawei Technologies to Hengtong was completed last week, a major milestone, all things taken into consideration, paving the way for us to close on the sale to Hengtong of our 30% ownership, which we anticipate occurring early in the second quarter as we complete some final logistical steps that have taken a bit longer due to the current global environment.

In addition to redeeming $77 million of 11.5% notes with the net proceeds from the completed sale of Global Marine Group, we expect to further reduce the amount of principal outstanding on our 11.5% notes with the net proceeds from the sale of HMN.

Finally, with the sale of GMG, we also reduced our overall consolidated indebtedness with the elimination of the Marine segment debt of approximately $66 million, noninclusive of any relief from the elimination of GMG's pension liability.

Suffice to say, I'm very pleased that we are delivering on our plans to reduce our debt and our corporate expenses. Strategic assessment of the portfolio of companies is a continual process for us. From inception in mid 2014, when we made our first acquisition, through today and into the future, that process will not change. As we look to continue to execute on the debt reduction strategy that began over a year ago, sale of Global Marine Group is not a culmination of that strategy, but rather just 1 step toward our goal of majorly reducing, if not completely eliminating, our holdco debt.

Essentially, our goal is to transition HC2 from being a debt story to a growth and innovation story, with an emphasis around our existing portfolio holdings of broadcasting, energy and life sciences, while we explore strategic options on DBM global.

We noted in previous earnings calls that the evaluation process of our portfolio companies was ongoing. To that point, last month, we publicly announced that we were in advanced discussions to divest our investment in Continental Insurance and that we were exploring strategic options for DBM Global, including a potential sale or refinancing to assist in our debt reduction plan. First, we have been very pleased with Continental Insurance since we added it to the platform in December 2015. Since that time, we've grown our total adjusted capital base nearly fourfold in less than 5 years.

While we've always been proponents of the opportunities to continue increasing shareholder value through the acquisition of additional blocks of LTC insurance, it, however, became definitively apparent during the back half of Q4 that both the management fee and dividend possibilities would not meet our long-term expectations and objectives going forward.

With all of our businesses, we are constantly taking in new information in changing economic and regulatory environments as well as listening to and evaluating various opportunities. With insurance, the opportunity to strategically exit at this stage would also allow us to continue with our long-term goal of debt reduction while focusing on in simplifying our overall corporate structure.

While we have not yet signed a definitive agreement, we believed that the process was far enough along that it was important to provide our shareholders with an update in context surrounding this potential sale of Continental, as well as grant the potential acquirer exclusivity as we further advance our discussions that began a number of months ago.

DBM Global, which has been another excellent performer since our acquisition in 2014, has been a perfect example of how HC2 can make a timely purchase and help grow particular asset. Over the past 5 years, we have assisted DBM in the acquisition process, and most recently, we secured and arranged the financing for their GrayWolf transaction, which has proven to be an attractive addition to DBM's overall business structure, further helping DBM to significantly increase its adjusted EBITDA from $46 million on a pro forma basis for the calendar year 2014 to $76 million in 2019.

With a strong adjusted backlog of $826 million, we continue to believe in the prospects for DBM and its success over the long term. As with insurance, we've been reviewing potential strategic alternatives including subsidiary refinancing for DBM, which we believe will continue -- contribute to the evolution and simplification of HC2's business model and capital structure.

All of this said, given the current environment, we are also well aware that it has suddenly become a much more challenging environment since our announcement last month. Our strategic processes, however, remain ongoing. But to be clear, if we are unable to receive what we believe is appropriate value for insurance or construction, can always address debt and interest expense reduction with financing at the subsidiary level and revisit the sales when the economy rebounds.

We are excited at the prospects for a streamlined sharply focused and financially flexible HC2. We believe that by focusing on our higher growth assets at HC2, we will be best positioned for the long term to create additional shareholder value above and beyond what many think our assets are worth today.

Let me now walk through each segment to give you a sense of why we're so excited about our future. First, our growing broadcast segment, which we've discussed in detail on prior calls, and where we've seen a significant change from a year ago with our over the broadcast -- over-the-air broadcast platform.

A bit of a refresher, what is an over-the-air distribution platform? Over-the-air, or OTA, is a method of distributing content from 1 central system, a transmitter, to multiple devices at one time, including TVs, mobile devices, et cetera. Basically, it's back to the days of your father's broadcast television, the basic transmission of free content over wireless spectrum. However, unlike 30 years ago, one doesn't have to have a 10-foot antenna on a roof of a home or apartment building. You can now receive 1 of the 35 licensed television signals in your area or DMAs, as they are called, that are broadcast over the air with an inexpensive $30 antenna and can watch NBC, CBS, ABC, FOX, CW, et cetera, which are mandated via their FCC license to broadcast their content free of charge. This has driven many households to cord cut or eliminate cable TV and get content from over-the-air stations while utilizing their broadband connection for the subscription-based over-the-top content or OTT, like Netflix, ESPN, Apple Plus, Disney+ et cetera. This cord cutting phenomenon continues to rapidly escalate with OTA households now nearing 20 million or nearly 50 million people, according to Nielsen, up from just 16 million households in 2017.

Our platform capitalizes on this trend with our national footprint of 210 operating television stations and is soon to be operating 40 additional silent broadcast licenses across the country, at which point we will have a presence in DMAs that represent close to 80% of the U.S. population.

As important, technology advancements now allow for the delivery of up to 6 channels for each station, 2 in high-def and 4 in standard def, definition, for a total of 6 potential revenue streams for each station. This is much different than years ago where you can only broadcast 1 channel per station, in Los Angeles, for instance, where we have 4 stations, we could deliver up to 24 channels of content over the air, a virtual skinny bundle multichannel video programming distributor model.

Throughout the industry, peers are commenting and adjusting their models based on the OTA growth. Specifically, recent remarks from a broadcast peer called a migration back to OTA and over the air renaissance, and we could not agree more. Younger demographics are subscribing to Netflix, ESPN, Apple Plus and then complementing these OTT services through the purchase of a simple digital antenna that will go in their living room window to provide them with free OTA television. The beauty of our strategy and our platform is that it is complementary to any content provider or service. It's not an either/or but an in addition to as there is really no other way to get in front of the 50 million viewers and their eyeballs as they leave cable TV behind.

What is great about our platform is that there are multiple ways for HC2 to make money. Let me discuss a few different models that can be deployed. One, lease capacity to third-party content providers based on a rate per OTA household in that market have launched, as we've done with CBS with their launch of their new DABL lifestyle network and many others. This model is very similar to a cell tower model with very attractive margins and substantial operating leverage. In this model, we've seen a step-up in rates per household as the OTA market continues to increase and demand exceeds supply.

In addition, the national footprint is a more value-added proposition and a one-stop shop where we have pricing power as a result. The revenue share model, number two, is with content providers ad-based revenue stream, sharing the content providers ad-based revenue stream as we are doing with the launch of Cheddar news and [Altice One Network] and beIN SPORTS.

This model could be exceedingly attractive as an ad-based model considering the number of ad dollars available today. Of course, the stronger the content, the higher the ad dollars. I've always said that with 1 station, you will not attract the high-quality content provider, but with a national footprint, you will attract a different higher quality provider as evidenced by bringing in beIN SPORTS, DABL and Cheddar to HC2 broadcasting.

The third is to provide our own content and control 100% of the ad revenue as we do with our Azteca America network.

Each, of course, has its advantages and disadvantages. But with our 210 stations, growing to 250 with 6 potential revenue streams per station, we have a tremendous amount of capacity. As I've said, because we now have a unique national footprint, we are now fielding incoming calls from high-quality content providers who are losing eyeballs as cable subscribers decline. In the past few months alone, we've signed up, as I mentioned, Cheddar, which is the Altice company and beIN SPORTS, which is the entity that controls much of the European soccer rights as well as CBS and their DABL networks. This, along with the number of networks that we have existing on our platform today. Live sports and news can be particularly valuable content, and our recent agreements are beginning to validate a reason for entering the broadcast business.

We also believe there are other valuable nontraditional ways such as offloading of mobile traffic to utilize the spectrum as we look to maximize the full capacity within our overall network. As of today, with our 210 stations, we are in 91 DMAs in total across the U.S. and Puerto Rico. These 91 DMAs represent 74% of the total U.S. TV households, according to Nielsen. When we complete the build-out of an additional 40 licenses that we plan to bring online in 2020, we expect to have presence in approximately 100 DMAs

that represent nearly 80% of the total U.S. TV households, including 9 of the top 10 and 34 of the top 35 DMAs. This would make us the largest over-the-air broadcast distribution platform in the U.S. while we've significantly reduced costs and increased our efficiency with Azteca America network structure so that the network group is now positively contributing to the broadcasting segment, the ramp-up of stations has naturally increased our expenses on the station group side. For instance, when bringing a station online, we incur basic monthly tower rent, electricity and internet expense while we wait to ramp up revenue, which can take some time. There is no question, though, as the OTA market continues to expand, we will attract more and more quality content providers and even nontraditional content providers.

While our station base alone has substantial asset value and continues to appreciate as we turn our focus to the top line and ramp up our customer base, we believe we will experience significant margin expansion and high marginal contribution to our cash flow due to our low-cost structure and fixed overhead. This all, of course, equates to significant positive adjusted EBITDA and significant long-term value for our shareholders.

We also continue to see a lot of potential with respect to our energy segment and believe it will be a much larger contributor over the long-term and become a material part of our overall structure as we move forward. We first entered this business in 2014 through the purchase of a majority interest in American Natural Gas, which we recently renamed American Natural Energy. This entity designs, builds, owns, operates and maintains domestic CNG commercial fueling stations for transportation. This was a strategic acquisition based on the thesis that compressed nat gas, or CNG, would become a primary alternative as commercial vehicles transition away from environmentally unfriendly diesel fuel and enjoy the benefits of a much lower cost product.

As the American transportation sector transitions to a low-carbon economy, we believe CNG will play a key role in reducing emissions, extending the lives of vehicles and notably reducing fuel costs. Today, there are 175,000 commercially available nat gas vehicles on U.S. roads, spanning all weight classes and vehicle applications, and more and more fleets are converting to compressed nat gas vehicles driven by the lower fuel and maintenance costs. Between the lower cost of natural gas compared to diesel over the long term and the reduced maintenance expenses than traditional diesel fleets, companies switching to compressed nat gas vehicles see a full return on investment in 18 to 24 months.

We believe, given the abundance of natural gas reserves in the U.S., the use of CNG for fueling and the emergence of renewable natural gas, or RNG, as a low-carbon footprint fuel source, provide a viable, cost efficient, clean emissions alternative to the status quo. We made significant progress in 2019 at ANG, acquiring 20 additional fueling stations in the Southeast U.S. and now have a network of approximately 60 stations, making us one of the largest owners and operators of CNG stations in the U.S., nearly doubling the volume of our gasoline gallons equivalent distribution. And we were further aided by the renewal of the AFTC or Alternative Fuels Tax Credit near the end of 2019.

The AFTC was renewed for 3 years, retroactive to January 1, 2018, which provides us with a $0.50 per gallon tax credit on every gallon equivalent distributed. It has reenergized the industry, and we are expecting a strong 2020, thanks in part due to the tax credit. Further, as the tax credit is shared with our customers, it incentivizes them to continue to expand their compressed nat gas fleets and, thus, increase the volume of CNG usage at our stations.

Seeing the opportunity with respect to natural gas and having patience in a long-term outlook is paying off right now for HC2. It took vision to see the opportunity in 2014, and we have executed very well on that vision over the past few years at ANG.

With environmental concerns consistently at the forefront of everyone's mind, we remain very optimistic about the long-term possibilities for value creation at energy as we believe the role CNG will play in the future will grow exponentially with respect to fueling commercial vehicles.

In addition to these high-growth segments, we are also very excited about our Pansend Life Sciences portfolio, particularly our investments in MediBeacon and R2 Technologies, where we also saw excellent progress in 2019 and have high hopes for moving forward to realize value.

In 2019, MediBeacon entered into an exclusive commercial agreement with Huadong Medicine, a leading pharmaceutical company in China, granting Huadong exclusive rights to MediBeacon's portfolio of assets in Greater China. Under the agreement, MediBeacon will receive royalty payments on net sales in Greater China and other Asia Pacific countries. In addition, Huadong made an initial equity investment of $15 million to fund MediBeacon through the upcoming FDA pivotal clinical trials and approval process, valuing MediBeacon at a post-money valuation of $315 million. Huadong will also make a second equity investment of $15 million at a predetermined post-money valuation of $415 million upon MediBeacon achieving U.S. FDA approval for its TGFR measurement system, which measures kidney function in real time.

We, at HC2, have invested a total of $25 million in MediBeacon through Pansend and, thus, we are poised to realize substantial value from this investment.

Looking ahead, we expect the last clinical trial to begin in the back half of 2020 for MediBeacon's TGFR system. Because the system has already received FDA breakthrough device designation, the trial will be highly visible as all will be able to see the results. This is a major benefit of receiving this designation as we expect considerable attention will be paid as the trial concludes in early 2021, which will put us in a stronger position to ultimately maximize the value of MediBeacon. We remain deliberate in our approach, which we believe will position us best to realize an appropriate and strong valuation at the right time.

In addition to MediBeacon, R2 Technologies also entered into a strategic partnership with Huadong in 2019. Under an exclusive distribution agreement, Huadong will distribute R2 lightning devices and products in Greater China and other Asia Pacific countries. In addition, Huadong made a $10 million equity investment in R2 at a post-money valuation of $60 million that is funding the company's next phase of product and market development.

We expect commercial sales for R2 devices in the U.S. to begin in the second half of 2020. We are very excited about the potential for these investments to provide us with significant return on investment and maximize value for shareholders.

To sum up, 2019 was a year of considerable progress for HC2 as we grew adjusted EBITDA, reduced nonoperating corporate expenses and began the path forward to transforming our balance sheet and optimizing our capital structure as we begin to pivot from an early stage debt story to a next stage growth and innovation story to allow us to maximize the full potential of our businesses.

2020 has already started strong with the divestiture of our Marine business, the debt reduction plan taking hold and ongoing progress with cost cutting. As we move forward with our insurance and construction strategic processes, we believe we are firmly on the path to strengthening our balance sheet and transforming HC2 into a long-term growth and innovative company.

HC2's portfolio is uniquely positioned. And this management team not only remains committed to capitalizing on the value created over the years at DBM, but also driving growth and value within our energy and broadcast segments and life science subsidiaries, all while continuing our efforts to further reduce overhead and improve margins. At that point, we firmly believe these efforts will enhance shareholder value longer term.

Finally, we welcome Ms. Julie Springer as the newest Independent Director to our Board last month. Our Nominating and Governance committee went through a long and robust process searching for the right director who not only had the requisite skill set to complement the Board, but also add to the diversity of our Board. The Board had been looking for a qualified candidate with deep marketing expertise. And

adding a proven leader in marketing and branding like Julie will help HC2 communicate our long-term strategy of evolving to a growth and innovation story.

With that, I'll now turn the call over to our CFO, Mike Sena, who will discuss some of our financial highlights.

Michael J. Sena, HC2 Holdings, Inc. - CFO [4]

Thank you, Phil. Let's review our fourth quarter and full year performance. Consolidated total net revenue for the fourth quarter 2019 was $498.4 million compared to $524.9 million in the prior year period as lower revenues from the Construction, Telecommunications and Marine segments were partially offset by increases in revenue from Insurance, net of eliminations, and Energy segments. Net loss attributable to common and participating preferred stockholders for the fourth quarter of 2019 was $31.4 million or $0.66 per share compared to a net loss of $16.1 million or $0.36 per share in the prior year period.

Fourth quarter 2019 results included $50.4 million in goodwill impairment, mostly at Continental, which I'll touch upon more in a minute. Our prior year period results included a bargain purchase gain of $6.3 million related to the completing -- to completing the acquisition of Humana's long-term care business, KMG America Corporation as well as a $29.2 million gain on the recapture of one of Continental Insurance's reinsurance treaties.

At the company's core operating subsidiaries, which comprise HC2's construction, marine services, energy and telecom segments, adjusted EBITDA for the fourth quarter of 2019 increased 53% to $43.5 million compared to $28.5 million in the prior year period. The increase of $15 million was primarily attributable to Energy, which recognized $10.6 million in AFTC revenues from the renewal of the fuel tax credit for 2018 and 2019, as Phil pointed out.

Total adjusted EBITDA, which excludes our insurance segment, more than doubled to $36.7 million in the fourth quarter of 2019 compared to adjusted EBITDA of $15.1 million in the prior year period. The increase in year-over-year adjusted EBITDA during the fourth quarter was driven by the improvements from our core subsidiaries as well as reduced losses at broadcasting and a meaningful reduction in nonoperating corporate expenses to end the year.

I'd like to highlight the significant reductions in costs at the broadcasting segment. In addition, focusing on the build-out of the OTA platform, the team has done a great job executing on restructuring efforts, principally the Azteca America network, which was generating significant losses at the time of acquisition.

For the full year 2019, our core subsidiaries increased their adjusted EBITDA contribution by $22.4 to $126.8 million. And Broadcasting and Life Sciences companies saw reduced losses. We generated total adjusted EBITDA, excluding the insurance segment, of $90.8 million, 104% increase compared to adjusted EBITDA of $44.5 million in the prior year, as we saw improvements in results across most of our subsidiaries. Again, I would also like to note the decrease in adjusted EBITDA losses for nonoperating corporate, which decreased by $8 million, which I'll touch on later.

Let's just take a couple of minutes to go into a bit more detail in a few of our segments. At Construction, we recorded adjusted EBITDA for the fourth quarter 2019 of $20.8 million, an increase of $1.4 million over the prior year period. Construction performed strongly for the full year 2019 as well, generating adjusted EBITDA for the year of $75.7 million, driven by completion of certain large-scale DBM global commercial fabrication and erection projects as well as contributions from GrayWolf Industrial. As of December 31, 2019, reported backlog was $498 million. Adjusted backlog, which takes into consideration awarded but not yet signed contracts at DBM Global and GrayWolf, was a combined $826 million. Near record

adjusted backlog, mainly consisting of smaller to medium-sized projects, which provides Construction with significant visibility into 2020 and 2021. The adjusted backlog is a testament to the success of the combination of DBM and GrayWolf's capabilities, enabling them to cross-sell additional services to customers.

At Marine Services, we recorded adjusted EBITDA for the fourth quarter 2019 of $9.3 million, an increase of $2.4 million over the prior year period. For the full year 2019, the segment generated a combined adjusted EBITDA of $30.7 million, which was slightly lower than the prior year period.

Excluding results from our HMN joint venture, 2019 adjusted EBITDA for our recent marine divestiture, Global Marine Group, was $25.7 million, which I should note included the impact of an unfavorable $5 million litigation settlement recorded at GMG's SBSS joint venture.

At Energy, we recorded adjusted EBITDA in the fourth quarter of $12.4 million compared to adjusted EBITDA of $0.8 million in the prior year period. As Phil noted in his remarks, the segment benefited in the quarter from our portion of the renewal of the alternative fuels tax credit, or AFTC, which was retroactive to January 1, 2018, as well as the acquisition of 20 CNG stations at the end of the second quarter. As a note, approximately half of the $10.6 million of AFTC revenues recognized in the fourth quarter was related to CNG sales for the acquired AMP stations for the full year 2018 and 2019. The AFTC was extended through December 31, 2020.

As a note, it is typical that the AFTC is only renewed for the current year and 1-year forward rather than for multiple years in advance. The full retroactive credit from 2018, 2019 and the year forward for 2020 points to the ongoing support for compressed natural gas.

We also think this will be an important business development tool for ANG and the broader industry as adoption of CNG continues. The gross tax credit, which equates to $0.50 per gasoline gallon equivalent is shared with our customers as an incentive for them to continue the conversion of their fleets to CNG. And over time, larger CNG fleets would mean greater volumes for our stations.

Meanwhile, at Insurance, we generated pretax adjusted operating income for the fourth quarter of $10.5 million, an increase of $1.2 million over the prior year period. For the full year 2019, pretax AOI increased by $85.1 to $85.7 million. The year-over-year improvement was driven by the KIC block, which contributed incremental net investment income and policy premiums partially offset the related benefits paid and increases in claim reserves. Further, the legacy CGI block benefited from higher net investment income attributable to higher average invested assets as a result of reinvestment of premiums and income received. The legacy block also benefited from a decrease in benefits and expenses related to favorable claims activity during the year, principally in the first half 2019. This was partially offset by an increase in SG&A across the platform, primarily attributable to headcount additions related to the acquisition of the KIC block.

During the fourth quarter, we recorded $47 million of goodwill impairment at the segment, entirely related to our initial long-term care block acquisition back in 2015 and unrelated to the KIC acquisition in 2018. The goodwill test for insurance is a simple comparison of book value to fair value. If the fair value is lower than the book value, it results in an impairment.

In 2019, driven by GAAP operating results, Continental's book value grew to approximately $500 million, inclusive of almost $199 million of accumulated other comprehensive income. The increase in book value in 2019 was largely driven by 2019 net income, excluding the impact of the goodwill impairment of $99 million.

Put simply, the overall book value increased by $99 million before the goodwill impairment and excluding the impact of AOCI during 2019. In addition, there were several factors that occurred in the fourth quarter of 2019 that impacted the fair value of the insurance segment, primarily regarding our expectations with

respect to levels of future management fees under our investment management agreement along with our expectation of future dividends at the recent and ongoing discussions with our domestic regulator.

It is important to point out that these factors do not have a major impact on the operations of the business but they do impact our ability to capture value that would otherwise be effectively trapped in the insurance company for the foreseeable future. As a result of the above, our book value at CGI exceeded fair value, and the company recognized a goodwill impairment charge of $47 million.

As of December 31, 2019, Insurance had cash and invested assets of $4.5 billion, total GAAP assets of $5.6 billion and an estimated $338.2 million of total adjusted capital. At the end of 2019, HC2 had consolidated cash, cash equivalents and investments of $4.6 billion, which includes cash and investments associated with HC2's insurance segment. Excluding Insurance, consolidated cash was $68.5 million.

I'd also like to touch on corporate expenses for a minute, which significantly decreased throughout 2019. A portion of the $4. 8 million reduction in the fourth quarter was related to a reduction in bonus expense and a clawback of deferred cash compensation for management. Since inception of HC2 in 2014, management's bonus has been based on the growth in HC2's net asset value or NAV from the beginning to the end of the year in excess of a hurdle rate established by the Board's compensation committee at the beginning of the year. 12% of that excess is shared with management. However, the allocated amount may be reduced by the compensation committee by exercising negative discretion, which it has done in the past.

Because there was a decline in NAV in 2019 compared to 2018, the plan, which was established at HC2's inception and has not been changed to benefit management, requires deferred cash compensation to be clawed back. And a clawback of approximately $800,000 was recorded in the fourth quarter. In addition, the corporate bonus plan for management includes a high watermark. As a result, NAV growth in 2020 is going to be measured off the higher 2018 mark and would still need to clear a set hurdle rate before any share of NAV growth would be available at the management. In addition to the decrease in bonus and clawback on the accrued bonus, on a year-over-year basis, we saw reductions in nearly all of our expense categories. We take our corporate expenditures seriously, and we continue to focus on finding ways to reduce our corporate cost without sacrificing our dedication to a strong compliance environment that is essential in a complex public company as we head into 2020 and focus on other strategic initiatives.

That said, our Q4 corporate adjusted EBITDA loss of $2.7 million, which includes the impact of the deferred bonus clawback required under the terms of the bonus plan, should not be viewed as a run rate for 2020. As we've noted on past calls, our expenses are typically higher in the first half of the year compared to the second half of the year.

Earlier this month, we announced a partial redemption of our 11.5% notes that will reduce our note principal by $77 million. Upon the closing of the sale of our 30% interest in HMN, which we now expect to occur early in the second quarter as we complete some final logistical steps that have taken a bit longer due to the current global environment, we plan to announce another partial redemption from HC2's portion of the net proceeds.

Both redemptions will be completed in compliance with our 11.5% notes indenture and the combined decrease in aggregate principal outstanding will provide significant interest savings, both in advance of our June payment and on an annualized basis.

Our current plan for 2020 is to upstream over $40 million in cash from our subsidiaries. While we have the capacity to upstream additional cash from our subsidiaries if the need arises, we currently intend to keep capacity at our subsidiaries as they and we execute on our strategic plans. In addition, we entered into a new revolving credit line, which will provide $15 million of additional liquidity.

We remain very comfortable with our overall liquidity position in 2020, while we continue to focus on further expense reductions and pursuing our strategic initiatives to reduce holding company debt and unlock value within the HC2 portfolio.

We will now open the line for questions. Operator?

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Questions and Answers

Operator [1]

(Operator Instructions) Our first question will come from Sarkis Sherbetchyan of B. Riley Financial Inc.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [2]

First question just really relates to the liquidity levers to the holding company. Mike, I think you just mentioned $40 million of cash upstream from the subsidiaries to the holdco. Maybe if you can give us a more detailed breakdown of the liquidity levers, especially after you anticipate on paying down the 11.5%, I think you mentioned $77 million.

Michael J. Sena, HC2 Holdings, Inc. - CFO [3]

Sure. Thanks, Sarkis. We -- with the -- over $40 million is really what we have planned, and it's broken down the normal cash flow levers that we had last year around DBM, insurance and PTGI. We have additional capacity down there that we would draw on to the extent we need to. But right now, that's our plan based on our strategic options going forward. We expect to have pretty significant savings from the buyback that we talked about of the $77 million. And so we -- in addition, we're going to do another redemption when we close on HMN.

So the $77 million is $9 million of interest savings. And then we, of course, have the first closing of HMN, which has been pushed out slightly just because of the things going on in the world. Administratively, we expect it to take a little longer than we originally thought.

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [4]

Yes. Sarkis, if I can just add to that, that's obviously a very good question, and it's something that we have all planned out and are crossing the Ts and dotting the Is on, but there's no reason to -- for us to be

concerned with that, with meeting those liquidity needs. And especially as we look to things going forward, we're going to see additional cost savings on the overhead. And we haven't seen anything from a disruption perspective from -- on the operations side. We feel like we're in pretty good shape. We've got the revolver there as well, which we thought was very important for us to have that as we look to move into 2020.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [5]

Okay. I guess, if we can maybe now touch on just -- you mentioned reducing the corporate overhead. I think everyone's just kind of interested on really understanding what the level of corporate expense, maybe you're targeting for fiscal '20, right? I mean, if I compare the upstream figure you just cited, the levers and then add up the interest level pro forma for what you're going to pay down plus the corporate expense, I'm having a little bit of a difficult time kind of bridging the gap. Can you maybe kind of help us understand the opportunity in reducing overhead?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [6]

Yes, I'll tell you one right off the top that we're all over, and that's on the real estate. We've been out looking at additional space. And the beauty of our setup here is HC2 doesn't have the long-term lease, so we can exit relatively quickly, if necessary. And I think we'll save a good chunk of change going forward with that in mind. There's other things that we -- as you look at the corporate overhead from a legal perspective, we've done a lot of work on both acquisitions, et cetera, over the number of years. And that's typically been a -- not a sizable piece, but a piece that we can -- that is much more variable, and that will come down. And there are other kind of nits and nats. There's not a lot of things that you can do on the reporting side. But over the last number of years, we've had -- as we've kind of ramped up, we have seen expenses kind of increase to probably more than we had hoped. And now we clearly have made, over the last 12 months, made a conscientious decision to really slow down on some of these things that we've been looking at, which will really, I think, drop to the bottom line and get our expenses more in line with, quite frankly, where they should be. And that's a top priority for us. It hasn't gone unnoticed. You're not the only one that's asked that question over time. But we've already had a nice move with the reduction of that corporate overhead.

And there are a number of different things that we can do and that we are doing that will continue to get that in line. Because quite frankly, we're not there yet. We've got some more wood to chop, but you can't do this stuff overnight. And when we look at our model, there's no doubt that from a liquidity perspective, we have internally bridged that gap. It's tough for me to think of what your -- how you're looking at it and what expenses you have on your spreadsheet, but I know that internally, we are very comfortable with where we are and fully expect that to continue to improve as we go throughout the year.

Michael J. Sena, HC2 Holdings, Inc. - CFO [7]

So Sarkis, we've talked about over $53 million of cash flows from -- coming up from the subs. We do have some cash on the balance sheet, and we do have additional capacity that we will pull up. And all of these

are a bunch of moving pieces as far as our strategic plans and when the timing of things roll in. So we have the ability to pull more up depending on where we are with our debt reduction strategy going through 2019, if that makes sense.

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [8]

And in addition to that, from a refinancing -- from a refinancing perspective at the subsidiary level there are things where the holding company -- there are situations where the holding company will benefit, benefit meaning cash on the balance sheet as there are certain things that we're doing with a focus on that. Not that we have to do but, again, when you talk about different levers, those are out there.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [9]

Okay. Just kind of switching gears here, talking a little bit about the Insurance segment. I thought that's been a division that you guys were pretty proud of and focused on as far as the kind of cash flow drivers. So a little bit surprised to see that it's kind of been mentioned for the sale process. Maybe talk about that in a little bit more detail. And maybe also, what were the factors that kind of drove this impairment charge in the segment?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [10]

Yes. So I'll start with why going down the path. This -- the insurance business, I was, quite frankly, very high on. It's a business that I structured. It's the -- from inception, I've always believed that there's an opportunity here. And as a result of the certain things that I was looking at when we formed HC2, I was keen on getting into this space, with the objective of the asset management fee and growing that and growing the assets over time.

When we first kicked off this strategy, we had an understanding of a certain management fee that we were going to get and possible dividends associated with that. It's clear, and it has become more clear, and especially with regards to various meetings and discussions that we've had, starting in 2019 and, quite frankly, became more definitive as the year came on and especially in the fourth quarter, that we realized that there was risk around the management fee. And it's no secret that there are -- I don't want to say, competitors, but the competition has also been under pressure with regards to management fee reductions. And while we were hopeful that we were going to be able to work something out, we've had certain meetings that took place in December, quite frankly, that that kind of changed how we thought about the business and changed our comfort level going forward with regards to the management fees that we had structured in our initial plan and especially as it relates to the dividends. There was hope that there -- and expectations that we would be able to extract certain dividends out of the company. And again, dealing with long-term care and the rate increases that, quite frankly, seem to be ongoing from a necessity perspective have really put a -- have tempered our enthusiasm around the dividend aspect. And I think, quite frankly, the combination between the 2, when you look at long-term care, you have to look at the risk parameters around it. And are we comfortable and am I comfortable looking at that cash flow stream that we believe there's risk to it and a decent amount of risk to it. Now, it's not going away, but

it's not comfortable, I don't feel comfortable, quite frankly, having certain amount of capital at risk and looking at the dividend streams going forward.

So I think I can look at that business. And granted there's a return on capital from a dividend stream, but I think I can take that capital and allocate it elsewhere and generate a better return for shareholders. And there's no magic to it other than that. The business has become -- it's still a good business. There's no question about it. But again, there's no secret that certain regulatory authorities have questioned the management fees of some of the bigger players in the industry, and there's no reason to believe that, that is not -- and will not and has not trickled down to us. So that's pretty much it. And at one point, we kind of looked at it and said, okay, where do we want to go with this? What do we want to do? And in looking at that cash flow stream going forward and the potential or I should say the lack of dividends, we just came to that conclusion. No more, no less than that.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [11]

Okay. And the factors on the impairment?

Michael J. Sena, HC2 Holdings, Inc. - CFO [12]

Yes. So basically, it's a measurement of your fair value to your -- fair value to your book value. So the book value of the insurance company at the end of the year was about -- before the impairment was about $500 million, had almost $200 million of AOCI. So excluding that, the book value was $300 million. So when you're measuring your goodwill compared to your -- I mean, your book value to your fair value for your impairment test, if the fair value is lower than the book value, you have to take an impairment. And so even without the factors that Phil described that have been impacting the fair value, we still would have had an impairment because the insurance company had $99 million of net income in 2019 before the impact of goodwill. So you had a book value increase by $100 million. So unless your fair value followed that, you're going to have an impairment.

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [13]

And just one last point to that. I think from past conference calls, we expected and anticipated our dividends to be -- or I'm sorry, our management fee to be $13 million, $14 million, $15 million and potentially going higher. And without question, that is not going to be the case going forward, at least with this asset base. And it really became a, not an issue, but a question for us as we look at, as we look to either continue building this business or exit.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [14]

Okay. Just switching over to broadcasting real quick. You mentioned the build-out for broadcasting over the next 24 months. Any kind of target on the DMM spend in that division?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [15]

Yes, de minimis. We've done the bulk of our CapEx. Keep in mind that building out a station is about $150,000 to $200,000. Not a lot. And it depends on whether you're co-located with an existing station as well. And if you're co-located with an existing station, you tend to have additional savings. So the stations that are coming online, I believe, should be around 40 stations. It's not a tremendous amount of CapEx. It is maybe -- and some of these are partially built out. But from a maximum perspective, you could be looking at $5 million, $6 million maximum. So not a lot of CapEx.

Sarkis Sherbetchyan, B. Riley FBR, Inc., Research Division - Associate Analyst [16]

And do you feel comfortable that the Broadcasting segment has enough to kind of make way with that growth platform?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [17]

Yes, absolutely. We are extremely excited about this. And it's one of the things, as we looked at our business going forward, where our emphasis is going to be, where do we want to focus and where do we think we're going to have a great success. And the fact that we have this platform, these are all licensed stations. It's a very unique platform. You're seeing a tremendous amount of cord cutting. And quite frankly, there's more content out there that needs to get in front of people. And this is back to the old push versus pull phenomenon, i.e., search phenomenon. But as you see the amount of content out there that is -- necessitates getting in front of what we call eyeballs, we have a natural platform for that, that's very unique.

And in looking at the competition, they have a different model. There's a different model out there. It's an affiliate model. And quite frankly, one of the benefits that we have is we -- I don't want to say we have a blank slate because we do have a number of networks on there, but we have a tremendous amount of capacity to host super high-quality content providers, and we're in discussions with people around that today as a result of kind of our one-stop shop. We can put people on 210 stations today, quite frankly, almost overnight. And that's a pretty attractive value-add proposition for any content provider.

And now granted, there's -- if you look at the number of cable subscribers in the marketplace, there's 80 million households. The over the air market is 20 million households and growing. So if you are a cable network and you are on a cable provider, you do not have a natural distribution platform. And as you lose eyeballs, and it is evident in the cable industry, you have to pick those up elsewhere. The only natural place to pick those up is in the over the air market. And 20 million households is a pre -- is a very high number, and it's increasing and increasing and increasing.

If you look at the 5 biggest areas for -- or 5 biggest DMAs for over the air viewership, they're in like Dallas and Los Angeles. Those are massive markets. To lose 25% of your viewership or not -- to have 25% of your viewership not on cable in those certain markets, you got to have -- you have to find a way to get in front of those viewers. We are that way. We are that platform.

And we're seeing that growth continue monthly, and everybody is seeing that growth monthly with the declining number of not only the cable subs, but the DBS market. The DBS market is, quite frankly, fallen off a cliff. So we are the natural alternative. And as I said in the earnings statement, that it's not an either/or, but in addition to. We're a phenomenal complement for any provider, any content producer, quite frankly, that wants to capitalize on the entire marketplace because you can't just do that with -- in the Internet -- over the Internet or over cable.

This market and this strategy was not -- you couldn't do this 20 years ago or 25 years ago. And the time is right because of the technology change, the cord cutting and, quite frankly, the just sheer amount of content out there. And it goes back to what I've said that you could have the best -- the most high-quality content around, but if you don't have a distribution platform, nobody can see it. So we're a natural complement to those types of entities in the marketplace. And we're seeing now, because we are getting recognized, we're getting incoming phone calls just by virtue of some of the things that we're doing out in the marketplace.

Operator [18]

Our next question will come from Nick Brown of Zazove Associates.

Nicholas Brown, Zazove Associates, LLC - Partner, Convertible Bond Analyst & Senior Research Analyst [19]

Actually, I have 2 questions. First on the HMN sale. Maybe I misheard, but could you explain what you meant when you said -- I think you said you completed the sale last week, but then you said it's not going to close until early second quarter. I just want to know what you meant by completing the sale unless I misheard.

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [20]

Sure. As you know, we signed up -- the purchase of HMN via Hengtong, that deal was signed in the fall. What took place last week was the purchase by Hengtong of the 51% of HMN owned by Huawei. That closing essentially was a step for us that we were waiting for in order to close our 30-plus percent sale. So that had to take place first. It closed. And quite frankly, in this marketplace, we're very pleased that it closed because we thought it might even be delayed, but the fact that, that deal was closed and our deal -- and our closing was conditional on that, that's what we were talking about from a delay in the closing of our piece. But the fact that, that close means that ours will close, it's just a function of whether it's -- we were hoping by the end of the month, but looks like it's going to be pushed into the first week or 2 of April.

Nicholas Brown, Zazove Associates, LLC - Partner, Convertible Bond Analyst & Senior Research Analyst [21]

Okay. That's helpful. The timing, especially. And then the other question on the potential insurance sale. What is it about? I mean, I understand why the economics aren't attractive to you anymore, given the changes, but what makes it still attractive to other parties?

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [22]

Well, if you have an existing insurance portfolio, you may have different capital allocator that is looking at a different type of return. When we think about our capital allocation or our cost of debt and our cost of capital in general, we've got to make some decent money on -- or decent return on our capital. And then looking at growing this business, yes, the deal that we did with Humana was a great deal. I'm not saying that there won't be others out there in the marketplace like that. But the expectation is that they could -- it could necessitate some capital. And the question is to really grow this business, do we want to allocate additional capital to grow the business based on what we are seeing now with the management fees where we expect them to be as well as the potential issues with the dividend. And others may have different return parameters, may have a different infrastructure that can and could and may be willing to accommodate those adjustments that are taking place in the market. But quite frankly, we're not.

Operator [23]

This will conclude our question-and-answer session. At this time, I'd like to turn the floor back over to Phil Falcone for any closing comments.

Philip Alan Falcone, HC2 Holdings, Inc. - Chairman, President & CEO [24]

Okay. Thank you, everybody, for joining us today. As always, we will have people here, both Mike, myself and we'll be available to answer questions either today or throughout the week. We appreciate you joining. We know how busy everybody can be and how tumultuous the market can be. So we appreciate your time, and be safe. Thank you very much.

Operator [25]

The conference has now concluded. We thank you for attending today's presentation, and you may now disconnect your lines.