

# **INTERIM MANAGEMENT'S DISCUSSION AND ANALYSIS**

## **For the three and six months ended June 30, 2008 and 2007**

### **Dated: July 30, 2008**

The following review and analysis of Torstar Corporation's (the "Company" or "Torstar") operations and financial position for the three and six months ended June 30, 2008 and 2007 is supplementary to, and should be read in conjunction with the audited consolidated financial statements of Torstar Corporation for the year ended December 31, 2007 set forth in the Company's Annual Report for such fiscal year and incorporated by reference in the Company's renewal Annual Information Form dated March 18, 2008.

Torstar reports its financial results under Canadian generally accepted accounting principles ("GAAP") in Canadian dollars. Per share amounts are calculated using the weighted average number of shares outstanding for the applicable period.

#### Non-GAAP Measures

Management uses both operating profit, as presented in the consolidated statements of income, and EBITDA as measures to assess the performance of the reporting units and business segments. EBITDA is a measure that is also used by many of Torstar's shareholders, creditors, other stakeholders and analysts as a proxy for the amount of cash generated by the reporting unit or segment. EBITDA is not the actual cash provided by operating activities and is not a recognized measure of financial performance under GAAP. Torstar calculates EBITDA as the reporting unit or segment's operating profit before restructuring provisions, interest, taxes, depreciation and amortization. Torstar's method of calculating EBITDA may differ from other companies and accordingly, may not be comparable to measures used by other companies.

#### Forward-looking statements

Certain statements in this MD&A and in the Company's oral and written public communications may constitute forward-looking statements that reflect management's expectations regarding the Company's future growth, results of operations, performance and business prospects and opportunities as of the date of this report. Generally, these forward-looking statements can be identified by the use of forward-looking terminology such as "anticipate", "believe", "plan", "forecast", "expect", "intend", "would", "could", "if", "may" and similar expressions. All such statements are made pursuant to the "safe harbour" provisions of applicable Canadian securities legislation. These statements reflect current expectations of management regarding future events and operating performance, and speak only as of the date of this report. The Company does not intend, and disclaims any obligation to, update any forward-looking statements, whether written or oral, or whether as a result of new information or otherwise.

By their very nature, forward-looking statements require management to make assumptions and are subject to inherent risks and uncertainties. There is a significant risk that predictions, forecasts, conclusions or projections will not prove to be accurate, that management's assumptions may not be accurate and that actual results, performance or achievements may differ significantly from such predictions, forecasts, conclusions or projections expressed or implied by such forward-looking statements. We caution readers to not place undue reliance on the forward-looking statements in this MD&A as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, outlooks, expectations, goals, estimates or intentions expressed in the forward-looking statements. In addition, forward-looking statements are provided for the purpose of providing information about management's current expectations and plans relating to the future. Readers are cautioned that reliance on such information may not be appropriate for other purposes.

These factors include, but are not limited to: general economic conditions in the principal markets in which the Company operates, the Company's ability to operate in highly competitive industries, the Company's ability to compete with other forms of media, the Company's ability to

attract advertisers, cyclical and seasonal variations in the Company's revenues, newsprint costs, labour disruptions, foreign exchange fluctuations, restrictions imposed on existing credit facilities, reliance on its printing operations, reliance on technology and information systems, litigation, and uncertainties associated with critical accounting estimates.

We caution that the foregoing list is not exhaustive of all possible factors, as other factors could adversely affect our results. For more information, please see the discussion starting on page 24 of the Company's 2007 Annual Report concerning the effect certain risk factors could have on actual results, as well as the discussion in the Company's current Annual Information Form, which is incorporated herein by reference.

In addition, a number of assumptions, including those assumptions specifically identified throughout this MD&A, were applied in making the forward-looking statements set forth in this MD&A. Some of the key assumptions include, without limitation, assumptions regarding the performance of the North American economy; tax laws in the countries in which we operate; continued availability of printing operations; continued availability of financing on appropriate terms; exchange rates; market competition; and successful development of new products. There is a risk that some or all of these assumptions may prove to be incorrect.

## **OVERVIEW**

Torstar Corporation is a broadly based media company listed on the Toronto Stock Exchange (TS.B). Torstar reports its operations in two segments: Newspapers and Digital; and Book Publishing. The Newspapers and Digital Segment includes the Star Media Group led by the Toronto Star, Canada's largest daily newspaper and digital properties including thestar.com, toronto.com, Wheels.ca, Workopolis, and Olive Canada Network; and Metroland Media Group, publishers of community and daily newspapers in Ontario. Its Book Publishing Segment represents Harlequin Enterprises Limited, a leading global publisher of books for women. Torstar also has investments in CTVglobemedia Inc. ("CTVgm") and Black Press Limited which are accounted for as Associated Businesses, using the equity method.

## **OPERATING RESULTS – Second quarter and year to date 2008**

### **Overall Performance**

Total revenue was \$399.5 million in the second quarter of 2008, up \$2.5 million from \$397.0 million in the second quarter of 2007. Newspapers and Digital revenue decreased \$0.4 million to \$280.6 million as growth at Metroland Media Group's community newspapers, Star Media Group's digital properties and the jointly-owned Metro dailies almost completely offset the decline at the daily newspapers. Book Publishing revenue was \$118.9 million in the second quarter, up \$2.9 million from \$116.0 million in the same period last year. Underlying revenues were up \$6.3 million in the quarter with strong growth in the North America Retail division partially offset by a decrease of \$3.4 million from the unfavourable impact of foreign exchange rates.

Year to date total revenue was \$751.2 million, down \$23.2 million from \$774.4 million in the same period last year. Newspapers and Digital revenue was \$522.6 million year to date, down \$11.4 million from \$534.0 million last year. Book Publishing revenue was \$228.6 million year to date, down \$11.8 million

from last year as a \$14.2 million decline from the unfavourable impact of foreign exchange rates more than offset underlying growth of \$2.4 million.

Operating profit, after deducting a \$4.4 million restructuring provision, was \$46.0 million in the second quarter of 2008, up \$1.3 million from \$44.7 million in 2007. Excluding the restructuring provision, operating profit was \$50.4 million in the second quarter, up \$5.7 million from 2007. Newspapers and Digital Segment operating profit was \$36.1 million in the second quarter, down \$0.9 million from \$37.0 million in 2007. Book Publishing operating profit was \$18.5 million in the second quarter of 2008, up \$6.0 million from \$12.5 million in 2007. Corporate costs were \$4.2 million in the second quarter of 2008, down \$0.6 million from the second quarter of 2007.

Year to date operating profit, before restructuring provisions, was \$72.6 million, down \$6.5 million from \$79.1 million in the same period last year. Including the \$25.2 million restructuring provision, operating profit was \$47.4 million year to date. Newspapers and Digital Segment operating profit was \$46.6 million in the first six months of 2008, down \$10.4 million from \$57.0 million last year. Year to date Book Publishing operating profit was \$34.7 million in 2008, up \$3.1 million from \$31.6 million in 2007. Corporate costs were \$8.7 million year to date in 2008 down \$0.8 million from \$9.5 million in 2007.

In the second quarter of 2008, a restructuring provision of \$4.4 million was recorded related to non-voluntary staff reductions at Metroland Media Group. Year to date, restructuring provisions of \$25.2 million have been recorded including \$20.8 million for the first quarter voluntary and non-voluntary staff reductions in the newspapers. The restructurings will result in a net reduction of 250 employees with expected annual savings of \$17.0 million.

Earnings before restructuring provisions, interest, taxes, depreciation and amortization (“EBITDA” – see Non-GAAP measures), was \$64.8 million in the second quarter of 2008, up \$6.0 million from \$58.8 million in 2007. Year to date, EBITDA was \$101.1 million, down \$6.0 million from \$107.1 million in 2007.

	Second Quarter		Year to Date	
	2008	2007	2008	2007
Newspapers and Digital	\$49,223	\$49,850	\$72,551	\$82,539
Book Publishing	19,781	13,716	37,198	34,045
Corporate	(4,159)	(4,810)	(8,697)	(9,482)
EBITDA, excluding restructuring provisions	\$64,845	\$58,756	\$101,052	\$107,102

Interest expense was \$7.1 million in the second quarter of 2008, down \$1.5 million from \$8.6 million in the second quarter of 2007. Year to date interest expense was \$14.9 million, down \$2.4 million from \$17.3 million last year. The decrease reflected lower average debt levels and slightly lower effective interest rates in 2008. The average net debt (long-term debt and bank overdraft net of

cash and cash equivalents) was \$637.9 million in the second quarter of 2008, down from \$684.3 million in the second quarter of 2007. Torstar's effective interest rate was 4.4% in the second quarter and 4.7% year to date in 2008 down from 5.0% and 5.2% in the same periods in 2007. Net debt was \$636.4 million at June 30, 2008, down \$3.0 million from \$639.4 million at March 31, 2008 and up \$16.1 million from \$620.3 million at December 31, 2007.

Torstar reported a non-cash foreign exchange gain of \$0.1 million in the second quarter of 2008 and \$0.9 million year to date. Non-cash foreign exchange losses of \$1.8 million were reported in the second quarter and year to date in 2007. These gains/losses arose from the translation of foreign-currency denominated assets and liabilities into Canadian dollars. The amount of the gain or loss in any period will vary depending on the movement in relative value of the Canadian dollar and on whether Torstar has a net asset or net liability position in the foreign currency.

Torstar reported income from associated businesses of \$4.9 million in the second quarter of 2008 down \$5.5 million from \$10.4 million in the second quarter of 2007. Year to date, income from associated businesses was \$3.7 million in 2008 down \$7.2 million from \$10.9 million in 2007.

Torstar's income from CTVgm was \$6.8 million in the second quarter of 2008, down \$1.4 million from \$8.2 million in the second quarter of 2007. Year to date Torstar's income from CTVgm was \$6.4 million, down \$2.3 million from \$8.7 million in the same period last year. Net income before the Part II fee adjustment noted below improved at CTVgm in both the quarter and year to date as softness in conventional television advertising revenues was more than offset by strength in specialty television advertising revenues and lower interest expense due to lower levels of debt. The lower income reported by Torstar is attributable to a provision for Canadian Radio-television and Telecommunications Commission ("CRTC") Part II license fees during the second quarter and an adjustment to CTVgm's future income tax assets for a reduction in Canadian federal income tax rates that was made in the first quarter. In late 2006, the Trial Division of the Canadian Federal Court ruled that the CRTC Part II license fees were an illegal tax and that the broadcasters (including CTVgm) were not required to pay them for their fiscal years after 2006. Based on that decision CTVgm ceased to accrue Part II fees and reversed its existing accrual, which was reported by Torstar in the fourth quarter of 2007. In April 2008, the Federal Court of Appeal reversed the Trial Court decision and found that the fees are a valid regulatory charge. In June 2008, the Canadian Association of Broadcasters filed an application for leave to appeal to the Supreme Court. During the second quarter of 2008, CTVgm has made a provision for Part II fees for fiscal 2007 and 2008.

Torstar reported a loss from Black Press of \$2.0 million in the second quarter of 2008 compared with income of \$2.2 million in the second quarter of 2007. Year to date Torstar has reported a loss from Black Press of \$2.9 million in 2008

compared with income of \$2.1 million in the same period last year. \$2.1 million of the decrease in the second quarter and year to date related to adjustments made to Black Press's future tax assets. Operating results were down in the second quarter as the U.S. newspapers were negatively impacted by the U.S. economy and sub-prime mortgage crisis and higher amortization expense was incurred from acquisitions. The Canadian newspaper business continued to perform well. Year to date, Black Press results were also negatively impacted by the mark to market of its financial derivatives.

During the second quarter of 2008, Torstar reported a net gain of \$6.8 million from unusual items. In the quarter, Torstar recognized a gain of \$9.2 million on the disposition of excess land and a loss of \$2.4 million on the write-down of its portfolio investment in U.S. based LiveDeal Inc. to fair market value. On an after-tax basis the unusual items contributed \$5.6 million of net income or \$0.07 per share.

Torstar's effective tax rate was 27.2% in the second quarter of 2008 compared with 32.8% in the second quarter of 2007. Year to date, Torstar's effective tax rate was 23.7% in 2008 compared with 35.4% in the same period last year. The lower effective tax rate in the second quarter includes the mix-of-income impact from items that were taxed at a capital gains rate and lower foreign losses that were not tax-effected. Year to date, the effective rate was impacted by these items as well as by one-time adjustments to tax expense recorded in the first quarter of both 2008 and 2007. The full year 2008 tax rate is expected to be approximately 31%.

Torstar reported net income of \$37.0 million in the second quarter of 2008, up \$6.9 million from \$30.1 million in 2007. Year to date Torstar reported net income of \$33.5 million, down \$12.3 million from \$45.8 million in the same period last year. Net income per share was \$0.47 in the second quarter of 2008, an increase of \$0.09 from net income of \$0.38 per share in the second quarter of 2007. Net income per share was \$0.43 in the first six months of 2008, down \$0.15 from \$0.58 in the same period last year. Excluding the impact of the restructuring provisions and unusual items net income per share would have been \$0.44 in the second quarter and \$0.58 year to date.

The average number of shares outstanding was 78.8 million in the second quarter and year to date 2008. In 2007, an average of 78.6 million shares was outstanding during the second quarter and 78.5 million during the first six months.

The following chart provides a continuity of earnings per share from 2007 to 2008:

	Second Quarter	Year to Date
Net income per share 2007	\$0.38	\$0.58
<b>Changes</b>		
• <b>Operations</b>	0.09	0.00
• <b>Restructuring provisions</b>	(0.04)	(0.22)
• <b>Income from associated businesses</b>	(0.06)	(0.08)
• <b>Non-cash foreign exchange</b>	0.03	0.06
• <b>Unusual items</b>	0.07	0.07
• <b>One-time tax expense adjustments</b>	0.00	0.02
Net income per share 2008	\$0.47	\$0.43

### **SEGMENT OPERATING RESULTS - Newspapers and Digital Segment**

The Newspapers and Digital Segment includes the Star Media Group; Metroland Media Group; and Transit Television Network (“Transit TV”).

Star Media Group includes the Toronto Star, with the largest circulation and readership of any daily newspaper in Canada; Torstar’s interests in Sing Tao Daily and the Toronto, Ottawa, Vancouver, Edmonton, Calgary and Halifax editions of Metro; thestar.com; toronto.com; Wheels.ca, Yourhome.ca, Healthzone.ca, Parentcentral.ca and Torstar Media Group Television (“TMG TV”). Star Media Group also includes Workopolis, Olive Canada Network and the Torstar Digital corporate group.

Metroland Media Group publishes in print and online more than 100 community newspapers and three daily newspapers – The Hamilton Spectator, the Waterloo Region Record and the Guelph Mercury. It is also the publisher of Gold Book Directories, a number of specialty publications, and operates several consumer shows throughout Ontario. Metroland Media Group has ten web press facilities which print the Metroland newspapers but also engage in commercial printing.

Transit TV is a U.S. based operation that delivers full motion, broadcast-quality information and entertainment to passengers on buses and rail transit on screens mounted in the vehicle.

The following tables set out, in \$000’s, the results for the reporting units within the Newspapers and Digital Segment for the three months ended June 30, 2008 and 2007.

	Operating Revenue		Operating Profit (Loss)		Profit Margin	
	2008	2007	2008	2007	2008	2007
Metroland Media	\$153,769	\$151,886	\$31,825	\$31,357	20.7%	20.6%
Star Media	126,186	128,367	5,596	8,275	4.4%	6.4%
Transit TV	683	724	(1,370)	(2,617)	n/a	n/a
Segment Total	\$280,638	\$280,977	\$36,051	\$37,015	12.8%	13.2%

	Depreciation and Amortization		EBITDA		EBITDA Margin	
	2008	2007	2008	2007	2008	2007
Metroland Media	\$3,910	\$3,823	\$35,735	\$35,180	23.2%	23.2%
Star Media	8,488	8,094	14,084	16,369	11.2%	12.8%
Transit TV	774	918	(596)	(1,699)	n/a	n/a
Segment Total	\$13,172	\$12,835	\$49,223	\$49,850	17.5%	17.7%

The following tables set out, in \$000's, the results for the reporting units within the Newspapers and Digital Segment for the six months ended June 30, 2008 and 2007.

	Operating Revenue		Operating Profit (Loss)		Profit Margin	
	2008	2007	2008	2007	2008	2007
Metroland Media	\$279,959	\$284,919	\$48,137	\$51,261	17.2%	18.0%
Star Media	241,557	247,802	1,704	11,197	0.7%	4.5%
Transit TV	1,053	1,242	(3,219)	(5,495)	n/a	n/a
Segment Total	\$522,569	\$533,963	\$46,622	\$56,963	8.9%	10.7%

	Depreciation and Amortization		EBITDA		EBITDA Margin	
	2008	2007	2008	2007	2008	2007
Metroland Media	\$7,816	\$7,611	\$55,953	\$58,872	20.0%	20.7%
Star Media	16,565	16,084	18,269	27,281	7.6%	11.0%
Transit TV	1,548	1,881	(1,671)	(3,614)	n/a	n/a
Segment Total	\$25,929	\$25,576	\$72,551	\$82,539	13.9%	15.5%

Total revenue of the Newspapers and Digital Segment was \$280.6 million in the second quarter of 2008, down \$0.4 million from \$281.0 million in the second quarter of 2007. Year to date total revenue of the Newspapers and Digital Segment was \$522.6 million down \$11.4 million from \$534.0 million in the same period last year. Digital revenues were 5.8% of the total in the second quarter of 2008 and 5.7% year to date, up from 4.3% and 4.1% in the same periods in 2007.

The Newspapers and Digital Segment was positively affected by the calendar during the second quarter of 2008. Most stores are closed for two days on Easter weekend and advertisers, accordingly, tend to reduce their advertising spend around that weekend. Easter weekend was in the first quarter of 2008 and in the second quarter of 2007. Year to date, there was no impact from the calendar.

#### Metroland Media Group

Revenues were \$153.8 million in the second quarter of 2008, up \$1.9 million from \$151.9 million in the second quarter of 2007 with growth at the community newspapers and Gold Book directories more than offsetting declines at the daily newspapers. Year to date revenues were \$280.0 million in 2008, down \$4.9 million from \$284.9 million in the same period last year. Advertising revenue at the community newspapers was up 2.2% in the quarter benefiting from underlying growth as well as the calendar. The daily newspapers continued to face challenges with National advertising revenues in the second quarter. Distribution revenues were up at both the community and daily newspapers for the quarter and year to date.

Metroland Media Group's EBITDA was \$35.7 million in the second quarter, up \$0.5 million from \$35.2 million in the second quarter of 2007. Year to date EBITDA was \$56.0 million in 2008, down \$2.9 million from \$58.9 million last year. Cost savings continued during the quarter with lower staff costs from the restructuring efforts undertaken in 2007 and the first quarter of 2008. These savings were partially offset by higher pension costs.

Operating profit was \$31.8 million in the second quarter of 2008, up \$0.4 million from \$31.4 million in the second quarter of 2007. Year to date operating profit was \$48.1 million in 2008, down \$3.2 million from \$51.3 million in the same period last year.

#### Star Media Group

Star Media Group had revenues of \$126.2 million in the second quarter of 2008, a decrease of \$2.2 million from \$128.4 million in the second quarter of 2007. Year to date revenues were \$241.6 million in 2008, down \$6.2 million from \$247.8 million in the same period last year.

Revenue grew over 30% at the SMG digital properties in the second quarter and year to date with strong performance at Olive Canada Network and thestar.com. The jointly-owned Sing Tao and Metro newspapers provided revenue growth in the second quarter and year to date from a combination of new products and market expansion. Advertising revenue at the Toronto Star was down 10.5% in the second quarter of 2008 and 11.8% year to date with the National and Retail advertising categories continuing to be challenging.

Star Media Group's EBITDA was \$14.1 million in the second quarter of 2008, down \$2.3 million from \$16.4 million in the second quarter of 2007. Year to date EBITDA was \$18.3 million in 2008, down \$9.0 million from \$27.3 million in the same period last year. Cost savings were realized by the Toronto Star in the quarter and year to date from reduced newsprint consumption (including the positive impact of the web-width reduction in 2007) and lower payroll costs from the restructuring efforts undertaken in 2007 and the first quarter of 2008. Newsprint prices were relatively flat year over year in the second quarter and 6.0% lower year to date.

The Star Media Group had an operating profit of \$5.6 million in the second quarter of 2008, down \$2.7 million from \$8.3 million in the second quarter of 2007. Year to date operating profit was \$1.7 million in 2008, down \$9.5 million from \$11.2 million in the same period last year.

#### Transit TV

Transit TV had an EBITDA loss of \$0.6 million in the second quarter of 2008, an improvement of \$1.1 million from a loss of \$1.7 million in the same period last year. Year to date the EBITDA loss was \$1.7 million in 2008, an improvement of \$1.9 million from a loss of \$3.6 million in 2007. The improvement reflected the continued focus on cost containment by Transit TV's management.

In early 2008, Torstar announced a strategic sales relationship with IdeaCast Inc., (a U.S. provider of custom television content and advertising to health clubs) and a letter of intent giving IdeaCast an option to acquire Transit TV in the second quarter of 2008. In April 2008, IdeaCast provided notice that it does not intend to exercise its option to acquire Transit TV within the option period. During the second quarter of 2008, Torstar and IdeaCast reached an agreement on the extension of the sales relationship. Torstar's carrying value in Transit TV's net assets at June 30, 2008 was approximately \$17.9 million.

#### **Segment Operating Results – Book Publishing**

The Book Publishing Segment reports the results of Harlequin, a leading global publisher of books for women. Harlequin publishes books around the world in a variety of genres and formats, selling through the retail channel and directly to the consumer by mail and the Internet. Harlequin's publishing operations are comprised of three divisions: North America Retail, North America Direct-To-Consumer and Overseas.

The following tables set out, in \$000's, a summary of operating results for the Book Publishing Segment and a continuity of revenue and operating profit, including the impact of foreign currency movements, for the three and six months ended June 30, 2008 and 2007.

	Second Quarter		Year to Date	
	2008	2007	2008	2007
Revenue	\$118,868	\$115,988	\$228,587	\$240,444
EBITDA	\$19,781	\$13,716	\$37,198	\$34,045
Depreciation & amortization	1,245	1,214	2,465	2,420
Operating profit	\$18,536	\$12,502	\$34,733	\$31,625
EBITDA margin	16.6%	11.8%	16.3%	14.2%
Operating profit margin	15.6%	10.8%	15.2%	13.2%

	Second Quarter	Year to Date
Reported revenue, prior year	\$115,988	\$240,444
Impact of currency movements and foreign exchange contracts	(3,409)	(14,226)
Change in underlying revenue	6,289	2,369
Reported revenue, current year	\$118,868	\$228,587
Reported operating profit, prior year	\$12,502	\$31,625
Impact of currency movements and foreign exchange contracts	(842)	(3,119)
Change in underlying operating profit	6,876	6,227
Reported operating profit, current year	\$18,536	\$34,733

Book Publishing revenues were up \$6.3 million in the second quarter of 2008 excluding the impact of foreign exchange. North America Retail was up \$6.1 million, North America Direct-To-Consumer was down \$1.4 million and Overseas was up \$1.6 million. Year to date, Book Publishing revenues were up \$2.4 million excluding the impact of foreign exchange. North America Retail was up \$3.3 million, North America Direct-To-Consumer was down \$2.6 million and Overseas was up \$1.7 million.

Book Publishing operating profits were up \$6.9 million in the second quarter of 2008 excluding the impact of foreign exchange. North America Retail was up \$5.3 million, North America Direct-To-Consumer was up \$0.3 million and Overseas was up \$1.3 million. Year to date Book Publishing operating profits were up \$6.2 million excluding the impact of foreign exchange. North America Retail was up \$5.3 million, North America Direct-To-Consumer was up \$0.6 million and Overseas was up \$0.3 million.

North America Retail operating profits were up \$5.3 million in the second quarter on revenue growth from a strong publishing schedule, improved net sales rates and positive adjustments to returns provisions. Higher promotional spending in the quarter and year to date was offset by product cost savings arising from the mix of product.

North America Direct-To-Consumer operating profits were up \$0.3 million in the second quarter and \$0.6 million year to date despite lower revenues. Revenue was down in the quarter and year to date as the revenue growth from Internet book and digital sales was not sufficient to offset the decrease from fewer books sold in the traditional direct mail business. Lower costs, primarily reduced advertising and promotion spending in the traditional direct mail business offset the lower revenues in both the quarter and year to date.

Overseas operating profits were up \$1.3 million in the second quarter of 2008 with higher profits across most of the major markets. Japan's digital product sales continued to grow with the sale of digital manga (comics) content to SoftBank Creative Corp., (a division of Softbank Corp., one of the largest providers of cell phone services in Japan) beginning in the second quarter.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Overview**

Funds are generally used for capital expenditures, debt repayment and distributions to shareholders. Long-term debt is used to supplement funds from operations and as required for acquisitions. It is expected that future cash flows from operating activities, combined with the credit facilities available will be adequate to cover forecasted financing requirements.

In the second quarter of 2008, \$29.5 million of cash was generated by operations, \$20.2 million was used for investing activities and \$14.8 million was used for financing activities. Year to date, \$40.6 million of cash was generated by operations, \$25.5 million was used for investing activities and \$14.4 million was used for financing activities.

### **Operating activities**

Operating activities provided cash of \$29.5 million in the second quarter of 2008, consistent with the second quarter of 2007 as higher operating results were offset by an increase in non-cash working capital. Year to date, operating activities provided cash of \$40.6 million, up \$6.4 million from the same period in 2007 as the lower operating results were offset by an adjustment for pension expense in excess of pension funding and a decrease in non-cash working capital.

Non-cash working capital increased by \$13.4 million in the second quarter of 2008 primarily from increased accounts receivables. Year to date non-cash working capital increased by \$12.4 million as cash was used to pay corporate taxes and accounts payable.

### **Investing activities**

During the second quarter of 2008, \$20.2 million was used for investments, up from \$11.3 million in the second quarter of 2007. Year to date \$25.5 million was

used for investments, up \$9.7 million from \$15.8 million in the same period last year.

Additions to property plant and equipment were \$5.5 million in the second quarter of 2008 and \$9.6 million year to date. This was down from \$7.3 million and \$12.7 million in the same periods last year.

Investments of \$17.9 million were made in the second quarter including the acquisition of Central Ontario Web and eyeReturn Marketing. On the purchase of eyeReturn Marketing there is a further \$6.5 million of purchase price owing over the next three years as detailed in the contractual obligations section below. Year to date, investments of \$18.7 million were made, including Torstar's share of Workopolis' acquisition of Brainhunter Inc. in the first quarter.

Cash of \$3.1 million was received in the second quarter of 2008 on the sale of excess land. The balance of the proceeds (\$6.2 million) was received in the form of a mortgage which matures December 12, 2009 but can be paid earlier at the option of the purchaser.

#### **Financing activities**

Cash of \$14.8 million was used by financing activities during the second quarter of 2008 primarily for the payment of dividends. In the second quarter of 2007, \$14.4 million was used for the payment of dividends and \$22.5 million for the repayment of bankers' acceptance.

Year to date Torstar has paid \$28.9 million of dividends and issued \$14.4 million of bankers' acceptance. In the same period last year Torstar paid \$28.8 million of dividends and repaid \$9.0 million of bankers' acceptance.

#### **Long-term debt**

At June 30, 2008, Torstar had long-term debt of \$669.9 million outstanding. The debt consisted of U.S. dollar bankers' acceptance of \$105.0 million, Canadian dollar bankers' acceptance of \$465.3 million and Canadian dollar medium term notes of \$100.0 million decreased by \$0.4 million related to fair value hedge adjustments.

Torstar's long-term credit facility for \$800 million is also designated as a standby line in support of letters of credit. At June 30, 2008, \$573.2 million was drawn under the facility and a \$27.5 million letter of credit was outstanding relating to the executive retirement plan. The remaining credit of \$199.3 million is considered to be adequate to cover forecasted financing requirements.

During the second quarter of 2008, Torstar entered into two interest rate swap agreements that fix the interest rate of U.S. \$80 million of borrowings at approximately 4.2% (plus the credit spread, currently 0.6%) for seven years ending May 2015.

**Contractual obligations**

There were no material changes in Torstar's significant contractual obligations during the second quarter of 2008 other than as noted below.

The acquisition of eyeReturn Marketing included \$6.5 million of deferred purchase price payments. These payments will be made equally in June 2009, 2010 and 2011 and are contingent on certain conditions being met. Torstar has accrued these payments as part of the purchase price in accounts payable and long-term liabilities based on the payment dates.

**Foreign Exchange**

As of June 30, 2008, Torstar has entered into forward foreign exchange contracts to sell \$17.5 million U.S. dollars during the next two quarters of 2008 at an average rate of \$1.00 and \$10.0 million U.S. dollars in 2009 at an average rate of \$1.02.

**KEY FACTORS AND RELATED RISKS**

There have been no material changes in any risks or uncertainties facing Torstar since the year ended December 31, 2007.

**OUTLOOK**

Harlequin and Metroland Media Group grew in the second quarter while the Star Media Group continued to face revenue challenges from the soft economy in Southern Ontario and the structural pressures facing large daily newspapers. We expect this pattern to continue for the remainder of the year.

After a very strong second quarter, we expect Harlequin's growth to moderate in the second half of the year resulting in solid growth for the year as a whole. The U.S. economy could have a negative impact on Harlequin's results, but to date, there is no evidence of this. From a foreign exchange perspective, if the Canadian dollar remains at its current level relative to the U.S. dollar and overseas currencies through the rest of the year, it is anticipated that there would be a modest negative year over year foreign exchange impact of approximately \$0.4 million in the last six months of the year. The full year impact is estimated to be \$3.5 million, \$3.1 million of which has been reported in the first six months.

Metroland Media Group returned to its growth track in the second quarter with both revenue and profit growth, finishing the quarter with a strong June. We expect this positive momentum to continue into the second half of the year which, aided by cost reductions, should result in good profit growth for Metroland Media Group for the second half of the year.

Star Media Group had a difficult second quarter as lower revenues at the Toronto Star outweighed continued progress in the digital businesses and other publications. We expect the revenue challenges for the Toronto Star to continue

into the second half of the year but that they will be partially offset by growth in the Star Media Group's other businesses. In particular we expect strong growth at our two leading digital businesses – Workopolis and Olive Canada Network.

The Southern Ontario economic outlook continues to cause uncertainty for Torstar's newspapers. Cost challenges for the newspapers include the expectation of higher year over year newsprint pricing in the last six months of 2008 and increasing distribution costs as gas prices continue to rise. The newspapers undertook restructurings during the first six months of 2008. The combination of voluntary and non-voluntary staff reductions will result in a net reduction of 250 positions with savings expected to be \$17.0 million annually. \$7.0 million of the savings is expected to be realized in the second half of 2008 mitigating the impact of the cost challenges referred to above.

### **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

There have been no changes in Torstar's internal controls over financial reporting that occurred during the second quarter of 2008, the most recent interim period, that have materially affected, or are reasonably likely to materially affect, Torstar's internal controls over financial reporting.

### **CHANGES IN ACCOUNTING POLICIES**

The Canadian Institute of Chartered Accountants has confirmed that the use of International Financial Reporting Standards ("IFRS") will be required for interim and annual financial statements related to fiscal years beginning on or after January 1, 2011. At that date, Torstar will be required to prepare financial statements in accordance with IFRS. Torstar is currently reviewing the standards to determine the potential impact on its consolidated financial statements.

### **SUMMARY OF QUARTERLY RESULTS**

(In thousands of dollars except for per share amounts)

	<b>Quarter Ended</b>			
	<b>June 30/08</b>	<b>March 31/08</b>	<b>Dec. 31/07</b>	<b>Sept. 30/07</b>
Revenue	\$399,506	\$351,650	\$402,930	\$369,200
Net income (loss)	\$36,962	(\$3,457)	\$47,182	\$8,419
Net income (loss) per Class A voting and Class B non-voting share				
Basic	\$0.47	(\$0.04)	\$0.60	\$0.11
Diluted	\$0.47	(\$0.04)	\$0.60	\$0.11

	Quarter Ended			
	June 30/07	March 31/07	Dec. 31/06	Sept. 30/06
Revenue	\$396,965	\$377,442	\$414,610	\$366,216
Net income	\$30,053	\$15,737	\$36,068	\$7,667
Net income per Class A voting and Class B non-voting share				
Basic	\$0.38	\$0.20	\$0.46	\$0.10
Diluted	\$0.38	\$0.20	\$0.46	\$0.10

The summary of quarterly results illustrates the cyclical nature of revenues and operating profit in the Newspapers and Digital Segment. The fourth and second quarters are generally the strongest for the newspapers.

Restructuring provisions have impacted the level of net income in several quarters. Restructuring provisions were \$4.4 million in the second quarter of 2008, \$20.8 million in the first quarter of 2008, \$7.5 million in the fourth quarter of 2007, \$11.7 million in the fourth quarter of 2006 and \$7.0 million in the third quarter of 2006.

#### **OTHER**

At June 30, 2008, Torstar had 9,897,767 Class A voting shares and 68,975,360 Class B non-voting shares outstanding. More information on Torstar share capital is provided in Note 8 of the interim consolidated financial statements.

At June 30, 2008, Torstar had 5,209,206 options to purchase Class B non-voting shares outstanding to executives and non-executive directors. More information on Torstar's stock option plan is provided in Note 9 of the interim consolidated financial statements.

Additional information relating to Torstar including the Annual Information Form is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on Torstar's corporate website at [www.torstar.com](http://www.torstar.com).

**Torstar Corporation**  
**Consolidated Balance Sheets**  
*(Dollars in Thousands)*  
*(Unaudited)*

*June 30*  
2008

*December 31*  
2007

**Assets**

**Current:**

Cash and cash equivalents	\$44,415	\$34,096
Receivables	250,627	263,779
Inventories <i>(note 5)</i>	33,775	31,807
Prepaid expenses	64,861	61,325
Prepaid and recoverable income taxes	7,068	3,097
Future income tax assets	19,749	19,010

<b>Total current assets</b>	<b>420,495</b>	<b>413,114</b>
-----------------------------	----------------	----------------

Property, plant and equipment (net)	319,134	330,391
Investment in associated businesses <i>(note 7)</i>	436,856	434,294
Goodwill (net)	567,107	562,120
Other assets	197,808	182,948
Future income tax assets	39,377	37,970

<b>Total assets</b>	<b>\$1,980,777</b>	<b>\$1,960,837</b>
---------------------	--------------------	--------------------

**Liabilities and Shareholders' Equity**

**Current:**

Bank overdraft	\$10,886	\$3,616
Accounts payable and accrued liabilities	198,719	208,217
Income taxes payable	8,840	17,065

<b>Total current liabilities</b>	<b>218,445</b>	<b>228,898</b>
----------------------------------	----------------	----------------

Long-term debt <i>(note 2)</i>	669,907	650,798
Other liabilities	93,770	89,678
Future income tax liabilities	72,360	73,702

**Shareholders' equity:**

Share capital <i>(note 8)</i>	390,340	388,036
Contributed surplus	11,319	9,929
Retained earnings	539,622	535,242
Accumulated other comprehensive loss <i>(note 6)</i>	(14,986)	(15,446)

<b>Total shareholders' equity</b>	<b>926,295</b>	<b>917,761</b>
-----------------------------------	----------------	----------------

<b>Total liabilities and shareholders' equity</b>	<b>\$1,980,777</b>	<b>\$1,960,837</b>
---	--------------------	--------------------

*(See accompanying notes)*

**Torstar Corporation**  
**Consolidated Statements of Income**  
*(Dollars in Thousands)*  
*(Unaudited)*

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 30</i>		<i>June 30</i>	
	2008	2007	2008	2007
<b>Operating revenue</b>				
Newspapers and digital	\$280,638	\$280,977	\$522,569	\$533,963
Book publishing	118,868	115,988	228,587	240,444
	<b>\$399,506</b>	<b>\$396,965</b>	<b>\$751,156</b>	<b>\$774,407</b>
<b>Operating profit</b>				
Newspapers and digital	\$36,051	\$37,015	\$46,622	\$56,963
Book publishing	18,536	12,502	34,733	31,625
Corporate	(4,175)	(4,824)	(8,730)	(9,510)
Restructuring provisions <i>(note 12)</i>	(4,408)		(25,225)	
	46,004	44,693	47,400	79,078
Interest	(7,069)	(8,583)	(14,879)	(17,317)
Foreign exchange	112	(1,782)	906	(1,797)
Income of associated businesses	4,934	10,425	3,697	10,926
Unusual items <i>(note 15)</i>	6,781		6,781	
	50,762	44,753	43,905	70,890
Income and other taxes	(13,800)	(14,700)	(10,400)	(25,100)
<b>Net income</b>	<b>\$36,962</b>	<b>\$30,053</b>	<b>\$33,505</b>	<b>\$45,790</b>
Earnings per Class A and Class B share <i>(note 8(b))</i> :				
Net income - Basic	\$0.47	\$0.38	\$0.43	\$0.58
Net income - Diluted	\$0.47	\$0.38	\$0.43	\$0.58

*(See accompanying notes)*

**Torstar Corporation**  
**Consolidated Statements of Comprehensive Income**  
*(Dollars in Thousands)*  
*(Unaudited)*

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 30</i>		<i>June 30</i>	
	2008	2007	2008	2007
Net income	<b>\$36,962</b>	\$30,053	<b>\$33,505</b>	\$45,790
Other comprehensive income (loss), net of tax:				
Unrealized foreign currency translation adjustment	(1,633)	(6,877)	3,543	(6,235)
Reclassification adjustment for unrealized loss on available-for-sale financial assets included in net income	1,602		1,602	
Unrealized loss on available-for-sale financial assets		(521)	(1,602)	(521)
Unrealized change in fair value of cash flow hedges	3,614	6,237	(1,887)	6,968
Realized loss (gain) on cash flow hedges transferred to net income	(173)	97	(1,196)	139
Other comprehensive income (loss)	<b>3,410</b>	(1,064)	<b>460</b>	351
Comprehensive income	<b>\$40,372</b>	\$28,989	<b>\$33,965</b>	\$46,141

*(See accompanying notes)*

**Torstar Corporation**  
**Consolidated Statements Of Changes In**  
**Shareholders' Equity**  
*(Dollars in Thousands)*  
*(Unaudited)*

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 30</i>		<i>June 30</i>	
	2008	2007	2008	2007
<b>Share capital (note 8)</b>	<b>\$390,340</b>	<b>\$387,407</b>	<b>\$390,340</b>	<b>\$387,407</b>
<b>Contributed surplus</b>				
Balance, beginning of period	\$10,629	\$7,922	\$9,929	\$7,466
Stock-based compensation expense	690	743	1,390	1,199
Balance, end of period	<b>\$11,319</b>	<b>\$8,665</b>	<b>\$11,319</b>	<b>\$8,665</b>
<b>Retained earnings</b>				
Balance, beginning of period	\$517,233	\$493,235	\$535,242	\$491,999
Net income	36,962	30,053	33,505	45,790
Dividends	(14,573)	(14,547)	(29,125)	(29,048)
Balance, end of period	<b>\$539,622</b>	<b>\$508,741</b>	<b>\$539,622</b>	<b>\$508,741</b>
<b>Accumulated other comprehensive loss</b>				
Balance, beginning of period as previously reported	(\$18,396)	(\$9,227)	(\$15,446)	
Unrealized foreign currency translation adjustment losses				(\$9,116)
Cumulative impact of accounting changes relating to financial instruments				(1,526)
Adjusted balance, beginning of period	(18,396)	(9,227)	(15,446)	(10,642)
Other comprehensive income (loss)	3,410	(1,064)	460	351
Balance, end of period (note 6)	<b>(\$14,986)</b>	<b>(\$10,291)</b>	<b>(\$14,986)</b>	<b>(\$10,291)</b>
<b>Total shareholders' equity</b>	<b>\$926,295</b>	<b>\$894,522</b>	<b>\$926,295</b>	<b>\$894,522</b>

*(See accompanying notes)*

**Torstar Corporation**  
**Consolidated Statements of Cash Flows**  
*(Dollars in Thousands)*  
*(Unaudited)*

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 30</i>		<i>June 30</i>	
	2008	2007	2008	2007
<b>Cash was provided by (used in)</b>				
Operating activities	\$29,459	\$29,272	\$40,643	\$34,240
Investing activities	(20,212)	(8,907)	(25,470)	(15,763)
Financing activities	(14,801)	(34,656)	(14,399)	(35,052)
(Decrease) increase in cash	(5,554)	(14,291)	774	(16,575)
Effect of exchange rate changes	(261)	(1,848)	2,275	(1,880)
Cash, beginning of period	39,344	41,548	30,480	43,864
<b>Cash, end of period</b>	<b>\$33,529</b>	<b>\$25,409</b>	<b>\$33,529</b>	<b>\$25,409</b>
<b>Operating activities:</b>				
Net income	\$36,962	\$30,053	\$33,505	\$45,790
Depreciation	13,300	13,692	26,974	27,278
Amortization	1,132	371	1,452	746
Future income taxes	1,153	1,654	(214)	3,278
Income of associated businesses	(4,934)	(10,425)	(3,697)	(10,926)
Dividend received from associated business	1,161		1,161	
Other <i>(note 13)</i>	(5,919)	1,477	(6,117)	(2,618)
	42,855	36,822	53,064	63,548
Increase in non-cash working capital	(13,396)	(7,550)	(12,421)	(29,308)
Cash provided by operating activities	\$29,459	\$29,272	\$40,643	\$34,240
<b>Investing activities:</b>				
Additions to property, plant and equipment	(\$5,508)	(\$7,305)	(\$9,606)	(\$12,667)
Acquisitions and investments <i>(note 14)</i>	(17,908)	(1,477)	(18,681)	(3,148)
Proceeds on sale of property <i>(note 15)</i>	3,125		3,125	
Other	79	(125)	(308)	52
Cash used in investing activities	(\$20,212)	(\$8,907)	(\$25,470)	(\$15,763)
<b>Financing activities:</b>				
Issuance of bankers' acceptance			\$14,479	\$13,541
Repayment of bankers' acceptance	(\$87)	(\$22,519)	(\$87)	(22,519)
Dividends paid	(14,447)	(14,421)	(28,884)	(28,799)
Exercise of stock options		2,376		2,484
Other	(267)	(92)	93	241
Cash used in financing activities	(\$14,801)	(\$34,656)	(\$14,399)	(\$35,052)
<b>Cash represented by:</b>				
Cash and cash equivalents	\$44,415	\$32,300	\$44,415	\$32,300
Bank overdraft	(10,886)	(6,891)	(10,886)	(6,891)
	\$33,529	\$25,409	\$33,529	\$25,409

*(See accompanying notes)*

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

*(Dollar amounts in thousands unless otherwise stated)*

---

**1. ACCOUNTING POLICIES**

The accounting policies used in the preparation of these unaudited interim consolidated financial statements conform with those in Torstar Corporation's December 31, 2007 audited annual consolidated financial statements except as noted below. These interim financial statements do not include all of the disclosures included in the annual financial statements and accordingly should be read in conjunction with the annual consolidated financial statements.

On January 1, 2008, the Company adopted the CICA Handbook Section 1535 "Capital Disclosures", Section 3031 "Inventories", Section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation" as described in Note 1(s) of the annual consolidated financial statements, with no restatement of prior periods.

**Capital Disclosures**

Section 1535 establishes standards for disclosure of both qualitative and quantitative information that enable users to evaluate the entity's objectives, policies and processes for managing capital; the disclosure and compliance with any externally imposed capital requirements and the consequences of any non-compliance. The required disclosures are included in Note 4 to these interim financial statements.

**Inventories**

Section 3031 prescribes the measurement of inventories at the lower of cost and net realizable value, with guidance on cost determination including the allocation of overheads and other costs to inventory. Reversals of previous write-downs to net realizable value are permitted when there is a subsequent increase in the value of inventories.

The required disclosures are included in Note 5 to these interim financial statements. Inventories are stated at the lower of cost and net realizable value. The cost of finished goods and work in progress includes raw materials, translation and related printing and production costs. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs necessary to make the sale. Provisions are made for slow moving and obsolete inventory.

**Financial instruments**

Sections 3862 and 3863 together replace Section 3861 "Financial Instruments – Disclosures and Presentation", revising and enhancing its disclosure requirements while carrying forward unchanged its presentation requirements. These new sections emphasize disclosures of the nature and extent of risks arising from financial instruments to which the entity is exposed and how those risks are managed. The

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

*(Dollar amounts in thousands unless otherwise stated)*

---

Company has included the required disclosures in Note 3 to these interim financial statements.

The Company has classified its cash equivalents, short-term investments and derivative financial instruments that are not designated as hedges as held-for-trading. They are presented at their fair value and the gains or losses arising on the revaluation at the end of each period are included in net income. The carrying values of these instruments approximate their fair values.

Accounts receivables are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities and are measured at amortized cost. The long term debt instruments have been classified as other financial liabilities and are measured at amortized cost as the Company has the ability and intention to hold to maturity. Transaction costs related to the long term debt instruments are capitalized and amortized over the term of the instrument.

Portfolio investments are classified as available-for-sale and are measured at fair value except for securities that do not have a quoted market price in an active market which are carried at cost. Any changes in the fair value are recognized in other comprehensive income except for other than temporary impairment losses which are recognized in net income.

Derivative financial instruments that are designated as cash flow hedges, such as the floating to fixed interest rate swap agreements and forward exchange contracts are presented at their fair value. The gains or losses arising from the revaluation at the end of each period are included in other comprehensive income to the extent of hedge effectiveness. For effective fair value hedges, such as the fixed to floating interest rate swap agreements, changes in the fair value of the hedging derivative are recorded in net income. The carrying value of the hedged item is adjusted for unrealized gains or losses attributable to the hedged risk and also recognized in net income.

There was no impact from these changes in accounting policies on net income for the three and six months ended June 30, 2008.

#### Future accounting changes

##### Goodwill and Intangible assets

In January 2008, the CICA issued Section 3064 "Goodwill and Intangible assets" which will replace Section 3062 "Goodwill and Other Intangible assets" and Section 3450 "Research Development Costs" and will apply to the Company effective January 1, 2009. The standard provides guidance on the criteria for recognition of intangible assets and clarifies the application of the matching concept to revenues

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)*

and expenses whether the assets are acquired or internally generated. The Company has not yet determined the impact of adopting this standard on the consolidated financial statements.

**International Financial Reporting Standards**

The CICA has confirmed that the use of International Financial Reporting Standards (“IFRS”) will be required for interim and annual financial statements related to fiscal years beginning on or after January 1, 2011. At this date, the company will be required to prepare financial statements in accordance with IFRS. The company is currently reviewing the standards to determine the potential impact on its consolidated financial statements.

**2. LONG-TERM DEBT**

	As at June 30, 2008	As at December 31, 2007
Bankers' acceptance:		
Cdn. dollar denominated	\$465,300	\$444,632
U.S. dollar denominated	<u>104,987</u>	<u>108,001</u>
	<u>570,287</u>	<u>552,633</u>
Medium Term Notes:		
Cdn. dollar denominated	100,000	100,000
Fair value hedge	<u>(380)</u>	<u>(1,835)</u>
	<u>99,620</u>	<u>98,165</u>
	<u>\$669,907</u>	<u>\$650,798</u>

- a) All bankers' acceptance with a term of less than one year have been classified as long-term debt as the Company has the ability to refinance these amounts under its existing long-term credit facilities. The interest rate spread above the bankers' acceptance rate if in Canadian dollars, or LIBOR rate if in U.S. dollars, at June 30, 2008 was 0.6% and varies based on the Company's long-term credit rating. The carrying values of the bankers' acceptance approximate their fair value at June 30, 2008.

The Company is party to three interest rate swap agreements with major Canadian chartered banks that fix the interest rate on \$250 million of Canadian dollar borrowings for five years ending September 2011. As a result, the Company will pay quarterly a fixed rate of 4.3% per annum (plus the interest rate spread based on the Company's long term credit rating, currently 0.6%) and will receive quarterly floating rate payments based on 90 day bankers' acceptance

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

*(Dollar amounts in thousands unless otherwise stated)*

---

rates. These swap contracts have been designated as hedges. The fair value of these swap agreements was \$3.4 million unfavourable at June 30, 2008.

The average rate on Canadian dollar bank borrowings outstanding at June 30, 2008 was 3.7%. Including the effect of the above noted swap arrangements, the effective rate was 4.4%.

In May 2008, the Company entered into two interest rate swap agreements that fix the interest rate on U.S. \$80 million of borrowings at approximately 4.2% (plus the credit spread, currently 0.6%) for seven years ending May 2015. These swap contracts have been designated as hedges. The fair value of these swap arrangements was \$0.9 million favourable at June 30, 2008.

At June 30, 2008 bank debt outstanding included U.S. borrowings of U.S. \$103.1 million at an average rate of 2.9%. Including the effect of the above noted swap arrangements, the effective rate was 4.5%.

- b) The Company issued in September 2005 \$75 million 3.85% medium term notes which mature on September 8, 2010. The Company has entered into interest rate swap agreements effectively converting this debt into floating rate debt based on 90-day bankers' acceptance rate plus 0.39%. The Company also issued in September 2005 \$25 million 3.7% medium term notes which mature on September 9, 2009. The Company has entered into an interest rate swap agreement effectively converting this debt into floating rate debt based on 90-day bankers' acceptance rates plus 0.36%. Interest on the medium term notes as well as the payments under the swap agreements is paid semi-annually. The swap agreements have been designated as hedges and mature on the due dates of the respective notes.

The effective interest rate on the medium term notes outstanding at June 30, 2008 was 3.5%. The fair value of the medium term notes was \$3.5 million favourable at June 30, 2008. The fair value of the Canadian interest rate swap agreements related to the medium term debt issuance noted above were \$0.4 million unfavourable at June 30, 2008. In accordance with the accounting policy for a fair value hedge, the debt has been decreased by \$0.4 million to \$99.6 million. There was no impact on net income or other comprehensive income.

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)***3. FINANCIAL INSTRUMENTS**Classification

	As at June 30, 2008
Financial assets:	
Held for trading, measured at fair value	
Cash and cash equivalents	\$44,415
Loans and receivables, measured at amortized cost	
Accounts receivable	236,556
Other receivables	<u>14,071</u>
	<u>250,627</u>
Available for sale, measured at cost	
Portfolio investments <sup>1</sup>	4,070
Available for sale, measured at fair value	
Portfolio investments <sup>1</sup>	1,144
Derivatives designated as effective hedges, measured at fair value	
Foreign currency hedges <sup>1</sup>	343
Interest rate swaps – cash flow hedges <sup>1</sup>	(2,506)
Interest rate swaps – fair value hedges <sup>1</sup>	(380)
Financial liabilities, measured at fair value	
Bank overdraft	10,886
Financial liabilities, measured at amortized cost	
Long term debt	669,907
Accounts payable and accrued liabilities	198,719

<sup>1</sup> These amounts are included in Other assets and Other liabilities

Risk management

The Company is exposed to various risks related to its financial assets and liabilities. These risk exposures are managed on an ongoing basis.

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)***Credit risk**

In the normal course of business, the Company is exposed to credit risk from its accounts receivable from customers. The carrying amounts for accounts receivable are net of applicable allowances for doubtful accounts and returns, which are estimated based on past experience, specific risks associated with the customer and other relevant information.

The Company is also exposed to credit-related losses in the event of non-performance by counterparties to derivative instruments. The Company manages its counterparty risk by only accepting major financial institutions with high credit ratings, as approved by the Board of Directors, as counterparties.

The maximum exposure to credit risk is the carrying value of the financial assets.

The following table sets out details of the age of receivables and allowance for doubtful accounts and returns:

	As at June 30, 2008
Gross accounts receivable:	
Current	\$256,300
Up to three months past due date	71,442
Three to twelve months past due date	19,652
Impaired	<u>7,598</u>
	354,992
Allowance for doubtful accounts	(17,969)
Returns provision	<u>(100,467)</u>
	<u>\$236,556</u>

**Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due or at reasonable cost. The Company manages liquidity risk primarily by maintaining sufficient unused capacity within its long term debt facilities. The unused capacity at June 30, 2008 was approximately \$199 million.

**Market risk**

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Company's income or the value of its financial instruments.

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

*(Dollar amounts in thousands unless otherwise stated)*

---

b) Foreign currency risk

The Company is exposed to foreign currency risk through Harlequin's international operations. The most significant foreign currency exposure is to movements in the U.S. dollar/Cdn. dollar exchange rate. The Company manages the U.S. dollar/Cdn. dollar exchange rate risk on its operating results through the use of derivative financial instruments as detailed in Note 11. The Company also manages the U.S. dollar/Cdn. dollar exchange rate risk on its balance sheet by maintaining U.S. dollar denominated debt, as detailed in Note 2, in order to provide a hedge against its net U.S. dollar denominated assets.

b) Interest rate risk

The Company is exposed to interest rate risk on the bankers' acceptance issued at floating rates under its bank loan facility. The Company manages this risk through the use of interest rate swap contracts to fix the interest rate as detailed in Note 2.

An assumed 1% increase in short term interest rates during the six month period ended June 30, 2008 would have decreased net income by \$0.7 million, with an equal but opposite effect for an assumed 1% decrease in interest rates.

The Company does not engage in trading or other speculative activities with respect to derivative financial instruments.

Fair value of financial instruments

The carrying values of the Company's financial instruments approximate their fair values unless otherwise noted.

#### **4. CAPITAL MANAGEMENT**

The Company's capital management objectives are to maintain financial flexibility in order to preserve its capacity to meet its financial commitments, to pay dividends and to meet its potential obligations resulting from internal growth and acquisitions.

The Company defines capital as:

- Shareholders' equity
- Long term debt
- Bank overdraft net of cash and cash equivalents

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)*

Total managed capital was as follows:

	As at June 30, 2008	As at December 31, 2007
Shareholders' equity	\$926,295	\$917,761
Long term debt	669,907	650,798
Bank overdraft	10,886	3,616
Cash and cash equivalents	<u>(44,415)</u>	<u>(34,096)</u>
	<u>\$1,562,673</u>	<u>\$1,538,079</u>

The Company manages its capital structure in accordance with changes in economic conditions. In order to maintain or adjust its capital structure, the Company may elect to adjust the amount of debt outstanding, adjust the amount of dividends paid to shareholders, return capital to its shareholders, repurchase its shares in the marketplace or issue new shares.

The Company is meeting all its financial commitments. The Company's credit facilities are subject to financial tests and other covenants with which it was in compliance at June 30, 2008.

There have been no changes in the Company's approach to capital management during the period.

The Company is not subject to any externally imposed capital requirements.

**5. INVENTORIES**

	As at June 30, 2008	As at December 31, 2007
Finished goods	\$10,152	\$9,921
Work in progress	11,773	9,739
Raw materials	<u>11,850</u>	<u>12,147</u>
	<u>\$33,775</u>	<u>\$31,807</u>

The Company has expensed inventory costs of \$107.2 million (2007 - \$120.1 million) for the six months ended June 30, 2008 and \$56.9 million (2007 - \$60.5 million) for the quarter ended June 30, 2008.

The Company recorded a writedown of \$1.9 million for the six months ended June 30, 2008 (2007 - \$3.2 million) and \$1.1 million (2007 - \$1.8 million) for the quarter ended June 30, 2008.

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)***6. ACCUMULATED OTHER COMPREHENSIVE LOSS (NET OF TAX)**

	As at January 1, 2008	Other Comprehensive Income (Loss)	As at June 30, 2008
Foreign currency translation adjustment	(\$17,096)	3,543	(\$13,553) <sup>1</sup>
Unrealized gains (losses) on cash flow hedges	1,650	(3,083)	(1,433) <sup>2</sup>
	<u>(\$15,446)</u>	<u>\$460</u>	<u>(\$14,986)</u>

<sup>1</sup>Net of future income tax benefit of \$568.<sup>2</sup>Net of future income tax benefit of \$730.**7. INVESTMENT IN ASSOCIATED BUSINESSES**

The Company's Investment in associated businesses includes a 20% equity interest in CTVglobemedia Inc. ("CTVgm"), a 19.35% equity interest in Black Press Ltd. and a 30% equity interest in Q-ponz Inc. The Investment in associated businesses is comprised of the following:

	2008	2007
Balance, beginning of year	\$434,294	\$416,320
Income of associated businesses	3,697	10,926
Dividends received	(1,161)	
Change in investee foreign currency translation adjustment	<u>26</u>	<u>(1,540)</u>
Balance, end of period	<u>\$436,856</u>	<u>\$425,706</u>

Outlined below is summarized financial information for 100% of CTVgm, including fair value adjustments, as at May 31, 2008 and November 30, 2007 and for the six months ended May 31, 2008 and May 31, 2007.

	May 31, 2008	November 30, 2007
<b>Balance Sheet</b>		
Current assets	\$742,065	\$770,170
Property, plant and equipment	515,841	533,305
Goodwill and other intangible assets	3,428,056	3,515,033
Other assets	<u>338,944</u>	<u>194,240</u>
	<u>\$5,024,906</u>	<u>\$5,012,748</u>

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)*

Current Liabilities	\$469,214	\$448,254
Long-term debt	2,026,630	2,091,143
Other liabilities and non-controlling interests	457,429	433,610
Shareholders' equity	<u>2,071,633</u>	<u>2,039,741</u>
	<u>\$5,024,906</u>	<u>\$5,012,748</u>

	<b>Six months ended</b>	
	<b>May 31, 2008</b>	<b>May 31, 2007</b>
<b>Statement of Income</b>		
Revenues <sup>1</sup>	\$1,108,860	\$868,215
Net income	\$31,890	\$43,670

<sup>1</sup>For the six months ended May 31, 2007, CTVgm accounted for its investment in CHUM by the equity method and accordingly the revenue for that period does not include CHUM's revenues.

**8. SHARE CAPITAL**

a) A summary of changes to the Company's share capital is as follows:

Class A shares (voting)

At June 30, 2008 there were 9,897,767 Class A shares outstanding with a stated value of \$2,689. During the six months ended June 30, 2008, 9,835 Class A shares were converted to Class B shares.

Class B shares (non-voting)

	<u>Shares</u>	<u>Amount</u>
December 31, 2007	68,838,975	\$386,054
Converted from Class A	9,835	3
Issued under Employee Share Purchase Plan	109,829	1,778
Dividend reinvestment plan	16,121	241
Other	600	9
June 30, 2008	<u>68,975,360</u>	<u>\$388,085</u>
Total Class A and Class B shares	<u>78,873,127</u>	\$390,774
Reduction for RSU Trust shares		(434)
Share Capital		<u>\$390,340</u>

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)*

## b) Earnings per share

Basic per share amounts have been determined by dividing net income by the weighted average number of Class A and Class B shares outstanding during the period after deducting the unvested shares held by the RSU Trust. Diluted per share amounts have taken into consideration the dilutive effect of stock options; the employees share purchase plan and the unvested shares held by the RSU Trust. The weighted average number of Class A and Class B shares outstanding (in thousands) were:

	<i>Three months ended June 30</i>		<i>Six months ended June 30</i>	
	2008	2007	2008	2007
Basic	78,831	78,605	78,782	78,518
Diluted	78,845	78,714	78,796	78,614

**9. STOCK-BASED COMPENSATION**

The Company has five stock-based compensation plans: an executive share option plan, an employee share purchase plan, an executive restricted share unit ("RSU") plan, a deferred share unit ("DSU") plan for employees and a DSU plan for non-employee directors.

## a) A summary of changes in the executive share option plan is as follows:

	Share options	Weighted average exercise price
December 31, 2007	5,112,654	\$22.57
Granted	586,552	\$18.78
Forfeited or expired	<u>(490,000)</u>	(\$25.47)
June 30, 2008	<u>5,209,206</u>	\$21.87

Options exercisable at June 30, 2008 are as follows:

Range of exercise price	Share options exercisable	Weighted average exercise price
\$15.75 – 19.61	781,109	\$18.36
\$20.30 – 22.20	2,007,801	\$21.65
\$25.50 – 29.01	<u>1,050,637</u>	\$27.35
\$15.75 – 29.01	<u>3,839,547</u>	\$22.54

The fair value of the executive share options granted in 2008 was estimated to be \$2.24 per option at the date of grant using the Black-Scholes option pricing model

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)*

with the assumptions of a risk free interest rate of 4.1%, expected dividend yield of 3.9%, expected volatility of 15.1% and an expected time until exercise of 6 years.

## b) RSU Plan

A summary of changes in the RSU plan is as follows:

	Units	Weighted average issue price
December 31, 2007	190,503	\$20.14
Granted	117,223	\$18.97
Vested and issued	(2,723)	\$20.30
Forfeited	<u>(996)</u>	\$19.61
June 30, 2008	<u>304,007</u>	\$19.69

- c) The Company has recognized in 2008 compensation expense totalling \$1.7 million (2007 - \$1.5 million) for the stock options granted in 2005 to 2008, RSUs granted in 2006 to 2008 and the employee share purchase plans originating in 2006 to 2007.
- d) The Company has a DSU Plan for executives and non-employee directors. As at June 30, 2008, 305,013 units were outstanding at a value of \$3.7 million. The Company has entered into a derivative instrument in order to offset its exposure to 298,600 units. Changes in the fair value of this instrument are recorded as compensation expense and offset the impact of changes in the value of the outstanding deferred share units.

**10. EMPLOYEE FUTURE BENEFITS**

The Company maintains a number of defined benefit plans and defined contribution plans, which provide pension benefits to its employees in Canada and the United States. Post employment benefits other than pensions are also available to employees, primarily in the Canadian newspapers operations, which provide for various health and life insurance benefits.

The Company has expensed net pension benefit costs of \$7.2 million for the six months ended June 30, 2008 (2007 - \$5.9 million) and \$3.7 million for the quarter ended June 30, 2008 (2007 - \$2.7 million). With respect to post-employment benefits other than pensions, for the six months and quarter ended June 30, 2008 the net benefit cost was \$1.9 million and \$0.9 million respectively (2007 - \$2.0 million and \$1.0 million respectively).

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS***(Dollar amounts in thousands unless otherwise stated)***11. FORWARD FOREIGN EXCHANGE CONTRACTS AND OPTIONS**

As described in Note 15 of the Company's December 31, 2007 annual financial statements, the Company has entered into various forward foreign exchange contracts. The Company has entered into forward foreign exchange contracts which establish a rate of exchange of Canadian dollar per U.S. dollar of \$1.05 for U.S. \$34 million in 2008 and \$1.02 for U.S. \$10 million in 2009. The net fair value of these contracts was \$0.3 million favourable at June 30, 2008.

**12. RESTRUCTURING PROVISIONS**

The Company recorded restructuring provisions of \$25.2 million for the six months ended June 30, 2008, including \$4.4 million during the quarter ended June 30, 2008, related to voluntary and non-voluntary staff reductions in the Newspapers and Digital Segment.

Accounts payable and accrued liabilities include \$28.3 million for restructuring provisions at June 30, 2008 (\$10.7 million at December 31, 2007). The change in the liability during 2008 includes payments of \$2.2 million related to provisions made in 2008, \$4.2 million related to provisions made in 2007 and \$1.2 million for provisions made prior to 2007.

**13. OTHER CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES**

	<i>Three months ended</i>		<i>Six months ended</i>	
	<i>June 30</i>		<i>June 30</i>	
	2008	2007	2008	2007
Foreign Exchange	(\$112)	\$1,782	(\$906)	\$1,797
Post employment benefits	1,239	(1,416)	1,478	(5,923)
Stock-based compensation expense	(423)	631	(52)	1,923
Unusual items	(6,781)		(6,781)	
Other	<u>158</u>	<u>480</u>	<u>144</u>	<u>(415)</u>
	<u>(\$5,919)</u>	<u>\$1,477</u>	<u>(\$6,117)</u>	<u>(\$2,618)</u>

**14. ACQUISITIONS**

During the six month period ended June 2008, the Company completed a number of acquisitions in its Newspaper and Digital segment for cash of \$18.4 million, which were accounted for by the purchase method. The acquisitions include Central Ontario Web, eyeReturn Marketing and Torstar's share of Workopolis' acquisition of the specialist online employment board business of Brainhunter Inc. The purchase of eyeReturn Marketing includes future obligations of \$6.5 million, which are payable annually from June 2009 through 2011 in three equal instalments of approximately \$2.2 million. The total purchase price of these acquisitions (including the future

**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

*(Dollar amounts in thousands unless otherwise stated)*

---

obligations) has been allocated \$5.8 million to fixed assets, \$0.5 million to working capital, \$5.4 million to intangible assets, \$5.4 million to goodwill and \$7.8 million to other assets. The above allocations are preliminary.

**15. UNUSUAL ITEMS**

In the second quarter of 2008, the company recognized a gain of \$9.2 million from the sale of excess land in Vaughan. The net proceeds from this sale were \$9.3 million of which \$6.2 million is a mortgage which matures in December 2009. The mortgage includes interest at a rate of 6.0% per annum until March 2009 and 9.5% per annum thereafter until maturity. The purchaser may prepay the whole or part of the principal at any time.

During the second quarter of 2008, the Company recorded a writedown of \$2.4 million to reflect an other-than-temporary decline in fair value on its investment in LiveDeal, Inc. (which is classified as available-for-sale).

**16. COMPARATIVE FINANCIAL STATEMENTS**

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation of the 2008 financial statements.