

XYRATEX LTD  
Form 6-K  
February 17, 2009

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 6-K**

**REPORT OF FOREIGN PRIVATE ISSUER PURSUANT TO RULE 13a-16 OR 15d-16 UNDER**  
**THE SECURITIES EXCHANGE ACT OF 1934**

February 17, 2009

Commission File Number:0001284823

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**XYRATEX LTD**

(Translation of registrant's name into English)

**Langstone Road,**

**Havant**

**PO9 1SA**

**United Kingdom**

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or 40-F.

Form 20-F  Form 40-F

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Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1)

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7)

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to rule 12g3-2(b) under the Securities Exchange Act of 1934. Yes  No

If  is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-

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**FOR IMMEDIATE RELEASE**

**Xyratex Ltd Announces Final Results for the Fourth Quarter and Fiscal Year 2008**

**Havant, UK, February 17, 2009** Xyratex Ltd (Nasdaq: XRTX), a leading provider of enterprise class data storage subsystems and storage process technology, today announced final results for the fourth quarter and fiscal year ended November 30, 2008. These results represent an update to the preliminary results announced on January 6, 2009.

The only change from the results announced on January 6 is related to the specific provision representing inventory and future vendor claims. This provision was associated with a specific Networked Storage Solutions customer product forecast which indicated a transition to an updated version sooner than originally planned, giving rise to an exposure on long lead time components. Within its preliminary results the Company provided what it believed would be its maximum probable exposure of \$9.5 million.

Following a thorough assessment of the exposure and mitigation opportunities, it has been concluded that the total provision required is \$2 million and hence the Company has been able to write back \$7.5 million of the preliminary provision.

The updated and final results for Xyratex Ltd for the fourth quarter and fiscal year ended November 30, 2008 are summarized below:

- Revenues for the fourth quarter were \$285.4 million, an increase of 15.1% compared to revenues of \$248 million for the same period last year. Revenues for the full year were \$1,049.7 million, an increase of 12.7%, compared to revenues of \$931.6 million for fiscal year 2007.
- Fourth quarter GAAP net loss was \$55.7 million, or \$1.92 per diluted share compared to GAAP net income of \$11.7 million in the same period last year.
- A GAAP net loss for fiscal year 2008 of \$47.9 million, or \$1.64 per diluted share compared to a GAAP net income of \$28.1 million for fiscal year 2007.
- Fourth quarter non-GAAP net income of \$0.4 million, or \$0.02 per diluted share compared to non-GAAP net income of \$13.1 million in the same quarter a year ago.
- A non-GAAP net income for fiscal year 2008 of \$16.2 million, or a diluted earnings per share of \$0.56 compared to non-GAAP net income of \$37.5 million, or \$1.26 per diluted share, for fiscal year 2007(1).
- Gross profit margin in the fourth quarter of 12.5%, compared to 18.5% in the same period last year and 17.6% in the prior quarter.

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These results will be reflected in the Company's Annual Report on Form 20-F to be issued shortly.

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(1) Non-GAAP net income (loss) and diluted earnings (loss) per share excludes (a) amortization of intangible assets, (b) equity compensation expense, (c) specified non-recurring or non-cash items, such as the impairment of goodwill and the valuation allowance against a deferred tax asset, and (d) the related tax effects. Reconciliation of non-GAAP net income and diluted earnings per share to GAAP net income and GAAP diluted earnings per share is included in a table immediately following the condensed consolidated statements of cash flow below.

The intention in providing these non-GAAP measures is to provide supplemental information regarding the Company's operational performance whilst recognizing that they have material limitations and that they should only be referred to with reference to the corresponding GAAP measure.

The Company believes that the provision of these non-GAAP financial measures is useful to investors and investment analysts because it enables comparison to the Company's historical operating results, those of competitors and other industry participants and also provides transparency to the measures used by management in operational and financial decision making. In relation to the specific items excluded: (a) intangible assets represent costs incurred by the acquired business prior to acquisition, are not cash costs and will not be replaced when the assets are fully amortized and therefore the exclusion of these costs provides management and investors with better visibility of the costs required to generate revenue over time; (b) equity compensation expense is non-cash in nature, is outside the control of management during the period in which the expense is incurred and in addition has not been measured consistently as a result of the implementation of FAS 123R; (c) the impairment of goodwill and the valuation allowance against the deferred tax asset is non-recurring, non-cash and is not comparable across periods or with other companies; (d) the exclusion of the related tax effects of excluding items (a) to (c) is necessary to show the effect on net income of the change in tax expense that would have been recorded if these items had not been incurred.

#### **Safe Harbor Statement**

This press release contains forward looking statements. These statements relate to future events or our future financial performance. These statements are only predictions and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Factors that might cause such a difference include our inability to compete successfully in the competitive and rapidly changing marketplace in which we operate, failure to retain key employees, changes in our customers volume requirements, cancellation or delay of projects and adverse general economic conditions in the United States and internationally. These risks and other factors include those listed under "Risk Factors" and elsewhere in our

Annual Report on Form 20-F as filed with the Securities and Exchange Commission (File No. 000-50799). In some cases, you can identify forward-looking statements by terminology such as may, will, should, expects, intends, plans, anticipates, believes, estimates, continue, or the negative of these terms or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements.

### **About Xyratex**

Xyratex is a leading provider of enterprise class data storage subsystems and storage process technology. The company designs and manufactures enabling technology that provides OEM and disk drive manufacturers with data storage products to support high-performance storage and data communication networks. Xyratex has over 20 years of experience in research and development relating to disk drives, storage systems and high-speed communication protocols.

Founded in 1994 in an MBO from IBM, and with headquarters in the UK, Xyratex has an established global base with R&D and operational facilities in Europe, the United States and South East Asia.

For more information, visit [www.xyratex.com](http://www.xyratex.com).

### **Contacts:**

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## XYRATEX LTD

## UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended,		Year Ended	
	November 30,	November 30,	November 30,	November 30,
	2008	2007	2008	2007

(US dollars in thousands, except per share amounts)

Revenues:								
Networked Storage Solutions	\$	222,300	\$	187,216	\$	855,770	\$	693,990
Storage Infrastructure		63,127		60,772		193,946		237,643
Total revenues		285,427		247,988		1,049,716		931,633
Cost of revenues								
		249,827		202,133		891,139		762,582
Gross profit:								
Networked Storage Solutions		18,643		28,165		107,275		100,573
Storage Infrastructure		17,234		18,046		52,566		69,716
Equity compensation		(277)		(356)		(1,264)		(1,238)
Total gross profit		35,600		45,855		158,577		169,051
Operating expenses:								
Research and development		22,726		19,370		85,897		77,559
Selling, general and administrative		15,984		16,532		63,686		61,977
Amortization of intangible assets		1,223		2,485		4,882		7,304
Impairment of goodwill		34,256				34,256		
Total operating expenses		74,189		38,387		188,721		146,840
Operating income (loss)		(38,589)		7,468		(30,144)		22,211
Other income								
								890
Interest income, net		166		1,030		1,618		3,283
Income (loss) before income taxes		(38,423)		8,498		(28,526)		26,384
Provision (benefit) for income taxes		17,324		(3,229)		19,383		(1,725)
Net income (loss)	\$	(55,747)	\$	11,727	\$	(47,909)	\$	28,109
Net earnings (loss) per share:								
Basic	\$	(1.92)	\$	0.40	\$	(1.64)	\$	0.97
Diluted	\$	(1.92)	\$	0.39	\$	(1.64)	\$	0.94
Weighted average common shares (in thousands), used in computing net earnings (loss) per share:								
Basic		29,096		29,100		29,157		28,985
Diluted		29,096		29,758		29,157		29,866

## XYRATEX LTD

## UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	November 30, 2008	November 30, 2007
	(US dollars and amounts in thousands)	
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 28,013	\$ 70,678
Accounts receivable, net	140,879	122,327
Inventories	128,183	91,662
Prepaid expenses	2,746	2,994
Deferred income taxes	1,000	3,000
Other current assets	4,430	8,275
<b>Total current assets</b>	<b>305,251</b>	<b>298,936</b>
Property, plant and equipment, net	47,229	37,421
Intangible assets, net	11,162	54,175
Deferred income taxes	9,545	19,743
<b>Total assets</b>	<b>\$ 373,187</b>	<b>\$ 410,275</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 111,295	\$ 96,046
Employee compensation and benefits payable	9,745	13,280
Deferred revenue	8,386	15,212
Income taxes payable	2,573	1,165
Other accrued liabilities	27,599	11,311
<b>Total current liabilities</b>	<b>159,598</b>	<b>137,014</b>
Long-term debt		
<b>Total liabilities</b>	<b>159,598</b>	<b>137,014</b>
<b>Shareholders equity</b>		
Common shares of Xyratex Ltd (in thousands), par value \$0.01 per share 70,000 authorized, 29,146 and 29,117 issued and outstanding	291	291
Additional paid-in capital	366,067	356,268
Accumulated other comprehensive income	(13,603)	1,847
Accumulated deficit	(139,166)	(85,145)
<b>Total shareholders equity</b>	<b>213,589</b>	<b>273,261</b>
<b>Total liabilities and shareholders equity</b>	<b>\$ 373,187</b>	<b>\$ 410,275</b>



## XYRATEX LTD

## UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended	
	November 30, 2008	November 30, 2007
	(US dollars in thousands)	
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$ (47,909)	\$ 28,109
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	15,770	13,683
Amortization of intangible assets	4,882	7,304
Impairment of intangible assets	34,256	
Non-cash equity compensation	7,646	8,057
Loss on sale of assets	185	341
Changes in assets and liabilities, net of impact of acquisitions and divestitures		
Accounts receivable	(18,552)	(17,003)
Inventories	(36,521)	1,449
Prepaid expenses and other current assets	1,455	(2,956)
Accounts payable	15,249	11,150
Employee compensation and benefits payable	(3,535)	(3,365)
Deferred revenue	(6,826)	(1,091)
Income taxes payable	1,408	(476)
Deferred income taxes	16,944	(1,616)
Other accrued liabilities	2,718	(2,266)
Net cash provided by (used in) operating activities	(12,830)	41,320
<b>Cash flows from investing activities:</b>		
Investments in property, plant and equipment	(25,763)	(16,974)
Acquisition of intangible assets		(4,833)
Acquisition of business, net of cash received		(1,661)
Net cash used in investing activities	(25,763)	(23,468)
<b>Cash flows from financing activities:</b>		
Payments of short-term borrowings		(7,000)
Repurchases of common shares	(6,116)	
Proceeds from issuance of shares	2,044	2,905
Net cash used in financing activities	(4,072)	(4,095)
Change in cash and cash equivalents	(42,665)	13,757
Cash and cash equivalents at beginning of period	70,678	56,921
Cash and cash equivalents at end of period	\$ 28,013	\$ 70,678

## XYRATEX LTD

## SUPPLEMENTAL INFORMATION

Three Months Ended  
 November 30, 2008      November 30, 2007      November 30, 2008  
 (US dollars in thousands, except  
 per share amounts)

## Summary Reconciliation Of GAAP Net Income To Non-GAAP Net Income

GAAP net income (loss)	cal-align:bottom;padding-left			
	\$ (55,747)	\$ 11,472,909		
Operating revenue	11,330	12,231	37,151	41,053
Operating expenses	9,178	10,073	28,948	32,515
Operating income	2,152	2,158	8,203	8,538
Company's 50% share of operating income	1,076	1,080	4,102	4,269
Less amortization of intangible assets	105	105	314	314
Equity in earnings of TNI	971	975	3,788	3,955

TNI makes weekly distributions of its earnings and for the 13 weeks ended June 25, 2017 and June 26, 2016 we received \$1,213,000 and \$1,501,000 in distributions, respectively. In the 39 weeks ended June 25, 2017 and June 26, 2016 we received \$3,633,000 and \$5,230,000 in distributions, respectively.

Star Publishing's 50% share of TNI depreciation and certain general and administrative expenses associated with its share of the operation and administration of TNI are reported as operating expenses (income) in our Consolidated Statements of Income and Comprehensive Income. These amounts totaled \$128,000 and \$162,000 in the 13 weeks ended June 25, 2017 and June 26, 2016, respectively and \$428,000 and \$(1,000) in the 39 weeks ended June 25, 2017 and June 26, 2016, respectively.

Annual amortization of intangible assets is estimated to be \$418,000 for the 52 or 53 weeks ending June 2018, 2019 and \$314,000 in 2020.

Madison Newspapers, Inc.

We have a 50% ownership interest in MNI, which publishes daily and Sunday newspapers, and other publications in Madison, Wisconsin, and other Wisconsin locations, and operates their related digital platforms. Net income or loss of MNI (after income taxes) is allocated equally to us and The Capital Times Company ("TCT"). MNI conducts its business under the trade name Capital Newspapers.

Summarized results of MNI are as follows:

(Thousands of Dollars)	13 Weeks Ended		39 Weeks Ended	
	June 25 2017	June 26 2016	June 25 2017	June 26 2016
Operating revenue	15,070	16,263	46,493	49,602

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Operating expenses, excluding workforce adjustments, depreciation and amortization	12,649	13,160	38,576	39,819
Workforce adjustments	81	13	236	32
Depreciation and amortization	348	410	1,044	1,303
Operating income	1,992	2,680	6,637	8,448
Net income	1,291	1,699	4,492	5,347
Equity in earnings of MNI	645	850	2,246	2,678

MNI makes quarterly distributions of its earnings and in the 13 weeks ended June 25, 2017 and June 26, 2016 we received dividends of \$500,000 and \$1,750,000, respectively. In the 39 weeks ended June 25, 2017 and June 26, 2016 we received dividends of \$2,750,000 and \$5,750,000, respectively.

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## 3 GOODWILL AND OTHER INTANGIBLE ASSETS

Changes in the carrying amount of goodwill are as follows:

(Thousands of Dollars)	39 Weeks Ended	
	June 25	2017
Goodwill, gross amount	1,532,458	
Accumulated impairment losses	(1,288,729	)
Goodwill, beginning of period	243,729	
Goodwill acquired in business combinations	250	
Goodwill, end of period	243,979	

In the 13 weeks ended June 25, 2017, the Company purchased a weekly publication in the same market as one of our existing operations. The acquisition resulted in recording \$250,000 of additional goodwill.

Identified intangible assets consist of the following:

(Thousands of Dollars)	June 25	September 25
	2017	2016
Nonamortized intangible assets:		
Mastheads	23,644	23,644
Amortizable intangible assets:		
Customer and newspaper subscriber lists	687,221	687,182
Less accumulated amortization	571,376	552,472
	115,845	134,710
Noncompete and consulting agreements	28,524	28,524
Less accumulated amortization	28,524	28,524
	—	—
Other intangible assets, net	139,489	158,354

Annual amortization of intangible assets for the 52 or 53 weeks ended June 2018 to June 2022 is estimated to be \$18,685,000, \$16,321,000, \$15,249,000, \$14,824,000 and \$11,934,000, respectively.

In January 2017, the Financial Accounting Standards Board ("FASB") issued a new standard simplifying the assessment of a goodwill impairment. The new standard maintains a qualitative and quantitative assessment but eliminates the Step 2 of the quantitative assessment. The new standard also changes the way a goodwill impairment is calculated. For companies with zero or negative carrying value, the new standard requires disclosure of the amount of goodwill for those reporting units. The adoption of the new standard is required in 2019. Early adoption of the standard is permitted for impairment tests performed after January 1, 2017. The Company has elected to early adopt this standard for its 2017 goodwill impairment test.

## 4 DEBT

On March 31, 2014, we completed a comprehensive refinancing of our debt (the "2014 Refinancing"), which included the following:

\$400,000,000 aggregate principal amount of 9.5% Senior Secured Notes (the "Notes"), pursuant to an Indenture dated as of March 31, 2014 (the "Indenture").

\$250,000,000 first lien term loan (the "1<sup>st</sup> Lien Term Loan") and \$40,000,000 revolving facility (the "Revolving Facility") under a First Lien Credit Agreement dated as of March 31, 2014 (together the "1<sup>st</sup> Lien Credit Facility").

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\$150,000,000 second lien term loan under a Second Lien Loan Agreement dated as of March 31, 2014 (the “2<sup>d</sup> Lien Term Loan”).

Debt is summarized as follows:

(Thousands of Dollars)			Interest Rates (%)
	June 25 2017	September 26 2016	June 25 2017
Revolving Facility	—	—	6.72
1 <sup>st</sup> Lien Term Loan	58,984	101,304	7.29
Notes	385,000	385,000	9.50
2 <sup>nd</sup> Lien Term Loan	124,496	130,863	12.00
	568,480	617,167	
Unamortized debt issue costs	(23,124)	(26,271)	)
Less current maturities of long-term debt	32,138	25,070	
Total long-term debt	513,218	565,826	

Our weighted average cost of debt, excluding amortization of debt financing costs at June 25, 2017, is 9.8%.

At June 25, 2017, aggregate minimum required maturities of debt excluding amounts required to be paid from future excess cash flow computations total \$13,388,000 for the remainder of 2017, \$25,000,000 in 2018, \$26,145,000 in 2019, zero in 2020, zero in 2021 and \$503,947,000 thereafter.

In April 2015, the FASB issued a new standard for the presentation of debt issuance costs. The new standard streamlined the balance sheet presentation of debt related valuations. Debt issuance costs were previously recognized as deferred charges and presented as an asset while debt discounts and premiums are treated as adjustments to the related debt. Under the new standard, debt issuance costs are now recognized as reductions to the related debt. The adoption of this standard reclassified certain amounts within our Consolidated Balance Sheets. We adopted the new standard in 2017, as required, and adopted this standard retrospectively. As a result, we have reclassified \$26,271,000 of Other long-term assets to a reduction of long-term debt, net of current maturities in the September 25, 2016 Consolidated Balance Sheet.

## Notes

The Notes are senior secured obligations of the Company and mature on March 15, 2022. At June 25, 2017, the principal balance of the Notes totaled \$385,000,000.

## Interest

The Notes require payment of interest semiannually on March 15 and September 15 of each year, at a fixed annual rate of 9.5%.

## Redemption

We may redeem some, or all, of the principal amount of the Notes at any time. Prior to March 15, 2018, we may redeem the Notes subject to a make whole provision for the interest through March 15, 2018. On or after March 15, 2018, we may redeem the Notes as follows:

Period Beginning Percentage of Principal Amount

March 15, 2018	104.75
March 15, 2019	102.38
March 15, 2020	100.00

If we sell certain of our assets or experience specific kinds of changes of control, we must, subject to certain exceptions, offer to purchase the Notes at 101% of the principal amount. Any redemption of the Notes must also satisfy any accrued and unpaid interest thereon.

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We may repurchase Notes in the open market at any time. In the 39 weeks ended June 26, 2016, we purchased \$15,000,000 principal amount of Notes in privately negotiated transactions which resulted in a gain on extinguishment of debt totaling \$1,250,000. The gain is recorded in Other, net in the Consolidated Statements of Income and Comprehensive Income.

### Covenants and Other Matters

The Indenture and the 1<sup>st</sup> Lien Credit Facility contains restrictive covenants as discussed more fully below. However, certain of these covenants will cease to apply if the Notes are rated investment grade by either Moody's Investors Service, Inc. or Standard & Poor's Ratings Group and there is no default or event of default under the Indenture.

### 1<sup>st</sup> Lien Credit Facility

The 1<sup>st</sup> Lien Credit Facility consists of the \$250,000,000 1<sup>st</sup> Lien Term Loan that matures in March 2019 and the \$40,000,000 Revolving Facility that matures in December 2018. The 1<sup>st</sup> Lien Credit Facility documents the primary terms of the 1<sup>st</sup> Lien Term Loan and the Revolving Facility. The Revolving Facility may be used for working capital and general corporate purposes (including letters of credit). At June 25, 2017, after consideration of letters of credit, we have approximately \$33,818,000 available for future use under the Revolving Facility.

### Interest

Interest on the 1<sup>st</sup> Lien Term Loan, which has a principal balance of \$58,984,000 at June 25, 2017, accrues, at our option, at either (A) LIBOR plus 6.25% (with a LIBOR floor of 1.0%) or (B) 5.25% plus the higher of (i) the prime rate at the time, (ii) the federal funds rate plus 0.5%, or (iii) one month LIBOR plus 1.0% (with a floor of 2.0%). Interest is payable quarterly.

The 1<sup>st</sup> Lien Term Loan was funded with an original issue discount of 2.0%, or \$5,000,000, which is being amortized as debt financing and administration costs over the life of the 1<sup>st</sup> Lien Term Loan.

Interest on the Revolving Facility, which has a principal balance of zero at June 25, 2017, accrues, at our option, at either (A) LIBOR plus 5.5%, or (B) 4.5% plus the higher of (i) the prime rate at the time, (ii) the federal funds rate plus 0.5%, or (iii) one month LIBOR plus 1.0%.

### Principal Payments

Quarterly principal payments of \$6,250,000 are required under the 1<sup>st</sup> Lien Term Loan, with additional payments required to be made based on 90% of excess cash flow of Lee Legacy ("Lee Legacy Excess Cash Flow"), as defined, or from proceeds of asset sales, which are not reinvested, as defined, from our subsidiaries other than Pulitzer Inc. ("Pulitzer") and its subsidiaries (collectively, the "Pulitzer Subsidiaries"). For excess cash flow calculation purposes Lee Legacy constitutes the business of the Company, including MNI, but excluding Pulitzer and TNI. We may voluntarily prepay principal amounts outstanding or reduce commitments under the 1<sup>st</sup> Lien Credit Facility at any time without premium or penalty, upon proper notice and subject to certain limitations as to minimum amounts of prepayments.

Quarterly, the Company is required to prepare a Lee Legacy Excess Cash Flow calculation, which is generally determined as the cash earnings of our subsidiaries other than the Pulitzer Subsidiaries and includes adjustments for changes in working capital, capital spending, pension contributions, debt principal payments and income tax payments or refunds. Any excess cash flow as calculated is required to be paid to the 1<sup>st</sup> Lien lenders 45 days after the end of the quarter. For the 13 weeks ended June 25, 2017, the required Lee Legacy Excess Cash Flow payment was \$1,589,000.





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2017 payments made, or required to be made for the remainder of the year, under the 1<sup>st</sup> Lien Term Loan are summarized as follows:

(Thousands of Dollars)	13 Weeks Ended		13 Weeks Ending	
	December 25 2016	March 26 2017	June 25 2017	September 24 2017
Mandatory	6,250	6,250	6,250	6,250
Voluntary	11,000	7,500	5,000	—
Excess cash flow payment	70	—	—	1,589
	17,320	13,750	11,250	7,839

## Covenants and Other Matters

The 1<sup>st</sup> Lien Credit Facility requires that we comply with certain affirmative and negative covenants customary for financing of this nature, including a maximum total leverage ratio, which is only applicable to the Revolving Facility.

The 1<sup>st</sup> Lien Credit Facility restricts us from paying dividends on our Common Stock. This restriction no longer applies if Lee Legacy leverage is below 3.25x before and after such payments. Further, the 1<sup>st</sup> Lien Credit Facility restricts or limits, among other things, subject to certain exceptions, the ability of the Company and its subsidiaries to: (i) incur indebtedness, (ii) enter into mergers, acquisitions and asset sales, (iii) incur or create liens and (iv) enter into transactions with certain affiliates. The 1<sup>st</sup> Lien Credit Facility contains various representations and warranties and may be terminated upon occurrence of certain events of default. The 1<sup>st</sup> Lien Credit Facility also contains cross-default provisions tied to the terms of each of the Indenture and 2<sup>nd</sup> Lien Term Loan.

2<sup>nd</sup> Lien Term Loan

The 2<sup>nd</sup> Lien Term Loan, which has a balance of \$124,496,000 at June 25, 2017, bears interest at a fixed annual rate of 12.0%, payable quarterly, and matures in December 2022.

## Principal Payments

There are no scheduled mandatory amortization payments required under the 2<sup>nd</sup> Lien Term Loan.

Quarterly, we are required to prepare a calculation of excess cash flow of the Pulitzer Subsidiaries ("Pulitzer Excess Cash Flow"). Pulitzer Excess Cash Flow is generally determined as the cash earnings of the Pulitzer Subsidiaries including adjustments for changes in working capital, capital spending, pension contributions, debt principal payments and income tax payments. Pulitzer Excess Cash Flow also includes a deduction for interest costs incurred under the 2<sup>nd</sup> Lien Term Loan.

Prior to March 31, 2017, we were required to offer the Pulitzer Excess Cash Flow to the 2<sup>nd</sup> Lien Lenders to prepay the 2<sup>nd</sup> Lien Term Loan at par, which payment the 2<sup>nd</sup> Lien Lenders could accept or reject. After March 31, 2017, Pulitzer Excess Cash Flow is used to prepay the 2<sup>nd</sup> Lien Term Loan, at par. Pulitzer Excess Cash Flow payments are required to be paid 45 days after the end of the quarter. For the 13 weeks ended June 25, 2017, Pulitzer Excess Cash Flow totaled \$5,549,000, which will be used to repay the 2<sup>nd</sup> Lien Term Loan in August 2017, at par.

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Pulitzer Excess Cash Flow and the related payments on the 2<sup>nd</sup> Lien Term Loan for the previous four quarters are as follows:

For the Period Ending (Thousands of Dollars)	Pulitzer Excess Cash Flow	Payment Date	Payment Amount (not rejected)
June 26, 2016	1,583	Q4 2016	299
September 25, 2016	—	Q1 2017	—
December 25, 2016	930	Q2 2017	174
March 26, 2017	4,488	Q3 2017	4,488

Subject to certain other conditions in the 2<sup>nd</sup> Lien Term Loan, the balance of the 2<sup>nd</sup> Lien Term Loan will be repaid at par from proceeds from asset sales by the Pulitzer Subsidiaries that are not reinvested. For the 39 weeks ended June 25, 2017 and June 26, 2016, we repaid \$1,705,000 and \$3,546,000, respectively, on the 2<sup>nd</sup> Lien Term Loan, at par, with net proceeds from the sale of Pulitzer assets.

Voluntary payments under the 2<sup>nd</sup> Lien Term Loan are subject to call premiums as follows:

Period Beginning Percentage of Principal Amount

March 31, 2017	106
March 31, 2018	103
March 31, 2019	100

## Covenants and Other Matters

The 2<sup>nd</sup> Lien Term Loan requires that we comply with certain affirmative and negative covenants customary for financing of this nature, including the negative covenants under the 1<sup>st</sup> Lien Credit Facility discussed above. The 2<sup>nd</sup> Lien Term Loan contains various representations and warranties and may be terminated upon occurrence of certain events of default. The 2<sup>nd</sup> Lien Term Loan also contains cross-default provisions tied to the terms of the Indenture and 1<sup>st</sup> Lien Credit Facility.

In connection with the 2<sup>nd</sup> Lien Term Loan, we entered into a Warrant Agreement dated as of March 31, 2014 (the “Warrant Agreement”). Under the Warrant Agreement, certain affiliates or designees of the 2<sup>nd</sup> Lien Lenders received on March 31, 2014 their pro rata share of warrants to purchase, in cash, an initial aggregate of 6,000,000 shares of Common Stock, subject to adjustment pursuant to anti-dilution provisions (the “Warrants”). The Warrants represent, when fully exercised, approximately 10.1% of shares of Common Stock outstanding at March 30, 2014 on a fully diluted basis. The exercise price of the Warrants is \$4.19 per share.

The Warrant Agreement contains a cash settlement provision in the event of a change of control prior to March 31, 2018 as well as other provisions requiring the Warrants to be measured at fair value and included in other liabilities in our Consolidated Balance Sheets. We remeasure the fair value of the liability each reporting period, with changes reported in other, net non-operating income (expense). The initial fair value of the Warrants was \$16,930,000. See Note 9.

In connection with the issuance of the Warrants, we entered into a Registration Rights Agreement dated as of March 31, 2014 (the “Registration Rights Agreement”). The Registration Rights Agreement requires, among other matters, that we use our commercially reasonable efforts to maintain the effectiveness for certain specified periods of a shelf registration statement related to the shares of Common Stock to be issued upon exercise of the Warrants.

## Security

The Notes and the 1<sup>st</sup> Lien Credit Facility are fully and unconditionally guaranteed on a joint and several first-priority basis by each of the Company's material domestic subsidiaries, excluding MNI, the Pulitzer Subsidiaries and TNI (the "Lee Legacy Assignors"), pursuant to a first lien guarantee and collateral agreement dated as of March 31, 2014 (the "1<sup>st</sup> Lien Guarantee and Collateral Agreement").

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The Notes, the 1<sup>st</sup> Lien Credit Facility and the subsidiary guarantees are secured, subject to certain exceptions, priorities and limitations, by perfected security interests in all property and assets, including certain real estate, of the Lee Legacy Assignors, other than the capital stock of MNI and any property and assets of MNI (the “Lee Legacy Collateral”), on a first-priority basis, equally and ratably with all of the Lee Legacy Assignors' existing and future obligations. The Lee Legacy Collateral includes, among other things, equipment, inventory, accounts receivables, depository accounts, intellectual property and certain of their other tangible and intangible assets.

Also, the Notes and the 1<sup>st</sup> Lien Credit Facility are secured, subject to certain exceptions, priorities and limitations in the various agreements, by first-priority security interests in the capital stock of, and other equity interests owned by, the Lee Legacy Assignors (excluding the capital stock of MNI). The Notes and 1<sup>st</sup> Lien Credit Facility are subject to a Pari Passu Intercreditor Agreement dated March 31, 2014.

The Notes, the 1<sup>st</sup> Lien Credit Facility and the subsidiary guarantees are also secured, subject to permitted liens, by a second-priority security interest in the property and assets of the Pulitzer Subsidiaries that become subsidiary guarantors (the “Pulitzer Assignors”) other than assets of or used in the operations or business of TNI (collectively, the “Pulitzer Collateral”). In June 2015 the Pulitzer Assignors became a party to the 1<sup>st</sup> Lien Guarantee and Collateral Agreement on a second lien basis.

Also, the Notes and the 1<sup>st</sup> Lien Credit Facility are secured, subject to certain exceptions, priorities, and limitations in the various agreements, by second-priority security interests in the capital stock of, and other equity interests in, the Pulitzer Assignors and Star Publishing’s interest in TNI.

The 2<sup>nd</sup> Lien Term Loan is fully and unconditionally guaranteed on a joint and several first-priority basis by the Pulitzer Assignors, pursuant to a Second Lien Guarantee and Collateral Agreement dated as of March 31, 2014 (the “2<sup>nd</sup> Lien Guarantee and Collateral Agreement”) among the Pulitzer Assignors and the 2<sup>nd</sup> Lien collateral agent.

Under the 2<sup>nd</sup> Lien Guarantee and Collateral Agreement, the Pulitzer Assignors have granted (i) first-priority security interests, subject to certain priorities and limitations in the various agreements, in the Pulitzer Collateral and (ii) have granted first-priority lien mortgages or deeds of trust covering certain real estate, as collateral for the payment and performance of their obligations under the 2<sup>nd</sup> Lien Term Loan.

Also, under the 2<sup>nd</sup> Lien Guarantee and Collateral Agreement, the Lee Legacy Assignors have granted (i) second-priority security interests, subject to certain priorities and limitations in the various agreements, in the Lee Legacy Collateral, and (ii) have granted second-priority lien mortgages or deeds of trust covering certain real estate, as collateral for the payment and performance of their obligations under the 2<sup>nd</sup> Lien Term Loan. Assets of, or used in the operations or business of, MNI are excluded.

The rights of each of the collateral agents with respect to the Lee Legacy Collateral and the Pulitzer Collateral are subject to customary intercreditor and intercompany agreements.

## Other

In connection with the 2014 Refinancing, we capitalized \$37,819,000 of debt financing costs. Amortization of debt financing costs totaled \$1,297,000 and \$3,148,000 in the 13 weeks and 39 weeks ended June 25, 2017, respectively, and \$1,132,000 and \$4,211,000 in the 13 and 39 weeks ended June 26, 2016, respectively. Amortization of such costs is estimated to total \$4,170,000 in 2017, \$4,163,000 in 2018, \$4,009,000 in 2019, \$4,063,000 in 2020 and \$4,248,000 in 2021. At June 25, 2017, we have \$23,124,000 of unamortized debt financing costs recorded as a reduction of Long-term debt in our Consolidated Balance Sheets.

## Liquidity

At June 25, 2017, after consideration of letters of credit, we have approximately \$33,818,000 available for future use under our Revolving Facility. Including cash, our liquidity at June 25, 2017 totals \$58,790,000. This liquidity amount excludes any future cash flows. We expect all interest and principal payments due in the next twelve months will be satisfied by existing cash and our cash flows, which will allow us to maintain an adequate level of liquidity. The Warrants, if and when exercised, would provide additional liquidity in an amount up to \$25,140,000 subject to a reduction for any amounts the Company may elect to use to repay our 1<sup>st</sup> Lien Term Loan and/or the Notes.

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Final maturities of our debt range from December 2018 through December 2022.

There are numerous potential consequences under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, if an event of default, as defined, occurs and is not remedied. Many of those consequences are beyond our control. The occurrence of one or more events of default would give rise to the right of the applicable lender(s) to exercise their remedies under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, respectively, including, without limitation, the right to accelerate all outstanding debt and take actions authorized in such circumstances under applicable collateral security documents.

Our ability to operate as a going concern is dependent on our ability to remain in compliance with debt covenants and to repay, refinance or amend our debt agreements as they become due. The Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan have only limited affirmative covenants with which we are required to maintain compliance. We are in compliance with our debt covenants at June 25, 2017.

**5 PENSION, POSTRETIREMENT AND POSTEMPLOYMENT DEFINED BENEFIT PLANS**

We have several noncontributory defined benefit pension plans that together cover selected employees. Benefits under the plans were generally based on salary and years of service. Effective in 2012, substantially all benefits are frozen and only a small amount of additional benefits are being accrued. Our liability and related expense for benefits under the plans are recorded over the service period of employees based upon annual actuarial calculations. Plan funding strategies are influenced by government regulations. Plan assets consist primarily of domestic and foreign corporate equity securities, government and corporate bonds, hedge fund investments and cash.

In addition, we provide retiree medical and life insurance benefits under postretirement plans at several of our operating locations. The level and adjustment of participant contributions vary depending on the specific plan. In addition, St. Louis Post-Dispatch LLC, provides postemployment disability benefits to certain employee groups prior to retirement. Our liability and related expense for benefits under the postretirement plans are recorded over the service period of active employees based upon annual actuarial calculations. We accrue postemployment disability benefits when it becomes probable that such benefits will be paid and when sufficient information exists to make reasonable estimates of the amounts to be paid.

We use a fiscal year end measurement date for all of our pension and postretirement medical plan obligations.

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The net periodic postretirement cost (benefit) components for our postretirement plans are as follows:

PENSION PLANS  (Thousands of Dollars)	13 Weeks		39 Weeks	
	Ended		Ended	
	June 25	June 26	June 25	June 26
	2017	2016	2017	2016
Service cost for benefits earned during the period	21	49	63	147
Interest cost on projected benefit obligation	1,349	1,515	4,047	4,545
Expected return on plan assets	(1,969)	(2,174)	(5,907)	(6,522)
Amortization of net loss	736	599	2,208	1,797
Amortization of prior service benefit	(34)	(34)	(102)	(102)
Pension expense (benefit)	103	(45)	309	(135)
POSTRETIREMENT MEDICAL PLANS  (Thousands of Dollars)	13 Weeks		39 Weeks	
	Ended		Ended	
	June 25	June 26	June 25	June 26
	2017	2016	2017	2016
Service cost for benefits earned during the period	—	16	12	48
Interest cost on projected benefit obligation	91	156	323	468
Expected return on plan assets	(264)	(331)	(792)	(993)
Amortization of net gain	(254)	(273)	(734)	(819)
Amortization of prior service benefit	(365)	(365)	(1,095)	(1,095)
Curtailment gains	—	—	(3,741)	—
Postretirement medical benefit	(792)	(797)	(6,027)	(2,391)

Amortization of net gains (losses) and prior service benefits are recorded as compensation in the Consolidated Statements of Income and Comprehensive Income.

In March 2017, we notified certain participants in one of our post employment medical plans of changes to their plan, which included notice that the plan will terminate on December 31, 2017. These changes resulted in a non-cash curtailment gain of \$3,741,000, which is recorded in gain on sales of assets and other, net in the Consolidated Statements of income and Comprehensive Income. These changes also reduced the postemployment benefit obligation by \$5,158,000 and reduced accumulated other comprehensive loss by \$1,417,000.

Based on our forecast at June 25, 2017, we do not expect to make contributions to our pension trust and postretirement medical plans for the remainder of fiscal 2017.

## 6 INCOME TAXES

We recorded income tax expense of \$1,843,000 and \$9,253,000 related to income before taxes of \$8,130,000 and \$34,358,000 for the 13 and 39 weeks ended June 25, 2017, respectively. For the 13 and 39 weeks ended June 26, 2016, we recorded \$3,037,000 and \$22,571,000 in income tax expense related to income before taxes of \$7,404,000 and \$57,929,000, respectively. The effective income tax rates for the 13 weeks ended June 25, 2017 and June 26, 2016 were 22.7% and 41.0%, respectively. The effective income tax rates for the 39 weeks ended June 25, 2017 and June 26, 2016 were 26.9% and 39.0%, respectively. The mark-to-market adjustments to value the Warrants is the primary cause of the reduction in the effective income tax rates in 2017. The primary differences between these rates and the U.S. federal statutory rate of 35% are due to the effect of state taxes, non-deductible expenses, adjustments to reserves for uncertain tax positions, including any related interest, and mark-to-market adjustments to value the



Warrants.

We file a consolidated federal tax return, as well as combined and separate tax returns in approximately 27 state and local jurisdictions. We have various income tax examinations ongoing which are at different stages of completion, but generally our income tax returns have been audited or closed to audit through 2009. See Note 10 for a discussion of our tax audits.

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At September 25, 2016, we had approximately \$57,392,000 of state net operating loss tax benefits and a federal net operating loss carryforward of approximately \$58,618,000. Due to our federal and state net operating loss carryforwards and based on historical levels of performance, we do not expect to make any significant income tax payments in the current fiscal year.

**7 EARNINGS PER COMMON SHARE**

The following table sets forth the computation of basic and diluted earnings per common share:

(Thousands of Dollars and Shares, Except Per Share Data)	13 Weeks		39 Weeks	
	Ended		Ended	
	June 25 2017	June 26 2016	June 25 2017	June 26 2016
Income attributable to Lee Enterprises, Incorporated:	5,995	4,092	24,296	34,557
Weighted average common shares	56,668	55,735	56,401	55,398
Less weighted average restricted Common Stock	(2,515 )	(2,524 )	(2,491 )	(2,222 )
Basic average common shares	54,153	53,211	53,910	53,176
Dilutive stock options and restricted Common Stock	1,302	1,114	1,492	783
Diluted average common shares	55,455	54,325	55,402	53,959
Earnings per common share:				
Basic	0.11	0.08	0.45	0.65
Diluted	0.11	0.08	0.44	0.64

For the 13 and 39 weeks ended June 25, 2017, 7,327,000 and 6,617,000, weighted average shares, respectively, were not considered in the computation of diluted earnings per common share because the exercise prices of the related stock options and Warrants were in excess of the fair market value of our Common Stock. For the 13 and 39 weeks ended June 26, 2016, 6,919,000 and 7,643,000, weighted average shares, respectively, were not considered in the computation of diluted earnings per common share because the exercise prices of the related stock options and Warrants were in excess of the fair market value of our Common Stock.

**8 STOCK OWNERSHIP PLANS**

A summary of stock option activity during the 39 weeks ended June 25, 2017 follows:

(Thousands of Dollars and Shares, Except Per Share Data)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding, September 25, 2016	1,698	2.42		
Exercised	(336 )	1.54		
Cancelled	(88 )	14.02		
Outstanding, June 25, 2017	1,274	1.85	3.9	437
Exercisable, June 25, 2017	1,274	1.85	3.9	437

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## Restricted Common Stock

The table below summarizes restricted Common Stock activity during the 39 weeks ended June 25, 2017:

(Thousands of Shares, Except Per Share Data)	Shares	Weighted Average Grant Date Fair Value
Outstanding, September 25, 2016	2,462	2.74
Vested	(741 )	3.59
Granted	823	3.34
Cancelled	(50 )	2.89
Outstanding, June 25, 2017	2,494	2.69

Total unrecognized compensation expense for unvested restricted Common Stock at June 25, 2017 is \$3,302,000, which will be recognized over a weighted average period of 1.5 years.

## 9FAIR VALUE MEASUREMENTS

We utilize FASB ASC Topic 820, Fair Value Measurements and Disclosures, to measure and report fair value. FASB ASC Topic 820 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FASB ASC Topic 820 establishes a three-level hierarchy of fair value measurements based on whether the inputs to those measurements are observable or unobservable, which consists of the following levels:

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets.

Level 3 - Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following methods and assumptions are used to estimate the fair value of each class of financial instruments for which it is practicable to estimate value.

The carrying amounts of cash equivalents, accounts receivable and accounts payable approximate fair value because of the short maturity of those instruments. Investments totaling \$6,818,000, including our 17% ownership of the nonvoting common stock of TCT and a private equity investment, are carried at cost. As of June 30, 2017, based on the most recent data available, the approximate fair value of the private equity investment is \$8,039,000, which is a level 3 fair value measurement.

The fair value of floating rate debt, which consists of our 1<sup>st</sup> Lien Term Loan, is \$58,836,000, based on an average of private market price quotations. Our fixed rate debt consists of \$385,000,000 principal amount of the Notes and \$124,496,000 principal amount under the 2<sup>nd</sup> Lien Term Loan. At June 25, 2017, based on private market price quotations, the fair values were \$393,662,000 and \$129,164,000 for the Notes and 2<sup>nd</sup> Lien Term Loan, respectively. These represent level 2 fair value measurements.

As discussed more fully in Note 4, we recorded a liability for the Warrants issued in connection with the Warrant Agreement. The liability was initially measured at its fair value and we remeasure the liability to fair value each reporting period, with changes reported in other non-operating income (expense). The initial fair value of the Warrants

was \$16,930,000. The fair value of Warrants at June 25, 2017, March 26, 2017 and September 25, 2016 is \$1,342,000, \$4,382,000 and \$11,760,000, respectively. Fair value is determined using the Black-Scholes option pricing model. These represent level 2 fair value measurements.

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10 COMMITMENTS AND CONTINGENT LIABILITIES

Income Taxes

Commitments exclude unrecognized tax benefits to be recorded in accordance with FASB ASC Topic 740, Income Taxes. We are unable to reasonably estimate the ultimate amount or timing of cash settlements with the respective taxing authorities for such matters. See Note 6.

We file income tax returns with the Internal Revenue Service ("IRS") and various state tax jurisdictions. From time to time, we are subject to routine audits by those agencies and those audits may result in proposed adjustments. We have considered the alternative interpretations that may be assumed by the various taxing agencies, believe our positions taken regarding our filings are valid, and that adequate tax liabilities have been recorded to resolve such matters. However, the actual outcome cannot be determined with certainty and the difference could be material, either positively or negatively, to the Consolidated Statements of Operations and Comprehensive Income (Loss) in the periods in which such matters are ultimately determined. We do not believe the final resolution of such matters will be material to our consolidated financial position or cash flows.

We have various income tax examinations ongoing and at various stages of completion, but generally our income tax returns have been audited or closed to audit through 2009.

Legal Proceedings

We are involved in a variety of legal actions that arise in the normal course of business. Insurance coverage mitigates potential loss for certain of these matters. While we are unable to predict the ultimate outcome of these legal actions, it is our opinion that the disposition of these matters will not have a material adverse effect on our Consolidated Financial Statements, taken as a whole.

Multiemployer Pension Plans

The Company contributes to three multiemployer pension plans. In June 2017, a union contract covering certain of our employees under a multiemployer pension plan expired resulting in a partial withdrawal from one of the multiemployer plans. The Company recorded an estimate of the partial withdrawal liability resulting in a \$2,600,000 increase in both Other long-term liabilities in the Consolidated Balance Sheet and Workforce adjustments and other in the Consolidated Statement of Income and Comprehensive Income. Once the multiemployer pension plan's administrators finalize the partial withdrawal liability, it will be paid in equal installments over a twenty year period.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion includes comments and analysis relating to our results of operations and financial condition as of and for the 13 weeks and 39 weeks ended June 25, 2017. This discussion should be read in conjunction with the Consolidated Financial Statements and related Notes thereto, included herein, and our 2016 Annual Report on Form 10-K.

NON-GAAP FINANCIAL MEASURES

We use non-GAAP financial performance measures for purposes of evaluating our performance and liquidity. We believe that each of the non-GAAP measures presented provides useful information to investors by allowing them to view our businesses through the eyes of our management and Board of Directors, facilitating comparison of results across historical periods, and providing a focus on the underlying ongoing operating performance and liquidity of our businesses. The non-GAAP financial measures we use are as follows:

Adjusted EBITDA is a non-GAAP financial performance measure that enhances a financial statement user's overall understanding of the operating performance of the Company. The measure isolates unusual, infrequent or non-cash transactions from the operating performance of the business. This allows users to easily compare operating performance among various fiscal periods and understand how management measures the performance of the business. This measure also provides users with a benchmark that can be used when forecasting future operating performance of the Company that excludes unusual, nonrecurring or one time transactions. Adjusted EBITDA is also a component of the calculation used by stockholders and analysts to determine the value of our business when using the market approach, which applies a market multiple to financial metrics. It is also a measure used to calculate the leverage ratio of the Company, which is a key financial ratio monitored and used by the Company and its investors. Adjusted EBITDA is defined as net income (loss), plus nonoperating expenses (income), net, income tax expense (benefit), depreciation, amortization, loss (gain) on sale of assets, impairment charges, workforce adjustment costs, stock compensation and our 50% share of EBITDA from TNI and MNI, minus equity in earnings of TNI and MNI and curtailment gains.

Adjusted Income (Loss) and Adjusted Earnings (Loss) Per Common Share are non-GAAP financial performance measures that we believe offer a useful metric to evaluate overall performance of the Company by providing financial statement users the operating performance of the Company on a per share basis excluding the impact of changes in the warrant valuation as well as unusual and infrequent transactions. It is defined as income (loss) attributable to Lee Enterprises, Incorporated and earnings (loss) per common share adjusted to exclude the impact of the warrant valuation, unusual matters and those of a substantially non-recurring nature.

Cash Costs is a non-GAAP financial performance measure of operating expenses that are settled in cash and is useful to investors in understanding the components of the Company's cash operating costs. Generally, the Company provides forward-looking guidance of Cash Costs, which can be used by financial statement users to assess the Company's ability to manage and control its operating cost structure. Cash Costs is defined as compensation, newsprint and ink, other operating expenses and certain unusual matters, such as workforce adjustment costs. Depreciation, amortization, impairment charges, other non-cash operating expenses and other unusual matters are excluded. Cash Costs are also presented excluding workforce adjustments, which are paid in cash.

We also present revenue and certain operating expense trends on a Same Property basis which excludes the operating results of the Daily Herald in Provo, UT, which was sold in August 2016, and the acquisition of a weekly publication in 2017. Same Property results are useful to investors in understanding the revenue and operating expense trends excluding the impact of changes due to operations no longer owned by the Company or were recently acquired.

A table reconciling Adjusted EBITDA to net income (loss), the most directly comparable measure under GAAP, is set forth in Item 2, included herein, under the caption "Reconciliation of Non-GAAP Financial Measures".

Reconciliations of adjusted income (loss) and adjusted earnings (loss) per common share to income (loss) attributable to Lee Enterprises, Incorporated and earnings (loss) per common share, respectively, the most directly comparable measures under GAAP, are set forth in Item 2, included herein, under the caption "Overall Results".

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The subtotals of operating expenses representing cash costs can be found in tables in Item 2, included herein, under the captions "13 Weeks Ended June 25, 2017" and "39 Weeks Ended June 25, 2017".

Same Property trends can be found in tables in Item 2, included herein, under the captions "13 Weeks Ended June 25, 2017" and "39 Weeks Ended June 25, 2017".

These non-GAAP financial measures should not be considered in isolation from or as a substitute for the related consolidated GAAP measures, and should be read together with financial information presented on a GAAP basis.

#### RECONCILIATION OF NON-GAAP FINANCIAL MEASURES (UNAUDITED)

The table below reconciles the non-GAAP financial performance measure of adjusted EBITDA to net income, the most directly comparable GAAP measure:

(Thousands of Dollars)	13 Weeks Ended		39 Weeks Ended	
	June 25 2017	June 26 2016	June 25 2017	June 26 2016
Net Income	6,287	4,367	25,105	35,358
Adjusted to exclude				
Income tax expense	1,843	3,037	9,253	22,571
Non-operating expenses, net	12,433	17,251	36,447	21,877
Equity in earnings of TNI and MNI	(1,616 )	(1,825 )	(6,034 )	(6,633 )
Loss (gain) on sale of assets, net	(61 )	(354 )	(3,777 )	(1,763 )
Depreciation and amortization	10,296	10,868	30,993	32,752
Workforce adjustments and other	3,902	424	6,372	1,616
Stock compensation	481	550	1,564	1,714
Add:				
Ownership share of TNI and MNI EBITDA (50%)	2,246	2,625	7,943	9,145
Adjusted EBITDA	35,811	36,943	107,866	116,637

#### CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of results of operations and financial condition are based upon our Consolidated Financial Statements, which have been prepared in accordance with Generally Accepted Accounting Principles ("GAAP"). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. We evaluate these estimates and judgments on an ongoing basis.

We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Our critical accounting policies include the following:

- Goodwill and other intangible assets;
- Pension, postretirement and postemployment benefit plans;



- Income taxes;
- Revenue recognition; and
- Uninsured risks.

Additional information regarding these critical accounting policies can be found under the caption “Management's Discussion and Analysis of Financial Condition and Results of Operations” in our 2016 Annual Report on Form 10-K.

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IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In March 2017, the Financial Accounting Standards Board ("FASB") issued a new standard to improve the presentation of pension and postretirement benefit expense. The new standard requires that the service cost component of pension and postretirement benefits expense is recognized as compensation expense, while the remaining components of the expense are presented outside of operating income. The current presentation includes all components of the expense as Compensation in our Consolidated Statements of Income and Comprehensive Income. The adoption of the new standard is required in 2019.

In August 2016, the FASB issued a new standard to conform the presentation in the statement of cash flows for certain transactions, including cash distribution from equity method investments, among others. The adoption of the new standard is required in 2020. The adoption of this standard will reclassify certain cash receipts within the Consolidation Statements of Cash Flows.

In March 2016, the FASB issued a new standard with improvements to the accounting for employee share-based payments. The new standard simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes and statutory tax withholding requirements, as well as classification in the statement of cash flows. The adoption of the new standard is required in 2018. We have not determined the potential effects on the Consolidated Financial Statements.

In February 2016, the FASB issued a new standard for the accounting treatment of leases. The new standard is based on the principle that entities should recognize assets and liabilities arising from leases. The new standard does not significantly change the lessees' recognition, measurement and presentation of expenses and cash flows from the previous accounting standard. Leases are classified as finance or operating. The new standards primary change is the requirement for entities to recognize a lease liability for payments and a right of use asset representing the right to use the leased asset during the term on operating lease arrangements. Lessees are permitted to make an accounting policy election to not recognize the asset and liability for leases with a term of twelve months or less. Lessors' accounting under the new standard is largely unchanged from the previous accounting standard. In addition, the new standard expands the disclosure requirements of lease arrangements. Lessees and lessors will use a modified retrospective transition approach, which includes a number of practical expedients. The adoption of this new standard is required in the first quarter of fiscal year 2020 with early adoption permitted. We have not determined the potential effects on the Consolidated Financial Statements.

In May 2014, the FASB issued new accounting requirements for the recognition of revenue from contracts with customers. The new requirements include additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In April and May 2016, the FASB also issued clarifying updates to the new standard specifically to address certain core principles including the identification of performance obligations, licensing guidance, the assessment of the collectability criterion, the presentation of taxes collected from customers, noncash considerations, contract modifications, and completed contracts at transition. The adoption of these requirements is required in 2019.

We currently anticipate adopting the new revenue recognition standard in the fiscal year beginning October 1, 2018. We are currently evaluating the impact that the updated guidance will have on our financial statements and related disclosures.

EXECUTIVE OVERVIEW

Lee Enterprises, Incorporated is a leading provider of local news and information, and a major platform for advertising, in the markets we serve, which are located primarily in the Midwest, Mountain West and West regions of the United States. With the exception of St. Louis, Missouri, our 50 markets, across 22 states, are principally midsize or small. Through our print and digital platforms, we reach an overwhelming majority of adults in our markets.

Our products include:

47 daily and 35 Sunday newspapers with print and digital subscribers totaling 0.8 million and 1.1 million, respectively, for the 13 weeks ended June 25, 2017. We estimate that almost three million people read our printed daily newspapers each day; and

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♣ Nearly 300 weekly newspapers and classified and niche publications.

Our markets have established retail bases, and most are regional shopping hubs. We are located in four state capitals. Six of our top ten markets by revenue include major universities, and seven are home to major corporate headquarters. We believe that all of these factors have had a positive impact on advertising revenue. Community newspapers and their associated digital media remain a valuable source of local news and information attracting large local audiences and are an effective means for local advertisers to reach their customers. We believe our audiences across these communities tend to be loyal readers who actively seek our content and serve as an attractive target for our advertisers.

We do not face significant competition from other local daily newspapers in most of our markets, although there is competition for audience in those markets from other media. In our top ten markets by revenue, only one has significant local daily print competition.

Our primary source of revenue is advertising and marketing services, followed by subscription revenue. Over the last several years, the advertising industry has experienced a shift from print and other traditional media towards digital advertising as readership has also shifted from print to digital. In addition, our printed newspaper paid subscription and single copy unit sales have declined. We have offset some of our declines in print advertising and marketing services revenue by growing our digital advertising revenue. Subscription revenue has been maintained by increasing subscription rates which includes full access, selling premium day sections and increasing the number of paid digital subscribers.

We have a full access subscription model, which provides subscribers with complete digital access, including desktop, mobile, tablet and replica editions. These are offered as packages with print home delivery or as digital-only subscriptions, with subscription rates reflective of the expanded access.

We continue to transform our business model and carefully manage our costs to maintain strong cash flows and margins.

On June 30, 2017, in the Company's fourth fiscal quarter of 2017, the Company purchased the assets of the Dispatch-Argus serving Moline and Rock Island, Illinois for \$7,150,000 plus an adjustment for working capital. The purchase included one daily newspaper, a weekly publication, two niche publications as well as the related digital platforms. The purchase was funded with cash on the balance sheet and will be consolidated with the Company results in the 13 weeks ended September 24, 2017.

## IMPAIRMENT OF GOODWILL AND OTHER ASSETS

We have significant amounts of goodwill and identified intangible assets. Since 2007 we have recorded impairment charges totaling almost \$1.3 billion to reduce the value of certain of these assets. Should general economic, market or business conditions decline, and have a negative impact on our stock price or projected future cash flows, we may be required to record additional impairment charges in the future. Such impairment charges would not impact our reported cash flows or debt covenant compliance.

## DEBT AND LIQUIDITY

We have a substantial amount of debt, as discussed more fully in Note 4 of the Notes to Consolidated Financial Statements, included herein. Since February 2009, we have satisfied all interest payments and substantially all principal payments due under our debt facilities with our cash flows and asset sales.

As of June 25, 2017, our debt consists of the following:

\$400,000,000 aggregate principal amount of 9.5% Senior Secured Notes (the "Notes"), pursuant to an Indenture dated as of March 31, 2014 (the "Indenture"), of which \$385,000,000 is outstanding at June 25, 2017;

\$250,000,000 first lien term loan (the "1st Lien Term Loan") and \$40,000,000 revolving facility (the "Revolving Facility") under a First Lien Credit Agreement dated as of March 31, 2014 (together, the "1st Lien Credit Facility"), of which \$58,984,000 is outstanding at June 25, 2017; and

\$150,000,000 second lien term loan under a Second Lien Loan Agreement dated as of March 31, 2014 (the "2nd Lien Term Loan"), of which \$124,496,000 is outstanding at June 25, 2017.

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Our ability to make payments on our indebtedness will depend on our ability to generate future cash flows from operations. Cash generated from future asset sales could serve as an additional source of repayment. This ability, to a certain extent, is subject to general economic, financial, competitive, business, legislative, regulatory and other factors that are beyond our control.

At June 25, 2017, after consideration of letters of credit, we have approximately \$33,818,000 available for future use under our Revolving Facility. Including cash, our liquidity at June 25, 2017 totals \$58,790,000. This liquidity amount excludes any future cash flows. Our adjusted EBITDA has been strong for the last seven years and has exceeded \$145,000,000 in each year from 2011 through the trailing twelve months ended June 25, 2017, but there can be no assurance that such performance will continue. We expect all interest and principal payments due in the next twelve months will be satisfied by our cash flows from operations and certain asset sales, which will allow us to maintain an adequate level of liquidity.

At June 25, 2017, the principal amount of our outstanding debt totaled \$568,480,000. The June 25, 2017 principal amount of our debt, net of cash, is 3.75 times our trailing twelve months adjusted EBITDA.

Final maturities of our debt range from December 2018 through December 2022.

There are numerous potential consequences under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, if an event of default, as defined, occurs and is not remedied. Many of those consequences are beyond our control. The occurrence of one or more events of default would give rise to the right of the applicable lender(s) to exercise their remedies under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, respectively, including, without limitation, the right to accelerate all outstanding debt and take actions authorized in such circumstances under applicable collateral security documents.

Our ability to operate as a going concern is dependent on our ability to remain in compliance with debt covenants and to repay, refinance or amend our debt agreements as they become due, if necessary. The Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan have only limited affirmative covenants with which we are required to maintain compliance. We are in compliance with our debt covenants at June 25, 2017.

Due to our federal and state net operating loss carryforwards and based on historical levels of performance, we do not expect to make any significant income tax payments in the current year.

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13 WEEKS ENDED JUNE 25, 2017

Operating results, as reported in the Consolidated Financial Statements, are summarized below.

(Thousands of Dollars, Except Per Share Data)	13 Weeks Ended		Percent Change	Same Property
	June 25 2017	June 26 2016		
Advertising and marketing services revenue:				
Retail	51,946	58,937	(11.9 )	(10.6 )
Classified	22,434	25,707	(12.7 )	(11.8 )
National	4,273	4,626	(7.6 )	(6.3 )
Niche publications and other	2,594	3,024	(14.2 )	(14.3 )
Total advertising and marketing services revenue	81,247	92,294	(12.0 )	(10.8 )
Subscription	47,410	47,160	0.5	1.6
Digital services	3,435	3,541	(3.0 )	(2.2 )
Commercial printing	2,521	3,116	(19.1 )	(17.6 )
Other	4,742	4,835	(1.9 )	(1.6 )
Total operating revenue	139,355	150,946	(7.7 )	(6.6 )
Operating expenses:				
Compensation	51,577	57,218	(9.9 )	(9.1 )
Newsprint and ink	6,123	6,604	(7.3 )	(7.4 )
Other operating expenses	48,571	53,356	(9.0 )	(6.8 )
Workforce adjustments and other	3,902	424	NM	NM
Cash costs	110,173	117,602	(6.3 )	(4.9 )
	29,182	33,344	(12.5 )	(12.2 )
Depreciation and amortization	10,296	10,868	(5.3 )	
Gain on sales of assets and other, net	(61 )	(354 )	NM	
Equity in earnings of associated companies	1,616	1,825	(11.5 )	
Operating income	20,563	24,655	(16.6 )	
Non-operating expense, net	(12,433 )	(17,251 )	(27.9 )	
Income before income taxes	8,130	7,404	9.8	
Income tax expense	1,843	3,037	(39.3 )	
Net income	6,287	4,367	44.0	
Net income attributable to non-controlling interests	(292 )	(275 )	6.2	
Income attributable to Lee Enterprises, Incorporated	5,995	4,092	46.5	
Other comprehensive income (loss), net of income taxes	55	(43 )	NM	
Comprehensive income attributable to Lee Enterprises, Incorporated	6,050	4,049	49.4	
Earnings per common share:				
Basic	0.11	0.08	37.5	
Diluted	0.11	0.08	37.5	

References to the "2017 Quarter" refer to the 13 weeks ended June 25, 2017. Similarly, references to the "2016 Quarter" refer to the 13 weeks ended June 26, 2016. Due to the disposition of the Daily Herald in Provo, UT in August of 2016 and the weekly publication purchased in 2017, all of the revenue and operating expense trends discussed below are on a same property basis, unless otherwise noted.

Advertising and Marketing Services Revenue

In the 2017 Quarter, advertising and marketing services revenue decreased \$9,833,000, or 10.8%, compared to the 2016 Quarter. Retail advertising decreased 10.6%. The decrease in advertising and marketing services revenue is due to reduced advertising volume primarily from large retailers and big box stores. Digital retail advertising on a stand-alone basis, which is the largest digital advertising category, increased 8.3%, partially offsetting print declines.

Classified revenue decreased \$3,004,000, or 11.8%, in the 2017 Quarter as we continue to experience a reduction in print advertising in automotive, employment and real estate in most of our markets which combined declined 27.4%.



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While other classified revenue, which include obituaries and legal notices, declined 4.0% in the 2017 Quarter. Digital classified revenue on a stand-alone basis increased 7.3%.

National advertising decreased \$287,000, or 6.3%, and digital national advertising on a stand-alone basis increased 6.1%.

Niche publications and other decreased \$429,000, or 14.3%, in the 2017 Quarter. Declines were due to elimination of products that do not meet our profit margin standards.

On a stand alone basis, digital advertising and marketing services revenue increased 7.8% to \$23,626,000 in the 2017 Quarter, representing 29.2% of total advertising and marketing services revenue. Total digital revenue, including, TownNews.com, advertising and marketing services and all other digital business was \$27,062,000 in the 2017 Quarter, an increase of 6.4% over the 2016 Quarter. TownNews.com generates the majority of its revenue from content management services at our properties as well as 1,600 other newspapers and other media operations. Print advertising, including preprints and print marketing services revenue, decreased 16.7%.

## Subscription and Other Revenue

Subscription revenue increased \$755,000, or 1.6%, in the 2017 Quarter. The increase in the 2017 Quarter is due to sound pricing principles and additional premium content revenue.

Our average daily newspaper circulation, including TNI, MNI and digital subscribers, totaled 0.8 million in the 2017 Quarter. Sunday circulation totaled 1.1 million.

Digital services revenue decreased \$79,000, or 2.2%, due to a reduction in online surveys. These declines are partially offset by revenue at TownNews.com which increased \$0.2 million, or 5.5%. Commercial printing revenue decreased \$537,000, or 17.6%, in the 2017 Quarter due to decreased volume for existing customers at several of our largest markets.

In the 2017 Quarter, our mobile, tablet, desktop and app sites, including TNI and MNI, attracted an average of 225.7 million monthly page views, a 6.5% increase compared to the 2016 Quarter. Audience engagement is also increasing as pages per user session increased in the 2017 Quarter.

## Operating Expenses

Operating expenses for the 2017 Quarter decreased 4.7%. Excluding workforce adjustments, cash costs decreased 8.0% in the 2017 Quarter.

Compensation expense decreased \$5,158,000, or 9.1%, in the 2017 Quarter, driven by a decline in average full-time equivalent employees of 9.7%.

Newsprint and ink costs decreased \$486,000, or 7.4%, in the 2017 Quarter, as a result of a reduction in newsprint volume of 13.9% from unit reductions and from basis weight changes. The declines were partially offset by higher prices. See Item 3, "Commodities", included herein, for further discussion and analysis of the impact of newsprint prices on our business.

Other operating expenses decreased \$3,523,000, or 6.8%, in the 2017 Quarter. Other operating expenses include all operating costs not considered to be compensation, newsprint, depreciation, amortization, or workforce adjustments

and other. The largest costs included are delivery, postage, outsourced printing, digital cost of goods sold, facility expenses among others. Cost reductions were primarily related to lower subscriber delivery cost from declines in print volumes and a decrease in postage costs, primarily related to a reduction in direct mail advertising volumes.

Workforce adjustment and other costs totaled \$3,902,000 in the 2017 Quarter compare to \$424,000 in the 2016 Quarter. The 2017 Quarter includes a \$2,600,000 expense to record an estimate of a partial withdrawal liability from one of our multiemployer pension plans.

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For fiscal 2017, we expect cash cost excluding workforce adjustments, to decrease 6.5%.

## Results of Operations

On a GAAP basis, depreciation expense decreased \$312,000, or 7.2%, and amortization expense decreased \$260,000, or 4.0%, in the 2017 Quarter. Sales of operating assets resulted in a net gain of \$61,000 in the 2017 Quarter compared to a \$354,000 gain in the 2016 Quarter.

Equity in earnings of TNI and MNI decreased \$209,000 in the 2017 Quarter.

The factors noted above resulted in operating income of \$20,563,000 in the 2017 Quarter compared to \$24,655,000 in the 2016 Quarter.

## Nonoperating Income and Expense

Interest expense decreased \$1,452,000, or 9.2%, to \$14,331,000 in the 2017 Quarter due to lower debt balances. Our weighted average cost of debt, excluding amortization of debt financing costs, increased to 9.8% at the end of the 2017 Quarter compared to 9.6% at the end of the 2016 Quarter, as our Notes and 2<sup>nd</sup> Lien Term Loan balances are now a greater percentage of our outstanding debt due to the ongoing reduction of the 1<sup>st</sup> Lien Term Loan, our lowest cost of debt.

We recognized \$1,438,000 of debt financing and administrative costs in the 2017 Quarter compared to \$1,196,000 in the 2016 Quarter.

Due to the fluctuation in the price of our Common Stock, we recorded non-operating income of \$3,040,000 in 2017 Quarter and a non-operating expense of \$415,000 in the 2016 Quarter, related to the changes in the value of the Warrants.

## Overall Results

We recognized income tax expense of \$1,843,000, resulting in an effective tax rate of 22.7% in the 2017 Quarter compared to 41.0% in the 2016 Quarter. See Note 6 of the Notes to the Consolidated Financial Statements, included herein, for a discussion of the difference between the expected federal income tax rate and the actual tax rates.

As a result of the factors noted above, income attributable to Lee Enterprises, Incorporated totaled \$5,995,000 in the 2017 Quarter compared to \$4,092,000 in the 2016 Quarter. We recorded earnings per diluted common share of \$0.11 in the 2017 Quarter and \$0.08 in the 2016 Quarter. Excluding the warrant fair value adjustment, as detailed in the table below, diluted earnings per common share, as adjusted, were \$0.05 in the 2017 Quarter, compared to \$0.08 the 2016 Quarter. Per share amounts may not add due to rounding.

	13 Weeks Ended			
	June 25 2017		June 26 2016	
(Thousands of Dollars, Except Per Share Data)	Amount	Per Share	Amount	Per Share
Income attributable to Lee Enterprises, Incorporated, as reported	5,995	0.11	4,092	0.08
Adjustments:				
Warrants fair value adjustment	(3,040)	)	415	
	(3,040)	)(0.05	)415	0.01
Income attributable to Lee Enterprises, Incorporated, as adjusted	2,955	0.05	4,507	0.08



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39 WEEKS ENDED JUNE 25, 2017

Operating results, as reported in the Consolidated Financial Statements, are summarized below. Certain prior period amounts have been reclassified to conform with the current year presentation.

(Thousands of Dollars, Except Per Share Data)	39 Weeks Ended		Percent Change	Same Property
	June 25 2017	June 26 2016		
Operating revenue:				
Retail	162,822	184,302	(11.7 )	(10.0 )
Classified	66,457	76,548	(13.2 )	(12.2 )
National	14,977	17,006	(11.9 )	(10.8 )
Niche publications and other	7,559	8,806	(14.2 )	(13.8 )
Total advertising and marketing services revenue	251,815	286,662	(12.2 )	(10.8 )
Subscription	141,306	144,249	(2.0 )	(1.0 )
Digital services	10,390	10,271	1.2	1.4
Commercial printing	7,818	9,385	(16.7 )	(15.5 )
Other	15,402	15,619	(1.4 )	(1.2 )
Total operating revenue	426,731	466,186	(8.5 )	(7.2 )
Operating expenses:				
Compensation	159,047	174,733	(9.0 )	(8.0 )
Newsprint and ink	19,216	19,343	(0.7 )	(0.7 )
Other operating expenses	150,109	166,332	(9.8 )	(7.5 )
Workforce adjustments	6,372	1,616	NM	NM
Cash costs	334,744	362,024	(7.5 )	(6.0 )
	91,987	104,162	(11.7 )	(11.4 )
Depreciation and amortization	30,993	32,752	(5.4 )	
Gain on sales of assets and other, net	(3,777 )	(1,763 )	NM	
Equity in earnings of associated companies	6,034	6,633	(9.0 )	
Operating income	70,805	79,806	(11.3 )	
Non-operating expense, net	(36,447 )	(21,877 )	66.6	
Income before income taxes	34,358	57,929	(40.7 )	
Income tax expense	9,253	22,571	(59.0 )	
Net income	25,105	35,358	(29.0 )	
Net income attributable to non-controlling interests	(809 )	(801 )	1.0	
Income attributable to Lee Enterprises, Incorporated	24,296	34,557	(29.7 )	
Other comprehensive loss, net of income taxes	1,004	(129 )	NM	
Comprehensive income attributable to Lee Enterprises, Incorporated	25,300	34,428	(26.5 )	
Earnings per common share:				
Basic	0.45	0.65	(30.8 )	
Diluted	0.44	0.64	(31.3 )	

References to the "2017 Period" refer to the 39 weeks ended June 25, 2017. Similarly, references to the "2016 Period" refer to the 39 weeks ended June 26, 2016. Due to the disposition of the Daily Herald in Provo, UT in August of 2016 and the weekly publication purchased in 2017, all of the revenue and operating expense trends discussed below are on a same property basis, unless otherwise noted.

Advertising and Marketing Services Revenue

In the 2017 Period, advertising and marketing services revenue decreased \$30,331,000, or 10.8%, compared to the 2016 Period. Retail advertising decreased 10.0%. The decrease in retail advertising revenue is due to reduced advertising volume primarily from large retail, big box stores and classifieds. Digital retail advertising on a stand-alone basis increased 9.8%, partially offsetting print declines.

Classified revenue decreased \$9,217,000, or 12.2%, in the 2017 Period as we continue to experience a reduction in print advertising from automotive, employment and real estate in most of our markets which combined declined 25.0%.

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While other classified revenue, which includes obituaries and legal notices, declined \$1,307,000, or 4.2%, in the 2017 Period, digital classified revenue on a stand-alone basis increased 7.7%.

National advertising decreased \$1,809,000, or 10.8%. Digital national advertising on a stand-alone basis increased 3.7%.

Niche publications and other decreased \$1,205,000, or 13.8%, in the 2017 Period. Declines were due to elimination of products that do not meet our profit margin standards.

On a stand-alone basis, digital advertising and marketing services revenue increased 8.6% to \$68,798,000, in the 2017 Period, representing 27.3% of total advertising and marketing services revenue. Total digital revenue including TownNews.com advertising and marketing services and all other digital business totaled \$79,189,000 in the 2017 Period, an increase of 7.6% over the 2016 Period. TownNews.com generates the majority of its revenue from content management services at our properties as well as 1,600 other newspapers and other media operations. Print advertising, including preprints and print marketing services revenue, decreased 16.4%.

### Subscription and Other Revenue

Subscription revenue decreased \$1,360,000, or 1.0%, in the 2017 Period.

Our average daily newspaper circulation, including TNI, MNI and digital subscribers, totaled 0.9 million in the 2017 Period. Sunday circulation totaled 1.2 million.

Digital services revenue increased \$146,000, or 1.4%, due to TownNews.com, offset by a decrease in online surveys revenue. Commercial printing revenue decreased \$1,429,000, or 15.5%, in the 2017 Period due to decreased volume from several of our existing customers.

### Operating Expenses

Operating expenses for the 2017 Period decreased 5.5%. Excluding workforce adjustments, cash costs decreased 7.4% in the 2017 Period.

Compensation expense decreased \$13,826,000, or 8.0%, in the 2017 Period, driven by a decline of 8.0% in average full time equivalent employees and lower self-insured medical costs.

Newsprint and ink costs decreased \$132,000, or 0.7%, in the 2017 Period, as a result of a 12.9% reduction in newsprint volume partially offset by price increases. See Item 3, "Commodities", included herein, for further discussion and analysis of the impact of newsprint on our business.

Other operating expenses decreased \$12,169,000, or 7.5%, in the 2017 Period. Other operating expenses include all operating costs not considered to be compensation, newsprint, depreciation, amortization, or workforce adjustments and other. The largest costs included are delivery, postage, outsourced printing, digital cost of goods sold, facility expenses among others. Cost reductions were primarily related to lower subscriber delivery cost from declines in print volumes and a decrease in postage costs, as a result to a reduction in direct mail advertising volumes.

Workforce adjustment costs totaled \$6,372,000 and \$1,616,000 in the 2017 Period and 2016 Period, respectively. The 2017 Period includes a \$2,600,000 expense to record an estimate of a partial withdrawal liability from one of our multiemployer pension plans.

Results of Operations

On a GAAP basis, depreciation expense decreased \$885,000, or 6.8%, and amortization expense decreased \$874,000, or 4.4%, in the 2017 Period. Sales of operating assets and other, net including a \$3,741,000 curtailment gain resulted in a net gain of \$3,777,000 in the 2017 Period compared to a net gain of \$1,763,000 in the 2016 Period.

Equity in earnings in associated companies decreased \$599,000 in the 2017 Period.

The factors noted above resulted in operating income of \$70,805,000 in the 2017 Period compared to \$79,806,000 in the 2016 Period.



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## Nonoperating Income and Expense

Interest expense decreased \$5,287,000, or 10.7%, to \$43,919,000 in the 2017 Period due to lower debt balances.

Due to the fluctuation in the price of our Common Stock, we recorded non-operating income of \$10,418,000 in 2017 Period and non-operating expense of \$404,000 in the 2016 Period, related to the changes in the value of the Warrants.

In the 2016 Period, we recognized a \$30,646,000 gain on an insurance settlement. The settlement represents our share of a subrogation recovery arising from the settlement of claims for damages suffered as a result of a 2009 loss at one of the Lee Legacy production facilities.

We recognized \$3,463,000 of debt financing costs in the 2017 Period compared to \$4,563,000 in the 2016 Period related to our 2014 refinancing. We also recognized \$1,250,000 gain on extinguishment of debt in the 2016 Period.

## Overall Results

We recognized income tax expense of \$9,253,000, resulting in an effective tax rate of 26.9% in the 2017 Period compared to 39.0% in the 2016 Period. See Note 6 of the Notes to the Consolidated Financial Statements, included herein, for a discussion of the difference between the expected federal income tax rate and the actual tax rates.

As a result of the factors noted above, income attributable to Lee Enterprises, Incorporated totaled \$24,296,000 in the 2017 Period compared to \$34,557,000 in the 2016 Period. We recorded earnings per diluted common share of \$0.44 in the 2017 Period and \$0.64 in the 2016 Period. Excluding unusual matters, as detailed in the table below, diluted earnings per common share, as adjusted, were \$0.25 in the 2017 Period and \$0.28 in the 2016 Period. Per share amounts may not add due to rounding.

	June 25		39 Weeks Ended	
	2017	2016	June 26	2016
(Thousands of Dollars, Except Per Share Data)	Amount	Per Share	Amount	Per Share
Income attributable to Lee Enterprises, Incorporated, as reported	24,296	0.44	34,557	0.64
Adjustments:				
Warrants fair value adjustment	(10,418 )		404	
Gain on insurance settlement	—		(30,646 )	
	(10,418 )		(30,242 )	
Income tax effect of adjustments, net	—		10,726	
	(10,418 )	(0.19 )	(19,516 )	(0.36 )
Income attributable to Lee Enterprises, Incorporated, as adjusted	13,878	0.25	15,041	0.28

## LIQUIDITY AND CAPITAL RESOURCES

## Operating Activities

Cash provided by operating activities was \$59,433,000 in the 2017 Period and \$65,827,000 in the 2016 Period. We recorded net income of \$25,105,000 in the 2017 Period and \$35,358,000 in the 2016 Period. Non-cash debt financing costs charged to expense totaled \$3,463,000 in the 2017 Period compared to \$4,563,000 in the 2016 Period. Changes in depreciation and amortization, deferred income taxes, and operating assets and liabilities accounted for the bulk of the change in cash provided by operating activities in the 2017 Quarter.



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### Investing Activities

Cash required for investing activities totaled \$2,356,000 in the 2017 Period compared to cash provided by investing activities of \$29,611,000 in the 2016 Period. In the 2016 Period, we received \$30,646,000 related to an insurance settlement. Capital spending totaled \$3,232,000 in the 2017 Period compared to \$5,793,000 in the 2016 Period. We received \$1,830,000 and \$3,983,000 of proceeds from sales of assets in the 2017 Period and the 2016 Period, respectively.

We anticipate that funds necessary for capital expenditures, which are expected to total up to \$6,000,000 in 2017, and other requirements, will be available from internally generated funds or availability under our Revolving Facility.

### Financing Activities

Cash required for financing activities totaled \$49,089,000 in the 2017 Period and \$84,700,000 in the 2016 Period. Debt reduction accounted for the majority of the usage of funds in both the 2017 Period and the 2016 Period.

### Liquidity

At June 25, 2017, after consideration of letters of credit, we have approximately \$33,818,000 available for future use under our Revolving Facility. Including cash, our liquidity at June 25, 2017 totals \$58,790,000. This liquidity amount excludes any future cash flows. We expect all interest and principal payments due in the next twelve months will be satisfied by our cash flows, which will allow us to maintain an adequate level of liquidity. The Warrants, if and when exercised, would provide additional liquidity in an amount up to \$25,140,000.

The purchase of the Dispatch-Argus, in our fourth fiscal quarter for \$7,150,000 plus an adjustment for working capital, used a portion of the available liquidity as of June 25, 2017.

At June 25, 2017, the principal amount of our outstanding debt totals \$568,480,000. The June 25, 2017 principal amount of debt, net of cash, is 3.75 times our trailing 12 months adjusted EBITDA.

The 2014 Refinancing significantly extended our debt maturity profile with final maturity of the majority of our debt in 2022. As a result, refinancing risk has been substantially reduced for the next several years.

There are numerous potential consequences under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, if an event of default, as defined, occurs and is not remedied. Many of those consequences are beyond our control. The occurrence of one or more events of default would give rise to the right of the applicable lender(s) to exercise their remedies under the Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan, respectively, including, without limitation, the right to accelerate all outstanding debt and take actions authorized in such circumstances under applicable collateral security documents.

Our ability to operate as a going concern is dependent on our ability to remain in compliance with debt covenants and to refinance or amend our debt agreements as they become due, or earlier if available liquidity is consumed. The Notes, 1<sup>st</sup> Lien Credit Facility and 2<sup>nd</sup> Lien Term Loan have only limited affirmative covenants with which we are required to maintain compliance. We are in compliance with our debt covenants at June 25, 2017.

In February 2017 our filing of a replacement Form S-3 registration statement ("Shelf") with the SEC, was declared effective and expires February 2020. The Shelf registration gives us the flexibility to issue and publicly distribute various types of securities, including preferred stock, common stock, warrants, secured or unsecured debt securities, purchase contracts and units consisting of any combination of such securities, from time to time, in one or more

offerings, up to an aggregate amount of \$750,000,000. SEC issuer eligibility rules require us to have a public float of at least \$75,000,000 in order to use the Shelf. Subject to maintenance of the minimum level of equity market float and the conditions of our existing debt agreements, the Shelf may enable us to sell securities quickly and efficiently when market conditions are favorable or financing needs arise. Under our existing debt agreements, net proceeds from the sale of any securities may be used generally to reduce debt.

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### CHANGES IN LAWS AND REGULATIONS

#### Energy Costs

Energy costs can be volatile, and may increase in the future as a result of carbon emissions and other regulations being considered by the United States Environmental Protection Agency.

#### Health Care Costs

The Affordable Care Act was enacted into law in 2010.

We expect the requirements under the Affordable Care Act will continue to evolve. Our future health care costs are expected to increase based on analysis published by the United States Department of Health and Human Services, input from independent advisors and our understanding of the current provisions of the Affordable Care Act, such as:

- Certain preventive services provided without additional charge to employees;
- Automatic enrollment of new employees;
- Higher maximum age for dependent coverage;
- Elimination of lifetime benefit caps; and
- Free choice vouchers for certain lower income employees.

We do not expect the Affordable Care Act will have a significant impact on our postretirement medical benefit obligation liability.

#### Pension Plans

In 2012, the Surface Transportation Extension Act of 2012 ("STEА") was signed into law. STEА provides for changes in the determination of discount rates that result in a near-term reduction in minimum funding requirements for our defined benefit pension plans. STEА will also result in an increase in future premiums to be paid to the Pension Benefit Guarantee Corporation ("PBGC").

In 2014, the Highway and Transportation Funding Act ("HATFA") was signed into law. HATFA generally extends the relief offered under STEА and further increases premiums to be paid to the PBGC.

#### Income Taxes

Certain states in which we operate periodically consider changes to their corporate income tax rates. Until such changes are enacted, the impact of such changes cannot be determined.

#### Wage Laws

In 2016, the Department of Labor ("DOL") published its final rule updating overtime regulations and minimum pay regulations for exempt employees. Among other things, the final rule established a new minimum rate for all exempt employees of \$913 per week, which is more than double the previous limit. The final rule was scheduled to be effective beginning December 1, 2016. However, a federal district court issued a preliminary injunction on the rule becoming final. The DOL recently submitted a Request for Information on the overtime rule, which is the process used by the DOL to obtain public comment. Until a final court ruling is issued or there are any changes to the regulations, the Company cannot determine what impact this rule will have, if any.

The United States and various state and local governments are considering increasing their respective minimum wage rates. Most of our employees earn an amount in excess of the current United States or state minimum wage rates. However, until changes to such rates are enacted, the impact of the changes cannot be determined.

#### INFLATION

Price increases (or decreases) for our products or services are implemented when deemed appropriate by us. We continuously evaluate price increases, productivity improvements, sourcing efficiencies and other cost reductions to mitigate the impact of inflation.

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### Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk stemming from changes in interest rates and commodity prices. Changes in these factors could cause fluctuations in earnings and cash flows. In the normal course of business, exposure to certain of these market risks is managed as described below.

#### INTEREST RATES ON DEBT

Our debt structure, which is predominantly fixed rate, significantly reduces the potential impact of an increase in interest rates. At June 25, 2017, 10.4% of the principal amount of our debt is subject to floating interest rates. Our primary exposure is to LIBOR. A 100 basis point increase to LIBOR would, if in excess of LIBOR minimums discussed more fully below, decrease income before income taxes on an annualized basis by approximately \$589,840 based on \$58,984,000 of floating rate debt outstanding at June 25, 2017.

Our debt under the 1<sup>st</sup> Lien Term Loan is subject to minimum interest rate levels of 1.0%. Based on interest rates in June 2017, LIBOR rates are in excess of the minimum rate.

We regularly evaluate alternatives to hedge our interest rate risk, but have no hedging instruments in place.

#### COMMODITIES

Annualized newsprint capacity reductions in North America since the beginning of 2017 and scheduled newsprint reductions in Asia and West Europe tonnes may not be sufficient to reduce the current downward pricing pressure on newsprint.

Price change announcements are influenced primarily by the balance between supply capacity and demand, domestic and export, and the producer's ability to mitigate input cost pressures taking the U. S. dollar to Canadian dollar exchange rate into consideration. The extent to which future price changes occur is subject to negotiations with each newsprint producer at the time newsprint is ordered. Average cost per metric ton was approximately 9% higher during the third fiscal quarter 2017 compared to the same quarter a year ago because of price increases in the first 3 quarters of calendar year 2016. We expect to cycle these price increases in our fiscal 4th quarter.

Our long term supply strategy takes potential capacity closures into consideration and aligns the Company with suppliers most likely to continue to supply the North American newsprint market and our print locations.

A \$10 per tonne price increase for 30 pound newsprint would result in an annualized reduction in income before income taxes of approximately \$483,000, based on anticipated consumption in 2017, excluding consumption of TNI and MNI and the impact of LIFO accounting. Such prices may also decrease. We manage significant newsprint inventories, which will temporarily mitigate the impact of future price increases.

#### SENSITIVITY TO CHANGES IN VALUE

At June 25, 2017, the fair value of floating rate debt, which consists primarily of our 1<sup>st</sup> Lien Term Loan, is \$58,836,000, based on an average of private market price quotations. Our fixed rate debt consists of \$385,000,000 principal amount of the Notes and \$124,496,000 principal amount under the 2<sup>nd</sup> Lien Term Loan. At June 25, 2017, based on an average of private market price quotations, the fair values were \$393,662,000 and \$129,164,000 for the Notes and 2<sup>nd</sup> Lien Term Loan, respectively.





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Item 4. Controls and Procedures

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Under the supervision and with the participation of our senior management, including our chief executive officer and chief financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the period covered by this Quarterly Report on Form 10-Q (the "Evaluation Date"). Based on this evaluation, our chief executive officer and chief financial officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective such that the information relating to the Company, including our consolidated subsidiaries, required to be disclosed in our SEC reports (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes in our internal control over financial reporting that occurred during the 13 weeks ended June 25, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II  
OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in a variety of legal actions that arise in the normal course of business. Insurance coverage mitigates potential loss for certain of these matters. While we are unable to predict the ultimate outcome of these legal actions, it is our opinion that the disposition of these matters will not have a material adverse effect on our Consolidated Financial Statements, taken as a whole.

Item 6. Exhibits  
Number Description

- 31.1 Rule 13a-14(a)/15d-14(a) certification
- 31.2 Rule 13a-14(a)/15d-14(a) certification
- 32 Section 1350 certification

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LEE ENTERPRISES, INCORPORATED

/s/ Ronald A. Mayo  
Ronald A. Mayo  
Vice President, Chief Financial Officer and Treasurer

August 4, 2017

(Principal Financial and Accounting Officer)

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