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Troubles mount for publisher

GateHouse Media halts trading on NYSE

By MARY STONE

Perinton-based GateHouse Media Inc. is the latest in a string of three publicly traded newspaper publishers this year to have toppled off the New York Stock Exchange under the weight of rising debt and plummeting stock prices.

To make matters worse, newspaper companies nationwide soon will flood the market as they look to sell their properties; some analysts expect GateHouse's newspapers to be heaped among them.

Last week, stock in the publisher was trading at 60 cents a share when the NYSE stopped trading it. In July, the exchange had issued an operational trading halt when GateHouse shares dropped below a dollar.

In the last 52 weeks of trading, prices have tanked from $17.43 to 51 cents a

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GATEHOUSE

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share. NYSE officials said. To return to floor trading, the NYSE states GateHouse would have to maintain a trading price above $1.10 for a full day.

But if for 30 days the stock continues to close below $1 a share, the company could be delisted unless it can bring its share price above a dollar within the next six months.

GateHouse plans to release its second-quarter financial results today before the market opens.

Media experts are intrigued by the rise and fall of GateHouse, in particular for its velocity.

In fall 2006, with the newspaper industry already mired in a long string of circulation declines, GateHouse Media appeared to defy reason with a soaring stock price its first day on the trading floor. For its initial public offering, GateHouse stock rose 22 percent from its offering price of $18 to a high of $21.95 its first day.

The company stood out to investors for its consistent dividend yield as well as the company's hyperlocal strategy: amassing small-town newspapers, in proximity, that could be streamlined to operate for less than they were under private, separate ownership.

And given the competition among metro dailies, smaller markets seemed like a smart bet. In a recession, those small markets are less appealing to investors, experts say.

Curse of debt

Since its exceptional IPO, GateHouse fell under the expanding decline of the newspaper business, experts explain. Along the way, those challenges got compounded in a recessionary climate that makes the debt-laden company even more vulnerable than many counterparts.

Industry analyst and former publisher of *Financial World* magazine Douglas McIntyre said most publishing companies are built on debt, but with in excess of $1.2 billion in long-term debt and a little more than $10 million in cash, GateHouse certainly stands out.

Cash at GateHouse has dropped from $12.2 million at the end of 2007 and from $90 million at the end of 2006.

"If you take a look at Gannett or New York Times or Washington Post, the debt at those companies is substantially less compared to what it is at GateHouse, and the market knows that.

"And the reason that you can tell is that the companies that have the really severe debt service problems traded down really sharply, and the companies that have less severe problems are down not as much," McIntyre said. "It's relative."

When GHS shares were down 80 percent from the year before, shares for another major U.S. newspaper publisher, McClatchy Co., were down 70 percent, McIntyre said, while shares for Rochester Democrat and Chronicle parent company Gannett Co Inc. were down 50 percent.

Companies with big debt have been shut out of NYSE trading. In February, Sun-Times Media Group in Chicago stopped trading and in March, Pennsylvania-based Journal Register Co. was forced to stop too. Both now trade in the over-the-counter markets.

The Journal Register's business model is similar to that of GateHouse. Both companies own hundreds of newspaper publications in geographic clusters to leverage cost synergies.

The difference is the Journal Register focuses on larger metropolitan markets such as New Haven, Conn., and Detroit. GateHouse concentrates on small to midsize markets such as Canandaigua or Naples, though the company's newspapers extend well beyond New York to five geographic regions: the Northeast, Western, Northern Midwest, Southern Midwest and Atlantic states.

Since its delisting, the Journal Register has had to look to likely bidders for its newspapers. The same concern could be in store for GateHouse, McIntyre said, if it is not already.

"I don't know if they have taken any moves to sell things. There certainly isn't any public information to indicate they've started to auction anything off, but if they don't meet their debt covenants (financial agreements with creditors), they may not have a choice, which is what happened at the Journal Register."

If GateHouse does have to sell its publications, it might have trouble getting the price it wants. With more publications going on the market, and fewer public companies to acquire them, GateHouse will have to compete to sell, McIntyre said.

"There is going to be a big rotation in newspaper ownership. If you look at the Journal Register ... it's almost certain they will auction almost all of those properties off over the next three or four months.

"And the next two companies that look like they're going to fall into that situation are McClatchy and GateHouse, and it really isn't that the newspapers are doing badly, but they're doing badly enough that they can't handle the debt service of these

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companies," McIntyre said.

Local operations

GateHouse locally owns a handful of weekly shopper publications, in addition to the daily paper in Canandaigua and some 10 suburban weeklies it acquired through the $18 million purchase of Messenger Post Newspapers.

In early 2007, GateHouse continued a string of acquisitions, including a network of Massachusetts publications in a $70 million deal that included two daily newspapers and three weekly newspapers.

The Rochester Business Journal's request to speak to GateHouse representatives was not responded to.

Daniel Kennedy, assistant professor at Northeastern University's School of Journalism, has been speculating about the fate of GateHouse-owned publications in his neighborhood.

In talking to financial analysts about the company, he said GateHouse's focus on small community weeklies did make a lot of sense two years ago. In light of a recession, it does not.

"For them to be suddenly hit with two things at the same time, one of which is this drastic change in the newspaper business, and the other a more traditional recession, all of a sudden their strategy of taking on all of this debt did not look like such a good idea," Kennedy said. "Obviously this appears to have affected everybody, but apparently the companies who have been the most affected by this are McClatchy, GateHouse and of course Journal Register too."

Kennedy, in talking to newsroom workers in Massachusetts, said the rank and file are worried about the future. Curiously though, Kennedy said, GateHouse's corporate management does not appear to be.

"What I find really interesting about this is when I talk to people around GateHouse, and unfortunately I haven't been able to go far up the ladder because they're not the most accessible people in the world, but from what I've heard, I don't detect an awful lot of panic," Kennedy said.

"You get down into the ranks, and people are afraid for their jobs, but you talk to people who seem to have some access to what the people above them are thinking, they seem to have some faith that management is going to pull them out of this," Kennedy added. "And I'm not sure what they base that on. I have talked to at least one outside analyst that doesn't think things are really that bad, and I've talked to several other analysts that think things are terrible—that they could really cease to exist by the end of the year."

If GateHouse decides not to sell its newspapers, its options are slim. McIntyre said the company could try to get its debt refinanced, but with the nation in the middle of a credit crisis, that would be difficult.

"They could try to convert debt to equity, but right now they're dealing with a 40-cent stock price, so all that would do is dilute investors down to a nickel. Really their only other reasonable option is to try to sell papers," he said.

"So you're going to have a lot of newspapers coming onto the market, and they'll all be coming on for the same reason. They will be sold by leveraged companies to owners who are much less leveraged."

Experts say Gannett is one of the few newspaper publishers in any kind of position to acquire more properties. The more likely owners for these newspapers will be private owners, McIntyre said.

"None of these public newspaper companies are going to be buying more newspapers now. They've got too many problems now," he said. "Take Rochester: If Rochester (GateHouse properties) were to get sold, there's a good chance it will go to some private interest, maybe some local interest—some group that has a significant stake in the community.

"In many cases, private owners are not being driven only by profit. In many cases, private owners are driven by things like civic pride or an interest in journalism, so I think it is probably less likely that you'll have pressure on a private owner, particularly one who walks through the door knowing what's going on, to be tolerant of some level of loss," McIntyre said.

Media experts have been intrigued by the rise and fall of GateHouse, particularly its velocity.

And while circulation rates are not expected to increase or even level off anytime soon, small to midsize newspapers still have potential to earn money, Kennedy said.

"What people tell me is that these local community newspapers are at the moment a better business than large metropolitan papers, and they ought to be a good business, just not with the kind of debt that was loaded on them," Kennedy said.

And if public company ownership in the newspaper industry does return to private ownership, the new owners will have the same obstacles the newspaper business faced before public companies bought them, Kennedy said. To that, newspaper publishers will have to add new hurdles the Internet represents.

"It just seems like small local publishers had a difficult time a generation ago," Kennedy said. "Community Web sites and community blogs, which may not do real journalism, but do locally based conversations around issues, are in some ways more engaging than what the papers are doing. So I think (the new generation of owners) have that to contend with too."

The most likely private owners will have to tolerate falling operating income, which, McIntyre said, could slow or grow slightly as the country comes out of the recession. Automotive, real estate and employment advertising should start to return, but he said it will never be enough.

"So you may see a slowing of the downturn, but you're not going to see a rebound," he said. "The Internet fundamentally has done so much to undermine newspaper revenue and readership, and the Internet is not going to go away."

Over the near term, McIntyre said that newspapers will find buyers who, less inclined to cut costs, will be more inclined than public companies to keep journalists on board.

"But they're going to have to be people that are either immensely wealthy or people who buy the papers using very little debt, which allows them to have properties that have very modest operating income without some bank coming to their door every month hounding them for money," he said.

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