



CENGAGE LEARNING HOLDINGS II, INC.

**Second Quarter Report
Three and Six Months Ended September 30, 2018**

During the period covered by this report, Cengage Learning Holdings II, Inc. and its consolidated subsidiaries (the "Company") were not subject to the reporting requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended. However, the Company does have an obligation to comply with the terms of its Shareholder Agreement, dated as of March 31, 2014 (the "Shareholder Agreement"). The Shareholder Agreement includes references to certain provisions of the U.S. Securities and Exchange Commission's reporting requirements with modifications as agreed by all parties. The Company has complied with its obligations under the Shareholder Agreement and this report is made available pursuant to such obligations.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains both historical and forward-looking statements. All statements other than statements of historical fact are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. You can identify forward-looking statements because they contain words such as “believe,” “expect,” “may,” “will,” “should,” “could,” “seek,” “intend,” “plan,” “estimate,” “project,” “foresee,” “likely,” or “anticipate” or similar expressions that concern our strategies, objectives, plans, or goals. Although the forward-looking statements contained in this report reflect management’s current beliefs based upon information currently available to management and upon assumptions which management believes to be reasonable, actual results may differ materially from those stated in or implied by these forward-looking statements.

A number of factors could cause actual results or performance to differ materially from the results expressed or implied in the forward-looking statements, including the factors described in this quarterly report and those listed in the “Risk Factors” section of the Company’s Annual Report for the fiscal year ended March 31, 2018. These factors should be considered carefully and readers should not place undue reliance on the forward-looking statements. These risks and uncertainties include, without limitation:

- our ability to introduce new products, services or technologies;
- the impact of competition from established competitors and new businesses that have not traditionally participated in our markets, including the impact of new and enhanced product and service offerings and technology and competitors’ ability to adapt more quickly to new or emerging technologies and market conditions;
- the impact of used textbook and/or rental textbook programs and our ability to compete with them;
- the effect of increased accessibility of free or relatively inexpensive information and materials on pricing and demand for our products and services;
- the effect of changes in government programs and private lending practices relating to student aid and library funding;
- our ability to successfully implement our business strategy;
- the impact of technology developments and our ability to continue to make effective investments in our technology infrastructure;
- the seasonality of our business;
- our ability to adequately protect, maintain and enforce our intellectual property rights and proprietary rights and the adequacy of protections of our intellectual property under applicable laws;
- liabilities resulting from, and costs of defending against, litigation including piracy and intellectual property infringement claims;
- the impact of changes to laws and regulations applicable to us and our customers, including rules that could result in decreased programs offered by, and limit enrollments in, institutions of higher and continuing education including for-profit schools, as well as the enactment of the Tax Cuts and Jobs Act of 2017 (the “Tax Act”);
- our ability to attract and retain content providers and employees;
- our ability to attract and retain key authors, rights to our authors’ works, and avoid disputes with our authors;
- our ability and willingness to maintain licensing agreements with third-party content providers;
- failures or disruptions of our and our third-party providers’ hosting facilities and electronic delivery systems for our products and services;
- technology failures;
- our reliance on third-party providers of outsourced services and any failure of such providers to provide services effectively on a timely basis;
- our ability to adequately manage and develop our operational and managerial systems and processes including our enterprise resource planning software;
- changes in the availability and prices of paper and unanticipated increases in other operating costs;
- our ability to expand and conduct our operations outside the United States;

- the effect of fluctuations between foreign currencies and the United States dollar and our ability to effectively manage foreign currency exposure;
- our ability to identify, acquire and successfully integrate future acquisition targets;
- adverse changes in domestic and global economic and political conditions, including those related to the availability of credit, government and private loans for students and consequential decline in consumer demand for our products;
- reductions in enrollments at colleges and universities;
- our ability to win state adoptions;
- our dependence on third-party distributors, representatives and retailers;
- incurrence of impairment charges for goodwill, long-lived assets and identifiable intangible assets;
- the impact of business combinations in the markets in which we compete;
- our ability to react to changes in the economy or our industry;
- our debt agreements, which limit our flexibility in operating our business including, among other things, our ability under certain circumstances to engage in mergers or consolidations, sell assets and use the proceeds of such sale, pay distributions to our equity owners and/or buy back debt;
- potential security breaches or cyberattacks involving our technology infrastructure, our products and services, or our customers' credit and debit card and private data, which could subject us to material claims and additional costs and harm our reputation;
- our ability to comply with privacy laws;
- termination of at-will contracts to which we are a party could harm our business;
- increased availability of lower priced international versions of our products in the domestic market or higher prices for our products overseas may cause our sales to decline;
- changes in our credit ratings or macroeconomic conditions;
- the impact of being controlled by Principal Equityholders, whose interests may conflict with other stockholders; and
- our ability to maintain effective internal controls over financial reporting.

Although we have attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described in or implied by our forward-looking statements, other factors and risks may cause actions, events or results to differ materially from those anticipated, estimated or intended. We cannot assure you that forward-looking statements will prove to be accurate, as actual actions, results and future events could differ materially from those anticipated or implied by such statements. All forward-looking statements included in this report are expressly qualified in their entirety by the foregoing cautionary statements. These forward-looking statements are made as of the date of this report and, except as required by law, we undertake no obligation to update, amend, clarify or revise them to reflect new events or circumstances.

CENGAGE LEARNING HOLDINGS II, INC.
SECOND QUARTER REPORT
THREE AND SIX MONTHS ENDED SEPTEMBER 30, 2018
(UNAUDITED)

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CENGAGE LEARNING HOLDINGS II, INC.
Condensed Consolidated Balance Sheets
(UNAUDITED)

	As of	
	September 30, 2018	March 31, 2018
<i>(in millions, except share and per share amounts)</i>		
Assets		
Cash and cash equivalents	\$ 274.9	\$ 319.3
Accounts receivable, net	345.6	180.8
Inventories	110.1	116.8
Prepaid expenses and other current assets	80.8	58.3
Total current assets	811.4	675.2
Property, equipment and capitalized internal-use software, net	156.0	164.4
Pre-publication costs, net	209.1	232.2
Author advances	22.4	22.5
Identifiable intangible assets, net	960.1	1,009.9
Goodwill	1,629.3	1,633.2
Deferred tax assets	6.9	7.5
Deferred financing costs	2.8	3.4
Other non-current assets	25.8	24.5
Total assets	\$ 3,823.8	\$ 3,772.8
Liabilities and Stockholders' Equity		
Accounts payable and accrued expenses	\$ 291.0	\$ 276.6
Deferred revenue	259.8	178.9
Current portion of long-term debt	15.2	6.7
Income taxes payable	1.6	3.9
Other current liabilities	11.6	18.5
Total current liabilities	579.2	484.6
Long-term debt	2,239.8	2,244.9
Deferred tax liabilities	66.6	78.3
Other non-current liabilities	68.5	50.0
Total liabilities	2,954.1	2,857.8
Commitments and contingencies (Note 14)		
Preferred stock (\$0.01 par value, 50,000,000 shares authorized, none issued)	—	—
Common stock (\$0.01 par value, 300,000,000 shares authorized, 61,467,871 and 61,009,916 shares issued and outstanding as of September 30, 2018 and March 31, 2018, respectively)	0.6	0.6
Additional paid-in capital	1,226.3	1,224.7
Accumulated deficit	(305.0)	(270.9)
Accumulated other comprehensive loss	(52.2)	(39.4)
Total stockholders' equity	869.7	915.0
Total liabilities and stockholders' equity	\$ 3,823.8	\$ 3,772.8

See accompanying notes to the condensed consolidated financial statements.

CENGAGE LEARNING HOLDINGS II, INC.
Condensed Consolidated Statements of Operations
(UNAUDITED)

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017	2018	2017
Revenues	\$ 474.3	\$ 522.4	\$ 762.6	\$ 818.4
Cost of revenues, excluding amortization of pre-publication costs and identifiable intangible assets and depreciation stated below	188.9	198.6	337.2	338.4
Amortization of pre-publication costs	38.4	44.8	63.3	71.1
Amortization of identifiable intangible assets	1.2	1.0	2.4	1.8
Total cost of revenues, excluding depreciation stated below	228.5	244.4	402.9	411.3
Selling, general and administrative expenses, excluding depreciation stated below	117.0	111.6	233.8	215.0
Operational restructuring and other charges, net	0.7	1.8	4.8	1.6
Depreciation	17.6	17.5	34.6	37.3
Amortization of identifiable intangible assets	22.5	22.6	45.0	45.1
Other income, net	—	—	—	(0.2)
Total costs and expenses	386.3	397.9	721.1	710.1
Operating income	88.0	124.5	41.5	108.3
Other (expense) income, net	(0.1)	(1.3)	1.7	10.9
Interest income	0.9	0.5	1.8	1.0
Interest expense	(44.2)	(40.4)	(87.3)	(80.0)
Income (loss) before taxes	44.6	83.3	(42.3)	40.2
(Provision for) benefit from income taxes	(10.2)	(27.9)	8.2	(13.9)
Net income (loss)	\$ 34.4	\$ 55.4	\$ (34.1)	\$ 26.3

See accompanying notes to the condensed consolidated financial statements.

CENGAGE LEARNING HOLDINGS II, INC.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(UNAUDITED)

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017	2018	2017
Net income (loss)	\$ 34.4	\$ 55.4	\$ (34.1)	\$ 26.3
Other comprehensive (loss) income:				
Foreign currency translation adjustments	(1.7)	6.1	(12.8)	7.6
Comprehensive income (loss)	\$ 32.7	\$ 61.5	\$ (46.9)	\$ 33.9

See accompanying notes to the condensed consolidated financial statements.

CENGAGE LEARNING HOLDINGS II, INC.
Condensed Consolidated Statements of Cash Flows
(UNAUDITED)

<i>(in millions)</i>	Six Months Ended September 30,	
	2018	2017
Cash Flows from Operating Activities		
Net (loss) income	\$ (34.1)	\$ 26.3
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Amortization of pre-publication costs	63.3	71.1
Depreciation	34.6	37.3
Amortization of identifiable intangible assets	47.4	46.9
Amortization of debt discounts and deferred financing costs	4.1	4.1
Non-cash equity-based compensation expense	4.5	5.6
Operational restructuring and other charges, net	4.8	1.6
Cash payments for operational restructuring charges	(5.7)	(9.2)
Deferred income taxes	(11.6)	6.9
Changes in operating assets and liabilities, net of acquisitions	(64.8)	(34.4)
Other, net	0.6	0.3
Net cash provided by operating activities	<u>43.1</u>	<u>156.5</u>
Cash Flows from Investing Activities		
Acquisitions of businesses and investments in equity method investees, net of cash acquired	(1.5)	(1.6)
Additions to pre-publication costs	(46.7)	(50.9)
Additions to property, equipment and capitalized internal-use software	(30.0)	(36.7)
Other, net	(0.7)	(2.4)
Net cash used in investing activities	<u>(78.9)</u>	<u>(91.6)</u>
Cash Flows from Financing Activities		
Repayments of long-term debt	(0.1)	(27.9)
Dividend equivalents paid	(4.2)	—
Common stock repurchases for tax withholding for net settlement of equity awards	(3.0)	—
Common stock repurchases under share repurchase program	—	(61.0)
Net cash used in financing activities	<u>(7.3)</u>	<u>(88.9)</u>
Impact on Cash and Cash Equivalents from Changes in Foreign Currency	<u>(1.3)</u>	<u>0.2</u>
Net Decrease in Cash and Cash Equivalents	<u>(44.4)</u>	<u>(23.8)</u>
Cash and Cash Equivalents		
Beginning of period	<u>319.3</u>	<u>352.3</u>
End of period	<u>\$ 274.9</u>	<u>\$ 328.5</u>

See accompanying notes to the condensed consolidated financial statements.

CENGAGE LEARNING HOLDINGS II, INC.
Notes to the Condensed Consolidated Financial Statements
(UNAUDITED)

1. BASIS OF PRESENTATION

Basis of Presentation

Cengage Learning Holdings II, Inc., together with its consolidated subsidiaries (the “Company”), is a leading education and technology company built for learners, serving the higher education, school, professional, library and workforce training markets worldwide.

The Company has prepared the accompanying condensed consolidated financial statements and accompanying footnotes in accordance with the accounting policies described in its Annual Report for the fiscal year ended March 31, 2018 (the “2018 Annual Report”). Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted. You should read these financial statements in conjunction with the consolidated financial statements included in the 2018 Annual Report.

In the opinion of management, the financial statements include all adjustments (consisting of normal recurring adjustments) considered necessary by management to fairly state the financial position, results of operations and cash flows for the periods presented. The results of operations for the three and six months ended September 30, 2018 are not necessarily indicative of the results for the fiscal year ending March 31, 2019.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Although these estimates are based on management’s best knowledge of current events and actions that the Company may undertake in the future, actual results could differ from those estimates. These estimates include, but are not limited to, reserves for sales returns and inventory obsolescence, the allowance for doubtful accounts, deferred tax assets and liabilities, the valuation allowances for deferred tax assets, operational restructuring and other charges, legal and tax contingencies, purchase accounting and equity-based compensation, as well as future cash flows and fair values used in the assessment of the realizability of long-lived assets, goodwill and identifiable intangible assets.

Seasonality and Comparability

The Company’s revenues, operating profit and operating cash flows are impacted by the inherent seasonality of the academic calendar. This seasonality affects the Company’s working capital requirements and hence its overall financing needs. For example, the Company typically incurs a net cash deficit from all of its activities in the first and fourth quarters of the fiscal year. In addition, changes in customer ordering patterns may impact the comparison of the Company's results in a quarter with the same quarter of the previous year, or in a fiscal year with the prior fiscal year, where its customers may shift the timing of material orders for a number of reasons, including, but not limited to, changes in academic semester start dates or changes in inventory management practices.

As the Company continues to migrate its service offerings towards hosted digital solutions that are delivered over a period of time, the associated revenues will be recognized ratably over the applicable subscription period, with amounts billed in excess of revenues recognized reflected as deferred revenue. Deferred revenue represents amounts billed in advance to customers that will be recognized as revenues in subsequent periods as products and services are delivered to customers. The current portion of deferred revenue was \$259.8 million and \$178.9 million as of September 30, 2018 and March 31, 2018, respectively, and the non-current portion of deferred revenue was \$40.6 million and \$30.9 million as of September 30, 2018 and March 31, 2018, respectively.

CENGAGE LEARNING HOLDINGS II, INC.
Notes to the Condensed Consolidated Financial Statements
(UNAUDITED)

Concentration of Credit Risk

Customers accounting for 10% or more of the Company's total gross accounts receivable were as follows:

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Customer A	14%	11%
Customer B	15%	12%

No customer was individually greater than 10% of the Company's consolidated revenue for the three and six months ended September 30, 2018 and 2017.

New Accounting Standards and Accounting Changes

In August 2018, the Financial Accounting Standards Board (“FASB”) issued guidance on accounting for implementation costs incurred in a cloud computing arrangement that is a service contract. This update aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The amendments in this update are effective for fiscal years beginning after December 15, 2020 and interim periods within fiscal years beginning after December 15, 2021, with early adoption permitted. The Company is evaluating the impact of this update on its consolidated financial position, results of operations and cash flows.

In November 2016, the FASB issued guidance on the classification and presentation of restricted cash in the statement of cash flows which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019, with early adoption permitted. The adoption of this guidance is not expected to have a material impact on the Company’s consolidated cash flows.

In August 2016, the FASB issued guidance on the classification of certain cash flow transactions, consisting of the following: debt prepayment or debt extinguishment costs; the settlement of zero-coupon debt instruments; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and the application of the predominance principle. The amendments provide guidance for each of the eight issues for which GAAP guidance was previously unclear or did not exist, thereby reducing the current and potential future diversity in practice. The guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019, with early adoption permitted. The Company is evaluating the impact of this update on its consolidated financial position, results of operations and cash flows.

In February 2016, the FASB issued an updated standard to add Accounting Standard Codification (“ASC”) Topic 842, “Leases”, which will replace most of the existing leasing guidance in U.S. GAAP when it becomes effective. One of the most significant changes this update will institute is that for all leases the lessees will be required to recognize at the commencement date: a) a lease liability; and b) a right-of-use asset. The lease liability represents the lessee’s obligation to make lease payments and it is measured on a discounted basis. The right-of-use asset represents the lessee’s right to use, or control the use of, the underlying leased asset during the term of the lease. Additionally, the guidance requires improved disclosures to help users of financial statements better understand the nature and magnitude of lessees’ lease obligations. The amendments in this update are effective for the Company for fiscal years beginning after December 15, 2019 and interim periods within fiscal years beginning after December 15, 2020. The Company is evaluating the impact of this update on its consolidated financial position, results of operations and cash flows.

CENGAGE LEARNING HOLDINGS II, INC.
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In May 2014, the FASB issued an update to add ASC Topic 606, “Revenue from Contracts with Customers”, which will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The authoritative guidance provides that an entity should recognize revenues to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services through the application of the following steps:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Additionally, the guidance requires improved disclosures to help users of financial statements better understand the nature, amount, timing, and uncertainty of revenues that are recognized. The amendments in this update are to be applied on a retrospective basis, utilizing one of two different alternatives. In August 2015, the FASB approved a one year deferral of the effective date of the amended revenue recognition guidance. As a result, the amendments in this update are effective for the Company in the annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early application is permitted, with certain limitations. The Company is evaluating the potential effect of this new standard on its major revenue streams and contracts with customers, as well as the impact on its consolidated financial position, results of operations and cash flows. The Company plans to utilize the modified retrospective approach in implementing the new standard.

2. INVENTORIES

Inventories consisted of the following:

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Raw materials	\$ 0.1	\$ 0.2
Work-in-progress	0.3	0.5
Finished goods	109.7	116.1
Total inventories	\$ 110.1	\$ 116.8

3. OTHER BALANCE SHEET ACCOUNTS

The sales returns reserve and allowance for doubtful accounts included in accounts receivable, net, in the accompanying condensed consolidated balance sheets were as follows:

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Sales returns reserve	\$ 67.3	\$ 70.8
Allowance for doubtful accounts	15.1	12.7

The provision for estimated sales returns is reflected as a reduction of revenue during the period in which the revenue is recognized. The Company records the returns against its sales returns reserve in the period of receipt.

CENGAGE LEARNING HOLDINGS II, INC.
Notes to the Condensed Consolidated Financial Statements
(UNAUDITED)

Accounts payable and accrued expenses consisted of the following:

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Accounts payable	\$ 80.1	\$ 79.9
Accrued royalties	89.6	58.3
Accrued bonuses	41.0	58.3
Accrued interest payable	21.1	22.2
Other accrued expenses	59.2	57.9
	\$ 291.0	\$ 276.6

4. IDENTIFIABLE INTANGIBLE ASSETS

The Company's identifiable intangible assets, net were as follows:

<i>(in millions)</i>	As of			As of		
	September 30, 2018			March 31, 2018		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
Copyrights	\$ 728.0	\$ (224.4)	\$ 503.6	\$ 730.2	\$ (200.3)	\$ 529.9
Customer relationships	367.1	(109.5)	257.6	368.2	(97.6)	270.6
Trademarks	232.9	(69.7)	163.2	233.4	(62.1)	171.3
Technology and author/content rights	45.5	(9.8)	35.7	45.5	(7.4)	38.1
Total identifiable intangible assets	\$ 1,373.5	\$ (413.4)	\$ 960.1	\$ 1,377.3	\$ (367.4)	\$ 1,009.9

5. GOODWILL

The following table shows the changes in the carrying amounts of goodwill by segment:

<i>(in millions)</i>	Learning	Gale	International	Total
Balance as of March 31, 2018	\$ 1,326.1	\$ 204.8	\$ 102.3	\$ 1,633.2
Foreign currency translation adjustments	—	(0.9)	(3.0)	(3.9)
Balance as of September 30, 2018	\$ 1,326.1	\$ 203.9	\$ 99.3	\$ 1,629.3

6. OPERATIONAL RESTRUCTURING AND OTHER CHARGES

Fiscal Year 2019

During the first quarter of fiscal year 2019, the Company initiated a restructuring program in our Gale and International segments to better align our operations to current market conditions and position the business for growth. During the six months ended September 30, 2018, the Company incurred \$4.2 million of severance related costs, with related cash payments expected to be made through the third quarter of fiscal year 2020.

During the second quarter of fiscal year 2019, the Company initiated a restructuring program in our Learning segment to streamline our operations and incurred \$0.6 million of severance related costs, with related cash payments expected to be made through the first quarter of fiscal year 2020.

Fiscal Year 2018

During the first quarter of fiscal year 2018, the Company initiated a restructuring program related to its initiatives to better align discipline and delivery strategies, to improve the development and enhancements of its digital products and assess its operations, and to further support the shift from a textbook to a software sales and support model. The Company incurred \$1.5

CENGAGE LEARNING HOLDINGS II, INC.
Notes to the Condensed Consolidated Financial Statements

million of severance related costs during the six months ended September 30, 2017, and \$3.4 million in the aggregate in fiscal year 2018. The Company also incurred \$3.4 million of process reengineering consulting costs during the six months ended September 30, 2017, and \$7.4 million in the aggregate as of the end of fiscal year 2018. These charges were expensed as incurred.

Also during the first quarter of fiscal 2018, the Company exited an existing lease and ceased use of the space. As a result, the Company recorded a \$3.5 million non-cash charge to write-off the existing landlord inducement liability. In connection with exiting the existing facility, the Company received a \$12.0 million incentive payment from a third party that was included in other (expense) income, net, in the accompanying condensed consolidated statement of operations.

In the remainder of fiscal year 2018, the Company vacated two additional offices and recorded \$4.0 million of charges, net of non-cash write-offs and net of sublease estimates with remaining lease payments to be paid over the underlying remaining lease terms. Additionally, the Company initiated a restructuring program to better align its operations to current market conditions and in anticipation of its continued shift to a subscription/digital model resulting in a total of \$2.3 million of severance related costs in our Learning and International segments.

Operational restructuring and other charges recognized in the accompanying condensed consolidated statements of operations by segment were as follows:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017	2018	2017
Learning	\$ 0.6	\$ 1.0	\$ 0.6	\$ 1.1
Gale	0.1	—	4.0	—
International	—	—	0.2	—
Corporate	—	0.8	—	0.5
Total operational restructuring and other charges, net	0.7	1.8	4.8	1.6
Less: non-cash write-off	—	—	—	(3.5)
Total charges expected to be settled in cash	<u>\$ 0.7</u>	<u>\$ 1.8</u>	<u>\$ 4.8</u>	<u>\$ 5.1</u>

The following table summarizes cash activity for restructuring reserves, which is included in other current liabilities and other non-current liabilities in the accompanying condensed consolidated balance sheets:

<i>(in millions)</i>	Severance		Process reengineering consulting		Lease Exit and Other		Total	
	\$	\$	\$	\$	\$	\$	\$	\$
Balance as of March 31, 2018	2.7	—	3.7	6.4	—	6.4	—	6.4
Charges, net	4.8	—	—	4.8	—	4.8	—	4.8
Accretion Expense	—	—	0.1	0.1	0.1	0.1	—	0.1
Cash payments	(5.0)	—	(0.7)	(5.7)	(0.7)	(5.7)	—	(5.7)
Balance as of September 30, 2018	<u>2.5</u>	<u>—</u>	<u>3.1</u>	<u>5.6</u>	<u>3.1</u>	<u>5.6</u>	<u>—</u>	<u>5.6</u>
Balance as of March 31, 2017	3.0	2.8	—	5.8	—	5.8	—	5.8
Charges, net	1.5	3.2	(3.1)	1.6	(3.1)	1.6	—	1.6
Non-cash write-off	—	—	3.5	3.5	3.5	3.5	—	3.5
Cash payments	(2.9)	(5.8)	(0.4)	(9.1)	(0.4)	(9.1)	—	(9.1)
Balance as of September 30, 2017	<u>1.6</u>	<u>0.2</u>	<u>—</u>	<u>1.8</u>	<u>—</u>	<u>1.8</u>	<u>—</u>	<u>1.8</u>

CENGAGE LEARNING HOLDINGS II, INC.
Notes to the Condensed Consolidated Financial Statements

The Company's total restructuring liability was reported as follows:

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Other current liabilities	\$ 3.9	\$ 4.1
Other non-current liabilities	1.7	2.3
Total restructuring liability	<u>\$ 5.6</u>	<u>\$ 6.4</u>

7. DEBT

Debt, related maturities and interest rates were as follows as of September 30, 2018 and March 31, 2018:

<i>(in millions)</i>	Original Maturity	Interest Rate as of		September 30, 2018	March 31, 2018
		September 30, 2018	March 31, 2018		
Current portion:					
Term Loan	2023	6.42%	6.04%	\$ 15.0	\$ 6.4
Capital lease	2019			0.2	0.3
Total current portion of long-term debt				<u>15.2</u>	<u>6.7</u>
Non-current portion:					
Senior Notes	2024	9.50%	9.50%	620.0	620.0
Term Loan	2023	6.42%	6.04%	1,654.4	1,663.0
Capital lease	2019			—	0.1
Unamortized Term Loan discount				(11.4)	(12.7)
Unamortized deferred financing costs				(23.2)	(25.5)
Total non-current portion of long-term debt				<u>2,239.8</u>	<u>2,244.9</u>
Total debt				<u>\$ 2,255.0</u>	<u>\$ 2,251.6</u>

Scheduled principal payments due on the Company's debt as of September 30, 2018 for each of the years ended March 31 are as follows:

<i>(in millions)</i>	
Fiscal Years Ending March 31,	
Remainder of fiscal year 2019	\$ 6.5
2020	17.2
2021	17.1
2022	17.1
2023	17.1
Thereafter	2,214.6
Total	<u>\$ 2,289.6</u>

On June 7, 2016, Cengage Learning, Inc., a wholly-owned subsidiary of the Company, issued 9.50% senior notes ("Senior Notes") and amended and restated its senior secured term loan facility ("Term Loan") and its asset based lending revolving line of credit ("ABL Revolving Credit Facility").

In February 2017, the Company's board of directors approved an authorization of up to \$100 million to purchase in the open market its Senior Notes and/or Term Loan.

CENGAGE LEARNING HOLDINGS II, INC.
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Senior Notes

On June 7, 2016, Cengage Learning, Inc. issued \$620.0 million aggregate principal amount Senior Notes in a private placement, maturing June 15, 2024. The Senior Notes bear interest at a rate of 9.50% per annum, payable semi-annually in arrears on June 15 and December 15 of each year. Cengage Learning, Inc. has the option to redeem the Senior Notes, in whole or in part, at any time on or before June 15, 2019, at a redemption price equal to 100% of the principal amount of the notes plus an applicable premium and accrued interest, as defined in the indenture. The Company also has the option to redeem the Senior Notes, in whole or in part, at any time on or after June 15, 2019, at certain redemption prices as defined in the indenture. In addition, under the terms of the Senior Notes the Company may repurchase the Senior Notes in part, at any time, in the open market, in accordance with federal securities regulations.

The indenture related to the Senior Notes contains certain covenants that the Company may be subject to which restrict its and its subsidiaries' ability to, among other things: incur additional indebtedness or issue certain disqualified shares and preferred shares; create liens; pay dividends or distributions or redeem or repurchase equity; prepay subordinated debt or make certain investments; transfer and sell assets; engage in a consolidation or merger or sell, transfer or otherwise dispose of all or substantially all of its assets; and enter into certain transactions with affiliates. The Company will not be subject to these covenants if (i) the Senior Notes have Investment Grade Ratings from the relevant rating agencies, as defined in the terms of the Senior Notes, and (ii) no default has occurred and is continuing under the indenture. As of September 30, 2018, no default has occurred and the Company is compliant with all of the covenants of the indenture.

Term Loan

The Term Loan provides for senior secured term loans in an aggregate principal amount of \$1,710.0 million and matures on June 7, 2023. In addition, the Company may request one or more incremental credit facilities in an aggregate amount of up to \$500.0 million, plus additional amounts subject to certain requirements. Borrowings under the Term Loan bear interest at a rate equal to, at the Company's option, either (a) a LIBOR rate determined by reference to the costs of funds for Eurodollar deposits for the interest period relevant to such borrowing, adjusted for certain additional costs, subject to a 1.00% floor ("Eurocurrency Rate Loan"), or (b) a base rate determined by reference to the highest of (i) the federal funds rate plus 0.50%, (ii) the prime rate and (iii) the one-month adjusted LIBOR rate plus 1.00%, in each case plus an applicable margin. As of September 30, 2018, the Company elected to carry the Term Loan as a Eurocurrency Rate Loan with an effective interest rate of 6.42%.

The Company is required to repay 0.25% of the original principal amount of the Term Loan on the last business day of each quarter. Following the end of each fiscal year the Company must prepay a percentage between 0% and 50%, based on its total leverage ratio, of its Excess Cash Flow, as defined in the Term Loan agreement, within five business days after delivery of the financial statements. Based on the Company's March 31, 2018 consolidated financial statements, the Company determined there was no prepayment due under the Excess Cash Flow provision. Based on the Company's March 31, 2017 consolidated financial statements, the Company made a \$27.7 million principal prepayment in June 2017. Prepayments made under the Excess Cash Flow provision are used to satisfy prospective mandatory quarterly principal repayments. The Company is also required to prepay loans with net proceeds from asset sales, casualty events, or issuances of indebtedness, subject to, in the case of asset sales and casualty events, reinvestment rights by the Company within certain time restrictions. The Company may prepay or repurchase the Term Loan, in whole or in part, at any time, without penalty.

ABL Revolving Credit Facility

The availability of credit under the amended and restated five-year ABL Revolving Credit Facility, which expires on June 7, 2021, is equal to the lesser of (i) \$250.0 million and (ii) the Company's borrowing base. The borrowing base equals the sum of (i) 90% of eligible credit card receivables, plus (ii) 85% of eligible receivables, plus (iii) 85% of the orderly liquidation value of eligible inventory, plus (iv) 100% of cash not to exceed \$35.0 million. As of September 30, 2018 and March 31, 2018, the ABL Revolving Credit Facility had no outstanding borrowings and \$22.3 million and \$22.6 million, respectively, in issued and outstanding letters of credit. The Company's available borrowing base as of September 30, 2018, which is based on the balance sheet at August 31, 2018, was \$227.7 million, net of letters of credit.

The unused commitment fee ranges between 0.25% and 0.375%, based upon the average facility usage for the most recently ended fiscal quarter. Outstanding letters of credit are also subject to a quarterly letter of credit participation fee which varies between 1.75% and 2.25%, depending on the average daily availability. For both the three and six months ended September 30, 2018 and 2017, the commitment and participation fees were insignificant.

CENGAGE LEARNING HOLDINGS II, INC.
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8. EQUITY

Share Repurchase Programs

On June 6, 2017, the Company announced the extension of its \$65.0 million share repurchase authorization until May 31, 2018. The Company paid \$15.8 million and \$45.1 million for shares repurchased in the first and second quarters of fiscal year 2018, respectively. As of September 30, 2017, the Company completed this program repurchasing 7,259,913 shares for \$65.0 million in the aggregate. Repurchased shares were retired and returned to the status of authorized but unissued.

In addition, the Company repurchases shares from certain employees in order to satisfy employee tax withholding requirements in connection with the vesting of restricted stock units and delivery of the underlying shares. During the six months ended September 30, 2018 and 2017, the Company spent \$3.0 million and less than \$0.1 million, respectively, to acquire shares in connection with equity-based awards.

9. EQUITY-BASED COMPENSATION

The following table summarizes the Company's equity-based compensation expense recognized in selling, general and administrative expenses, excluding depreciation in the accompanying condensed consolidated statements of operations:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017	2018	2017
Stock options	\$ 0.4	\$ 1.2	\$ 0.8	\$ 2.2
Restricted stock units	1.7	1.8	3.7	3.4
Equity-based compensation expense	\$ 2.1	\$ 3.0	\$ 4.5	\$ 5.6

As of September 30, 2018, there was approximately \$11.7 million of total unrecognized compensation cost related to stock options and restricted stock units (RSUs) expected to be recognized over a weighted-average vesting period of 2.4 years. In addition, there was approximately \$4.5 million of unrecognized compensation cost related to non-vested performance-based RSUs as of September 30, 2018. No compensation cost related to the performance-based RSUs will be recognized until it is probable that the performance condition will be met.

10. INCOME TAXES

For interim income tax reporting, the Company estimates its annual effective tax rate and applies it to year-to-date ordinary income (loss). Tax jurisdictions with a projected or year-to-date loss for which a tax benefit cannot be realized are excluded. The tax effects of unusual or infrequently occurring items are reported in the interim period in which they occur. The effect of a change in tax laws or rates on a deferred tax liability or asset is recognized in the quarter in which the tax legislation is enacted.

The provision for income taxes was \$10.2 million and \$27.9 million for the three months ended September 30, 2018 and 2017, respectively. The benefit from income taxes was \$8.2 million for the six months ended September 30, 2018 directly attributable to the current year pre-tax loss, while the provision for income taxes was \$13.9 million for the same prior year period due to pre-tax income. The effective income tax rate was 22.9% and 33.5% for the three months ended September 30, 2018 and 2017, respectively, and 19.4% and 34.6% for the six months ended September 30, 2018 and 2017, respectively. The decrease in the Company's effective tax rate for the six months ended September 30, 2018 compared with the same prior year period was primarily attributable to the reduction of the U.S. federal statutory tax rate as a result of the Tax Cuts and Jobs Act of 2017 (the "Tax Act").

As of March 31, 2018, the Company had federal net operating loss ("NOL") carryforwards of \$378.2 million. These NOL carryforwards can be used to offset taxable income in future periods and reduce the Company's income taxes payable in those future periods. Most of these NOL carryforwards will expire if they are not used within certain periods. At this time, the Company considers it more likely than not that the Company will have sufficient future taxable income in the form of reversals of existing taxable temporary differences that will allow the Company to realize these existing and future U.S. tax attributes. However, it is possible that in a future period, the generation of deferred tax assets will exceed the taxable temporary differences and at that point a valuation allowance against the Company's federal and state net deferred tax asset may be required.

CENGAGE LEARNING HOLDINGS II, INC.
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11. FAIR VALUE MEASUREMENTS

Recurring Measurements

As of September 30, 2018 and March 31, 2018, the Company had no assets and liabilities measured at fair value on a recurring basis.

Non-Recurring Measurements

Non-financial assets and liabilities, which include goodwill, identifiable intangible assets, property, equipment and capitalized internal-use software, net, and various liabilities, are not required to be measured at fair value on a recurring basis. However, if an impairment test is required, the Company evaluates the non-financial assets and liabilities for impairment. If impairment is determined to have occurred, the asset or liability is required to be written down to its estimated fair value. During the three and six months ended September 30, 2018 and 2017, the Company did not recognize any impairments of its non-financial assets and liabilities.

Other Fair Value Disclosures

In addition to fair value disclosure requirements related to financial instruments carried at fair value, accounting standards require disclosures regarding the fair value of all of the Company's financial instruments. The carrying value and estimated fair value of long-term debt, including the current portion, is as follows:

<i>(in millions)</i>	As of		As of	
	September 30, 2018		March 31, 2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Senior Notes ⁽¹⁾	\$ 613.4	\$ 526.0	\$ 612.9	\$ 471.9
Term Loan ⁽²⁾	1,641.4	1,526.5	1,638.3	1,486.8

⁽¹⁾ The carrying amount for the Senior Notes is presented net of the unamortized deferred financing costs of \$6.6 million and \$7.1 million as of September 30, 2018 and March 31, 2018, respectively.

⁽²⁾ The carrying amount for the Term Loan as of September 30, 2018 and March 31, 2018, is presented net of the unamortized original issue discount and deferred financing costs of \$28.0 million and \$31.1 million, respectively.

The estimated fair values of the Company's Senior Notes and Term Loan are based on information from a pricing service or broker quotes and may not represent prices on which such debt may be transacted. Therefore, the debt is classified as Level 3 in the fair value hierarchy. The carrying values of cash and cash equivalents, accounts receivable, and accounts payable approximated their fair values as of September 30, 2018 and March 31, 2018, due to the short-term nature of these instruments.

12. SUPPLEMENTAL CASH FLOW INFORMATION

Details of "Changes in operating assets and liabilities, net of acquisitions" in the condensed consolidated statements of cash flows were:

<i>(in millions)</i>	Six Months Ended September 30,	
	2018	2017
Accounts receivable, net	\$ (163.3)	\$ (179.3)
Inventories	0.8	0.3
Prepaid expenses and other current assets	(11.4)	(12.2)
Author advances	(0.1)	0.2
Accounts payable and accrued expenses	26.6	80.5
Accrued interest payable	(1.2)	(1.2)
Deferred revenue	88.0	72.1
Income taxes payable	(2.1)	2.8
Other, net	(2.1)	2.4
	\$ (64.8)	\$ (34.4)

CENGAGE LEARNING HOLDINGS II, INC.
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Non-cash Investing Activities

Additions to pre-publication costs and property, equipment and capitalized internal-use software included in accounts payable and accrued expenses in the condensed consolidated balance sheets were as follows:

<i>(in millions)</i>	Six Months Ended September 30,	
	2018	2017
Additions to pre-publication costs	\$ 4.4	\$ 5.7
Additions to property, equipment and capitalized internal-use software	—	1.2

During the six months ended September 30, 2017, the Company acquired and accrued \$16.4 million of author/content rights that were paid in the third quarter of fiscal year 2018.

13. RELATED PARTY TRANSACTIONS

Due to related party relationships, it is possible that the terms of certain of the Company's past transactions are not the same as those that would result from transactions among wholly unrelated parties.

The Company has a master services agreement ("MSA") and a master distribution and licensing agreement ("MDLA") currently in place with a former affiliate of Cengage Learning Holdings II, L.P. (the "Predecessor" of the Company), the terms of which were agreed upon at the time the Predecessor and the former affiliate were related parties. Under the MSA, the Company provides the former affiliate with various services including those relating to business and technology, content management, customers and operations, management, fulfillment services and business information support. The former affiliate provides the Company with certain real estate services. The cost of each of the services provided under the MSA is based on a fixed fee. All services under the MSA are provided for a specified period of time, subject to extension by mutual agreement of the parties. The former affiliate can generally terminate those services in advance upon 90 days written notice without penalty.

Under the MDLA, the former affiliate is the Company's exclusive authorized distributor for sale and/or distribution of most of its academic and professional digital and print publications in Canada. Subject to the Company's prior approval on a product by product basis, the former affiliate also has the exclusive right to adapt, customize and translate the Company's publications for sale and distribution in Canada. The agreement sets certain other restrictions on the use of the Company's content. The former affiliate is required by the agreement to pay the Company royalties as a percentage of net sales for certain specified publications, adaptations of its textbooks, translations of its textbooks and certain of its customized products. The agreement also requires the affiliate to pay fixed technology platform fees and variable technology unit fees.

The MSA was assumed by the Company upon emergence from Chapter 11 bankruptcy on March 31, 2014 and renewed on December 1, 2017 for a term that will end on March 31, 2021, unless otherwise renewed. The MDLA was also assumed by the Company on March 31, 2014, on the same term length, but was amended effective March 17, 2017, and will end on December 31, 2029, unless canceled by one of the parties. Both agreements may be terminated upon material breach, bankruptcy or the mutual agreement of the parties.

The Company's total revenues from the former affiliate were \$8.2 million and \$8.6 million for the three months ended September 30, 2018 and 2017 respectively, and \$11.0 million and \$11.5 million for the six months ended September 30, 2018 and 2017, respectively. Expenses incurred to the former affiliate were \$0.3 million and \$0.3 million for the three months ended September 30, 2018 and 2017, respectively, and \$0.8 million and \$0.8 million for the six months ended September 30, 2018 and 2017, respectively. Outstanding receivables and payables with the former affiliate as of September 30, 2018 were \$5.7 million and \$0.1 million, respectively. Outstanding receivables and payables with the former affiliate as of March 31, 2018 were \$1.7 million and \$0.3 million, respectively.

14. COMMITMENTS AND CONTINGENCIES

Claims, Disputes and Legal and Regulatory Actions

From time to time, the Company may become involved in various claims, disputes and legal or regulatory proceedings that arise in the ordinary course of business or that relate to contractual and other obligations. The Company assesses its potential contingent and other liabilities by analyzing claims, disputes and legal and regulatory matters using available information and develops its views on estimated losses in consultation with its legal and other advisors. The Company determines whether a loss from a contingency should be accrued by assessing whether a loss is deemed probable and can be

CENGAGE LEARNING HOLDINGS II, INC.
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reasonably estimated. If the contingency is not probable or cannot be reasonably estimated, disclosure of the contingency shall be made when there is at least a reasonable possibility that a material loss for which the Company is responsible may have been incurred.

Adverse developments relating to claims, disputes and legal and regulatory proceedings in which the Company is or becomes involved could cause a change in its determination as to an unfavorable outcome and result in the need to recognize a material accrual. Should any of these matters result in a final adverse judgment, settlement or other final resolution involving material amounts, it could have a material adverse effect on the Company's financial position, results of operations and cash flows.

Based on a review of the information available at this time, the Company does not expect the total cost of resolving all other current claims, disputes and legal and regulatory proceedings will have a material adverse effect on the condensed consolidated financial position, results of operations or cash flows.

Warranties

Under the Company's standard terms and conditions of sale, it warrants ownership of and/or licensing rights to its products and may provide certain other warranties and indemnifications. The Company is not aware of any instances that would result in any material payments being made as a result of these warranties and indemnifications, and therefore, no reserve has been recorded in the condensed consolidated financial statements.

15. SEGMENT INFORMATION

The Company's three operating segments, which are consistent with its reportable business segments are:

Learning—in the United States, the Company produces a variety of digital and print educational solutions and associated services for the academic, skills and school markets.

Gale—the Company offers research platforms around the world which provide access to its original content, collections of primary source materials and aggregated periodicals to learners at libraries, colleges, universities, schools and businesses.

International—the Company distributes educational solutions across all major academic disciplines, provides English language teaching ("ELT") products and adapts its Learning offerings for use in multiple countries and territories around the world.

The accounting policies applied by the segments are the same as those applied by the Company. All transactions between reportable segments are eliminated upon consolidation. The Company allocates its corporate and shared services costs to each of its segments using either number of employees, specific identification or activity, or revenue. The Company discloses information about its reportable segments based on the measures used in assessing the performance of those reportable segments. These measures are on a constant currency basis, which removes the impact of changes in foreign currency exchange rates. To calculate constant currency basis, the Company converts current period and prior period results from local currency to U.S. dollars using standard internal currency exchange rates held constant for each year. As needed, the Company recasts segment information for the prior period based on its internally-derived standard currency exchange rates used for the current period in order to remove the impact of foreign currency exchange fluctuation.

The Company uses Adjusted Revenues and Adjusted EBITDA less Pre-Publication Costs to measure the operating performance of its segments because it believes that these measures provide a meaningful basis for reviewing the results of operations by eliminating the effects of financing decisions, as well as excluding the impact of activities not related to its ongoing operating business. Adjusted Revenues is defined as revenues before the impact of changes in foreign currency exchange rates. Adjusted EBITDA less Pre-Publication Costs is defined as net income (loss) before: benefit from (provision for) income taxes; interest expense, net; loss on early extinguishment of debt, net; other (income) expense, net in operating income (loss); amortization of identifiable intangible assets; depreciation; operational restructuring and other charges, net; amortization of pre-publication costs; other income (expense), net, below operating income (loss); equity-based compensation expense and non-core other operating expenses in the accompanying condensed consolidated statements of operations, less additions to pre-publication costs on an accrual basis. This measure also removes the impact of changes in foreign currency exchange rates on the items noted above. By reducing Adjusted EBITDA by pre-publication costs, the Company includes the impact of re-investment within the segments, primarily for content.

CENGAGE LEARNING HOLDINGS II, INC.
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Segment Adjusted Revenues, which only includes revenues from external customers, and the reconciliation to total revenues per the condensed consolidated statements of operations is as follows:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017 ⁽¹⁾	2018	2017 ⁽¹⁾
Learning	\$ 343.3	\$ 385.4	\$ 524.3	\$ 570.4
Gale	49.3	49.2	100.3	103.6
International	85.4	88.9	143.2	147.5
Segment Adjusted Revenues	478.0	523.5	767.8	821.5
Impact of foreign currency	(3.7)	(1.1)	(5.2)	(3.1)
Total Revenues	\$ 474.3	\$ 522.4	\$ 762.6	\$ 818.4

⁽¹⁾ Prior year amounts have been recast to current year standard internal currency exchange rates.

Segment Adjusted EBITDA less Pre-Publication Costs and the reconciliation to net income (loss) per the condensed consolidated statements of operations is as follows:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017 ⁽¹⁾	2018	2017 ⁽¹⁾
Learning	\$ 121.7	\$ 152.0	\$ 120.6	\$ 166.7
Gale	10.1	11.2	19.6	25.3
International	18.4	26.5	19.6	33.2
Total Segment Adjusted EBITDA less Pre-Publication Costs	150.2	189.7	159.8	225.2
Additions to pre-publication costs ⁽²⁾	23.0	26.3	41.8	48.0
Impact of foreign currency	(1.0)	(0.4)	(1.4)	(0.9)
Equity-based compensation expense	(2.1)	(3.0)	(4.5)	(5.6)
Non-core other operating expenses ⁽³⁾	(1.7)	(0.4)	(4.1)	(1.7)
Amortization of pre-publication costs	(38.4)	(44.8)	(63.3)	(71.1)
Operational restructuring and other charges, net	(0.7)	(1.8)	(4.8)	(1.6)
Depreciation	(17.6)	(17.5)	(34.6)	(37.3)
Amortization of identifiable intangible assets	(23.7)	(23.6)	(47.4)	(46.9)
Other (expense) income, net	(0.1)	(1.3)	1.7	11.1
Interest expense, net	(43.3)	(39.9)	(85.5)	(79.0)
(Provision for) benefit from income taxes	(10.2)	(27.9)	8.2	(13.9)
Net income (loss)	\$ 34.4	\$ 55.4	\$ (34.1)	\$ 26.3

⁽¹⁾ Prior year amounts have been recast to current year standard internal currency exchange rates.

⁽²⁾ Additions to pre-publication costs are excluded from segment Adjusted EBITDA less Pre-Publication Costs on a constant currency and accrual basis. The impact of foreign currency exchange related to additions to pre-publication costs was approximately \$0.1 million in all periods presented.

⁽³⁾ For the three and six months ended September 30, 2018, non-core other operating expenses includes primarily bank fees, severance costs, duplicate rent expense, net, incurred during the build-out phase of the Company's new headquarters in Boston, consulting costs, and management fees. For the three and six months ended September 30, 2017, non-core operating expenses includes primarily bank fees, relocation costs, and management fees.

16. SUBSEQUENT EVENTS

There were no material subsequent events identified through November 7, 2018, the date these financial statements were issued.

CENGAGE LEARNING HOLDINGS II, INC.
Management's Discussion and Analysis of
Financial Condition and Results of Operations

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to facilitate an understanding of the results of operations and financial condition of Cengage Learning Holdings II, Inc. and its consolidated subsidiaries ("us," "we" and "our").

Overview

We are a leading global provider of high-quality content and innovative digital learning solutions for the global academic, school, skills and research markets. We are a publisher of course materials in the United States higher education segment of the academic market, with strong positions across all major disciplines. Our offerings to customers include technology and academic services, including digital homework solutions and support services for use of our digital products, in response to market demand for more fully integrated solutions. In addition, operating under our Gale brand, we are a leading global provider of library reference materials with a vast collection of primary source content.

In the second quarter of fiscal year 2019, we launched Cengage Unlimited, a digital subscription service offering for our U.S. higher education business within our Learning segment. Cengage Unlimited provides access to all of our digital learning platforms, ebooks, online homework and study tools as well as free print rentals for a fixed price that can be subscribed to for one semester, one year or two years.

Our operations are comprised of three reportable business segments:

Learning—in the United States, we produce a variety of digital and print educational solutions and associated services for the academic, skills and school markets.

Gale—we offer research platforms around the world which provide access to our original content, collections of primary source materials and aggregated periodicals to learners at libraries, colleges, universities, schools and businesses.

International—we distribute educational solutions across all major academic disciplines, provide English language teaching ("ELT") products and adapt our Learning offerings for use in multiple countries and territories around the world.

This MD&A is provided as a supplement to, and should be read in conjunction with, our condensed consolidated financial statements and the accompanying notes and our Annual Report for the fiscal year ended March 31, 2018 (the "2018 Annual Report"). The following discussion and analysis of our financial condition and results of operations may contain forward-looking statements about our business, operations and industry that involve risks and uncertainties, such as statements regarding our plans, objectives, expectations and intentions. Our future results and financial condition may differ materially from those we currently anticipate. See "Special Note Regarding Forward-Looking Statements" earlier in this report. We refer to our fiscal year ended March 31, 2018, as fiscal year 2018, and fiscal year ended March 31, 2019, as fiscal year 2019.

Management reviews segment performance on a constant currency basis, which removes the impact of changes in foreign currency exchange rates by converting current period and prior period amounts from local currency to U.S. dollars using standard internal currency exchange rates held constant for each year. This allows us to evaluate underlying current operating performance in comparison to past operating performance. As needed, we recast segment information for the prior period based on our internally-derived standard currency exchange rates used for the current period in order to remove the impact of foreign currency exchange fluctuation.

To supplement our condensed consolidated financial statements presented in accordance with accounting principles generally accepted in the United States of America ("GAAP"), we have presented certain non-GAAP financial measures in addition to our GAAP results. We believe that these non-GAAP financial measures provide useful information for evaluating our business performance. We believe that the presentation of Adjusted Revenues and Adjusted EBITDA is appropriate to provide additional information to investors about certain material non-cash items and about unusual items that we do not expect to continue at the same level in the future as well as other items. Further, we believe Adjusted EBITDA provides a meaningful measure of operating profitability because we use it for evaluating our business performance and understanding certain significant items. This information should be considered as supplemental in nature and should not be considered in isolation or as a substitute for the related financial information prepared in accordance with GAAP. In addition, these non-GAAP financial measures may not be the same as similarly entitled measures reported by other companies.

Our definition of Adjusted EBITDA allows us to add back certain non-cash and other charges or costs that are deducted in calculating net income from continuing operations. However, these are expenses that may recur, vary greatly and can be difficult to predict. They can represent the effect of long-term strategies as opposed to short-term results. In addition, certain of these expenses can represent the reduction of cash that could be used for other corporate purposes.

CENGAGE LEARNING HOLDINGS II, INC.
Management's Discussion and Analysis of
Financial Condition and Results of Operations

We present the following non-GAAP financial measures in this report:

Measure	Definition
Adjusted Revenues	This measure is defined as revenues before the impact of changes in foreign currency exchange rates.
Adjusted EBITDA	This measure is defined as net income (loss) before: (benefit from) provision for income taxes; interest expense, net; loss on early extinguishment of debt, net; other (income) expense, net, in operating income (loss); amortization of identifiable intangible assets; depreciation; operational restructuring and other charges, net; amortization of pre-publication costs; other income (expense), net, below operating income (loss); equity-based compensation expense and non-core other operating expenses. This measure also removes the impact of changes in foreign currency exchange rates on the items noted above.
Adjusted EBITDA less Pre-Publication Costs	This measure reflects Adjusted EBITDA less additions to pre-publication costs on an accrual basis, which are costs incurred prior to the publication date of a title or release date of a product and represent activities associated with product development not limited to editorial review and fact verification, graphic art design and layout and the process of conversion from print to digital media or within various formats of digital media. In addition, pre-publication costs include the cost to procure perpetual rights for the use of content which have been developed by third parties and are to be included in our products. Costs are capitalized when the title is expected to generate probable future economic benefits and are amortized upon publication of the title over its estimated operating life cycle.
Adjusted EBITDA less Capital Expenditures	This measure reflects Adjusted EBITDA less additions to pre-publication costs and property, equipment and capitalized internal-use software on an accrual basis.

See "Reconciliations of Non-GAAP Financial Measures" for reconciliations to the most directly comparable financial measures prepared in accordance with GAAP.

Seasonality and Comparability

Our revenues, operating profit and operating cash flows are impacted by the inherent seasonality of the academic calendar. This seasonality affects our working capital requirements and hence our overall financing needs. For example, we typically incur a net cash deficit from all of the activities in our first and fourth quarters of our fiscal year which ends on March 31. In addition, changes in our customers' ordering patterns may impact the comparison of our results in a quarter with the same quarter of the previous year, or in a fiscal year with the prior fiscal year, where our customers may shift the timing of material orders for a number of reasons, including, but not limited to, changes in academic semester start dates or changes in inventory management practices.

As we continue to migrate our service offerings towards hosted digital solutions that are delivered over a period of time, the associated revenues will be recognized ratably over the applicable subscription period, with amounts billed in excess of revenues recognized reflected as deferred revenue. Deferred revenue represents amounts billed in advance from our customers that will be recognized as revenues in subsequent periods as products and services are delivered to customers. The current portion of deferred revenue was \$259.8 million and \$178.9 million as of September 30, 2018 and March 31, 2018, respectively, and the non-current portion of deferred revenue was \$40.6 million and \$30.9 million as of September 30, 2018 and March 31, 2018, respectively.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Although these estimates are based on management's best knowledge of current events and actions that we may undertake in the future, actual results could differ from those estimates. These estimates include, but are not limited to, reserves for sales returns and inventory obsolescence, the allowance for doubtful accounts, deferred tax assets and liabilities, the valuation allowances for deferred tax assets, operational restructuring and other charges, legal and tax contingencies, purchase accounting and equity-based compensation, as well as future cash flows and fair values used in the assessment of the realizability of long-lived assets, goodwill and identifiable intangible assets.

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Operational Restructuring and Other Charges

Fiscal Year 2019

During the first quarter of fiscal year 2019, we initiated a restructuring program in our Gale and International segments to better align our operations to current market conditions and position the business for growth. During the six months ended September 30, 2018, we incurred \$4.2 million of severance related costs in connection with this program.

During the second quarter of fiscal year 2019, we initiated a restructuring program in our Learning segment to streamline our operations and we incurred \$0.6 million of severance related costs in connection with this program.

Fiscal Year 2018

During the first quarter of fiscal year 2018, we initiated a restructuring program related to our initiatives to better align discipline and delivery strategies, to improve the development and enhancements of its digital products and assess our operations, and to further support the shift from a textbook to a software sales and support model. We incurred \$1.5 million of severance related costs in the six months ended September 30, 2017 and aggregate charges of \$3.4 million of severance related costs during fiscal year 2018. As of September 30, 2017, we had incurred aggregate charges of \$6.2 million of process reengineering consulting costs and during the remainder of fiscal year 2018 incurred an additional \$1.2 million of process reengineering consulting costs. These charges were expensed as incurred.

Also during the first quarter of fiscal year 2018, we exited an existing lease and ceased use of the space. As a result, we recorded a \$3.5 million non-cash charge to write-off the existing landlord inducement liability. In connection with exiting the existing space, we received a \$12.0 million incentive payment from a third party that was included in other (expense) income, net in the accompanying condensed consolidated statement of operations.

In the remainder of fiscal year 2018, we vacated two additional offices and recorded \$4.0 million of charges, net of non-cash write-offs and net of sublease estimates with remaining lease payments to be paid over the underlying remaining lease terms. Additionally, we initiated a restructuring program to better align our operations to current market conditions and in anticipation of our continued shift to a subscription/digital model resulting in a total of \$2.3 million of severance related costs in our Learning and International segments.

Additional information on operational restructuring and other charges is provided in Note 6, "Operational Restructuring and Other Charges" to our condensed consolidated financial statements.

Critical Accounting Policies

There were no significant changes to our critical accounting policies during the three and six months ended September 30, 2018. For further information on our critical accounting policies, refer to our 2018 Annual Report.

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Financial Performance

Consolidated Results of Operations

The Three and Six Months Ended September 30, 2018 Compared with September 30, 2017

<i>(in millions)</i>	Three Months Ended September 30,		Change		Six Months Ended September 30,		Change	
	2018	2017	\$	%	2018	2017	\$	%
Revenues	\$ 474.3	\$ 522.4	\$(48.1)	(9.2)%	\$ 762.6	\$ 818.4	\$ (55.8)	(6.8)%
Cost of revenues, excluding amortization of pre-publication costs and identifiable intangible assets and depreciation stated below	188.9	198.6	(9.7)	(4.9)%	337.2	338.4	(1.2)	(0.4)%
Amortization of pre-publication costs	38.4	44.8	(6.4)	(14.3)%	63.3	71.1	(7.8)	(11.0)%
Amortization of identifiable intangible assets	1.2	1.0	0.2	20.0 %	2.4	1.8	0.6	33.3 %
Total cost of revenues, excluding depreciation stated below	228.5	244.4	(15.9)	(6.5)%	402.9	411.3	(8.4)	(2.0)%
Selling, general and administrative expenses, excluding depreciation stated below	117.0	111.6	5.4	4.8 %	233.8	215.0	18.8	8.7 %
Operational restructuring and other charges, net	0.7	1.8	(1.1)	(61.1)%	4.8	1.6	3.2	200.0 %
Depreciation	17.6	17.5	0.1	0.6 %	34.6	37.3	(2.7)	(7.2)%
Amortization of identifiable intangible assets	22.5	22.6	(0.1)	(0.4)%	45.0	45.1	(0.1)	(0.2)%
Other income, net	—	—	—	NM	—	(0.2)	0.2	(100.0)%
Total costs and expenses	386.3	397.9	(11.6)	(2.9)%	721.1	710.1	11.0	1.5 %
Operating income	88.0	124.5	(36.5)	(29.3)%	41.5	108.3	(66.8)	(61.7)%
Other (expense) income, net	(0.1)	(1.3)	1.2	(92.3)%	1.7	10.9	(9.2)	(84.4)%
Interest income	0.9	0.5	0.4	80.0 %	1.8	1.0	0.8	80.0 %
Interest expense	(44.2)	(40.4)	(3.8)	9.4 %	(87.3)	(80.0)	(7.3)	9.1 %
Income (loss) before taxes	44.6	83.3	(38.7)	(46.5)%	(42.3)	40.2	(82.5)	(205.2)%
(Provision for) benefit from income taxes	(10.2)	(27.9)	17.7	(63.4)%	8.2	(13.9)	22.1	(159.0)%
Net income (loss)	<u>\$ 34.4</u>	<u>\$ 55.4</u>	<u>\$(21.0)</u>	(37.9)%	<u>\$ (34.1)</u>	<u>\$ 26.3</u>	<u>\$ (60.4)</u>	(229.7)%
Adjusted Revenues ⁽¹⁾⁽²⁾	\$ 478.0	\$ 523.5	\$(45.5)	(8.7)%	\$ 767.8	\$ 821.5	\$ (53.7)	(6.5)%
Adjusted EBITDA ⁽¹⁾⁽²⁾	\$ 173.2	\$ 216.0	\$(42.8)	(19.8)%	\$ 201.6	\$ 273.2	\$ (71.6)	(26.2)%
Adjusted EBITDA less Pre- Publication Costs ⁽¹⁾⁽²⁾	\$ 150.2	\$ 189.7	\$(39.5)	(20.8)%	\$ 159.8	\$ 225.2	\$ (65.4)	(29.0)%
Adjusted EBITDA less Capital Expenditures ⁽¹⁾⁽²⁾	\$ 137.9	\$ 177.3	\$(39.4)	(22.2)%	\$ 133.3	\$ 201.7	\$ (68.4)	(33.9)%

(1) See "Overview" for the definition of this non-GAAP financial measure, "Segment Operating Results" for discussion and "Reconciliations of Non-GAAP Financial Measures" for reconciliations to the most directly comparable financial measures prepared in accordance with GAAP.

(2) Prior year amounts have been recast to current year standard internal currency exchange rates.

NM = Not meaningful

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The Three Months Ended September 30, 2018 Compared with September 30, 2017

Revenues

Revenues for the three months ended September 30, 2018 decreased \$48.1 million, or 9.2%, to \$474.3 million, compared to the prior year period. The decrease was primarily due to a \$42.1 million decrease in the Learning segment largely related to the decline of new print textbook sales and higher deferred revenue related to growth in digital product sales, primarily related to Cengage Unlimited subscriptions, partially offset by revenue share from our rental partnerships, a \$3.5 million decline in the International segment, and unfavorable foreign exchange fluctuations of approximately \$2.6 million.

Costs and Expenses

Total cost of revenues, excluding depreciation for the three months ended September 30, 2018 decreased \$15.9 million, or 6.5%, compared to the prior year period. The decrease was primarily due to a \$3.1 million decrease in paper, print and bind, a \$13.3 million decrease in royalty expense primarily related to lower sales, an increased shift to digital product sales, and the acquisition of author/content rights in fiscal year 2018, a \$2.1 million decrease in distribution related expense, and a \$0.7 million decrease in software development. Additionally, amortization of pre-publication costs decreased \$6.4 million primarily related to the accelerated amortization of certain assets in fiscal year 2018 and a decrease in prepublication spend. These decreases were partially offset by a \$6.8 million increase in employee compensation and related costs associated with our key strategic investments in higher education digital product teams and infrastructure, including those related to Cengage Unlimited, a \$1.1 million increase in inventory obsolescence, and a \$2.4 million increase primarily related to enterprise-wide technology investments to support digital growth. Additionally, amortization of intangible assets increased \$0.2 million related to the acquisition of certain author/content rights in fiscal year 2018.

Selling, general and administrative expenses, excluding depreciation increased \$5.4 million, or 4.8%, to \$117.0 million for the three months ended September 30, 2018, primarily due to a \$2.8 million increase in sales and marketing costs primarily related to Cengage Unlimited, a \$2.8 million increase in outside service fees, and a \$1.0 million increase in rent expense, net, incurred during the build-out phase of our new headquarters in Boston. These increases were partially offset by a \$1.0 million decrease in employee compensation related costs.

Operational restructuring and other charges, net was \$0.7 million in the three months ended September 30, 2018. The \$0.7 million, net, is primarily related to severance costs incurred under the restructuring program in our Learning segment. Charges in the prior year period of \$1.8 million includes \$0.9 million of severance costs, \$0.5 million process reengineering consulting fees, and \$0.4 million of lease exit and other costs.

Depreciation increased \$0.1 million, or 0.6%, during the three months ended September 30, 2018, primarily related to certain assets that were placed in service, partially offset by a decrease related to certain assets becoming fully depreciated.

Amortization of identifiable intangible assets was \$22.5 million and \$22.6 million for the three months ended September 30, 2018 and 2017, respectively.

Non-Operating Items

Other (expense) income, net for the three months ended September 30, 2018 and 2017 was an expense of \$0.1 million and \$1.3 million, respectively, primarily related to foreign currency transaction losses.

Interest expense increased \$3.8 million, or 9.4%, to \$44.2 million for the three months ended September 30, 2018, primarily due to an increase in the LIBOR rate applicable to our Term Loan.

Benefit from income taxes was \$10.2 million and \$27.9 million for the three months ended September 30, 2018 and 2017, respectively, with a corresponding effective income tax rate of 22.9% and 33.5%, respectively. The decrease in the effective tax rate was almost entirely attributable to the enactment of the U.S. federal tax law changes in the third quarter of fiscal year 2018 under the Tax Cuts and Jobs Act of 2017 (the "Tax Act"), which lowered the corporate tax rate in the United States from 35% to 21%.

The Six Months Ended September 30, 2018 Compared with September 30, 2017

Revenues

Revenues for the six months ended September 30, 2018 decreased \$55.8 million, or 6.8%, to \$762.6 million. The decline was primarily due to lower revenues from our Learning segment, which decreased \$46.1 million, compared with the prior year period. The decrease in Learning revenue was primarily related to the decline of new print textbook sales, partially offset by an increase in core digital product sales and revenue share from our rental partnerships. Additionally, the International

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segment declined \$4.3 million primarily related to lower sales of higher education products and the Gale segment declined \$3.3 million primarily related to a decrease driven by lower sales from a large customer in Latin America.

Costs and Expenses

Total cost of revenues, excluding depreciation decreased \$8.4 million, or 2.0% during the six months ended September 30, 2018, primarily due to a \$2.2 million decrease in paper, print and bind, a \$13.3 million decrease in royalty expense primarily related to lower sales, an increased shift to digital product sales, and the acquisition of author/ content rights in fiscal year 2018, a \$1.6 million decrease in distribution related expenses, and a \$0.9 million decrease in inventory obsolescence. Additionally, amortization of pre-publication costs decreased \$7.8 million primarily related to the accelerated amortization of certain assets in fiscal year 2018 and a decrease in prepublication spend. These decreases were partially offset by a \$12.5 million increase in employee compensation and related costs associated with our key strategic investments in higher education digital product teams and infrastructure, including those related to Cengage Unlimited, a \$1.0 million increase in software development costs, and a \$4.0 million increase primarily related to enterprise-wide technology investments to support digital growth. Additionally, amortization of intangible assets increased \$0.6 million related to the acquisition of certain author/content rights in fiscal year 2018.

Selling, general and administrative expenses, excluding depreciation increased \$18.8 million, or 8.7%, to \$233.8 million for the six months ended September 30, 2018, primarily due to a \$8.2 million increase in employee compensation and other related costs to support our key strategic initiatives. In addition, there was a \$3.6 million increase in outside services fees, a \$1.6 million increase in rent expense, net, incurred during the build-out phase of our new headquarters in Boston, and a \$4.7 million increase in sales and marketing expenses primarily related to Cengage Unlimited.

Operational restructuring and other charges, net increased \$3.2 million to \$4.8 million in the six months ended September 30, 2018. The \$4.8 million charges, net, is primarily related to \$4.2 million of severance costs incurred under the restructuring program for our Gale segment and \$0.6 million of severance costs incurred under the restructuring program for our Learning segment. Charges, net, in the prior period of \$1.6 million included \$3.4 million related to process reengineering consulting fees and \$1.5 million of severance costs as well as a \$3.5 million non-cash write-off of a lease inducement liability in connection with the termination of an existing lease.

Depreciation decreased \$2.7 million, or 7.2%, during the six months ended September 30, 2018, primarily related to certain assets becoming fully depreciated, partially offset by an increase in depreciation on assets that were placed in service.

Amortization of identifiable intangible assets was \$45.0 million and \$45.1 million for the six months ended September 30, 2018 and 2017, respectively.

Non-Operating Items

Other (expense) income, net was \$1.7 million and \$10.9 million for the six months ended September 30, 2018 and 2017, respectively. Other income in the current period was due to foreign currency transaction gains. Other income in the prior year period was primarily related to an incentive payment received from a third party in connection with exiting an existing facility, partially offset by foreign currency transaction losses.

Interest expense increased \$7.3 million, or 9.1%, to \$87.3 million for the six months ended September 30, 2018, primarily due to an increase in the LIBOR rate applicable to our Term Loan.

Benefit from (provision for) income taxes was a benefit of \$8.2 million for the six months ended September 30, 2018, compared with a provision of \$13.9 million for the six months ended September 30, 2017. The current year benefit is directly attributable to a pre-tax loss during the six months ended September 30, 2018 compared to pre-tax income in the same prior year period.

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Segment Operating Results

The Three and Six Months Ended September 30, 2018 Compared with September 30, 2017

(in millions)	Three Months Ended September 30,		Change		Six Months Ended September 30,		Change	
	2018	2017 ⁽¹⁾	\$	%	2018	2017 ⁽¹⁾	\$	%
Adjusted Revenues ⁽²⁾								
Learning	\$ 343.3	\$ 385.4	\$ (42.1)	(10.9)%	\$ 524.3	\$ 570.4	\$ (46.1)	(8.1)%
Gale	49.3	49.2	0.1	0.2 %	100.3	103.6	(3.3)	(3.2)%
International	85.4	88.9	(3.5)	(3.9)%	143.2	147.5	(4.3)	(2.9)%
Total	\$ 478.0	\$ 523.5	\$ (45.5)	(8.7)%	\$ 767.8	\$ 821.5	\$ (53.7)	(6.5)%
Adjusted EBITDA ⁽²⁾⁽³⁾								
Learning	\$ 133.3	\$ 166.2	\$ (32.9)	(19.8)%	\$ 141.4	\$ 192.7	\$ (51.3)	(26.6)%
Gale	15.4	17.1	(1.7)	(9.9)%	30.2	37.4	(7.2)	(19.3)%
International	24.5	32.7	(8.2)	(25.1)%	30.0	43.1	(13.1)	(30.4)%
Total	\$ 173.2	\$ 216.0	\$ (42.8)	(19.8)%	\$ 201.6	\$ 273.2	\$ (71.6)	(26.2)%
Adjusted EBITDA less Pre-Publication Costs ⁽²⁾⁽³⁾								
Learning	\$ 121.7	\$ 152.0	\$ (30.3)	(19.9)%	\$ 120.6	\$ 166.7	\$ (46.1)	(27.7)%
Gale	10.1	11.2	(1.1)	(9.8)%	19.6	25.3	(5.7)	(22.5)%
International	18.4	26.5	(8.1)	(30.6)%	19.6	33.2	(13.6)	(41.0)%
Total	\$ 150.2	\$ 189.7	\$ (39.5)	(20.8)%	\$ 159.8	\$ 225.2	\$ (65.4)	(29.0)%
Adjusted EBITDA less Capital Expenditures ⁽²⁾⁽³⁾								
Learning	\$ 111.8	\$ 141.7	\$ (29.9)	(21.1)%	\$ 98.7	\$ 146.4	\$ (47.7)	(32.6)%
Gale	8.6	10.0	(1.4)	(14.0)%	16.8	23.3	(6.5)	(27.9)%
International	17.5	25.6	(8.1)	(31.6)%	17.8	32.0	(14.2)	(44.4)%
Total	\$ 137.9	\$ 177.3	\$ (39.4)	(22.2)%	\$ 133.3	\$ 201.7	\$ (68.4)	(33.9)%

(1) Prior year amounts have been recast to current year standard internal currency exchange rates.

(2) See "Overview" for the definition of this Non-GAAP financial measure and "Reconciliations of Non-GAAP Financial Measures" for reconciliations to the most directly comparable financial measures prepared in accordance with GAAP.

(3) We allocate our corporate and shared services costs to each of our segments using either number of employees, specific identification or activity, or revenue.

The Three Months Ended September 30, 2018 Compared with September 30, 2017

Learning Adjusted Revenues for the three months ended September 30, 2018 decreased \$42.1 million, or 10.9%, primarily due to lower sales into the school channel and continued secular decline of new print textbook sales in higher education, as well as an increase in deferred revenue growth of Cengage Unlimited subscriptions, partially offset by an increase in revenue share from our rental partnerships.

Gale Adjusted Revenues for the three months ended September 30, 2018 increased \$0.1 million, or 0.2%, primarily driven by an increase in archive sales in the International markets, partially offset by the continued print decline in the U.S.

International Adjusted Revenues for the three months ended September 30, 2018 decreased \$3.5 million, or 3.9%, primarily due to a decrease in the sales of higher education products in Australia and lower sales from a large customer in EMEA, partially offset by sales growth of ELT products in Latin America.

Learning Adjusted EBITDA less Pre-Publication Costs for the three months ended September 30, 2018 decreased \$30.3 million, or 19.9%, due to the contribution of lower Learning Adjusted Revenues and increases in costs primarily driven by our key strategic initiatives including investments in our school and on-line skills businesses and digital transformation, primarily Cengage Unlimited. These decreases were partially offset by lower print, paper, and bind expense and royalty expense. In addition, the increased investment in infrastructure was attributed and allocated to the operating segment.

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Gale Adjusted EBITDA less Pre-Publication Costs for the three months ended September 30, 2018 decreased \$1.1 million, or 9.8%, due to an increase in investments in infrastructure that was attributed and allocated to the operating segment, partially offset by timing of spending on pre-publication costs.

International Adjusted EBITDA less Pre-Publication Costs for the three months ended September 30, 2018 decreased \$8.1 million, or 30.6%, due to the contribution of lower International Adjusted Revenues and strategic investment initiatives in the expansion of go-to-market teams as well as operating investments across Asia, EMEA and Australia. In addition, there was an increase in investments in infrastructure that was attributed and allocated to the operating segment.

The Six Months Ended September 30, 2018 Compared with September 30, 2017

Learning Adjusted Revenues for the six months ended September 30, 2018 decreased \$46.1 million, or 8.1%, primarily due to lower sales into the school channel and continued secular decline of new print textbook sales in higher education, as well as an increase in deferred revenue growth of Cengage Unlimited subscriptions, partially offset by an increase in revenue share from our rental partnerships.

Gale Adjusted Revenues for the six months ended September 30, 2018 decreased \$3.3 million, or 3.2%, primarily driven by lower sales from a large customer in Latin America and the continued print decline in the U.S., partially offset by increased archive sales in the International markets.

International Adjusted Revenues for the six months ended September 30, 2018 decreased \$4.3 million, or 2.9%, primarily due to a decrease in the sales of higher education products in Australia and lower sales from a large customer in EMEA, partially offset by sales growth of ELT products in Latin America and higher education products in EMEA and Asia.

Learning Adjusted EBITDA less Pre-Publication Costs for the six months ended September 30, 2018 decreased \$46.1 million, or 27.7%, to \$120.6 million due to the contribution of lower Learning Adjusted Revenues and increases in costs primarily driven by our key strategic initiatives including investments in our school and on-line skills businesses and digital transformation, primarily Cengage Unlimited. These decreases were partially offset by lower print, paper, and bind expense, royalty expense, and a reduction in pre-publication spend. In addition, the increased investment in infrastructure was attributed and allocated to the operating segment.

Gale Adjusted EBITDA less Pre-Publication Costs for the six months ended September 30, 2018 decreased \$5.7 million, or 22.5%, primarily due to the flow through of decreased Gale Adjusted Revenue and an increase in investments in infrastructure that was attributed and allocated to the operating segment, partially offset by timing of spending on pre-publication costs.

International Adjusted EBITDA less Pre-Publication Costs for the six months ended September 30, 2018 decreased \$13.6 million, or 41.0% due to the contribution of lower International Adjusted Revenues and strategic investments in the expansion of go-to-market teams, operations support, and ELT pre-publications costs. In addition, there was an increase in investments in infrastructure that was attributed and allocated to the operating segment.

Reconciliations of Non-GAAP Financial Measures

The following table reconciles revenues to Adjusted Revenues:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017⁽¹⁾	2018	2017⁽¹⁾
Revenues	\$ 474.3	\$ 522.4	\$ 762.6	\$ 818.4
Impact of foreign currency	3.7	1.1	5.2	3.1
Adjusted Revenues	\$ 478.0	\$ 523.5	\$ 767.8	\$ 821.5

⁽¹⁾ Prior year amounts have been recast to current year standard internal currency exchange rates.

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The following table reconciles net income (loss) to Adjusted EBITDA, Adjusted EBITDA less Pre-Publication Costs and Adjusted EBITDA less Capital Expenditures:

<i>(in millions)</i>	Three Months Ended September 30,		Six Months Ended September 30,	
	2018	2017 ⁽¹⁾	2018	2017 ⁽¹⁾
Net income (loss)	\$ 34.4	\$ 55.4	\$ (34.1)	\$ 26.3
Impact of foreign currency	1.0	0.4	1.4	0.9
Equity-based compensation expense	2.1	3.0	4.5	5.6
Non-core other operating expenses ⁽²⁾	1.7	0.4	4.1	1.7
Amortization of pre-publication costs	38.4	44.8	63.3	71.1
Operational restructuring and other charges, net	0.7	1.8	4.8	1.6
Depreciation	17.6	17.5	34.6	37.3
Amortization of identifiable intangible assets	23.7	23.6	47.4	46.9
Other expense (income), net	0.1	1.3	(1.7)	(11.1)
Interest expense, net	43.3	39.9	85.5	79.0
Provision for (benefit from) income taxes	10.2	27.9	(8.2)	13.9
Adjusted EBITDA	173.2	216.0	201.6	273.2
Additions to pre-publication costs ⁽³⁾	(23.0)	(26.3)	(41.8)	(48.0)
Adjusted EBITDA less Pre-Publication Costs	150.2	189.7	159.8	225.2
Additions to property, equipment and capitalized internal-use software ⁽³⁾	(12.3)	(12.4)	(26.5)	(23.5)
Adjusted EBITDA less Capital Expenditures	\$ 137.9	\$ 177.3	\$ 133.3	\$ 201.7

⁽¹⁾ Prior year amounts have been recast to current year standard internal currency exchange rates.

⁽²⁾ For the three and six months ended September 30, 2018, non-core other operating expenses includes primarily bank fees, severance costs, duplicate rent expense, net, incurred during the build-out phase of our new headquarters in Boston, consulting costs, and management fees. For the three and six months ended September 30, 2017, non-core operating expenses includes primarily bank fees, relocation costs, and management fees.

⁽³⁾ Additions to pre-publication costs and property, equipment and capitalized internal-use software are excluded from segment Adjusted EBITDA less Pre-Publication Costs and Adjusted EBITDA less Capital Expenditures on a constant currency basis and accrual basis. The impact of foreign currency exchange related to additions to pre-publication and additions to property, equipment and capitalized internal-use software costs were immaterial in both the three and six months ended September 30, 2018 and 2017.

Liquidity and Capital Resources

<i>(in millions)</i>	As of	
	September 30, 2018	March 31, 2018
Cash and cash equivalents	\$ 274.9	\$ 319.3
Current portion of long-term debt	15.2	6.7
Long-term debt	2,239.8	2,244.9

Our principal sources of liquidity have historically been cash flows from operations and borrowings under our revolving credit facilities. Since our cash flows from operations are impacted by the inherent seasonality of our business whereby we typically generate operating cash during the second and third quarters of our fiscal year and utilize cash for operating activities throughout the first and fourth quarters of our fiscal year, the borrowings under our revolving credit facility may vary accordingly.

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Our principal uses of cash are to fund operating costs and capital expenditures, including investments in product and technology offerings, strategic acquisitions, the payment of interest and principal on our outstanding debt, and share repurchases. We expect our cash flows from operations, combined with availability under our revolving credit facility, to provide sufficient liquidity to fund our current obligations, debt service requirements, share repurchase program, projected working capital requirements, restructuring obligations, and capital spending over the next twelve months. In February 2017, our board of directors approved an authorization of up to \$100 million to purchase in the open market our 9.50% senior notes and/or senior secured term loan.

Share Repurchase Programs

On June 6, 2017, we announced the authorization to extend our current \$65.0 million share repurchase program until May 31, 2018. Under this program, \$15.8 million was paid in the first quarter of fiscal year 2018 and \$45.1 million was paid in the second quarter of fiscal year 2018. As of September 30, 2017, we completed this program, repurchasing 7,259,913 shares for \$65.0 million in the aggregate.

Long-term Debt

On June 7, 2016, Cengage Learning, Inc., our wholly owned subsidiary, issued senior notes ("Senior Notes") and amended and restated its senior secured term loan facility ("Term Loan") and its asset based lending revolving line of credit ("ABL Revolving Credit Facility").

Senior Notes

On June 7, 2016, Cengage Learning, Inc., our wholly owned subsidiary, issued \$620.0 million aggregate principal amount Senior Notes in a private placement, maturing June 15, 2024. The Senior Notes bear interest at a rate of 9.50% per annum, payable semi-annually in arrears on June 15 and December 15 of each year. Cengage Learning, Inc. has the option to redeem the Senior Notes, in whole or in part, at any time on or before June 15, 2019, equal to 100% of the principal amount of the notes plus an applicable premium and accrued interest, as defined in the indenture. We also have the option to redeem the Senior Notes, in whole or in part, at any time on or after June 15, 2019, at certain redemption prices as defined in the indenture. In addition, under the terms of the Senior Notes we may repurchase the Senior Notes in part, at any time, in the open market, in accordance with federal securities regulations.

All material, wholly owned domestic subsidiaries of Cengage Learning, Inc., subject to certain exceptions, will guarantee the Senior Notes, up to applicable legal limits. To date, there are no subsidiary guarantors of the Senior Notes.

The indenture related to the Senior Notes contains certain covenants that we may be subject to which restrict our and our subsidiaries' ability to, among other things: incur additional indebtedness or issue certain disqualified shares and preferred shares; create liens; pay dividends or distributions or redeem or repurchase equity; prepay subordinated debt or make certain investments; transfer and sell assets; engage in a consolidation or merger or sell, transfer or otherwise dispose of all or substantially all of our assets; and enter into certain transactions with affiliates. We will not be subject to these covenants if (i) the Senior Notes have Investment Grade Ratings from the relevant rating agencies, as defined in the terms of the Senior Notes, and (ii) no default has occurred and is continuing under the indenture. As of September 30, 2018, no default has occurred and we are compliant with all of the covenants of the indenture.

Term Loan

The Term Loan provides for senior secured term loans in an aggregate principal amount of \$1,710.0 million and matures on June 7, 2023. In addition, we may request one or more incremental credit facilities in an aggregate amount of up to \$500.0 million, plus additional amounts subject to certain requirements. Borrowings under the Term Loan bear interest at a rate equal to, at our option, either (a) a LIBOR rate determined by reference to the costs of funds for Eurodollar deposits for the interest period relevant to such borrowing, adjusted for certain additional costs, subject to a 1.00% floor ("Eurocurrency Rate Loan"), or (b) a base rate determined by reference to the highest of (i) the federal funds rate plus 0.50%, (ii) the prime rate and (iii) the one-month adjusted LIBOR rate plus 1.00%, in each case plus an applicable margin. As of September 30, 2018, we elected to carry the Term Loan as a Eurocurrency Rate Loan with an effective interest rate of 6.42%.

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We are required to repay 0.25% of the original principal amount of the Term Loan on the last business day of each quarter. Following the end of each fiscal year, we must prepay a percentage between 0% and 50%, based on our total leverage ratio, of our Excess Cash Flow, as defined in the Term Loan agreement, within five business days after delivery of the financial statements. Prepayments made under the Excess Cash Flow provision are used to satisfy prospective mandatory quarterly principal repayments. We are also required to prepay loans with net proceeds from asset sales, casualty events, or issuances of indebtedness, subject to, in the case of asset sales and casualty events, reinvestment rights by us within certain time restrictions. In accordance with the Excess Cash Flow provisions of the Term Loan facility, there was no prepayment due for fiscal year 2018 and we made a \$27.7 million principal payment for fiscal year 2017 in June 2017. We may prepay or repurchase the Term Loan, in whole or in part, at any time, without penalty.

The obligations under the Term Loan are unconditionally guaranteed by Cengage Learning Holdco, Inc., a Delaware corporation, on a limited recourse basis, and all of our direct and indirect material, wholly owned domestic restricted subsidiaries, subject to certain exceptions. The obligations will be secured by (i) second-priority security interests in all accounts receivable, loans receivable, other receivables, inventory, related books and records, certain related general intangibles (excluding intellectual property and equity interests), deposit accounts (other than deposit accounts holding solely proceeds of Non-ABL priority collateral (as defined below)), cash and proceeds of the foregoing of Cengage Learning, Inc. and each subsidiary guarantor (collectively, the "ABL priority collateral"), with the ABL Revolving Credit Facility secured by first-priority security interests therein, and (ii) first-priority security interests in substantially all assets of Cengage Learning, Inc. and each subsidiary guarantor, in each case whether owned on the closing date or thereafter acquired, other than the ABL priority collateral, including a pledge of our capital stock (prior to an IPO), the capital stock of future subsidiary guarantors and 65% of the voting capital stock of first-tier foreign subsidiaries that are not subsidiary guarantors, in each case subject to exceptions (collectively, the "Non-ABL priority collateral"), with the ABL Revolving Credit Facility secured by second-priority security interests therein.

The Term Loan agreement contains certain customary conditions to borrowing, restrictions, affirmative covenants, negative covenants and events of default. The Term Loan does not contain any financial maintenance covenants.

ABL Revolving Credit Facility

The availability of credit under the amended and restated five-year ABL Revolving Credit Facility, which expires on June 7, 2021, is equal to the lesser of (i) \$250.0 million and (ii) our borrowing base. The borrowing base equals the sum of (i) 90% of eligible credit card receivables, plus (ii) 85% of eligible receivables, plus (iii) 85% of the orderly liquidation value of eligible inventory, plus (iv) 100% of cash not to exceed \$35.0 million. As of September 30, 2018 and March 31, 2018, the ABL Revolving Credit Facility had no outstanding borrowings and \$22.3 million and \$22.6 million, respectively, in issued and outstanding letters of credit. Our available borrowing base as of September 30, 2018, which is based on the balance sheet at August 31, 2018, was \$227.7 million, net of letters of credit.

The unused commitment fee will range between 0.25% and 0.375%, based upon the average facility usage for the most recently ended fiscal quarter. Outstanding letters of credit are also subject to a quarterly letter of credit participation fee which will vary between 1.75% and 2.25%, depending on the average daily availability. For both the three and six months ended September 30, 2018 and 2017, the commitment and participation fees were insignificant.

We have the right to prepay outstanding borrowings under the ABL Revolving Credit Facility, in whole or in part, from time to time, without premium or penalty.

The obligations under the ABL Revolving Credit Facility are unconditionally guaranteed by Cengage Learning Holdco, Inc., on a limited recourse basis, and all of our future direct and indirect material, wholly owned domestic restricted subsidiaries, subject to certain exceptions. The guarantees of those obligations will be secured by (i) first-priority security interests in the ABL priority collateral, with the term loan facility secured by second-priority security interests therein, and (ii) second-priority security interests in the Non-ABL priority collateral, with the term loan facility secured by first-priority security interests therein.

The ABL Revolving Credit Facility also contains certain other customary conditions to borrowing, restrictions, affirmative covenants, negative covenants and events of default.

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Summary of Cash Flows

The following table sets forth our cash flows from operating, investing and financing activities:

<i>(in millions)</i>	Six Months Ended September 30,		Change	
	2018	2017	\$	%
Net cash provided by (used in)				
Operating activities	\$ 43.1	\$ 156.5	\$ (113.4)	(72.5)%
Investing activities	(78.9)	(91.6)	12.7	(13.9)%
Financing activities	(7.3)	(88.9)	81.6	(91.8)%
Impact on cash and cash equivalents from changes in foreign currency	(1.3)	0.2	(1.5)	NM
Net decrease in cash and cash equivalents	\$ (44.4)	\$ (23.8)	\$ (20.6)	86.6 %

NM = Not meaningful

Operating activities. Net cash used in operating activities for the six months ended September 30, 2018 increased \$113.4 million, primarily due to lower net income, lower deferred tax provision, and an increase in cash used by net working capital. The increase in cash used for net working capital was primarily driven by fiscal year 2018 incentive compensation payments made during the first quarter of fiscal year 2019 and a decrease in trade payable balances due to timing of purchases and payments. These uses of cash were partially offset by an increase in deferred sales, mainly driven by Cengage Unlimited, coupled with the timing of deferred revenue recognition, a decrease in deferred sales coupled with the timing of recognition of digital product sales, and a shift in inventory spend related to timing of the fall semester printing. These uses of cash were partially offset by the timing of trade payable payments and lower accounts receivable related to our typically lower seasonal first quarter billings.

Investing activities. Net cash used in investing activities for the six months ended September 30, 2018 decreased \$12.7 million primarily driven by a reduction in prepublication spend and the prior year timing of capital expenditures spend.

Financing activities. Net cash used in financing activities for the six months ended September 30, 2018 decreased \$81.6 million, primarily due to the prior year period cash used which included the \$27.7 million prepayment due under the Excess Cash Flow provision of the Term Loan facility and share repurchases of approximately \$61.0 million. The decrease in use of cash was partially offset by current year cash used of \$3.0 million to acquire shares in connection with net settlement of equity-based awards and \$4.2 million of dividend equivalents paid in connection with the delivery of shares under vested RSUs.

New Accounting Standards and Accounting Changes

See Note 1, "Basis of Presentation," to our condensed consolidated financial statements for a description of new accounting standards and accounting changes.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of September 30, 2018, we had \$1,669.4 million in outstanding variable rate debt under our Term Loan at face value. The effective interest rate for our Term Loan is based on a contractual minimum base interest rate, or LIBOR floor of 1.0%, plus the applicable margin. Currently, LIBOR is above the LIBOR floor and the debt is subject to variable rates. A 50 basis point increase in LIBOR on our current Term Loan balance would increase our annual interest expense by approximately \$8.3 million. Additionally, as of September 30, 2018, we had \$620.0 million in outstanding debt at a fixed rate of 9.50%.

LEGAL PROCEEDINGS

From time to time we may become involved in various claims, disputes and legal or regulatory proceedings that arise in the ordinary course of business and/or may be related to contractual or other obligations of ours. We assess our potential contingent and other liabilities by analyzing our claims, disputes and legal and regulatory matters using all available information. We also develop our views on estimated losses, if any, in consultation with our legal and other advisors. We determine whether a loss from a contingency should be accrued by assessing whether a loss is deemed probable and can be reasonably estimated. If the contingency is not probable or cannot be reasonably estimated, disclosure of the contingency shall be made when there is at least a reasonable possibility that a loss may have been incurred by us.

Adverse developments relating to claims, disputes and legal and regulatory proceedings in which we are or become involved could cause a change in our determination as to an unfavorable outcome and result in the need to recognize a material accrual. Should any of these matters result in a final adverse judgment, settlement or other final resolution involving material amounts, it could have a material adverse effect on our financial condition, results of operations and/or cash flows.

Based on a review of the information available at this time, we do not expect that the total cost of resolving current claims, disputes and legal regulatory proceedings will have a material adverse effect on our consolidated financial condition, results of operations or cash flows. For additional information, see Note 14, "Commitments and Contingencies" to our condensed consolidated financial statements.

RISK FACTORS

We encourage you to carefully consider the risk factors identified in the "Risk Factors" section in our 2018 Annual Report. These risk factors could materially affect our business, financial condition, and future results and could cause our actual business and financial results to differ materially from those contained in forward-looking statements made in this Quarterly Report or elsewhere by management from time to time. There have been no material changes during the six months ended September 30, 2018 to the risk factors disclosed in our 2018 Annual Report.

PURCHASES OF EQUITY SECURITIES BY THE ISSUER

There were no purchases of common stock by the Company during the second quarter of fiscal year 2019.