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NEWSPAPERS
Round a Bend

Big bets by Jeffrey Bezos and John Henry, along with recent moves by Warren Buffett, suggest that new views are developing about print media's worth.

The second in a series of four articles on media valuations.

By JOHN S. SANDERS

FEW ANALYSTS WERE SURprised by the surge in merger and acquisition activity that is taking place in sectors like television and telecommunications this year. The combination of a strengthening economy, record-low lending rates and improved financial markets supported landmark transactions like Gannett Co.'s $2.2 billion acquisition of Belo Corp.'s television stations and Verizon's recently announced purchase of Vodafone's stake in Verizon Wireless for $130 billion.

What is surprising, however, is the more subtle yet profound thunder that has characterized what is regarded as the media's most mature segment: newspapers. Over the past 12 months the newspaper sector has become even more vibrant and has turned some important corners. Purchase-price cash flow multiples have strengthened; newspapers are being acquired in larger markets again, and some of the best minds in the business world are diversifying into daily newspapers.

A year ago, the prevailing logic was that large-market papers were permanently distressed and offered diminishing economic potential, primarily because the markets they serve are much more fragmented and competitive. In contrast, publications in small and medium markets maintained a higher level of attractiveness. This paradigm was broken in 2013 with a number of large-market acquisitions. The activity reflects a new type of buyer and likely offers a window into the future of the newspaper industry.

A number of questions beg to be asked. Why does the pace of small-to-medium market newspaper acquisitions continue unabated? Why have we seen an increase in large-market acquisitions, as exemplified by Jeff Bezos' acquisition of the *The Washington Post* and John Henry's acquisition of the *The Boston Globe*? And yet in the midst of this flurry of acquisition activity, why would legendary investor Warren Buffett, who is also a large investor in newspapers, completely liquidate his holdings of Gannett stock?

The simple answer seems to be that even a mature industry can be quite profitable, and newspapers still offer an incomparable platform to jump up to the next generations of technology. In small- to medium-sized markets, newspapers can still be a strong business in their own right, attractive to a current cash-flow investor like Berkshire Hathaway, whereas a larger-market investment requires the vision and resources to lever newspapers into the future media marketplace.

The listing of major newspaper acquisitions in 2013 on this page shows an intriguing bifurcation. The small-to-medium market publications were all acquired by BH Media, the publishing subsidiary of Warren Buffett's Berkshire Hathaway. BH Media has extolled the virtues of operating in markets of this size. Newspapers occupy a predominant role in markets that are less cluttered by competition and technological fragmentation.

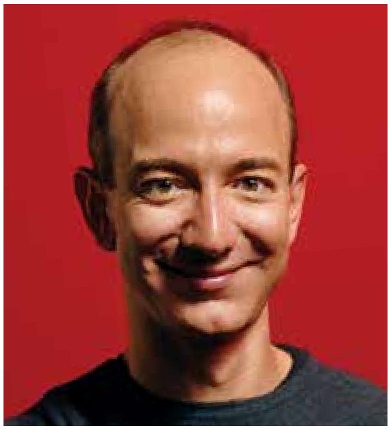
The three larger acquisitions were made by different individuals with a common characteristic: they are all entrepreneurs who made significant fortunes in the New Economy: Bezos with Amazon.com; Henry, an innovator in commodities trading, and John Georges, the owner of a Louisiana conglomerate that includes investments in entertainment and offshore energy.

THE DATA PARADOX

To a degree, the data on page 12, which compare 2012 and 2013 operational performance and valuations for the larger newspaper companies, explains the interest in newspapers. Admittedly, revenues and earnings before interest, income taxes, depreciation and amortization (EBITDA) continued to decline, although much less dramatically than in prior years.

Paradoxically, the overall enterprise value of the five companies *increased* by over 14% – from approximately $4.4 billion to $5.0 billion, driven by improving stock prices. The inflection implies that the market is finally seeing an end to the steep performance declines and a possible return to conservative growth.

Obviously, the destruction of the newspaper industry's entire value was catastrophic, dropping from approximately $161 billion in 2005 to $24 billion in 2011. While growth in 2012 was modest – to approximately $25 billion – this was the first time in seven years that the industry's economic value increased. Current multiples of recurring EBITDA range from 2.8x to 11.3x with an average of 5.9x for public companies (when not factoring in extraordinary items, such as intangible asset impairments or gains/losses on asset dispositions). This is an increase of over a full multiple relative to the average in 2012. The table on page 12 shows this and is also noteworthy because despite the competitive and technological forces that have depressed newspapers over the past decade, the industry still delivers EBITDA margins of approximately 20%. That level of performance is the envy of most industries.



Larger newspaper acquisitions have been made by entrepreneurs who made fortunes in the new economy, like Jeff Bezos.

BUFFETT AND BEZOS LOGIC

Buffett's decision to divest Gannett stock likely reflected the medium-market strategy, as Gannett operates newspapers in large markets and nationally (*USA Today*). Another factor probably was the recent performance of Gannett's stock, which has been good rather than disappointing. Since the market crash in 2009, Gannett stock has jumped from approximately $2 per share to over $25 today, with a 50% gain over the past year alone. Berkshire Hathaway acquired the stock in the 1990s and likely harvested a small gain, not even considering the dividends that were paid along the way.

The improved stock price performance of publicly traded newspaper companies in general creates a situation in which public multiples exceed those exhibited in recent private purchases of newspapers. While the terms of individual newspaper acquisitions are typically proprietary, private-market transaction multiples are currently falling in the 3.0 to 5.0 times EBITDA range. In some cases, 1.0 to 1.5 times revenue multiples are used as a benchmark.

Higher multiples may be clearly warranted for strategic acquisitions or other situations where cash flow can be increased rapidly. The $250 million purchase price for *The Washington Post* and several related businesses is

Major 2013 Newspaper Acquisitions

DATE	BUYER	SELLER	NEWSPAPER	PURCHASE PRICE	MSA* RANK	DAILY CIRCULATION
Aug. '13	Jeff Bezos	The Washington Post Co.	Washington Post (Graham Family)	$250 million	7	474,767
Aug. '13	John W. Henry & Co.	The New York Times Co.	The Boston Globe & Worcester Telegram and Gazette	$70 million	10	245,572
May '13	John Georges	The Manship Family	The Advocate (Baton Rouge)	undisclosed	69	98,000
March '13	BH Media	World Publishing Co.	Tulsa World	undisclosed	55	95,000
June '13	BH Media	Landmark Media	The Roanoke Times	undisclosed	159	76,000
Aug. '13	BH Media	ABARTA	The Press of Atlantic City	undisclosed	167	67,000
Feb. '13	BH Media	Landmark Media	The News & Record (Greensboro)	undisclosed	73	58,000

SOURCE: Company press releases *Metropolitan statistical area

Comparative Operating Performance and Valuations — 2012 to 2013

(Dollars in Millions)

	Year Ending March 30, 2012					Year Ending March 30, 2013				
COMPANY	REVENUE	RECURRING EBITDA	MARGIN	ENTERPRISE VALUE	EBITDA MULTIPLE	REVENUE	RECURRING EBITDA	MARGIN	ENTERPRISE VALUE	EBITDA MULTIPLE
McClatchy	$1,254.2	$378.1	30.1%	$1,623.4	4.3	$1,237.5	$348.6	28.2%	$1,827.5	5.2
Lee	748.0	172.8	23.1%	973.1	5.6	705.7	174.1	24.7%	919.5	5.3
New York Times	2,160.7	362.6	16.8%	1,615.8	4.5	2,006.0	288.6	14.4%	2,028.7	7.0
Daily Journal	33.1	10.4	31.4%	101.9	9.8	33.3	12.1	36.4%	137.1	11.3
A. H. Belo	454.2	30.6	6.7%	51.1	1.7	434.5	30.4	7.0%	84.5	2.8
Total	**$4,650.2**	**$954.5**	**20.5%**	**$4,365.3**	**4.6**	**$4,417.1**	**$853.8**	**19.3%**	**$4,997.3**	**5.9**
Percent Change	**-3.9%**	**-1.9%**		**-21.5%**	**-19.2%**	**-5.0%**	**-10.6%**		**+14.5%**	**+28.3%**

SOURCE: Publicly traded share-price data and company Securities and Exchange Commission filings

equivalent to less than 0.5 times revenue but over 10 times 2012 EBITDA for the company's newspaper division. In 2012, that unit's EBITDA margin was only about 4.1%.

What does Bezos' ownership portend for the company? If his past is a prologue, he will aggressively pursue innovative distribution methods and technological synergies, but continue to lever the publication's legacy of original (and expensive) long-form content and worldwide coverage.

Bezos' own management style indicates that he has a strong dedication to long-form treatments of subjects. He patiently waited years for the Kindle to succeed, believing that books still have a place in the crowded electronic media marketplace. At Amazon, PowerPoint presentations are all but banned (on the theory that bullet points encourage lazy thinking) in favor of narrative memos no more than six pages in length.

The Washington Post is clearly the flagship of the Bezos acquisition, but there is a small-market component as well. The acquisition includes the *Gazette* publications, which serve surrounding communities, as well as several other titles.

SMALLER LEANINGS

So with cautiously improving valuation fundamentals, 2013 witnessed a growing division of acquisitions based on market size. In small-to-medium markets, where newspapers still maintain a predominant position and reliable current cash flow, the investment opportunities are clear.

In addition to Berkshire Hathaway, other group owners have been expanding their holdings. Clearly, they share Buffet's sentiment in his investor letter that "papers delivering comprehensive and reliable information to tight-knit communities that also have a sensible Internet strategy will remain viable for a long time." Examples of this expansion include David Black's purchase of the 46,000 circulation *Daily Herald* in Everett, WA; Boone Newspapers' addition of the 11,000 circulation *Vicksburg Post* in Mississippi, and Ogden Newspaper's acquisition of the 20,000 circulation *Telegraph* in Nashua, NH.

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However, the buyer pool for small-to-medium newspapers is not limited to strategic buyers expanding their footprints. According to Gary Greene, a managing director with Cribb Greene & Associates, a leading newspaper brokerage firm, "If values for a company fall below the $15 million threshold for mid- and small-market newspapers, there is a solid independent buyer pool usually willing to pay higher multiples than the 4x or lower that the investment buyers look for."

Although the newspaper market will always be smaller and more specialized than other media like television and radio, "there is an active market for one-off mid- and small-market newspapers that come in under the $15 million threshold," according to Greene.

BIG MARKET IRONY

In larger markets, paradoxically, newspapers have suffered the most dramatic revenue and profit declines. The $70 million paid for *The Boston Globe* represents a 93% discount to the $1.1 billion paid by the New York Times Co. in 1993.

Ironically, however, these large publications still hold valuable assets in the form of iconic mastheads, incomparable newsroom infrastructure and long-time customer relationships that a new generation of entrepreneurs views as the best bet for jumpstarting new technologies, e-commerce and leveraging their existing businesses.

Henry, for example, already has a strong foothold in the Boston market through his ownership of the Boston Red Sox and the New England Sports Network.

Earlier this year, Buffet, widely regarded as the ablest investor in the U.S., referred to Jeff Bezos as the ablest CEO in the U.S. It seems no coincidence that both individuals have made calculated and aggressive investments into the newspaper industry in 2013.

Although each executive is pursuing a different strategy (many small-to-medium markets vs. a single large one), the value proposition still appears to be valid. Often the harvesting of a mature industry can yield surprisingly good results, and both investors have recognized that opportunity.

John S. Sanders is a principal with Bond & Pecaro in Washington, DC. He can be reached at (202) 775-8870 or johnsanders@bondpecaro.com.