

Methodology

*Rating the Newspaper and Magazine
Publishing Industry*

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Insight beyond the rating.

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Rating the Newspaper and Magazine Publishing Industry

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Introduction to DBRS Methodologies

- In general terms, DBRS ratings are opinions that reflect the creditworthiness of an issuer, a security or an obligation. They are opinions based on an analysis of historic trends and forward-looking measurements that assess an issuer's ability and willingness to make timely payments on outstanding obligations (whether principal, interest, dividend or distributions) with respect to the terms of an obligation.
- DBRS rating methodologies include consideration of general business and financial risk factors applicable to most industries in the corporate sector as well as industry-specific issues and more subjective factors, nuances and intangible considerations. Our approach is not based solely on statistical analysis but includes a combination of both quantitative and qualitative considerations.
- The considerations outlined in DBRS methodologies are not intended to be exhaustive. In certain cases, a major strength can compensate for a weakness and, conversely, there are cases where one weakness is so critical that it overrides the fact that the company may be strong in most other areas.
- To some extent, the business risk and financial risk profiles are interrelated. The financial risk for a company must be considered along with the business risks that it faces. In most cases, an entity's business risk will carry more weight in the final issuer rating than will its financial risk.

DBRS METHODOLOGY: A THREE-STAGE PROCESS

- (1) Calculate the business risk rating (BRR), looking at the strengths and challenges of the industry.
- (2) Rate the company on a straight issuer rating, without any reference to any security that may be rated. The company rating is a function of its own business risk and financial risk.
- (3) The third step is to rate the security, considering the level of collateral, ranking of the debt relative to other issues and recovery rates in liquidation in terms of non-investment-grade securities.

(1) *Business Risk Rating (BRR)*

- The industry business risk looks at these five factors:
 - Profitability and cash flow characteristics of the industry.
 - The competitive landscape.
 - Stability of the industry.
 - Regulation.
 - Any other inherent industry risks.
- Although there is an overlap in some instances (to some degree, in the long term, all five factors tend to relate to profitability and stability), DBRS has found that considering these five measures in a separate fashion is a useful way of approaching this analysis.
- Using the same factors across different industries provides a common base with which to compare the business risks of various industries, even when they are distinctly different. In all cases, DBRS uses historic performance and our experience to determine an opinion on the future, which is the primary focus. For additional discussion on industry BRRs, please refer to the Industry Business Risk Ratings and Industry Business Risk Rating Definitions sections in the appendix.

(2) *Company-Specific Factors*

- Is the company stronger, equal to or weaker than the industry and the business risk rating of the industry?
- The Company-Specific Business Risk Factors section examines specific business risks of the company versus the strengths of the company.
- Stage 2: The Financial Risk Profile section looks at the key financial ratios, which include the following:
 - Percentage of debt in the capital structure.
 - EBIT interest coverage.
 - Cash flow-to-debt.
 - Debt-to-EBITDA.
 - EBITDA-to-interest.
 - Current ratio.



- The company business risk combined with financial risk equals the issuer rating. The issuer rating is usually defined as the highest rating for unsecured debt issued by the company.

(3) Rating of the Security

- Stage 3 of the process is the rating of the security, which looks at the level of collateral ranking relative to other debt and the recovery in liquidation. The ranking can be notched one, two or more rating categories to recognize where the debt ranks in liquidation.
- It is important to note that the ratings for company-specific business and financial risks as provided under Stage 2 of this document should not be taken as final issuer ratings. For example, an individual company may fit into the “A” range with respect to the analysis of its business risk, but its financial metrics could be more in the BB category. It would be incorrect to believe that the final issuer rating in this case would be either “A” or BB. In determining the final issuer rating, both of these two major areas must be considered. For additional discussion on this topic, please refer to the Interrelationship between Business and Financial Risk section in the appendix.

Three Stages of DBRS Rating Analysis

Stage 1: Industry Business Risk Rating

Consider the overall business risk rating (BRR) for the industry.

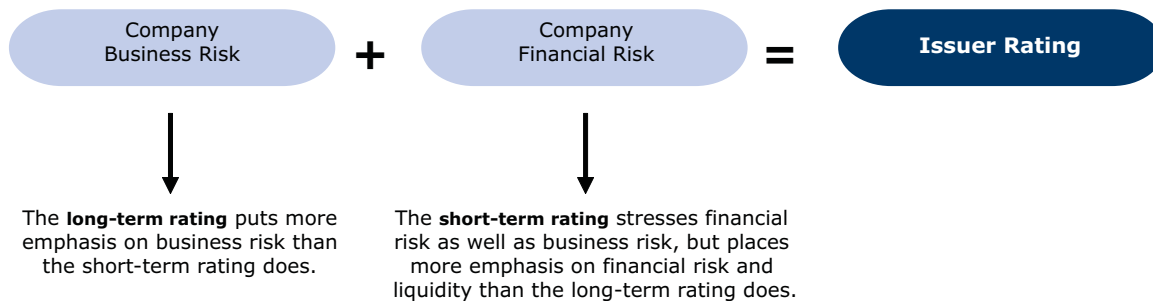


Stage 2: Issuer Rating

Consider the strength of the individual issuer:

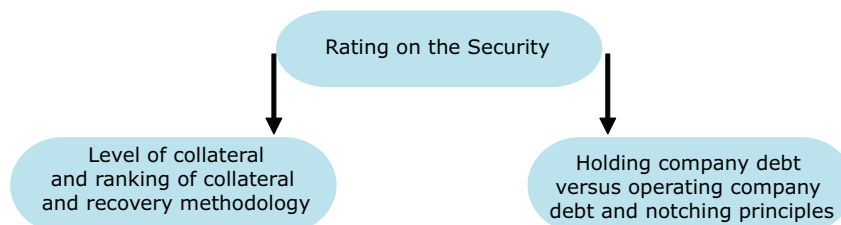
- (a) First assessing how the company’s BRR compares with the industry BRR.
- (b) Then assessing the company’s financial risk.

Taken together, these factors will determine the company’s issuer rating.



Stage 3: Rating the Security

Consider covenant and ranking issues that exist for specific securities, using the issuer rating to determine specific security ratings.



Stage 1: Industry Business Risk Rating for the Newspaper and Magazine Publishing Industry

DEFINITION OF THE INDUSTRY

- The newspaper and magazine publishing industry is defined to include all newspaper and magazine publishers. (Information and book publishers are also included in this methodology; see below for an explanation of additional factors that can affect ratings in these sectors.) Generally, newspapers allow for the publication of information on a broad range of topics, including providing a permanent copy of these topics which can be retained. Magazines tend to be more focused on both a particular topic and a potential demographic audience.
- Community newspapers and urban commuter dailies that are both distributed for free and reliant solely on advertising are also included. Magazines included cover the full spectrum of print periodicals, which are often specialized in focus.
- Web services offered on a subscription basis by media companies are also included in our analysis.

THE BUSINESS RISK RATING

- The business risk rating for the newspaper and magazine publication industry is BB (high), which is non-investment-grade and recognizes that this is a challenging industry that is undergoing a high degree of structural change as a result of a number of factors and trends. These include: (1) The business is being affected by competition from the Internet and other forms of media, which is driving advertising dollars away from print media and resulting in a decline in subscriptions. (2) Newspapers have historically relied on classified ads for a large portion of their advertising revenue. With the Internet taking this lucrative source of revenue away, newspapers have been forced to pursue more retail advertising, which can be more cyclical. (3) Magazines have a larger proportion of circulation revenue but this can be more discretionary than for newspapers. (4) Advertising revenue and magazine circulation are very sensitive to the state of the economy. (5) The industry is distribution intensive, which involves both high labour and energy costs. (6) The entire value chain is labour intensive, with relatively strong unions in the editorial and printing areas. (7) Paper used in printing is costly and energy intensive, as well as environment sensitive.
- Most major markets have only one or two direct newspaper competitors, and the industry has worked diligently on containing costs. In order to pursue new growth areas to stem subscriber pressure, newspaper companies have pursued online initiatives and in some cases launched free commuter papers to keep a broad audience.
- Other newspapers such as community papers have remained relevant, given their 100% coverage of a region and frequent distribution (weekly or more frequently). Retail advertising flyers continue to covet this direct household coverage.
- Magazines are highly competitive on both a regional and national basis. They are also increasingly pursuing online initiatives to capture incremental online revenue.
- Web, mobile and tablet platform-based distribution has not been extensive to date but is growing as publishers look at ways to capture both subscription and advertising from these innovative new platforms.

INDUSTRY PROFITABILITY AND CASH FLOW

- The profitability and cash flow of newspaper/magazine publishing is weak, as fixed costs tend to be high and difficult to adjust to both economic cycles and structural trends. However, with relatively modern equipment in place, capex levels are generally low. Some publishers outsource the printing function.
- The audience for newspapers is becoming older and, as this generation ages, the younger generation is turning to other platforms such as the Internet and, increasingly, mobile phones and tablets. Free dailies have been launched in an attempt to counter this but require start-up costs – to build a publication and readership base – and are solely reliant on advertising revenue. Magazine subscribers and readers cover specific demographic groups and this business is less affected by the ageing audience trend. However, the trend to new platforms does affect this segment.

- Newspaper/magazine publishing is both labour intensive (with strong unions) and somewhat capital intensive, given the high cost of printing presses and facilities.
- Distribution costs are very high, and both energy and labour intensive.
- Newsprint/magazine paper is also very energy intensive – and expensive – but very necessary in producing the final product.
- Advertising is very sensitive to the economy, and accounts for up to 80% of a newspaper's revenue (for magazines it accounts for roughly 50%).
- Newspaper classified ads for employment, retailing (food and merchandising) and auto advertising are all in decline.
- Subscriptions, which historically contribute 20% to 30% of a newspaper's revenue, with magazines above the 30% level, are difficult to grow in light of declining circulation.
- The outlook for profitability is for continued erosion of circulation and pressure on advertising, which means that cost-containment remains critical to achieve reasonable profitability.
- Magazines tend to be more national in advertising (although attempts are being made to provide regional issues of certain magazines) than newspapers. As a result, magazine revenue can be even more volatile than newspaper revenue.
- Community newspapers that offer free subscriptions but benefit from advertising are in some cases outperforming newspaper entities based on subscription models.
- Companies have had limited success in being able to charge for web subscriptions. Possible exceptions include dailies such as *The Wall Street Journal*.

INDUSTRY COMPETITIVE LANDSCAPE

- Competition is high for this industry, given the proliferation of media as well as the number of competing publications.
- Stiff competition has come from other forms of media, particularly the Internet, which is taking more than its share of advertising revenue growth.
- Newspaper versus newspaper competition is less severe than competition from other media sources.
- Few newspaper markets have more than two newspaper competitors.
- Newspapers tend to be more local and/or regional than national in nature, with some exceptions (for example, in the United States, *The Wall Street Journal*, *The New York Times* and *The Washington Post*).

INDUSTRY STABILITY

- Stability of revenue and EBITDA is low due to the cyclical and structural declining nature of advertising revenue.
- Advertising revenue for large urban dailies tends to be more local and regional (versus national), which adds some stability to revenue.
- Community newspapers serving local markets are generally more stable than subscription-oriented papers.
- Magazines, while deriving a lesser proportion of revenue from advertising, are dependent on the economy for advertising which can be more national. Magazines are also vulnerable to the buying patterns of consumers and businesses, given their more discretionary nature.
- Overall, revenue for newspaper and magazine publishers is very sensitive to the economy.

INDUSTRY REGULATION

- Regulation is not significant in the publishing business relative to other types of media such as television and radio. However, there can be general restrictions on concentration of publications within a market, cross-media ownership, and ensuring the diversity of sources (in an effort to promote pluralism).
- Regulation in newspapers and magazines tends to focus on self-discipline within the industry based on professionalism and fairness.
- Lawsuits can be initiated in response to aggressive coverage on issues and serve as a form of additional discipline for the industry.
- Tabloids tend to be more vulnerable with respect to legal actions.



OTHER INHERENT INDUSTRY CONSIDERATIONS

- While most newspapers and magazines have created online versions of their publications, to date most have not been successful in capturing enough revenue to in make up for the loss of advertising and circulation revenue.
- Some exceptions include well-entrenched financial dailies such as *The Wall Street Journal* and *The Financial Times*. Other publications have created their business from an online perspective and do not produce a printed version (*The Huffington Post* and News Corp's *The Daily* are good examples).
- To date, the subscription model for online and digital platforms continues to be developed with some of the most popular mobile and tablet device and software makers developing platforms that can make subscribing to digital content more straightforward for consumers.

BOOK PUBLISHERS

DBRS also rates book publishers; this includes publishers of books that cover major categories such as fiction, non-fiction, educational and trade books. The following factors are considered:

- Portfolio of authors and publications and their level of success in creating demand for their publications.
- Degree of competition from other publishers and other forms of media.
- Scale economies and the ability to leverage this in terms of production and distribution.
- Ability to adapt to increasing digitization of books and educational material.
- Susceptibility to economic cycles.

INFORMATION PUBLISHERS

DBRS rates information publishers; this includes providers of directories (print and online) and electronic information. The following factors are considered:

- Service portfolio and customer base.
- Position in markets serviced.
- Proportion of subscription- versus advertising-driven revenue in revenue mix.
- Degree of success in migrating from legacy print businesses to online/digital services.
- Scale economies.

While information publishers share many attributes and challenges with publishers of newspapers and magazines, DBRS notes that, in many cases, they are stronger in terms of profitability, competition and stability and individual DBRS ratings on such entities would reflect this.

Stage 2: Issuer Rating

To move from the generic industry BRR toward the issuer rating for a specific company, two tasks must be performed. Specifically, we must determine the business risk and the financial risk for the individual company.

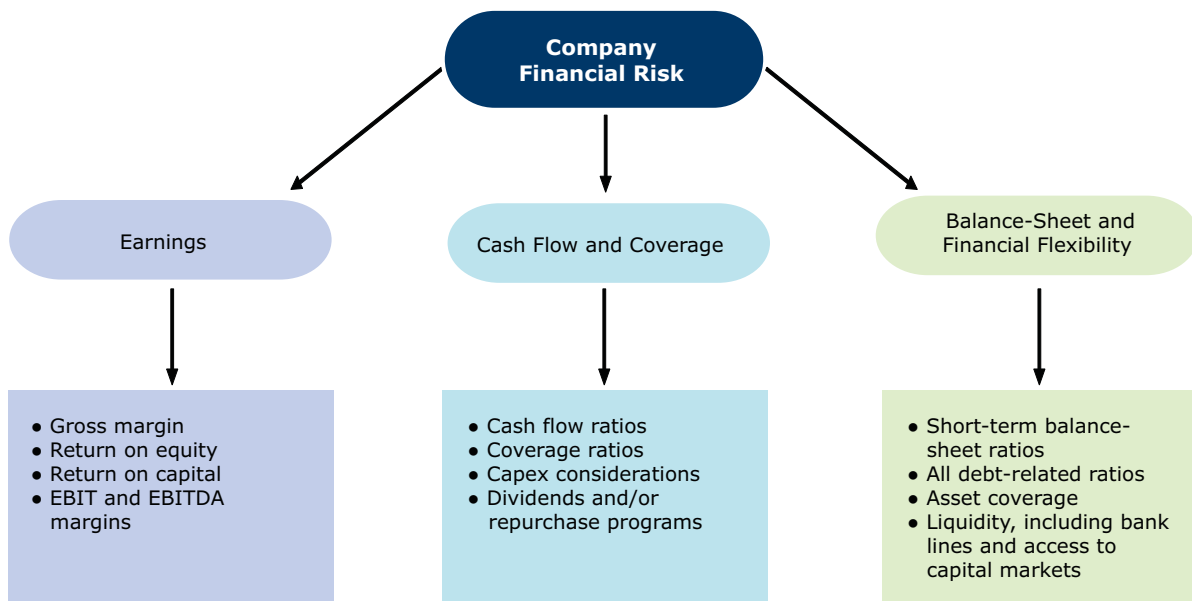
BUSINESS RISK PROFILE

- The business risk profile of the issuer may be better or worse than the industry average due to the presence of unique attributes or challenges that exist at the issuing entity. While not exhaustive, the list of critical factors outlined in the previous section could result in a specific issuer rating being different from the industry BRR.
- This methodology also provides some guidance on which factors are considered the most critical for the industry in question. Issuers may also have meaningful business lines in addition to the base business that extend beyond their most prominent industry, which could add significant attributes or challenges.

FINANCIAL RISK PROFILE

- The graphic below is a visual display of the key financial risk profile considerations that are discussed in the Company-Specific Financial Risk Factors section of this methodology, although even the detail provided there is not meant to be exhaustive.
- The discussion will note that DBRS often makes calculation adjustments in key ratios for risks related to a variety of areas. In some cases, a relationship with a parent or associated company will also be important.

Key Financial Risk Metrics





Company-Specific Business Risk Factors

- We now consider if an individual company in the newspaper and magazine publishing industry would be better, worse or the same as the industry BRR. Our focus here is on the critical business risk factors that relate to this industry in particular. The five critical factors used to determine the industry BRR are applied by DBRS to compare numerous industries and are thus more general in nature.
- By analyzing these key drivers (which will vary on an industry-by-industry basis), the essential strengths and challenges of each industry are captured in an accurate fashion, and transparency is provided. The analysis below is connected to the industry BRR in that the industry BRR establishes where an average company would be considered to score on the matrix. For example, an industry with a BRR of BBB would mean that the following matrix describes the scoring of an average company within the BBB column.

Company-Specific Business Risks – Critical Factors

| Rating Business Strength | A Superior | BBB Adequate | BB Weak | B Poor |
|--|--|---|--|---|
| Markets Served | • Serves lucrative and growing markets. | • Serves stable markets. | • Serves stable to weak markets. | • Serves markets with below-average growth. |
| Scale Economies | • Larger size enables efficiencies over various markets. | • Medium size allows some efficiencies over several markets. | • Medium to small size allows limited efficiencies in limited markets. | • Small size in concentrated markets limits efficiencies. |
| Cost-Containment | • Excellent in controlling labour, distribution and paper costs. | • Reasonable in containing major costs. | • Average in containing major costs. | • Weak in containing overall costs. |
| Subscription Trends | • Able to continue to grow subscriptions. | • Able to keep subscriptions stable. | • Moderate declines in subscriptions. | • High declines in subscriptions. |
| Audience Fragmentation | • Able to overcome market segmentation with creative marketing. | • Able to hold stable with some success in overcoming segmentation. | • Slowly losing audience as market segments. | • Continuing decline in advertising revenue as market segments. |
| Paper Intensity Energy Intensity Capital Intensity Labour Intensity | • High. | • High. | • High. | • High. |

COMMON BUSINESS CONSIDERATIONS

- There are two major considerations that were not included with the prior analysis but can have a meaningful impact on an individual company in any industry: country risk and corporate governance (which includes management). These areas tend to be regarded more as potential negative issues that could result in a lower rating than otherwise would be the case, although DBRS would certainly consider exceptional strength in corporate governance as a rating attribute.
- In most cases, our focus on the two areas is to ensure that the company in question does not have any meaningful challenges that are not readily identifiable when reviewing the other business risk considerations and financial metrics outlined in this methodology.

Country Risk

- Governments often intervene in their economies and occasionally make substantial changes that can significantly affect a company's ability to meet its financial obligations; therefore, considerations include the company's main location or country of operation, the extent of government intervention and support and the degree of economic and political stability.
- As such, the sovereign rating itself may in some cases become a limiting factor in an entity's rating, particularly when the sovereign has a lower rating and the entity does not have meaningful diversification outside its domestic economy.

Corporate Governance

- Effective corporate governance requires a healthy tension between management, the board of directors and the public. There is no single approach that will be optimal for all companies.
- A good board will have a profound impact on a company, particularly when there are significant changes, challenges or major decisions facing the company. DBRS will typically assess factors such as the appropriateness of board composition and structure, opportunities for management self-interest, the extent of financial and non-financial disclosure and the strength or weakness of control functions. For more detail on this subject, please refer to the DBRS criteria *Evaluating Corporate Governance*.
- With respect to the pivotal area of management, an objective profile can be obtained by assessing the following: the appropriateness of core strategies; the rigour of key policies, processes and practices; management's reaction to problem situations; the integrity of company business and regulatory dealings; the entity's appetite for growth, either organically by adding new segments or through acquisition; its ability to smoothly integrate acquisitions without business disruption; and its track record in achieving financial results. Retention strategies and succession planning for senior roles can also be considerations.

Company-Specific Financial Risk Factors

KEY METRICS

- Recognizing that any analysis of financial metrics may be prone to misplaced precision, we have limited our key metrics to a small universe of critical ratios. For each of these ratios, DBRS provides a range within which the issuer's financial strength would be considered as supportive for the same level of business risk as the newspaper and magazine publishing industry. For example, a company where the outlook for both business risk and financial risk metrics falls within the BBB category would, all else being equal, be expected to have an issuer rating in the BBB range.
- To be clear, the ratings in the matrix below should not be understood as the final rating for an entity with matching metrics. This would only be the case to the extent that the business risk of the company and a wide range of other financial metrics were also supportive. The final rating is a blend of both the business risk and financial risk considerations in their entirety.

Newspaper and Magazine Publishing Industry Financial Metrics

| Key Ratio | A | BBB | BB | B |
|---------------------------------|------------|-----------|-----------|------------|
| % Debt in the capital structure | Under 30% | 30%-45% | 45%-60% | Over 60% |
| EBIT coverage | Over 5.0x | 3.0x-5.0x | 1.5x-3.0x | Under 1.5x |
| Cash flow-to-debt | Over 30% | 20%-30% | 10%-20% | Under 10% |
| EBITDA-to-interest | Over 7.0x | 4.0x-7.0x | 2.0x-4.0x | Under 2.0x |
| Debt-to-EBITDA | Under 2.0x | 2.0x-3.5x | 3.5x-5.0x | Over 5.0x |
| Return on equity | Over 9% | 7%-9% | 5%-7% | Under 5.0% |

- Many factors are involved in the rating beyond the quantitative numbers shown above, so these numbers should not be construed as an indication of the final rating.
- The industry's capital intensity relates to the high capital costs of printing presses and facilities.
- The need for large accumulation of debt is sporadic. Otherwise, capital is needed to finance accounts receivable and inventory, net of payables.
- With the cyclical nature of the industry, the above ratios can fluctuate somewhat in any one year.
- While the data in the above table are recognized as key factors, they should not be expected to be fully adequate to provide a final financial risk rating for any company. The nature of credit analysis is such that it must incorporate a broad range of financial considerations, and this cannot be limited to a finite number of metrics, regardless of how critical these may be.
- DBRS ratings are based heavily on future performance expectations, so while past metrics are important, any final rating will incorporate DBRS's opinion on future metrics, a subjective but critical consideration.
- It is also not uncommon for a company's key ratios to move in and out of the ranges noted in the ratio matrix above, particularly for cyclical industries. In the application of this matrix, however, DBRS is typically focusing on multi-year ratio averages.
- Notwithstanding these potential limitations, the key ratios are very useful in providing a good starting point in assessing a company's financial risk.
- It is important to note that actual financial ratios for an entity can and will be influenced by both accounting and accounting choices. In Canada, this will include the shift to International Financial Reporting Standards (IFRS). DBRS acknowledges that IFRS and other accounting choices will have an impact on the financial metrics of the companies that it covers. The financial risk factors include ratios based on data from company financial statements that are based on Canadian Generally Accepted Accounting Principles (GAAP) and U.S. GAAP, for the most part. When company financial statements are based on GAAP in other countries, including IFRS, the ratios and ranges may need to be redefined.



- Recognizing that the metrics in the table above do not represent the entire universe of considerations that DBRS examines when evaluating the financial risk profile of a company, the following provides a general overview that encompasses a broader range of metrics and considerations that could be meaningful in some cases.

Overall Considerations in Evaluating a Company's Financial Risk Profile

In addition to the information already provided with respect to key financial metrics, the following financial considerations and ratios are typically part of the analysis for the newspaper and magazine publishing industry. As it is not possible to completely separate business and financial risks, note that many of the following ratios will relate to both areas.

EARNINGS

- DBRS earnings analysis focuses on core earnings or earnings before non-recurring items and in doing so considers issues such as the sources, mix and quality of revenue; the volatility or stability of revenue; the underlying cost base (e.g., the company is a low-cost producer); optimal product pricing; and potential growth opportunities. Accordingly, earnings as presented in the financial statements are often adjusted for non-recurring items or items not considered part of ongoing operations.
- DBRS generally reviews company budgets and forecasts for future periods. Segmented breakdowns by division are also typically part of DBRS analysis. Notwithstanding the focus on core earnings, note that actual net earnings is also a consideration in our analysis given the direct impact that this has on the capital structure.

Typical Earnings Ratios

- EBITDA interest coverage.
- EBIT interest coverage.
- EBITDA margins.
- Fixed charges coverage.
- Return on capital.

CASH FLOW AND COVERAGE

- DBRS cash flow analysis focuses on the core ability of the company to generate cash flow to service current debt obligations and other cash requirements as well as on the future direction of cash flow. From a credit analysis perspective, insufficient cash sources can create financial flexibility problems, even though net income metrics may be favourable.
- DBRS evaluates the sustainability and quality of a company's core cash flow by focusing on cash flow from operations and free cash flow before and after working capital changes. Using core or normalized earnings as a base, DBRS adjusts cash flow from operations for as many non-recurring items as relevant. As with earnings, the impact that non-core factors have on cash flow may also be an important reality.
- In terms of outlook, DBRS focuses on the projected direction of free cash flow, the liquidity and coverage ratios and the company's ability to internally versus externally fund debt reduction, future capital expenditures and dividend and/or stock repurchase programs, as applicable.

Typical Cash Flow Ratios

- Cash flow-to-debt.
- Capex-to-revenue.



BALANCE-SHEET AND FINANCIAL FLEXIBILITY CONSIDERATIONS

- As part of determining the overall financial risk profile, DBRS evaluates various other factors to measure the strength and quality of the company's assets and its financial flexibility. From a balance-sheet perspective, DBRS focuses on the quality and composition of assets, including goodwill and other intangibles; off-balance-sheet risk; and capital considerations such as the quality of capital, appropriateness of leverage to asset quality and the ability to raise new capital.
- DBRS also reviews the company's strategies for growth, including capital expenditures and plans for maintenance or expansion, and the expected source of funding for these requirements, including bank lines and related covenants. Where the numbers are considered significant and the adjustments would meaningfully affect the credit analysis, DBRS adjusts certain ratios for items such as operating leases, derivatives, securitizations, hybrid issues, off-balance-sheet liabilities and various other accounting issues.

Typical Balance-Sheet Ratios

- Percentage of debt in the capital structure.
- Gross debt-to-EBITDA.
- Net debt-to-EBITDA.

Stage 3: Rating the Security

With respect to Stage 3, the following comments describe how the issuer rating is used to determine ratings on individual securities:

- DBRS uses a hierarchy in rating long-term debt that affects issuers that have classes of debt that do not rank equally. In most cases, lower-ranking classes would receive a lower DBRS rating. For more detail on this subject, please refer to DBRS rating policy entitled "[Underlying Principles](#)."
- In some cases, issued debt is secured by collateral. This is more typical in the non-investment-grade spectrum. For more detail on this subject, please refer to [DBRS Rating Methodology for Leveraged Finance](#).
- The existence of holding companies can have a meaningful impact on individual security ratings. For more detail on this subject, please refer to the criteria [Rating Parent/Holding Companies and Their Subsidiaries](#).

Appendix

INDUSTRY BUSINESS RISK RATINGS

- DBRS uses the concept of business risk ratings (BRRs) as a tool in assessing the business strength of both industries and individual companies within many methodologies across the corporate finance area. (DBRS does not typically use this approach for most financial, government and public finance sectors, where the industry is more challenging to define and this approach is not as useful.)
- The BRR is assessed independently of financial risk, although in some cases there are subtle but important links. As an example, the very low business risk profile of many regulated utilities has historically allowed this sector to operate with debt levels that would not be acceptable for most other industry sectors. Given this reality, it is difficult to consider the utility industry's BRR without acknowledging to some degree that the industry operates with sizable debt levels. This type of relationship exists with many industries, although typically to a much lesser degree.
- When a BRR is applied to an industry, there is an acknowledgment that this is a general assessment and there may in fact be a wide disbursement in the business strength of individual entities within the industry. Nonetheless, this assessment is beneficial to enabling DBRS to clearly delineate our industry opinion and is a useful tool when comparing different industries. An industry BRR is defined as being representative of those entities that the market would consider as "established," meaning that the group of companies being considered would have at least reasonable critical mass and track records. As such, the BRR for an industry does not consider very small players, start-up operations or entities that have unusual strengths or weaknesses relative to the base industry.
- DBRS methodologies note whether they apply to global industries or more specific countries or regions. When analyzing individual credits, DBRS considers the degree to which regional considerations may differ from the geographic area applicable within the industry methodology. Many entities have business units that transcend industries and in these cases, more than one BRR would be considered, including the possible benefits or challenges that may exist when all businesses are analyzed as part of a combined group.
- The BRR is a tool that provides additional clarity regarding the business risk of the industry overall, but it should be viewed as just one aspect in the complex analysis of setting ratings and should by no means be seen as either a floor or ceiling for issuers within a given industry. Although DBRS does not anticipate volatility in an industry's BRR, changes are possible over time if there are meaningful structural developments in the industry. When such a change does occur, DBRS will make this clear and note any impact on related individual ratings within the industry as applicable.
- DBRS assesses five areas to establish the overall BRR for an industry. Although there is an overlap in some instances (to some degree, in the long term, all five factors tend to relate to profitability and stability), DBRS has found that considering these five measures in a separate fashion is a useful way of approaching its analysis. In all cases, DBRS uses historic performance and our experience to determine an opinion on the future, which is the primary focus.

Industry Profitability and Cash Flow

- When ratios such as return on equity, return on capital and a variety of cash flow metrics are considered, some industries are simply more profitable than others. While standard economics would suggest a reversion to the mean through new competitors, this often occurs at a very slow pace over a long time horizon and in some cases may not occur at all because of barriers to entry.
- The benefits from above-average profits and/or cash flow are substantial and include internal capital growth, easier access to external capital and an additional buffer to unexpected adversity from both liquidity and capital perspectives.
- Some industries and their participants have challenges or strengths in areas such as research and development (R&D), brand recognition, marketing, distribution, cost levels and a potentially wide variety of other tangibles and intangibles that affect their ability in the area of profitability.

Industry Competitive Landscape

- The competitive landscape provides information regarding future profitability for the industry and thus somewhat crosses over into the profitability and cash flow assessment, but competition is deemed worthy of separate consideration because of its critical nature.
- Participants in industries that lack discipline, produce commodity-like products or services, have low barriers to entry and exhibit ongoing pricing war strategies generally have difficulty attaining high profitability levels in the longer term. Certain industries benefit from a monopoly or oligopoly situation, which may relate to regulation.

Industry Stability

- This factor relates primarily to the degree of stability in cash flow and earnings, measuring the degree to which the industry and its participants are affected by economic or industry cycles. Stability is considered critical as industries with high peaks and troughs have to deal with higher risk at the bottom of a cycle. As such, to some degree, industries with lower but stable profitability are considered more highly than industries with higher average profitability that is more cyclical.
- Some of the key factors in considering stability include the nature of the cost structure (fixed or variable), diversification that provides counter-cyclical and the degree to which the industry interrelates with the overall economy. Depending on the industry, economic factors could include inflation or deflation, supply and demand, interest rates, currency swings and future demographics.

Industry Regulation

- Where applicable, regulation can provide support through stability and a barrier to entry, but it can also cause challenges and change the risk profile of an industry and its participants in a negative way, including the reality of additional costs and complications in enacting new strategies or other changes.
- As part of its analysis of regulation, DBRS also considers the likelihood of deregulation for a regulated industry, noting the many examples where this transition has proven to be a major challenge in the past.

Other Inherent Industry Considerations

- Each industry has its own set of unique potential risks that, even if managed well, cannot be totally eliminated. Specific risks, the ability to manage them and the range of potential outcomes vary industry by industry. Two of the most common risks are changing technology and operational risks.
- Some of the other more common risks are in the areas of legal, product tampering, weather, natural disasters, labour relations, currency, energy prices, emerging markets and pensions.



INDUSTRY BUSINESS RISK RATING DEFINITIONS

DBRS specifies the BRR for an industry in terms of our **Long-Term Obligations** rating scale. When discussing industry BRRs for an industry, DBRS typically provides either one specific rating or a limited range (such as BBB (high)/BBB). Using a range recognizes the fact that, by their nature, industry BRRs are less precise than a specific corporate or security rating as they represent an overall industry. In addition to relating to the industry level, these definitions also apply to the business risk of individual companies, which will fall more often in the very high and low categories (AA/AAA and B) than would be the case for an entire industry.

Industry Business Risk Ratings (BRRs)

| Rating | Business Strength | Comment |
|--------|-------------------|--|
| AA/AAA | Exceptional | An industry BRR of AA/AAA is considered unusually strong, with no meaningful weakness in any individual area. It may include pure monopolies that are deemed essential (the primary case being regulated utilities, where the risk of deregulation is believed to be very low). Common attributes include product differentiation, high barriers to entry and meaningful cost advantages over other industries or entities. These and other strengths provide exceptional stability and high profitability. It would be quite rare for an industry to have a BRR in this category. |
| A | Superior | Industry BRRs at the "A" level are considered well above average in terms of stability and profitability and typically have some barriers to entry related to capital, technology or scale. Industries that have, by their nature, inherent challenges in terms of cyclicity, a high degree of competition and technology risks would be unlikely to attain this rating category. |
| BBB | Adequate | Industry BRRs at the BBB level include many cyclical industries where other positive considerations are somewhat offset by challenges related to areas such as commodity products, labour issues, low barriers to entry, high fixed costs and exposure to energy costs. This rating category is considered average and many industries fall within it, with key considerations such as overall profitability and stability typically considered as neither above or below average. |
| BB | Weak | An industry at the BB level has some meaningful challenges. In addition to high cyclicity, challenges could include the existence of high technology or other risks. Long-standing industries that may have lost their key strengths through factors such as new competition, obsolescence or the inability to meet changing purchaser demands may fit here. The culmination of such factors results in an industry that does not generally score well in terms of stability and profitability. For an entire industry, this is typically the lowest BRR level. |
| B | Poor | While not common, there are cases where an industry can have a BRR of B. Such industries would typically be characterized by below-average strength in all or virtually all major areas. |



INTERRELATIONSHIP BETWEEN FINANCIAL AND BUSINESS RISK

Having in mind the prior discussion on the typical importance that DBRS places on certain financial metrics and business strengths for the newspaper and magazine publishing industry, we provide some guiding principles pertaining to the application of DBRS methodologies, the first one being that, in most cases, an entity's business risk will carry more weight in the final rating than its financial risk.

Based on this underlying concept, we provide the additional guidance for individual companies with varying business risks:

- **For an Entity with a Business Risk of AA (Exceptional):** A company with a business risk of AA will almost always be able to obtain an investment-grade issuer rating. When financial metrics are in the BBB range, an entity with a business risk of AA would typically be able to attain an "A"-range issuer rating.
- **For an Entity with a Business Risk of "A" (Superior):** Unless financial strength fails to exceed the B range, superior business strength will typically allow the final issuer rating to be investment grade. Very conservative financial risk may in some cases allow the final issuer rating to be within the AA range, but this should not be considered the norm.
- **For an Entity with a Business Risk of BBB (Adequate):** At this average level of business risk, the level of financial risk typically has the ability to result in a final issuer rating from as high as "A" to as low as B.
- **For an Entity with a Business Risk of BB (Weak):** At this weak level of business risk, conservative financial risk can, in some cases, take the final issuer rating into the BBB investment-grade range.
- **For an Entity with a Business Risk of B (Poor):** It is not typically possible for a company with a business risk of B to achieve a final investment-grade issuer rating.

DEFINITION OF ISSUER RATING

- DBRS Corporate rating analysis begins with an evaluation of the fundamental creditworthiness of the issuer, which is reflected in an "issuer rating". Issuer ratings address the overall credit strength of the issuer. Unlike ratings on individual securities or classes of securities, issuer ratings are based on the entity itself and do not include consideration for security or ranking. Ratings that apply to actual securities (secured or unsecured) may be higher, lower or equal to the issuer rating for a given entity.
- Given the lack of impact from security or ranking considerations, issuer ratings generally provide an opinion of default risk for all industry sectors. As such, issuer ratings in the banking sector relate to the final credit opinion on a bank that incorporates both the intrinsic rating and support considerations, if any.
- DBRS typically assigns issuer ratings on a long-term basis using its **Long Term Obligations** Rating Scale; however, on occasion, DBRS may assign a "short-term issuer rating" using its **Commercial Paper and Short Term Debt** Rating Scale to reflect the issuer's overall creditworthiness over a short-term time horizon.

SHORT-TERM AND LONG-TERM RATINGS

- For a discussion on the relationship between short- and long-term ratings and more detail on liquidity factors, please refer to the DBRS policy entitled "**Short-Term and Long-Term Rating Relationships**" and the criteria *DBRS Commercial Paper Liquidity Support Criteria for Corporate Non-Bank Issuers*.

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