HICKORY TECH CORP
Form 10-Q
May 13, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

ý	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	FOR THE QUARTERLY PERIOD ENDED March 31, 2003
	OR
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	FOR THE TRANSITION PERIOD FROM TO

Commission file number 0-13721

HICKORY TECH CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota	**41-1524393**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

221 East Hickory Street
Mankato, Minnesota 56002-3248
(Address of principal executive offices and zip code)

(800) 326-5789
(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ý No o

The total number of shares of the registrant s common stock outstanding as of March 31, 2003: 13,998,182.

HICKORY TECH CORPORATION

March 31, 2003

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For Three Months Ended	
(In Thousands Except Per Share Amounts)	**3/31/2003**	**3/31/2002**
OPERATING REVENUES:		
Telecom Sector	21,961	20,717
Information Solutions Sector	1,098	1,034
Enterprise Solutions Sector	3,911	3,361
TOTAL OPERATING REVENUES	26,970	25,112
COSTS AND EXPENSES:		
Cost of Sales, Enterprise Solutions	2,519	2,184
Operating Expenses, excluding Depreciation and Amortization	14,436	13,286
Depreciation	4,162	3,813
Amortization of Intangibles	326	361
TOTAL COSTS AND EXPENSES	21,443	19,644
OPERATING INCOME	5,527	5,468
OTHER INCOME (EXPENSE):		
Equity in Net Loss of Investees	(3)	(19)
Interest and Other Income	10	43
Interest Expense	(1,565)	(1,956)
TOTAL OTHER INCOME (EXPENSE)	(1,558)	(1,932)
INCOME BEFORE INCOME TAXES	3,969	3,536
INCOME TAXES	1,622	1,446
NET INCOME	$ 2,347	$ 2,090
Basic Earnings Per Share	$ 0.17	$ 0.15
Dividends Per Share	$ 0.11	$ 0.11
Weighted Average Common Shares Outstanding	13,994	13,961

Diluted Earnings Per Share	$	0.17	$	0.15
Weighted Average Common and Equivalent Shares Outstanding		14,007		14,063

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

March 31, 2003

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(In Thousands Except Share and Per Share Amounts)		**3/31/2003**		**12/31/2002**
ASSETS				
CURRENT ASSETS:				
Cash and Cash Equivalents	**$**	**2,111**	$	1,874
Receivables, Net of Allowance for Doubtful Accounts of $1,263 and $1,358		**11,048**		11,056
Income Taxes Receivable				3,222
Costs in Excess of Billings on Contracts		**1,687**		2,107
Inventories		**4,928**		5,059
Deferred Income Taxes		**951**		951
Other		**2,479**		2,840
TOTAL CURRENT ASSETS		**23,204**		27,109
INVESTMENTS		**6,742**		10,517
PROPERTY, PLANT AND EQUIPMENT		**248,969**		247,375
Less ACCUMULATED DEPRECIATION		**115,180**		111,101
PROPERTY, PLANT AND EQUIPMENT, NET		**133,789**		136,274
OTHER ASSETS:				
Goodwill		**25,086**		25,086
Intangible Assets, Net		**34,608**		34,669
Deferred Costs and Other		**6,127**		6,556
TOTAL OTHER ASSETS		**65,821**		66,311
TOTAL ASSETS	**$**	**229,556**	$	240,211
LIABILITIES & SHAREHOLDERS EQUITY				
CURRENT LIABILITIES:				
Accounts Payable	**$**	**3,297**	$	4,543
Accrued Expenses		**3,211**		3,719
Accrued Interest		**479**		512
Billings in Excess of Costs on Contracts		**139**		80
Advanced Billings and Deposits		**3,738**		3,741
Current Maturities of Long-Term Obligations		**1,405**		1,441
TOTAL CURRENT LIABILITIES		**12,269**		14,036
LONG-TERM OBLIGATIONS, Net of Current Maturities		**147,740**		157,599

DEFERRED INCOME TAXES		**4,377**		4,377
DEFERRED REVENUE AND BENEFITS		**5,541**		5,604
TOTAL LIABILITIES		**169,927**		181,616
COMMITMENTS AND CONTINGENCIES (Note 8)				
SHAREHOLDERS EQUITY:				
Common Stock, no par value, $.10 stated value				
Shares authorized: 100,000,000				
Shares outstanding: 13,998,182 in 2003 and 13,983,929 in 2002		**1,400**		1,398
Additional Paid-In Capital		**8,262**		7,885
Retained Earnings		**49,967**		49,312
TOTAL SHAREHOLDERS EQUITY		**59,629**		58,595
TOTAL LIABILITIES & SHAREHOLDERS EQUITY	**$**	**229,556**	$	240,211

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

March 31, 2003

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

Dollars In Thousands	For Three Months Ended 3/31/2003	3/31/2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	**$ 2,347**	$ 2,090
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	**4,488**	4,174
Gain on Sale of Assets	**(1)**	
Stock-Based Compensation	**257**	172
Employee Retirement Benefits and Deferred Compensation	**(34)**	96
Accrued Patronage Refunds	**(181)**	(285)
Equity in Net Loss of Investees	**3**	19
Provision for Losses on Accounts Receivable	**235**	452
Changes in Operating Assets and Liabilities:		
Receivables	**2,995**	3,127
Inventories	**131**	(145)
Billings and Costs on Contracts	**479**	374
Accounts Payable and Accrued Expenses	**(1,787)**	(2,625)
Advance Billings and Deposits	**(3)**	12
Deferred Revenue and Benefits	**(29)**	(120)
Other	**377**	567
Net Cash Provided By Operating Activities	**9,277**	7,908
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to Property, Plant and Equipment	**(1,735)**	(3,488)
Redemption of Investments	**4,100**	100
Proceeds from Sale of Assets	**60**	172
Net Cash Provided By (Used In) Investing Activities	**2,425**	(3,216)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments of Capital Lease Obligations	**(145)**	(105)
Repayments on Credit Facility	**(9,750)**	(4,250)
Proceeds from Issuance of Common Stock	**131**	210
Dividends Paid	**(1,540)**	(1,537)
Stock Repurchase	**(161)**	
Net Cash Used In Financing Activities	**(11,465)**	(5,682)

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		**237**		(990)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD		**1,874**		2,008
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$**	**2,111**	$	1,018

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

MARCH 31, 2003

PART 1. FINANCIAL INFORMATION

ITEM 1. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information necessary for a fair presentation of results of operations, financial position, and cash flows in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, the condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of Hickory Tech Corporation s (HickoryTech) results for the periods presented. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from these estimates. These unaudited interim condensed consolidated financial statements should be read in conjunction with HickoryTech s Annual Report on Form 10-K for the year ended December 31, 2002.

The consolidated financial statements of HickoryTech include Hickory Tech Corporation and its subsidiaries in the following three business segments: (i) Telecom Sector, (ii) Information Solutions Sector and (iii) Enterprise Solutions Sector. An investment in an unconsolidated partnership for the Information Solutions Sector is accounted for using the equity method. All intercompany transactions have been eliminated from the consolidated financial statements.

Certain reclassifications were made to the financial statements as of and for the three months ended March 31, 2002 to conform to the 2003 presentation. These reclassifications had no impact on previously reported operating revenue, net income or shareholders equity.

Operating expenses include all costs related to delivery of HickoryTech s communications services and products. These costs include all selling, general and administrative costs and all costs of performing services and providing related products, except for costs associated with the depreciation and amortization of property, plant and equipment and intangible assets.

NOTE 2. EARNINGS AND CASH DIVIDENDS PER COMMON SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the quarter. Shares used in the earnings per share assuming dilution calculation are based on the weighted average number of shares of common stock outstanding during the quarter increased by potentially dilutive common shares. Potentially dilutive common shares include stock options and stock subscribed under the employee stock purchase plan (ESPP).

	For Three Months Ended	
	3/31/2003	3/31/2002
Weighted Average Shares Outstanding	13,993,696	13,960,708
Stock Options (dilutive only)	2,535	92,553
Weighted Average Stock Subscribed (ESPP)	11,095	9,542
Weighted Average Dilutive Shares Outstanding	14,007,326	14,062,803

Options to purchase 555,835 shares and 76,650 shares for the three months ended March 31, 2003 and 2002, respectively, were not included in the computation of earnings per share assuming dilution calculation because their effect on earnings per share would have been antidilutive.

Cash dividends are based on the number of common shares outstanding at the respective record dates. Listed below are the number of shares outstanding as of the record date for the first quarter of 2003 and 2002.

Shares Outstanding on Record Date	2003	2002
First Quarter (Feb. 15)	14,003,335	13,971,484

Dividends per share is based on the quarterly dividend per share as declared by the HickoryTech Board of Directors.

During the first three months of 2003 and 2002, shareholders have elected to reinvest $66,000 and $60,000, respectively, of dividends into HickoryTech common stock pursuant to the HickoryTech Dividend Reinvestment Plan.

NOTE 3. COMPREHENSIVE INCOME

For the three months ended March 31, 2003 and 2002, comprehensive income was comprised solely of net income.

NOTE 4. INVENTORIES

Inventories, which consist of equipment for resale, materials and supplies, are stated at the lower of average cost or market.

NOTE 5. INTANGIBLE ASSETS

Effective January 1, 2002, HickoryTech adopted SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 142 established new standards related to how acquired goodwill and other intangible assets are to be recorded upon their acquisition as well as how they are to be accounted for after they have been initially recognized in the financial statements.

Effective with the adoption of this standard, HickoryTech is no longer amortizing acquired goodwill. Instead, SFAS No. 142 requires acquired goodwill to be evaluated for impairment using a two-step test based upon a fair value approach. The first step is used to identify potential impairment, while the second step calculates the amount of impairment, if any. Upon adoption of this standard, HickoryTech completed a transitional impairment test for its acquired goodwill, determining the fair value using primarily a discounted cash flow model. The determined fair value was sufficient to pass the first step impairment test, and therefore no impairment was recorded.

Additionally, upon adoption of SFAS No. 142, HickoryTech was required to reassess the useful lives of its other intangible assets. HickoryTech s other intangible assets primarily consist of wireless FCC licenses (FCC licenses). HickoryTech s FCC licenses have terms of ten years, but are renewable. The renewal of FCC licenses is a routine matter involving a nominal fee and HickoryTech has determined that no legal, regulatory, contractual, competitive, economic or other factors currently exist that limit the useful life of its FCC licenses. As such, effective with the adoption of SFAS No. 142, HickoryTech is no longer amortizing FCC licenses as they are deemed to be intangible assets that have indefinite lives. Prospectively, HickoryTech will continue to periodically reevaluate its determination of an indefinite useful life with regards to FCC licenses. SFAS No. 142 requires that indefinite lived intangible assets be tested for impairment by comparing the fair value of the assets to their carrying amount. Upon adoption of this standard, HickoryTech completed a transitional impairment test for FCC licenses, calculating fair value using primarily a discounted cash flow model and corroborating marketplace transactions, and determined that there was no impairment to be recorded. The FCC licenses were tested for impairment on an aggregate basis, which is consistent with HickoryTech s management of the wireless business within the Telecom Sector. HickoryTech also re-assessed the useful life of its other intangible assets and concluded that the existing lives of up to eight years should be continued.

On a prospective basis, HickoryTech is required to test both acquired goodwill and FCC licenses for impairment on an annual basis based upon a fair value approach. Additionally, goodwill shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of an entity below its carrying value. Other indefinite-lived intangible assets will be tested between annual tests if events or changes in circumstances indicate that the asset might be impaired.

HickoryTech will test for impairment of acquired goodwill and FCC licenses at the end of the fourth quarter of 2003, unless events or occurrences deem it necessary to test for impairment in an interim period.

The carrying value of HickoryTech s goodwill is $25,086,000 as of March 31, 2003 and December 31, 2002.

The components of HickoryTech s other intangible assets are shown in the following table:

	As of March 31, 2003		As of December 31, 2002	
(Dollars in Thousands)	**Gross Carrying Amount**	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Definite-Lived Intangible Assets				
Customers	$ 821	$ 263	$ 821	$ 237
Other Intangibles	150	100	185	100
Total	$ 971	$ 363	$ 1,006	$ 337
Indefinite-Lived Intangible Assets				
FCC Licenses	$ 34,000		$ 34,000	

Amortization expense related to the definite-lived intangible assets for the three months ended March 31, 2003 amounted to $26,000. Total estimated amortization expense for 2003 and the five years subsequent to 2003 is as follows: 2003 - $102,000; 2004 - $102,000; 2005 - $102,000; 2006 - $102,000; 2007 - $102,000 and 2008 - $74,000.

6

NOTE 6. RECENT ACCOUNTING DEVELOPMENTS

In June 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. SFAS No. 143 requires entities to record the fair value of the liability for legal obligations associated with an asset retirement in the period in which the obligation is incurred. When the liability is initially recorded, the entity capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset.

HickoryTech s incumbent local exchange carrier companies (ILECs) follow the provisions of SFAS No. 71, and therefore conform to the accounting principles as prescribed by the respective state public utilities commissions and other federal agencies and, where applicable, accounting principles generally accepted in the United States of America. On December 20, 2002, the Federal Communications Commission (FCC) notified carriers that they would not adopt SFAS No. 143 for regulatory accounting purposes. At January 1, 2003, HickoryTech determined the amount of asset retirement obligations required to be recorded for its ILEC companies under the provisions of SFAS No. 143 were not significant, and therefore the implementation of SFAS No. 143 on January 1, 2003 did not impact HickoryTech s financial position or results of operations.

HickoryTech s competitive local telephone companies (CLEC) also adopted SFAS No. 143 effective January 1, 2003. HickoryTech has determined that its competitive local telephone companies do not have a material legal obligation to remove long-lived assets as described by SFAS No. 143, and accordingly, adoption of SFAS No. 143 did not impact HickoryTech s financial position or results of operations.

HickoryTech also adopted the provisions of SFAS No. 143 for its wireless operations as of January 1, 2003. HickoryTech performed an analysis to identify all potential Asset Retirement Obligations. The legal obligations identified consist of obligations to remediate leased property where cell sites are located. However, based upon HickoryTech s experience and expectations, there is significant uncertainty as to whether third parties that own these leased properties would enforce their remediation rights related to the sites. Therefore, pursuant to the provisions of SFAS No. 143, HickoryTech did not record this potential asset retirement obligation upon adoption and will not record an obligation until such time as the fair value of the obligation can be reasonably estimated.

In April 2002, the FASB issued SFAS No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections. SFAS No. 145 rescinds FASB Statement No. 4, Reporting Gains and Losses from Extinguishment of Debt, and an amendment of that Statement, FASB Statement No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements. SFAS No. 145 also rescinds FASB Statement No. 44, Accounting for Intangible Assets of Motor Carriers, and amends FASB Statement No. 13, Accounting for Leases. HickoryTech adopted the provisions of SFAS No. 145 on January 1, 2003. Adoption of this standard had no impact on the financial statements presented in this Form 10-Q.

In June 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities, which replaces Emerging Issues Task Force (EITF) Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. HickoryTech has engaged in no activities in the first quarter of 2003 that are subject to the provisions of SFAS No. 146. Accordingly, the adoption of SFAS No. 146 did not impact HickoryTech s financial position or results of operations.

7

In December 2002, the FASB issued SFAS No. 148, Accounting for Stock-Based Compensation Transition Disclosure an amendment of SFAS No. 123 (SFAS No. 148). This Statement amends SFAS No. 123, Accounting for Stock-Based Compensation, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The provisions of SFAS No. 148 are effective for financial statements for fiscal years ending after December 15, 2002, and disclosure requirements shall be effective for interim periods beginning after December 15, 2002. The Company will continue to account for stock-based compensation to its employees and directors using the intrinsic value method prescribed by APB Opinion No. 25, and related interpretations. The Company adopted the provisions of SFAS No. 148 and has made certain disclosures required by SFAS No. 148 in the consolidated financial statements presented in this report. The adoption of SFAS No. 148 did not impact HickoryTech s financial position or results of operations.

In November 2002, the FASB issued Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. This interpretation elaborates on the disclosures required in financial statements concerning obligations under certain guarantees. It also clarifies the requirements related to the recognition of liabilities by a guarantor at the inception of certain guarantees. The disclosure requirements of this interpretation were effective for HickoryTech on December 31, 2002 but did not require any additional disclosures. The recognition provisions of the interpretation are effective for HickoryTech in 2003 and are applicable only to guarantees issued or modified after December 31, 2002. The adoption of Interpretation No. 45 does not have a material impact on the financial position or results of operations of HickoryTech.

NOTE 7. QUARTERLY SECTOR FINANCIAL SUMMARY

Business segment information for the first quarter of 2003 and 2002 is as follows. Certain amounts in 2002 have been reclassified to conform to the 2003 presentation.

(In Thousands)	Telecom	Information Solutions	Enterprise Solutions	Corporate and Eliminations	HickoryTech Consolidated
Three Months Ended 3/31/03					
Operating Revenue from Unaffiliated Customers	$ 21,961	$ 1,098	$ 3,911	$	$ 26,970
Intersegment Revenues	69	973		(1,042)	
Total	22,030	2,071	3,911	(1,042)	26,970
Depreciation and Amortization	3,845	544	61	38	4,488
Operating Income (Loss)	6,444	(539)	74	(452)	5,527
Interest Expense	5	18		1,542	1,565
Income Taxes	2,613	(259)	27	(759)	1,622
Net Income (Loss)	3,773	(373)	39	(1,092)	2,347
Identifiable Assets	201,718	8,917	9,363	9,558	229,556
Property, Plant and Equip., Net	127,195	5,845	537	212	133,789
Capital Expenditures	1,372	144	92	127	1,735
Three Months Ended 3/31/02					
Operating Revenue from					
Unaffiliated Customers	$ 20,717	$ 1,034	$ 3,361	$	$ 25,112
Intersegment Revenues	68	915		(983)	
Total	20,785	1,949	3,361	(983)	25,112
Depreciation and Amortization	3,538	510	70	56	4,174
Operating Income (Loss)	6,510	(525)	(151)	(366)	5,468
Interest Expense	5	14		1,937	1,956
Income Taxes	2,643	(244)	(69)	(884)	1,446
Net Income (Loss)	3,813	(352)	(99)	(1,272)	2,090
Identifiable Assets	246,450	8,445	9,104	13,542	277,541
Property, Plant and Equip., Net	129,859	4,836	643	146	135,484
Capital Expenditures	2,787	522	40	139	3,488

NOTE 8. CONTINGENCIES

HickoryTech is involved in certain contractual disputes in the ordinary course of business. HickoryTech does not believe the ultimate resolution of any of these existing matters will have a material adverse effect on its financial position, results of operations or cash flows.

NOTE 9. STOCK COMPENSATION

At March 31, 2003, HickoryTech has four stock-based employee compensation plans, which are described more fully in the HickoryTech Annual Report of Form 10-K for the year ended December 31, 2002. HickoryTech has elected to apply Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its employee and directors stock compensation plans.

In 2002, HickoryTech s Board of Directors modified the terms of the stock options of a retiring officer. The modification extended the period after retirement during which the officer can exercise options. This modification resulted in HickoryTech recognizing $173,000 of compensation expense during the first quarter of 2003.

If HickoryTech had elected to recognize compensation cost based on the fair value of the options as prescribed by SFAS No. 123, the following operating results would have occurred using the Black-Scholes option-pricing model to determine the fair value of the options:

(Dollars in Thousands)	For Three Months Ended 3/31/2003		3/31/2002	
Reported Net Income	**$**	**2,347**	$	2,090
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects		**257**		172
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		**(398)**		(369)
Pro Forma Net Income	**$**	**2,206**	$	1,893
Earnings per share:				
Basic - as reported	**$**	**0.17**	$	0.15
Basic - pro forma	**$**	**0.16**	$	0.14
Diluted - as reported	**$**	**0.17**	$	0.15
Diluted - pro forma	**$**	**0.16**	$	0.14

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION.

FORWARD-LOOKING STATEMENTS

Statements in this Form 10-Q that are not historical fact are forward-looking statements that are based on management s current expectations, estimates and projections about the industry in which HickoryTech operates and management s beliefs and assumptions. Such forward-looking statements are subject to important risks and uncertainties that could cause HickoryTech s future actual results to differ materially from such statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and probabilities, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements, whether as a result of new information, future events or otherwise. Factors that might cause such a difference include, but are not limited to, those contained in this Management s Discussion and Analysis (Item 2) and Exhibit 99 (Cautionary Statement for Purposes of the Safe Harbor Provision of the Private Securities Litigation Reform Act of 1995) to HickoryTech s Annual Report on Form 10-K for the year ended December 31, 2002, which is incorporated herein by reference. You are cautioned not to place undue reliance on these forward looking statements, which speak only as of the date on which they were made. Except as otherwise required by law, HickoryTech undertakes no obligation to update any of its forward-looking statements for any reason.

BUSINESSES

HickoryTech operates in three business segments: the Telecom, Information Solutions and Enterprise Solutions Sectors. Its largest and oldest business (since 1898) has been the operation of incumbent local exchange carriers (ILECs) or traditional wireline telephone service. The ILEC business is in HickoryTech s Telecom Sector. In 1998, HickoryTech began its competitive local exchange carrier (CLEC), competing for the telephone dial tone, data and long distance calling business in other ILECs territories. CLEC is in HickoryTech s Telecom Sector. HickoryTech also began its wireless operations in 1998 by acquiring its first wholly-owned wireless service license, an additional wireless service license in 1999 and two PCS licenses in 2001. These wireless operations, combined with ILEC and CLEC, form HickoryTech s Telecom Sector. Since 1964, HickoryTech s Information Solutions Sector has provided computer data processing and software, predominantly for HickoryTech s Telecom Sector operations and also to other telecommunications companies. HickoryTech acquired its Enterprise Solutions Sector in 1990 and it has operated as a leading telecommunications and data equipment distributor from a base in Minneapolis/St. Paul, Minnesota.

THE COMPANY

The eight subsidiaries of HickoryTech, all of which publicly operate and conduct business as HickoryTech, and the business segments in which they operate are:

TELECOM SECTOR

Mankato Citizens Telephone Company (MCTC)

Mid-Communications, Inc. (Mid-Comm)

Heartland Telecommunications Company of Iowa, Inc. (Heartland)

Cable Network, Inc. (CNI)

Crystal Communications, Inc. (Crystal)

Minnesota Southern Wireless Company (MSWC)

INFORMATION SOLUTIONS SECTOR

National Independent Billing, Inc. (NIBI)

ENTERPRISE SOLUTIONS SECTOR

Collins Communications Systems Co. (Collins)

HickoryTech and its subsidiaries are engaged in businesses that provide services to their customers for a fee. Many of these services are repetitive and recurring, and, as a result, backlog orders and seasonality are not significant factors. Working capital requirements primarily involve the funding of the construction and maintenance of telephone wireline and wireless fixed assets, the payroll costs of highly skilled labor and the inventory to service its telephone equipment customers.

The materials and supplies that are necessary for the operation of the businesses of HickoryTech and its subsidiaries are available from a variety of sources, and no future supply problems are anticipated. All of HickoryTech s ILEC and CLEC central office switches and wireless switches, as well as a majority of HickoryTech s equipment sold in its Enterprise Solutions Sector, are supplied by Nortel. Nortel is a leading supplier of communications equipment, and HickoryTech s dependence on this brand is not viewed as a significant risk.

INDUSTRY SEGMENTS

TELECOM SECTOR

HickoryTech s Telecom Sector provides local exchange wireline and wireless telephone service, long distance, dial-up Internet access and owns and operates fiber optic cable facilities. This sector includes three incumbent local exchange carriers (ILECs), MCTC, Mid-Comm and Heartland. MCTC and Mid-Comm provide telephone service in south central Minnesota, specifically Mankato (a regional hub) and eleven rural communities surrounding Mankato. The third ILEC, Heartland, provides telephone service for eleven rural communities in northwest Iowa.

The Telecom Sector also includes Crystal, a competitive local exchange carrier (CLEC). Crystal provides local telephone service, long distance and dial-up Internet access on a competitive basis. Crystal has customers in eight rural communities in Minnesota and six rural communities in Iowa that are not in HickoryTech s ILEC service areas.

HickoryTech also owns and operates fiber optic cable facilities (CNI) in Minnesota, which are used to transport interexchange communications as a service to telephone industry customers. HickoryTech s Minnesota ILECs and its CLEC are the primary users of the fiber optic cable facilities.

The Telecom Sector also owns and operates a wireless telephone business in south central Minnesota. The wireless telephone business consists of the A-side FCC wireless license to operate in Minnesota s Rural Service Area 10 (RSA 10), the Minneapolis/St. Paul Metro A-2 (Metro A-2) wireless license and two digital personal communications services (PCS) licenses covering the Minnesota Basic Trading Areas (BTAs) of Mankato-Fairmont and Rochester-Austin-Albert Lea.

MCTC derives its principal revenues and income from local services charged to subscribers in its service area, access services charged to interexchange carriers and the operation of a toll tandem switching center in Mankato, Minnesota. Revenues and income for Mid-Comm are also derived from local service charges in its area of operation and by providing access to long distance services for its subscribers through the toll center in Mankato. Local and interexchange telephone access for the two companies is provided on an integrated basis. The local and interexchange telephone access for both telephone companies utilize the same facilities and equipment and is managed and maintained by a common work force. Heartland derives its principal revenues and income from local services charged to subscribers in its service area in Iowa, as well as from providing interexchange access for its subscribers. Interexchange telephone access is provided by all three of HickoryTech s telephone subsidiaries by connecting the communications networks of interexchange and wireless carriers with the equipment and facilities of end users through its switched networks or private lines.

MCTC and Mid-Comm are Minnesota public utilities operating pursuant to indeterminate permits issued by the Minnesota Public Utilities Commission. Heartland is also a public utility, which operates pursuant to a certificate of public convenience and necessity issued by the Iowa Utilities Board. These state agencies regulate the services provided by MCTC, Mid-Comm and Heartland. CNI s operations are not subject to regulation by the state regulatory authority. Neither the Minnesota Public Utilities Commission nor the Iowa Utilities Board regulates the rate of return or profits of each of HickoryTech s ILEC operations. However, the Minnesota Public Utilities Commission regulates the prices and service levels provided by MCTC and Mid-Comm because each company s operations fall below the 50,000 customer line minimum level for rate regulation in Minnesota. In Iowa, Heartland s operations are not rate regulated by the Iowa Utilities Board. MCTC, Mid-Comm and Heartland are each required to file local service rates as tariffs with the applicable state public utilities commission. MCTC s and Mid-Comm s local service rates are below those of most Minnesota ILECs. Regardless of whether a particular rate is subject to regulatory review, the ability of HickoryTech and its subsidiaries to change rates will be determined by various factors, including economic and competitive circumstances.

As local exchange telephone companies, MCTC, Mid-Comm and Heartland provide end office switching and dedicated circuits to long distance interexchange carriers. These relationships allow HickoryTech s telephone subscribers to place long distance telephone calls and gain access to the telephone network. HickoryTech provides long distance access for all of the individual customers who select an alternative long distance carrier. The long distance interexchange carriers are significant customers of HickoryTech, but no carrier represents more than ten percent of HickoryTech s consolidated revenues.

Alternatives to HickoryTech service include customers leasing private line switched voice and data services in or adjacent to the territories served by HickoryTech, which permits the bypassing of local telephone switching facilities. In addition, microwave transmission services, wireless communications, fiber optic and coaxial cable deployment and other services provided by other companies permit bypass of the local exchange network. These alternatives to local exchange service represent a potential threat to HickoryTech s long-term ability to provide local exchange service at economical rates.

Competition in HickoryTech s ILEC service area exists in one of Heartland s exchanges. In the city of Hawarden, Iowa, the municipal city government overbuilt the city s telephone service infrastructure and is providing an alternative to HickoryTech s telephone service. The Hawarden CLEC has acquired approximately 1,000 access lines of that community s telephone business from HickoryTech. HickoryTech management does not believe there will be significant further impact from competition in Hawarden. HickoryTech constantly responds to competitive changes with active programs to market products and to engineer its infrastructure for higher customer satisfaction.

Competition also exists for some of the services provided to interexchange carriers, such as customer billing services, dedicated private lines, and network switching. This competition comes primarily from the interexchange carriers themselves. The provision of these services is of a contractual nature and is primarily controlled by the interexchange carriers. Other services, such as directory advertising and wireless communications, are open to competition. Competition is based primarily on service and experience.

The passage of the 1996 Telecommunications Act created the opportunity for HickoryTech to offer communications service in territories served by other telephone companies, and Crystal began operations in January 1998 as a new competitive local exchange carrier (CLEC). Crystal offers local service, long distance and dial-up Internet access services on a competitive basis to customers in towns in southern Minnesota and Iowa, which are not served by HickoryTech s Telecom Sector s service area. These service offerings provide customers alternatives to the incumbent telephone carrier in various communities and are offered under the brand name HickoryTech wireline service. These services are currently being offered to customers in eight rural communities in Minnesota, as well as six rural communities in Iowa. Crystal s primary strategy is to provide service by overbuilding with new telecommunications switching networks and telephone lines. Crystal also provides the long distance service and dial-up Internet access services to HickoryTech s subscribers in both ILEC and CLEC markets.

Crystal is not subject to regulation by the public utilities commissions in the states it serves regarding rates and services. CLEC activities require Crystal to file for authority to operate with the appropriate public utilities commission in each state it serves. Crystal competes directly against existing ILECs in the areas in which Crystal operates.

Crystal is not dependent upon any single customer or small group of customers. No one customer in Crystal accounts for ten percent or more of HickoryTech s consolidated revenues.

HickoryTech, through its subsidiary MSWC, owns and operates wireless telephone businesses in south central Minnesota and in the Minneapolis/St. Paul area. In south central Minnesota, MSWC provides wireless service for Minnesota s Rural Service Area 10 (RSA 10), under the brand name of HickoryTech Wireless. This business is in HickoryTech s Telecom Sector. This sector owns 100% of the A-side FCC wireless license to operate in seven counties in south central Minnesota. The area overlaps and is larger than HickoryTech s Minnesota ILEC and CLEC service areas and serves a population of approximately 230,000. This sector also owns the Minneapolis/St. Paul Metro A-2 (Metro A-2) wireless license, which was acquired on June 1, 1999. The Metro A-2 property surrounds the metropolitan Minneapolis/St. Paul area and is located in five Minnesota counties and in one Wisconsin county. Metro A-2 provides service to an area with a population of approximately 170,000. In addition, this sector also owns the PCS licenses for the Minnesota BTAs of Mankato-Fairmont and Rochester-Austin-Albert Lea. The two BTAs are located in 16 Minnesota counties and one Iowa county and provide service to an area with a population of approximately 493,000, some of which coincide with the previously mentioned wireless RSA 10 population of 230,000.

MSWC, which owns all four of the Company s FCC wireless licenses, derives its principal revenues and income from providing wireless telephone service to the retail customers in seven counties in south central Minnesota and from wireless roaming traffic. MSWC also derives roaming revenue from the six counties surrounding the metropolitan Minneapolis/St. Paul Metro A-2 area and roaming revenues from the PCS service territory that is comprised of 17 counties. MSWC directly competes against local wireless and PCS companies in southern Minnesota and in the Minneapolis/St. Paul area.

INFORMATION SOLUTIONS SECTOR

Through NIBI, HickoryTech s Information Solutions Sector provides data processing and related services, principally for HickoryTech, other local exchange telephone companies, CLECs, interexchange network carriers, wireless companies, municipalities and utilities. The Information Solutions Sector s principal activity is the provision of monthly batch processing of computerized data for HickoryTech as well as non-affiliated companies. Services for telephone company customers include the processing of long distance telephone calls from data sources and telephone switches, the preparation of the subscriber telephone bills, customer record keeping, carrier access bills and general accounting and payroll services. NIBI, under the brand name HickoryTech Information Solutions, also provides certain billing clearinghouse functions for interexchange carriers.

There are a number of companies engaged in supplying data processing services comparable to those furnished by the Information Solutions Sector. Competition is based primarily on price and service. HickoryTech s Information Solutions Sector has developed an integrated billing and management system called SuiteSolution. For internal use, SuiteSolution enables HickoryTech to become a full-service billing provider for all aspects of the telecommunications industry on a fully integrated basis. For external use, SuiteSolution can provide wireline or wireless carriers the individual benefits of a billing platform, or to integrated service providers, such as HickoryTech, a total system solution. SuiteSolution was implemented in the Company s CLEC businesses in 2002 and will be implemented in the Company s wireless business in 2003. SuiteSolution is currently available to external customers.

ENTERPRISE SOLUTIONS SECTOR

Through Collins, HickoryTech s Enterprise Solutions Sector provides telephone and data equipment sales and services as well as the sale, installation and service of voice over Internet Protocol business systems to companies primarily based in metropolitan Minneapolis/St. Paul, Minnesota. This sector also supports the business telephone system service for HickoryTech ILEC and CLEC operations in southern Minnesota and in Iowa. The customers in the Enterprise Solutions Sector s market are the individual business end users of telecommunications service with ongoing service requirement offerings. Products consist of telecommunication platforms such as Nortel on the voice side of the Enterprise Solutions business, and Cisco and Bay Networks (Nortel) equipment on the data side of its business. Enterprise Solutions specializes in the quality custom installation and maintenance of wide area networking, local networking and transport solutions in telecommunications for end user customers.

Revenues are primarily earned by the sales, installation and service of business telephone systems. Enterprise Solutions continues its commitment to service and support of its core product, Nortel, while identifying new opportunities such as call centers, computer telephone integration voice mail and interactive voice response systems.

HickoryTech s Enterprise Solutions Sector is not dependent upon any single customer or small group of customers. No one customer in the Enterprise Solutions Sector accounts for ten percent or more of HickoryTech s consolidated revenues.

There are companies competing in the equipment sales and service and voice over Internet Protocol communications products market in which Enterprise Solutions operates. Competition is based primarily on price and service. No one company is dominant in this field. Enterprise Solutions offers customer premises telephone and data equipment through well-trained and experienced market representatives with long-term customer relationships. The Enterprise Solutions Sector enjoys a very strong brand awareness and a reputation for quality service. Enterprise

Solutions has built a strong base of solid customers with ongoing needs and Enterprise Solutions goal is to derive 60-70% of its recurring revenue from sales to its existing customer base. The Enterprise Solutions Sector s activities are focused on the sale, installation and service of business telephone systems and data communications equipment to companies based in metropolitan Minneapolis/St. Paul, Minnesota. This sector also supports the business telephone system service for HickoryTech s ILEC and CLEC operations in Minnesota and Iowa.

RESULTS OF OPERATIONS

CONSOLIDATED OPERATING RESULTS

The following is a summarized discussion of consolidated results of operations. More detailed discussion of operating results by segment follows this discussion.

OPERATING REVENUES - Consolidated operating revenues were $1,858,000 or 7.4% higher in the first quarter of 2003 compared to the first quarter of 2002. The revenue increase in the first quarter of 2003 was primarily attributable to a higher volume of business in the Enterprise Solutions Sector and an increase in revenue in the Telecom Sector. The Enterprise Solutions increase is primarily the result of completing the final phase of work for a large specialty retailer. This project, which began in 2002, involved installing a voice over Internet Protocol network in a corporate office. The Telecom Sector increases can be primarily attributed to the increase in the CLEC customer base and the result of services provided under terms of a multi-year contract awarded to HickoryTech effective July 1, 2002 to provide Internet access and video conferencing to schools and libraries in south central Minnesota served by the Project SOCRATES distance-learning network.

COST OF SALES, ENTERPRISE SOLUTIONS - Cost of sales is related to the Enterprise Solutions Sector and was $335,000 or 15.3% higher in the first quarter of 2003 compared to the first quarter of 2002. The change in cost of sales is primarily the result of the change in sales volume in the Enterprise Solutions Sector. The gross profit margin in the Enterprise Solutions Sector was 35.6% and 35.0% for the quarters ended March 31, 2003 and 2002, respectively.

OPERATING EXPENSES (excluding Depreciation and Amortization) - Operating expenses excluding depreciation and amortization would have increased $1,150,000 or 8.7% in the first quarter of 2003 compared to the first quarter of 2002. Operating expenses in the first quarter of 2003 were higher largely due to increased expenses in the Telecom Sector related to the growth in CLEC customers and the costs associated with Project Socrates, a distance-learning network that provides Internet access and video conferencing to schools and libraries in south central Minnesota.

DEPRECIATION AND AMORTIZATION - Depreciation expense was $349,000 or 9.2% higher in the first quarter of 2003 compared to the first quarter of 2002. Increases in the ILEC, CLEC and Wireless network assets primarily account for the increase in depreciation expense. Amortization expense was $35,000 or 9.7% lower in the first quarter of 2003 compared to the first quarter of 2002.

OPERATING INCOME - Operating income was $5,527,000 which is $59,000 or 1.1% higher in the first quarter of 2003 compared to the first quarter of 2002. The increase in operating income was largely due to increased revenues in the

Enterprise Solutions Sector, and increased CLEC revenues in the Telecom Sector, which were offset by the increase in the cost of sales of the Enterprise Solutions Sector and the increase in operating expenses of the Telecom Sector.

INTEREST EXPENSE - Interest expense decreased $391,000 or 20.0% in the first quarter of 2003 compared to the first quarter of 2002. The decrease in interest expense in the first quarter of 2003 was primarily due to a decrease in the weighted average interest rate on HickoryTech s revolving credit facility from 5.2% to 4.3% in the first quarter of the years 2002 and 2003, respectively, and a decrease in total debt outstanding. The outstanding balance of the revolving credit facility was $148,250,000 at March 31, 2003 and $165,750,000 at March 31, 2002.

NET INCOME - Consolidated net income was $257,000 or 12.3% higher in the first quarter of 2003 compared to the first quarter of 2002. The increase in the operating revenues of the Telecom and Enterprise Solutions Sectors was partially offset by the increase in the Enterprise Solutions cost of sales and Telecom operating expenses.

SECTOR RESULTS OF OPERATIONS

TELECOM The following table provides a breakdown of the Telecom Sector operating results.

TELECOM SECTOR

(Dollars in Thousands)	For Three Months Ended 3/31/2003	3/31/2002
Revenues Before Intersegment Eliminations		
ILEC		
Local Service	**$ 3,799**	$ 3,802
Network Access	**8,324**	8,067
Intersegment	**69**	68
Other	**2,262**	2,327
Total ILEC	**14,454**	14,264
CLEC		
Local Service	**908**	699
Other	**1,306**	660
Total CLEC	**2,214**	1,359
Long Distance	**1,028**	913
Internet	**941**	847
Wireless		
Service	**2,447**	2,334
Home Roaming	**174**	194
Roaming	**772**	874
Total Wireless	**3,393**	3,402
Total Telecom Revenues	**$ 22,030**	$ 20,785
Total Telecom Revenues Before Intersegment Eliminations		
Unaffiliated Customers	**$ 21,961**	$ 20,717
Intersegment	**69**	68
	22,030	20,785
Operating Expenses, excluding Depr. and Amort.	**11,741**	10,737
Depreciation and Amortization	**3,845**	3,538
Operating Income	**$ 6,444**	$ 6,510

Net Income	**$**	**3,773**	$	3,813
Operating Income/(Loss)	**$**	**6,444**	$	6,510
Depreciation and Amortization		**3,845**		3,538
Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)	**$**	**10,289**	$	10,048
Capital Expenditures	**$**	**1,372**	$	2,787
ILEC Access Lines		**64,495**		66,212
CLEC Access Lines				
Overbuild		**8,035**		6,241
Unbundled Network Element (UNE)		**1,361**		1,188
Total Service Resale (TSR)		**4,875**		4,304
Total		**14,271**		11,733
Long Distance Customers		**36,610**		25,436
Internet Customers		**14,988**		13,517
Wireless Customers		**26,349**		26,091
Total Telecom Customers		**156,713**		142,989

Telecom Sector operating revenues before intersegment eliminations increased $1,245,000 or 6% in first quarter of 2003 compared to the first quarter of 2002. The increase in the first quarter of 2003 compared to the first quarter of 2002 was primarily due to growth in the CLEC, Long Distance and Internet service revenues as well as increased ILEC network access, and increased wireless service revenue, partially offset by decreases in roaming revenue and ILEC local service revenue.

ILEC local service revenue decreased $3,000 or 0.1% in the first quarter of 2003 compared to the first quarter of 2002. This decrease was due to a 1,717 or 2.6% decline in ILEC access lines between March 31, 2002 and March 31, 2003. The decline in access lines was offset by higher revenue from vertical services such as caller identification, call waiting and three-way calling in the first quarter of 2003 compared to the first quarter of 2002.

ILEC network access revenue increased $257,000 or 3.2% in the first quarter of 2003 compared to the first quarter of 2002. The increase in network access revenue in the first quarter of 2003 compared to the first quarter of 2002 was driven by higher demand for dedicated lines and high-speed circuits.

CLEC local service revenue increased $209,000 or 29.9% in the first quarter of 2003 compared to the first quarter of 2002. CLEC access lines increased 2,538 or 21.6% between March 31, 2002 and March 31, 2003, which was the primary reason for the increase.

Other CLEC revenue increased $646,000 or 97.9% in the first quarter of 2003 compared to the first quarter of 2002. Other revenue included network access, high-speed data revenues and digital TV, which generally grew along with the increase in access lines in the first quarter of 2003 compared to the first quarter of 2002. Another reason for the increase in other revenue in the first quarter of 2003 was the additional $370,000 of revenue recognized as a result of services provided under terms of a multi-year contract awarded to HickoryTech effective July 1, 2002 to provide Internet access and video conferencing to schools and libraries in south central Minnesota served by the Project SOCRATES distance-learning network.

Long distance revenue increased $115,000 or 12.6% in the first quarter of 2003 compared to the first quarter of 2002. HickoryTech experienced an 11,174 or 43.9% increase in its long distance customer base between March 31, 2002 and March 31, 2003. Although the customer base is increasing, revenue per customer is decreasing. The decrease in revenue per customer is primarily the result of optional long distance services available to customers, the increased use of Internet services and other alternatives to long distance services.

Internet revenue increased $94,000 or 11.1% in the first quarter of 2003 compared to the first quarter of 2002. The increase in revenue was caused primarily by an increase in Internet customers of 1,471 between March 31, 2002 and March 31, 2003. In addition to the increase in customers, Internet revenue increased due to a migration of Internet customers from low-price introductory rate plans to mid-range full-service Internet packages.

Wireless service revenue increased $113,000 or 4.8% in the first quarter of 2003 compared to the first quarter of 2002. Wireless customer counts increased 258 or 1% between March 31, 2002 and March 31, 2003. The increase in service revenue was largely a result of increased equipment revenue, offset by a decline in the average revenue per subscriber.

Wireless roaming revenue decreased $102,000 or 11.7% in the first quarter of 2003 compared to the first quarter of 2002. Roaming minutes from other wireless carriers   customers traveling into HickoryTech s wireless service territory have declined from historical levels, particularly due to technological changes among other wireless providers, which re-route the roaming minutes from HickoryTech s wireless service towers to other providers. In addition, other PCS wireless carriers have continued to build-out PCS licenses to carry their own customers   traffic rather than pay roaming to HickoryTech.

Operating expenses excluding depreciation and amortization would have increased $1,004,000 or 9.4% in the first quarter of 2003 compared to the first quarter of 2002. The increase in operating expenses was due primarily to the costs associated with the growth in CLEC customers and costs associated with Project SOCRATES, a distance-learning network that provides Internet access and video conferencing to schools and libraries in south central Minnesota.

Depreciation and amortization increased $307,000 or 8.7% in the first quarter of 2003 compared to the first quarter of 2002. Depreciation expense increased $113,000 or 5.1% for the first quarter of 2003 compared to the first quarter of 2002 for the increased network infrastructure associated with ILEC services. Depreciation expense increased $136,000 or 18.1% in the first quarter of 2003 compared to the first quarter of 2002 for the increased network infrastructure associated with CLEC services. Depreciation expense increased $124,000 or 23.3% in the first quarter of 2003 compared to the first quarter of 2002 for the networks associated with Wireless services. These increases were partially offset by a $66,000 decrease in amortization expense.

Total operating expenses increased $1,311,000 in the first quarter of 2003 compared to the first quarter of 2002 for the reasons described in the preceding two paragraphs.

Operating income decreased $66,000 or 1.0% in the first quarter of 2003 compared to the first quarter of 2002. Net income decreased $40,000 or 1.0% in the first quarter of 2003 compared to the first quarter of 2002. These decreases were for the reasons described above.

18

Earnings before Interest, Taxes, Depreciation and Amortization increased $241,000 or 2.4% in the first quarter of 2003 compared to the first quarter of 2002. EBITDA margins (i.e. EBITDA divided by revenues) for this sector were 46.7% and 48.3% for the three months ended March 31, 2003 and 2002, respectively. Despite the $1,245,000 increase in revenues, EBITDA increased only $241,000 due to the increase in operating expenses, excluding depreciation and amortization, as discussed above. EBITDA represents a non-GAAP financial measure. A reconciliation of this measure to the appropriate GAAP measure is included in the table above. HickoryTech defines EBITDA as operating income/(loss) excluding depreciation and amortization expense. EBITDA, which is not a measure of financial performance or liquidity under generally accepted accounting principles, is provided because management believes that EBITDA is a useful supplement to operating income/(loss) and other statements of operations data in understanding HickoryTech s ability to service and/or incur indebtedness and is useful in measuring the performance and relative value of HickoryTech s business. Because of the variety of methods used by companies and analysts to calculate EBITDA, and the fact that EBITDA calculations may not accurately measure a company s profitability or its ability to meet debt service requirements, caution should be used in relying on any EBITDA presentation. EBITDA should not be considered as an indicator of operating performance or whether cash flows will be sufficient to fund cash needs.

INFORMATION SOLUTIONS The following table provides a breakdown of the Information Solutions Sector operating results.

INFORMATION SOLUTIONS SECTOR

	For Three Months Ended	
(Dollars in Thousands)	**3/31/2003**	**3/31/2002**
Revenues Before Eliminations		
Unaffiliated Customers	**$ 1,098**	$ 1,034
Intersegment	**973**	915
	2,071	1,949
Operating Expenses, excluding Depr. and Amort.	**2,066**	1,964
Depreciation and Amortization	**544**	510
Operating Loss	**$ (539)**	$ (525)
Net Loss	**$ (373)**	$ (352)
Operating Loss	**$ (539)**	$ (525)
Depreciation and Amortization	**544**	510
Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)	**$ 5**	$ (15)
Capital Expenditures	**$ 144**	$ 522

Operating revenues from unaffiliated customers increased $64,000 or 6.2% in the first quarter of 2003 compared to the first quarter of 2002. The increase in operating revenues in the first quarter of 2003 was primarily due to the impact of a new customer relationship for monthly batch processing services using the WRITE2K billing platform.

Operating expenses excluding depreciation and amortization would have increased $102,000 or 5.2% in the first quarter of 2003 compared to the first quarter of 2002. There were several small variances that contributed to this change between periods. Expenses for the remainder of the year are expected to be comparable to the first quarter of 2003.

Depreciation and amortization expense increased $34,000 or 6.7% in the first quarter of 2003 compared to the first quarter of 2002. Depreciation expense in the first quarter of 2003 was $10,000 lower compared to the first quarter of 2002. Amortization expense increased $44,000 or 17.1% in the first quarter of 2003 compared to the first quarter of 2002.

Total operating expenses increased $136,000 in the first quarter of 2003 compared to the first quarter of 2002 for the reasons described in the preceding two paragraphs.

Operating loss increased $14,000 or 2.7% in the first quarter of 2003 compared to the first quarter of 2002. Net loss increased $21,000 or 6.0% in the first quarter of 2003 compared to the first quarter of 2002. The increase in operating loss and net loss was primarily attributable to the increase in operating expenses, depreciation and amortization, partially offset by the increase in revenue, discussed above.

Earnings before Interest, Taxes, Depreciation and Amortization increased $20,000 or 133.3% in the first quarter of 2003 compared to the first quarter of 2002. The EBITDA margin (i.e. EBITDA divided by revenues) for this sector was 0.2% in the first quarter 2003, compared to (0.8%) in the first quarter of 2002. The increase in EBITDA and the EBITDA margin was primarily due to increased operating revenues. EBITDA represents a non-GAAP financial measure. A reconciliation of this measure to the appropriate GAAP measure is included in the table above. HickoryTech defines EBITDA as operating income/(loss) excluding depreciation and amortization expense. EBITDA, which is not a measure of financial performance or liquidity under generally accepted accounting principles, is provided because management believes that EBITDA is a useful supplement to operating income/(loss) and other statements of operations data in understanding HickoryTech s ability to service and/or incur indebtedness and is useful in measuring the performance and relative value of HickoryTech s business. Because of the variety of methods used by companies and analysts to calculate EBITDA, and the fact that EBITDA calculations may not accurately measure a company s profitability or its ability to meet debt service requirements, caution should be used in relying on any EBITDA presentation. EBITDA should not be considered as an indicator of operating performance or whether cash flows will be sufficient to fund cash needs.

ENTERPRISE SOLUTIONS The following table provides a breakdown of the Enterprise Solutions Sector operating results.

ENTERPRISE SOLUTIONS SECTOR

	For Three Months Ended			
(Dollars in Thousands)		**3/31/2003**		**3/31/2002**
Revenues Before Intersegment Eliminations				
Installation	**$**	**1,958**	$	1,395
Service		**1,953**		1,966
		3,911		3,361
Cost of Sales		**2,519**		2,184
Operating Expenses, excluding Depr. and Amort.		**1,257**		1,258
Depreciation and Amortization		**61**		70
Operating Income (Loss)	**$**	**74**	$	(151)
Net Income (Loss)	**$**	**39**	$	(99)
Operating Income (Loss)	**$**	**74**	$	(151)
Depreciation and Amortization		**61**		70
	$	**135**	$	(81)

Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)				
Capital Expenditures	**$**	**92**	$	40

Operating revenues increased $550,000 or 16.4% in the first quarter of 2003 compared to the first quarter of 2002. Installation revenue was $563,000 or 40.4% higher in the first quarter of 2003 compared to the first quarter of 2002. The increase in installation revenue in first quarter of 2003 compared to the first quarter of 2002 was primarily a result of an increase in sales and installations of PBX systems of $272,000 and an increase in sales of data network equipment of $219,000. The majority of the increase in installation revenue was the result of completing the final phase of work for a large specialty retailer. This project, which began in 2002, involved installing a voice over Internet Protocol network in a corporate office. Service revenue was $13,000 or .7% lower in the first quarter of 2003 compared to the first quarter of 2002.

Cost of sales increased $335,000 or 15.3% in the first quarter of 2003 compared to the first quarter of 2002. Gross profit margin for this sector in the first quarter of 2003 and 2002 was 35.6% and 35.0%, respectively. The increase in cost of sales was the result of the increased installation efforts described above.

Operating expenses excluding depreciation and amortization would have decreased $1,000 or 0.1% in the first quarter of 2003 compared to the first quarter of 2002. Depreciation and amortization decreased $9,000 or 12.9% in the first quarter of 2003 compared to the first quarter of 2002.

Total operating expenses decreased $10,000 in the first quarter of 2003 compared to the first quarter of 2002 for the reasons described in the preceding two paragraphs.

Operating income was $74,000 in the first quarter of 2003 compared to operating loss of $151,000 in the first quarter of 2002. Net income in the first quarter of 2003 was $39,000 compared to a net loss of $99,000 in the first quarter of 2002. The income generated in the first quarter of 2003 as compared to the loss in the first quarter of 2002 resulted primarily from the changes in operating revenues described above.

Earnings before Interest, Taxes, Depreciation and Amortization increased $216,000 or 266.7% in the first quarter of 2003 compared to the first quarter of 2002. The EBITDA margin (i.e. EBITDA divided by revenues) for this sector was 3.5% in the first quarter of 2003 compared to (2.4%) in the first quarter of 2002. The changes in EBITDA and the EBITDA margin were primarily due to the increase in operating revenues. EBITDA represents a non-GAAP financial measure. A reconciliation of this measure to the appropriate GAAP measure is included in the table above. HickoryTech defines EBITDA as operating income/(loss) excluding depreciation and amortization expense. EBITDA, which is not a measure of financial performance or liquidity under generally accepted accounting principles, is provided because management believes that EBITDA is a useful supplement to operating income/(loss) and other statements of operations data in understanding HickoryTech s ability to service and/or incur indebtedness and is useful in measuring the performance and relative value of HickoryTech s business. Because of the variety of methods used by companies and analysts to calculate EBITDA, and the fact that EBITDA calculations may not accurately measure a company s profitability or its ability to meet debt service requirements, caution should be used in relying on any EBITDA presentation. EBITDA should not be considered as an indicator of operating performance or whether cash flows will be sufficient to fund cash needs.

LIQUIDITY AND CAPITAL RESOURCES

CASH FLOWS Cash provided by operations was $9,277,000 in the first quarter of 2003 compared to $7,908,000 in the first quarter of 2002. Cash flows from operations in the first quarter of 2003 and 2002 were primarily attributable to net income plus non-cash expenses for depreciation and amortization and a decrease in receivables, partially offset by decreases in accounts payable related to timing of payments. The increase in cash flows from operations in the first quarter of 2003 relative to the same period in 2002 was primarily due to a $257,000 increase in net income and a $1,787,000 reduction in accounts payable and accrued expenses during the first quarter of 2003, compared to a $2,625,000 reduction during the first quarter of 2002.

Cash flows provided by investing activities were $2,425,000 in the first quarter of 2003 compared to cash flows used of $3,216,000 for the same period in 2002. Capital expenditures relating to ongoing businesses were $1,735,000 during the first quarter of 2003 as compared to $3,488,000 for the same period in 2002. Capital expenditures were incurred primarily to construct additional network facilities to provide CLEC services and continued buildout of the PCS network in the Telecom Sector in 2002. In addition, there was a $4,100,000 redemption of investments in the first quarter of 2003, compared to $100,000 in the first quarter of 2002. The first quarter of 2003 redemption reflects the amount by which HickoryTech was permitted to reduce its equity investment in one of its lenders.

Cash flows used in financing activities were $11,465,000 for the first quarter of 2003 compared to $5,682,000 for the first quarter of 2002. Included in cash flows from financing activities are debt repayments and dividend payments. HickoryTech made payments on its revolving credit facility of $9,750,000 during the first quarter of 2003, and $4,250,000 during the first quarter of 2002. Dividend payments for the first quarter of 2003 were $1,540,000 compared to $1,537,000 for the same period in 2002. During the first quarter of 2003, HickoryTech also repurchased 16,100 common shares for $161,000.

WORKING CAPITAL Working capital (i.e. current assets minus current liabilities) was $10,935,000 as of March 31, 2003, compared to working capital of $13,073,000 as of December 31, 2002. The ratio of current assets to current liabilities was 1.9:1.0 as of March 31, 2003 and as of December 31, 2002. Management believes adequate internal and external resources are available to finance ongoing operating requirements, including capital expenditures, business development, debt service and the payment of dividends for at least the next twelve months.

LONG-TERM OBLIGATIONS - HickoryTech s long-term obligations as of March 31, 2003 were $147,740,000, excluding current maturities of $1,405,000. As of March 31, 2003, HickoryTech had a $182,750,000 credit facility with a syndicate of banks. The credit facility is comprised of a $125,000,000 revolving credit component and a $57,750,000 term loan component. The available line of credit on the $125,000,000 revolving credit component decreases in increments beginning in March 2004 with a final maturity date in September 2008. The term loan component requires equal quarterly principal payments of $250,000 during the period of March 2001 to December 2008, and $23,000,000 of principal payments per quarter for the first two quarters in 2009 and $6,000,000 in the third quarter of 2009. The weighted average interest rate associated with this credit facility varies with LIBOR and certain other rates and was 4.3% at March 31, 2003. HickoryTech has implemented fixed interest terms on various portions of the overall debt outstanding for varying terms. The longest fixed interest term, on $40,000,000 of the debt, is fixed until June 2003. As of March 31, 2003, HickoryTech had drawn $148,250,000 on this credit facility and had $34,500,000 of available credit. Management believes the remaining available credit is sufficient to cover future cash requirements.

HickoryTech s Information Solutions Sector leases certain computer equipment under capital lease arrangements. During the first quarter of 2003, this sector recorded no additions to property, plant and equipment related to these capital lease arrangements.

The following table sets forth HickoryTech s contractual obligations, along with the cash payments due each period:

		Payments Due by Year
(Dollars in Thousands)	**Total**	

		Remainder of 2003	2004 to 2006	2007 to 2008	2009 and after
Contractual Obligations					
Long-term Debt	$ 148,250	$ 750	$ 32,563	$ 62,937	$ 52,000
Interest on Long-term Debt	32,659	5,228	18,159	8,056	1,216
Capital Lease Obligations	895	296	599		
Interest on Capital Leases	64	33	31		
Operating Leases	3,862	861	1,810	465	726
Total Contractual Cash Obligations	$ 185,730	$ 7,168	$ 53,162	$ 71,458	$ 53,942

Interest on Long-term Debt is estimated using interest rated as of March 31, 2003.

The total commitment to HickoryTech on its revolving credit facility expires as follows:

		Amount of Commitment Expiration per Year
		Remainder
(Dollars in Thousands)	**Total**	**of 2003**

Table of Contents

Results of Operations

Revenue

(dollars in thousands)	Three months ended December 31, 2016	2015	Change
Pharmaceutical Distribution	$36,575,967	$35,194,679	3.9%
Other	1,663,654	1,577,815	5.4%
Intersegment eliminations	(70,356)	(63,448)	10.9%
Revenue	$38,169,265	$36,709,046	4.0%

Revenue increased by 4.0% from the prior year quarter. See discussions below under “Pharmaceutical Distribution” and “Other” for commentary regarding our revenue growth.

We currently expect our revenue in fiscal 2017 to increase between 6.5% and 8%. Our future revenue growth will continue to be affected by various factors such as industry growth trends, including drug utilization, the introduction of new innovative brand therapies, the likely increase in the number of generic drugs that will be available over the next few years as a result of the expiration of certain drug patents held by brand-name pharmaceutical manufacturers, price increases and price deflation, general economic conditions in the United States, competition within the industry, customer consolidation, changes in pharmaceutical manufacturer pricing and distribution policies and practices, increased downward pressure on government and other third party reimbursement rates to our customers, and changes in Federal government rules and regulations.

Pharmaceutical Distribution Segment

The Pharmaceutical Distribution segment grew its revenue by 3.9% from the prior year quarter. Intrasegment revenues between ABDC and ABSG have been eliminated in the presentation of total Pharmaceutical Distribution revenue. Intrasegment revenues primarily consisted of ABSG sales directly to ABDC customer sites or ABSG sales to ABDC facilities. Intrasegment revenues were $2.2 billion and $1.7 billion in the quarters ended December 31, 2016 and 2015, respectively.

ABDC’s revenue of $31.2 billion in the quarter ended December 31, 2016 increased 3.6% from the prior year period (before intrasegment eliminations). The increase in ABDC’s revenue was primarily due to the growth of some of ABDC's larger customers and due to overall market growth.

ABSG’s revenue of $7.5 billion in the quarter ended December 31, 2016 increased 10.3% from the prior year period (before intrasegment eliminations). The increase in ABSG’s revenue was due to strong overall performance, especially in the sale of oncology products (including sales to community oncologists), and increased sales in our third party logistics business.

A number of our contracts with customers, including GPOs, are typically subject to expiration each year. We may lose a significant customer if any existing contract with such customer expires without being extended, renewed, or replaced. During the three months ended December 31, 2016, no significant contracts expired. Over the next twelve months, only one significant contract is scheduled to expire. Our contract with Express Scripts expires in September 2017. Additionally, from time to time, other significant contracts may be renewed prior to their expiration dates. If those contracts are renewed at less favorable terms, they may also negatively impact our revenue, results of operations, and cash flows.

Other

Revenue in Other increased 5.4% from the prior year quarter primarily due to increased revenue from ABCS and MWI.

Table of Contents

Gross Profit

(dollars in thousands)	Three months ended December 31, 2016	2015	Change
Pharmaceutical Distribution	$755,245	771,968	(2.2)%
Other	309,361	281,680	9.8%
Intersegment eliminations	(13)	—	
Gain from antitrust litigation settlements	1,395	12,791	
LIFO expense	(28,308)	(101,562)	
Gross profit	$1,037,680	$964,877	7.5%

Gross profit increased 7.5%, or $72.8 million, from the prior year quarter. The increase was due to the decrease in LIFO expense of $73.3 million and the increase in gross profit of Other, partially offset by a decrease in gross profit of Pharmaceutical Distribution. The decrease in LIFO expense was primarily due to lower brand inflation and various other factors as noted below.

Our cost of goods sold for interim periods includes a LIFO provision that is based on our estimated annual LIFO provision. The annual LIFO provision, which we estimate on a quarterly basis, is affected by expected changes in inventory quantities, product mix, and manufacturer pricing practices, which may be impacted by market and other external influences, many of which are difficult to predict. Changes to any of the above factors may have a material impact to our annual LIFO provision.

Pharmaceutical Distribution gross profit decreased 2.2%, or $16.7 million, from the prior year quarter. Gross profit in the current year quarter was adversely impacted by prior year contract renewals in the second half of fiscal 2016 with a significant GPO customer and Kaiser at less favorable terms and lower price appreciation, offset in part by the incremental contribution from PharMEDium, which was acquired on November 6, 2015. As a percentage of revenue, Pharmaceutical Distribution gross profit margin of 2.06% in the quarter ended December 31, 2016 decreased 13 basis points from the prior year quarter primarily due to the above-mentioned contract renewals at less favorable terms, increased sales to some of our larger customers that typically have a lower gross profit margin, and lower price appreciation.

Gross profit in Other increased 9.8%, or $27.7 million, from the prior year quarter. The increase from the prior year quarter was primarily due to increased contributions from MWI and ABCS. As a percentage of revenue, gross profit margin in Other of 18.60% in the quarter ended December 31, 2016 increased from 17.85% in the prior year quarter, primarily due to improved gross profit margin at MWI.

We recognized gains of $1.4 million and $12.8 million from antitrust litigation settlements with pharmaceutical manufacturers during the quarters ended December 31, 2016 and 2015, respectively. The gains were recorded as reductions to cost of goods sold.

Operating Expenses

(dollars in thousands)	Three months ended December 31, 2016	2015 (As Revised)	Change
Distribution, selling, and administrative	$520,547	$525,077	(0.9)%
Depreciation and amortization	96,080	82,962	15.8%
Warrants expense	—	467,375	

Employee severance, litigation, and other	21,066	18,868	
Pension settlement charge	—	48,731	
Total operating expenses	$637,693	$1,143,013	(44.2)%

Distribution, selling, and administrative expenses decreased 0.9%, or $4.5 million, from the prior year quarter. As a percentage of revenue, distribution, selling, and administrative expenses were 1.36% in the current year quarter and represent a decrease of 7 basis points compared to the prior year quarter. The decrease in expenses in comparison to the prior year quarter was primarily due to initiatives taken in the second half of fiscal 2016 to improve operating efficiency across many of our businesses and certain administrative functions.

Table of Contents

Depreciation expense increased 9.8% from the prior year quarter due to an increase in the amount of capital projects being depreciated. Amortization expense increased 25.3% from the prior year quarter primarily due to the amortization of intangible assets originating from our November 6, 2015 acquisition of PharMEDium.

There was no Warrants expense in the current year quarter as the Warrants were exercised in March 2016 and August 2016.

Employee severance, litigation, and other for the quarter ended December 31, 2016 included a $16.0 million settlement of a state litigation proceeding (see Note 8 of the Notes to the Consolidated Financial Statements for further details) and $5.0 million of other costs. Employee severance, litigation, and other for the quarter ended December 31, 2015 included $16.1 million of deal-related transaction costs (primarily related to professional fees with respect to the PharMEDium acquisition) and $2.8 million of other costs.

Operating Income

(dollars in thousands)	Three months ended December 31, 2016	2015 (As Revised)	Change
Pharmaceutical Distribution	$374,002	$381,254	(1.9)%
Other	112,206	95,565	17.4%
Intersegment eliminations	(13)	—	
Total segment operating income	486,195	476,819	2.0%
Gain from antitrust litigation settlements	1,395	12,791	
LIFO expense	(28,308)	(101,562)	
Acquisition-related intangibles amortization	(38,229)	(31,210)	
Warrants expense	—	(467,375)	
Employee severance, litigation, and other	(21,066)	(18,868)	
Pension settlement	—	(48,731)	
Operating income (loss)	$399,987	$(178,136)	

Segment operating income is evaluated before gain from antitrust litigation settlements; LIFO expense; acquisition-related intangibles amortization; Warrants expense; employee severance, litigation, and other; and the pension settlement.

Pharmaceutical Distribution operating income decreased 1.9%, or $7.3 million, from the prior year quarter due to the decrease in gross profit, offset in part by the decrease in operating expenses. As a percentage of revenue, Pharmaceutical Distribution operating income margin decreased 6 basis points from the prior year quarter primarily due to the prior year contract renewals at less favorable terms, increased sales to some of our larger customers that typically have a lower gross profit margin, and lower price appreciation, offset in part by our initiatives to improve operating efficiency.

Operating income in Other increased 17.4%, or $16.6 million, from the prior year quarter primarily due to the gross profit increase of MWI and ABCS.

Interest expense, net and the respective weighted average interest rates in the quarters ended December 31, 2016 and 2015 were as follows:

2016 2015

(dollars in thousands)	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate
			(As Revised)	
Interest expense	$37,987	2.81%	$34,449	2.76%
Interest income	(1,015)	0.40%	(708)	0.28%
Interest expense, net	$36,972		$33,741	

Interest expense, net increased 9.6%, or $3.2 million, from the prior year quarter due to an increase of $127.1 million in average variable rate borrowings primarily due to the November 2015 variable-rate term loan borrowing to finance a portion

23

Table of Contents

of the PharMEDium acquisition. Additionally, our average borrowing rate was slightly higher during the current year quarter in comparison to the prior year quarter.

Income tax expense was $115.9 million in the current year quarter compared to an income tax benefit of $541.2 million in the prior year quarter. The tax benefit in the prior year quarter was the result of an IRS private letter ruling that entitled us to an income tax deduction equal to the fair value of the Warrants on the date of the exercise. Our income tax rate, excluding the effect of the Warrants, has also been favorably impacted in fiscal 2017 due to the growth of our international businesses.

Net income was $247.2 million in the quarter ended December 31, 2016 as compared to net income of $329.6 million in the prior year quarter. Net income was higher in the prior year quarter primarily due to the large income tax benefit, offset in part by the Warrants expense.

Liquidity and Capital Resources

The following table illustrates our debt structure at December 31, 2016, including availability under the multi-currency revolving credit facility, the receivables securitization facility, the revolving credit note, and the overdraft facility:

(in thousands)	Outstanding Balance	Additional Availability
Fixed-Rate Debt:		
$600,000, 1.15% senior notes due 2017	$599,365	$—
$400,000, 4.875% senior notes due 2019	397,850	—
$500,000, 3.50% senior notes due 2021	497,490	—
$500,000, 3.40% senior notes due 2024	496,399	—
$500,000, 3.25% senior notes due 2025	494,437	—
$500,000, 4.25% senior notes due 2045	493,920	—
Total fixed-rate debt	2,979,461	—
Variable-Rate Debt:		
Revolving credit note	—	75,000
Receivables securitization facility due 2019	500,000	950,000
Term loans due 2020	647,257	—
Multi-currency revolving credit facility due 2021	—	1,400,000
Overdraft facility due 2021 (£30,000)	8,615	28,456
Total variable-rate debt	1,155,872	2,453,456
Total debt	$4,135,333	$2,453,456

Our operating results have generated cash flows, which, together with availability under our debt agreements and credit terms from suppliers, have provided sufficient capital resources to finance working capital and cash operating requirements, and to fund capital expenditures, acquisitions, repayment of debt, the payment of interest on outstanding debt, dividends, and repurchases of shares of our common stock.

Our primary ongoing cash requirements will be to finance working capital, fund the repayment of debt, fund the payment of interest on debt, fund repurchases of our common stock, fund the payment of dividends, finance acquisitions, and fund capital expenditures and routine growth and expansion through new business opportunities. Future cash flows from operations and borrowings are expected to be sufficient to fund our ongoing cash requirements.

As of December 31, 2016 and September 30, 2016, our cash and cash equivalents held by foreign subsidiaries were $644.5 million and $582.9 million, respectively. We expect that our cash and cash equivalents held by foreign subsidiaries will grow, but it is generally based in U.S. dollar denominated holdings. Amounts held by foreign subsidiaries are generally subject to U.S. income taxation on repatriation to the U.S. We do not have any plans to repatriate these amounts to the U.S., as our foreign subsidiaries intend to indefinitely reinvest this cash in foreign investments or foreign operations.

We have increased seasonal needs related to our inventory build during the December and March quarters that, depending on our cash balance, can require the use of our credit facilities to fund short-term capital needs. The largest amount of intra-period borrowings under our revolving and securitization credit facilities that was outstanding at any one time during the three months ended December 31, 2016 was $21.5 million. We had $65.4 million of cumulative intra-period borrowings under our credit facilities during the three months ended December 31, 2016.

We have a $1.4 billion multi-currency senior unsecured revolving credit facility ("Multi-Currency Revolving Credit Facility"), which expires in November 2021, with a syndicate of lenders. Interest on borrowings under the Multi-Currency Revolving Credit Facility accrues at specified rates based on our debt rating and ranges from 70 basis points to 110 basis points over CDOR/LIBOR/EURIBOR/Bankers Acceptance Stamping Fee, as applicable (91 basis points over CDOR/LIBOR/EURIBOR/Bankers Acceptance Stamping Fee at December 31, 2016) and from 0 basis points to 10 basis points over the alternate base rate and Canadian prime rate, as applicable. We pay facility fees to maintain the availability under the Multi-Currency Revolving Credit Facility at specified rates based on our debt rating, ranging from 5 basis points to 15 basis points, annually, of the total commitment (9 basis points at December 31, 2016). We may choose to repay or reduce our commitments under the Multi-Currency Revolving Credit Facility at any time. The Multi-Currency Revolving Credit Facility contains covenants, including compliance with a financial leverage ratio test, as well as others that impose limitations on, among other things, indebtedness of subsidiaries and asset sales, with which we were compliant as of December 31, 2016.

We have a commercial paper program whereby we may from time to time issue short-term promissory notes in an aggregate amount of up to $1.4 billion at any one time. Amounts available under the program may be borrowed, repaid, and re-borrowed from time to time. The maturities on the notes will vary, but may not exceed 365 days from the date of issuance. The notes will bear interest, if interest bearing, or will be sold at a discount from their face amounts. The commercial paper program does not increase our borrowing capacity as it is fully backed by our Multi-Currency Revolving Credit Facility. There were no borrowings outstanding under our commercial paper program as of December 31, 2016.

We have a $1,450 million receivables securitization facility ("Receivables Securitization Facility"), which expires in November 2019. We have available to us an accordion feature whereby the commitment on the Receivables Securitization Facility may be increased by up to $250 million, subject to lender approval, for seasonal needs during the December and March quarters. Interest rates are based on prevailing market rates for short-term commercial paper or LIBOR plus a program fee. We pay a customary unused fee at prevailing market rates, annually, to maintain the availability under the Receivables Securitization Facility. The Receivables Securitization Facility contains similar covenants to the Multi-Currency Revolving Credit Facility, with which we were compliant as of December 31, 2016.

We have an uncommitted, unsecured line of credit available to us pursuant to a revolving credit note ("Revolving Credit Note"). The Revolving Credit Note provides us with the ability to request short-term unsecured revolving credit loans from time to time in a principal amount not to exceed $75 million. The Revolving Credit Note may be decreased or terminated by the bank or us at any time without prior notice. We also have a £30 million uncommitted U.K. overdraft facility ("Overdraft Facility"), which expires in February 2021, to fund short term normal trading cycle fluctuations related to our MWI business.

In February 2015, we entered into a $1.0 billion variable-rate term loan ("February 2015 Term Loan"), which matures in 2020. Through December 31, 2016, we elected to make principal payments, prior to the scheduled repayment dates, of $725 million on the February 2015 Term Loan, and as a result, our next required principal payment is due upon maturity. The February 2015 Term Loan bears interest at a rate equal either to a base rate plus a margin, or LIBOR, plus a margin. The margin is based on our public debt ratings and ranges from 75 basis points to 125 basis points over LIBOR (100 basis points at December 31, 2016) and 0 basis points to 25 basis points over a base rate. The February 2015 Term Loan contains similar covenants to the Multi-Currency Revolving Credit Facility, with which we were compliant as of December 31, 2016.

In November 2015, we entered into a $1.0 billion variable-rate term loan (the "November 2015 Term Loan"), which matures in 2020. Through December 31, 2016, we elected to make principal payments, prior to the scheduled repayment dates, of $600 million on the November 2015 Term Loan, and as a result, our next scheduled principal payment is due upon maturity. The November 2015 Term Loan bears interest at a rate equal either to a base rate, plus a margin, or LIBOR, plus a margin. The margin is based on our public debt ratings and ranges from 75 basis points to 125 basis points over LIBOR (100 basis points at December 31, 2016) and 0 basis points to 25 basis points over a base rate. The November 2015 Term Loan contains similar covenants to the Multi-Currency Revolving Credit Facility, with which we were compliant as of December 31, 2016.

In May 2016, our board of directors authorized a share repurchase program that, together with availability remaining under the previously approved August 2013 share repurchase program, permitted us to purchase up to $750 million in shares of our common stock, subject to market conditions. During the three months ended December 31, 2016, we purchased $118.8 million to complete our authorization under this program.

In November 2016, our board of directors authorized a new share repurchase program allowing us to purchase up to $1.0 billion in shares of our common stock, subject to market conditions. During the three months ended December 31, 2016, we purchased $111.1 million of our common stock under this program. As of December 31, 2016, we had $888.9 million of availability remaining under the November 2016 share repurchase program.

Table of Contents

We have market risk exposure to interest rate fluctuations relating to our debt. We manage interest rate risk by using a combination of fixed-rate and variable-rate debt. The amount of variable-rate debt fluctuates during the year based on our working capital requirements. We periodically evaluate financial instruments to manage our exposure to fixed and variable interest rates. However, there are no assurances that such instruments will be available in the combinations we want and/or on terms acceptable to us. There were no such financial instruments in effect at December 31, 2016.

We also have market risk exposure to interest rate fluctuations relating to our cash and cash equivalents. We had $1,791.1 million in cash and cash equivalents at December 31, 2016. The unfavorable impact of a hypothetical decrease in interest rates on cash and cash equivalents would be partially offset by the favorable impact of such a decrease on variable-rate debt. For every $100 million of cash invested that is in excess of variable-rate debt, a 10 basis point decrease in interest rates would increase our annual net interest expense by $0.1 million.

We have minimal exposure to foreign currency and exchange rate risk from our non-U.S. operations. Our largest exposure to foreign exchange rates exists primarily with the Euro, the U.K. Pound Sterling, the Canadian Dollar, and the Brazilian Real. Revenue from our foreign operations is less than one percent of our consolidated revenue. We may utilize foreign currency denominated forward contracts to hedge against changes in foreign exchange rates. We may use derivative instruments to hedge our foreign currency exposure, but not for speculative or trading purposes. As of December 31, 2016, we had one foreign currency denominated contract outstanding that hedges the foreign currency exchange risk of a C$35.0 million outstanding note.

Following is a summary of our contractual obligations for future principal and interest payments on our debt, minimum rental payments on our noncancelable operating leases and financing obligations, and minimum payments on our other commitments at December 31, 2016:

Payments Due by Period (in thousands)	Debt, Including Interest Payments	Operating Leases	Financing Obligations [1]	Other Commitments	Total
Within 1 year	$723,603	$62,202	$ 25,717	$ 139,175	$950,697
1-3 years	1,123,077	99,372	59,005	52,040	1,333,494
4-5 years	1,303,095	67,950	58,876	17,603	1,447,524
After 5 years	2,098,750	69,077	174,277	—	2,342,104
Total	$5,248,525	$298,601	$ 317,875	$ 208,818	$6,073,819

[1] Represents the portion of future minimum lease payments relating to facility leases where we were determined to be the accounting owner (see Note 1 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended September 30, 2016 for a more detailed description of our accounting for leases). These payments are recognized as reductions to the financing obligation and as interest expense and exclude the future noncash termination of the financing obligation.

We outsource to IBM Global Services a significant portion of our corporate and ABDC data center operations. The remaining commitment under our arrangement, which expires in January 2021, is approximately $101.5 million as of December 31, 2016, of which $44.2 million represents our commitment over the next twelve months, and is included in “Other commitments” in the above table.

We have commitments to purchase non-returnable product from pharmaceutical manufacturers. We are required to purchase product at prices that we believe will represent market prices. We currently estimate that our remaining purchase commitment under these agreements is approximately $89.5 million as of December 31, 2016, all of which represents our commitment over the next twelve months, and is included in "Other commitments" in the above table.

Our liability for uncertain tax positions was $92.2 million (including interest and penalties) as of December 31, 2016. This liability represents an estimate of tax positions that we have taken in our tax returns which may ultimately not be sustained upon examination by taxing authorities. Since the amount and timing of any future cash settlements cannot be predicted with reasonable certainty, the estimated liability has been excluded from the above contractual obligations table.

During the three months ended December 31, 2016, our operating activities used $430.4 million of cash in comparison to cash provided of $751.6 million in the prior year period. Cash used in operations during the three months ended December 31, 2016 was principally the result of an increase in merchandise inventories of $713.6 million and an increase in accounts receivable of $536.9 million, offset, in part by an increase in accounts payable of $247.8 million, net income of $247.2 million, and non-cash items of $200.4 million. The non-cash items were comprised primarily of $63.2 million of depreciation expense, $49.5 million of deferred income tax expense, and $43.1 million of amortization expense. We increased our merchandise inventories at December 31, 2016 to support the increase in business volume and, consistent with prior years, due to seasonal needs. The increase in accounts receivable was the result of our revenue growth and a gradual change in payment terms with our largest customer that began in

Table of Contents

May 2016 as part of a contract amendment that, among other things, extended the term of our relationship with the customer. The increase in accounts payable was primarily driven by the increase in merchandise inventories and the timing of payments to our suppliers.

We use days sales outstanding, days inventory on hand, and days payable outstanding to evaluate our working capital performance. The below financial metrics are calculated based upon a quarterly average and can be impacted by the timing of cash receipts and disbursements, which can vary significantly depending upon the day of the week in which the month ends.

	Three months ended December 31,	
	2016	2015
Days sales outstanding	22.7	20.8
Days inventory on hand	30.2	29.5
Days payable outstanding	56.5	55.0

The increase in days sales outstanding from the prior year period was the result of a gradual change in payment terms with our largest customer. We expect days sales outstanding to continue to increase through the first half of fiscal 2017 as a result of this change. The increase in days payable outstanding from the prior year period has benefited from the increase in purchases of merchandise inventories from certain pharmaceutical manufacturers with longer payment terms. We expect cash flows from operating activities in fiscal 2017 to be between $1.6 billion and $1.9 billion.

Our cash flows from operating activities can vary significantly from period to period based on fluctuations in our period end working capital. Additionally, any changes to payment terms with a significant customer or manufacturer supplier could have a material impact to our cash flows from operations. Operating cash flows during the three months ended December 31, 2016 included $37.0 million of interest payments and $87.6 million of income tax refunds, net of payments. Operating cash flows during the three months ended December 31, 2015 included $33.6 million of interest payments and $3.0 million of income tax payments, net of refunds.

During the three months ended December 31, 2015, our operating activities provided $751.6 million of cash. Cash provided by operations during the three months ended December 31, 2015 was principally the result of an increase in accounts payable of $1,623.3 million and net income of $329.6 million, offset, in part by an increase in merchandise inventories of $1,187.9 million. The increase in accounts payable was primarily driven by the increase in merchandise inventories and the timing of payments to our suppliers. We increased our merchandise inventories at December 31, 2015 to support the increase in business volume and due to seasonal needs.

Capital expenditures for the three months ended December 31, 2016 and 2015 were $137.3 million and $90.1 million, respectively. Significant capital expenditures in the three months ended December 31, 2016 included costs associated with expanding distribution capacity and technology initiatives, including costs related to enhancing and upgrading our enterprise resource planning systems. We currently expect to invest approximately $500 million for capital expenditures during fiscal 2017. Significant capital expenditures in the quarter ended December 31, 2015 included technology initiatives, including costs related to the development of track-and-trace technology, costs associated with expanding distribution capacity, and expansion of support facilities.

Cost of acquired companies, net of cash acquired, in the three months ended December 31, 2015 was $2,726.6 million and primarily consisted of our PharMEDium acquisition.

Net cash used in financing activities in the three months ended December 31, 2016 included $229.9 million in purchases of our common stock. Net cash provided by financing activities in the three months ended December 31, 2015 included $1.0 billion of borrowings under our November 2015 Term Loan, offset in part by $118.6 million in purchases of our common stock.

In November 2016, our board of directors increased the quarterly cash dividend by 7% from $0.340 per share to $0.365 per share. We anticipate that we will continue to pay quarterly cash dividends in the future. However, the payment and amount of future dividends remains within the discretion of our board of directors and will depend upon our future earnings, financial condition, capital requirements, and other factors.

Table of Contents

Cautionary Note Regarding Forward-Looking Statements

Certain of the statements contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this report are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Words such as "expect," "likely," "outlook," "forecast," "would," "could," "should," "can," "will," "project," "intend," "plan," "continue," "sustain," "synergy," "on track," "believe," "seek," "estimate," "anticipate," "may," "possible," "assume," variations of such words, and similar expressions are intended to identify such forward-looking statements. These statements are based on management's current expectations and are subject to uncertainty and change in circumstances. These statements are not guarantees of future performance and are based on assumptions that could prove incorrect or could cause actual results to vary materially from those indicated. Among the factors that could cause actual results to differ materially from those projected, anticipated, or implied are the following: unfavorable trends in brand and generic pharmaceutical pricing, including in rate or frequency of price inflation or deflation; competition and industry consolidation of both customers and suppliers resulting in increasing pressure to reduce prices for our products and services; changes in pharmaceutical market growth rates; substantial defaults in payment, material reduction in purchases by or the loss, bankruptcy or insolvency of a major customer; changes to the customer or supplier mix; the retention of key customer or supplier relationships under less favorable economics or the adverse resolution of any contract or other dispute with customers or suppliers; changes to customer or supplier payment terms; the disruption of AmerisourceBergen's cash flow and ability to return value to its stockholders in accordance with its past practices; risks associated with the strategic, long-term relationship between Walgreens Boots Alliance, Inc. and AmerisourceBergen, including with respect to the pharmaceutical distribution agreement and/or the global sourcing arrangement; changes in the United States healthcare and regulatory environment, including changes that could impact prescription drug reimbursement under Medicare and Medicaid; increasing governmental regulations regarding the pharmaceutical supply channel and pharmaceutical compounding; federal and state government enforcement initiatives to detect and prevent suspicious orders of controlled substances and the diversion of controlled substances; federal and state prosecution of alleged violations of related laws and regulations, and any related litigation, including shareholder derivative lawsuits or other disputes relating to our distribution of controlled substances; increased federal scrutiny and qui tam litigation for alleged violations of fraud and abuse laws and regulations and/or any other laws and regulations governing the marketing, sale, purchase and/or dispensing of pharmaceutical products or services and any related litigation; material adverse resolution of pending legal proceedings; declining reimbursement rates for pharmaceuticals; the acquisition of businesses that do not perform as expected, or that are difficult to integrate or control, including the integration of PharMEDium, or the inability to capture all of the anticipated synergies related thereto; regulatory action in connection with the production, labeling or packaging of products compounded by our compounded sterile preparations (CSP) business; declining economic conditions in the United States and abroad; financial market volatility and disruption; the loss, bankruptcy or insolvency of a major supplier; interest rate and foreign currency exchange rate fluctuations; managing foreign expansion, including non-compliance with the U.S. Foreign Corrupt Practices Act, anti-bribery laws and economic sanctions and import laws and regulations; malfunction, failure or breach of sophisticated information systems to operate as designed; risks generally associated with data privacy regulation and the international transfer of personal data; changes in tax laws or legislative initiatives that could adversely affect AmerisourceBergen's tax positions and/or AmerisourceBergen's tax liabilities or adverse resolution of challenges to AmerisourceBergen's tax positions; natural disasters or other unexpected events that affect AmerisourceBergen's operations; the impairment of goodwill or other intangible assets, resulting in a charge to earnings; and other economic, business, competitive, legal, tax, regulatory and/or operational factors affecting AmerisourceBergen's business generally. Certain additional factors that management believes could cause actual outcomes and results to differ materially from those described in forward-looking statements are set forth (i) elsewhere in this report, (ii) in Item 1A (Risk Factors), in the Company’s Annual Report on Form 10-K for the fiscal year ended September 30, 2016 and elsewhere in that report and (iii) in other reports filed by the Company pursuant to the Securities Exchange Act.

Table of Contents

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's most significant market risks are the effects of changing interest rates, foreign currency risk, and changes in the price and volatility of the Company's common stock. See the discussion under "Liquidity and Capital Resources" in Item 2 on page 24.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures that are intended to ensure that information required to be disclosed in the Company's reports submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. These controls and procedures also are intended to ensure that information required to be disclosed in such reports is accumulated and communicated to management to allow timely decisions regarding required disclosures.

The Company's Chief Executive Officer and Chief Financial Officer, with the participation of other members of the Company's management, have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a — 15(e) and 15d — 15(e) under the Exchange Act) and have concluded that the Company's disclosure controls and procedures were effective for their intended purposes as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

During the first quarter of fiscal 2017, there was no change in AmerisourceBergen Corporation's internal control over financial reporting that materially affected, or is reasonably likely to materially affect, internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

See Note 8 (Legal Matters and Contingencies) of the Notes to the Consolidated Financial Statements set forth under Item 1 of Part I of this report for the Company’s current description of legal proceedings.

ITEM 1A. Risk Factors

Our significant business risks are described in Item 1A to Form 10-K for the year ended September 30, 2016 to which reference is made herein.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) Issuer Purchases of Equity Securities

The following table sets forth the number of shares purchased, the average price paid per share, the total number of shares purchased as part of publicly announced programs, and the approximate dollar value of shares that may yet be purchased under the programs during each month in the quarter ended December 31, 2016.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Programs
October 1 to October 31	—	$ —	—	$ 118,760,836
November 1 to November 30	2,925,923	$ 63.07	2,814,017	$ 943,157,508
December 1 to December 31	702,488	$ 77.26	702,450	$ 888,885,792
Total	3,628,411		3,516,467	

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

None.

ITEM 5. Other Information

None.

Table of Contents

ITEM 6. Exhibits

(a) Exhibits:

10.1	Sixth Amendment and Restatement Agreement, dated as of November 18, 2016, among the Registrant, the borrowing subsidiaries party thereto, the lenders party thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed on November 22, 2016).
10.2	Amendment and Restatement Agreement, dated as of November 18, 2016, among the Registrant, the lenders party thereto and Bank of America, N.A., as Administrative Agent (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed on November 22, 2016).
10.3	Amendment and Restatement Agreement, dated as of November 18, 2016, among the Registrant, the lenders party thereto and JPMorgan Chase Bank, N.A., as Administrative Agent (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed on November 22, 2016).
10.4	Eleventh Amendment to Amended and Restated Receivables Purchase Agreement, dated as of November 18, 2016, among AmeriSource Receivables Financial Corporation, as seller, AmerisourceBergen Drug Corporation, as servicer, the Purchaser Agents and Purchasers party thereto, and The Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch, as administrator (incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K filed on November 22, 2016).
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer.
32	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer.
101	Financial statements from the Quarterly Report on Form 10-Q of AmerisourceBergen Corporation for the quarter ended December 31, 2016, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows, and (v) the Notes to Consolidated Statements.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	AMERISOURCEBERGEN CORPORATION
January 31, 2017	/s/ Steven H. Collis Steven H. Collis Chairman, President & Chief Executive Officer
January 31, 2017	/s/ Tim G. Guttman Tim G. Guttman Executive Vice President & Chief Financial Officer

Table of Contents

EXHIBIT INDEX

Exhibit Number	Description
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