RR Donnelley & Sons Co
Form 10-K
February 25, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2015
OR

¨ 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 1-4694

R. R. DONNELLEY & SONS COMPANY

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	36-1004130 (I.R.S. Employer Identification No.)
35 West Wacker Drive, Chicago, Illinois (Address of principal executive offices)	60601 (ZIP Code)

Registrant's telephone number, including area code—(312) 326-8000

Securities registered pursuant to Section 12(b) of the Act:

Title of each Class	Name of each exchange on which registered
Common Stock (Par Value $1.25)	NASDAQ

Indicated by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No þ

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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer þ	Accelerated filer ¨	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No þ

The aggregate market value of the shares of common stock (based on the closing price of these shares on the NASDAQ Stock Exchange—Composite Transactions) on June 30, 2015, the last business day of the registrant's most recently completed second fiscal quarter, held by nonaffiliates was $3,607,975,994.

As of February 19, 2016, 208,766,693 shares of common stock were outstanding.

Documents Incorporated By Reference

Portions of the registrant's proxy statement related to its annual meeting of stockholders scheduled to be held on May 19, 2016 are incorporated by reference into Part III of this Form 10-K.

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PART I

ITEM 1. BUSINESS

Company Overview

R.R. Donnelley & Sons Company ("RR Donnelley," the "Company," "we," "us," and "our"), a Delaware corporation, helps organizations communicate more effectively by working to create, manage, produce, distribute and process content on behalf of our customers. The Company assists customers in developing and executing multichannel communication strategies that engage audiences, reduce costs, drive revenues and increase compliance. R.R. Donnelley's innovative technologies enhance digital and print communications to deliver integrated messages across multiple media to highly targeted audiences at optimal times for clients in virtually every private and public sector. Strategically located operations provide local service and responsiveness while leveraging the economic, geographic and technological advantages of a global organization.

Segment Descriptions

The Company's segments and their product and service offerings are summarized below:

Publishing and Retail Services

The Publishing and Retail Services segment's primary product offerings include magazines, catalogs, retail inserts, books, directories and packaging. The Publishing and Retail Services segment accounted for 22.4% of the Company's consolidated net sales in 2015.

Variable Print

The Variable Print segment includes the Company's U.S. short-run and transactional printing operations. This segment's primary product offerings include commercial and digital print, office products, direct mail, labels, statement printing, forms and packaging. The Variable Print segment accounted for 33.4% of the Company's consolidated net sales in 2015.

Strategic Services

The Strategic Services segment includes the Company's logistics services, financial print products and related services, print management offerings, digital and creative solutions and book publishing. The Strategic Services segment accounted for 23.8% of the Company's consolidated net sales in 2015.

International

The International segment includes the Company's non-U.S. printing operations in Asia, Europe, Latin America and Canada. This segment's primary product and service offerings include magazines, catalogs, retail inserts, books, directories, direct mail, packaging, forms, labels, manuals, statement printing, commercial and digital print, logistics services and digital and creative solutions. Additionally, this segment includes the Company's business process outsourcing and Global Turnkey Solutions operations. Business process outsourcing provides transactional print and outsourcing services, statement printing, direct mail and print management offerings through its operations in Europe, Asia and North America. Global Turnkey Solutions provides outsourcing capabilities, including product configuration, customized kitting and order fulfillment for technology, medical device and other companies around the world through its operations in Europe, North America and Asia. The International segment accounted for 20.4% of the Company’s consolidated net sales in 2015.

Corporate

Corporate consists of unallocated selling, general and administrative activities and associated expenses including, in part, executive, legal, finance, communications, certain facility costs and LIFO inventory provisions. In addition, certain costs and earnings of employee benefit plans, such as pension and other postretirement benefits plan expense and share-based compensation, are included in Corporate and not allocated to the operating segments. Corporate also manages the Company’s cash pooling structures, which enables participating international locations to draw on the Company’s overseas cash resources to meet local liquidity needs.

Financial and other information related to these segments is included in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, and in Note 19, Segment Information, to the Consolidated Financial Statements. Additional information related to the Company’s International operations is included in Note 20, Geographic Area and Products and Services Information, to the Consolidated Financial Statements.

Proposed Spinoff Transactions

On August 4, 2015, the Company announced that its Board of Directors intends to create three independent public companies: (i) a financial communications services company with estimated 2015 net sales of approximately $1.0 billion ("Donnelley Financial Solutions"), (ii) a publishing and retail-centric print services company with estimated 2015 net sales of approximately $3.5 billion ("LSC Communications"), and (iii) a multichannel communications management company with estimated 2015 net sales of approximately $6.8 billion ("RR Donnelley & Sons Company"). Estimated 2015 net sales for each company reflects the elimination of intercompany transactions; as a result net sales for each company may differ on a standalone basis. Donnelley Financial Solutions is expected to consist of the Company's current financial reporting unit of the Company's Strategic Services segment. LSC Communications is expected to consist of the Company's current Publishing and Retail Services segment as well as the office products reporting unit from the Company's Variable Print segment, substantially all of the operations currently within the Europe reporting unit of the Company's International segment, certain Mexican operations currently within the Latin America reporting unit of the Company's International segment and the co-mail and related list services operations currently within the logistics reporting unit of the Company's Strategic Services segment. RR Donnelley & Sons Company is expected to consist of the current Variable Print segment except for the office products reporting unit that will become part of LSC Communications, the logistics reporting unit within the current Strategic Services segment except for the operations that will become part of LSC Communications, the sourcing and digital and creative solutions reporting units within the current Strategic Services segment, and the current International segment except for substantially all of the Europe reporting unit and certain Mexican operations that will become part of LSC Communications. The transaction is expected to take the form of a tax-free distribution to RR Donnelley shareholders of shares of stock in two new, independent, publicly traded companies, Donnelley Financial Solutions and LSC Communications.

The transactions are subject to customary conditions, including obtaining rulings from the Internal Revenue Service and/or tax opinions, execution of inter-company agreements and final approval by the Company's Board of Directors. The Company expects to complete the transactions in October 2016, but there can be no assurance that the transactions will be completed on the anticipated timeline or at all or that the terms of the transactions will not change. See Item 1A, Risk Factors, of Part I of this Annual Report on Form 10-K for certain risk factors relating to the proposed transactions. The disclosures within Item 7, Management Discussion and Analysis of Financial Condition and Results of Operations, of Part II of this Annual Report on Form 10-K are on a consolidated Company basis, reflect the Company's current operating and management structure, and do not take into account the proposed transactions.

Upon separation, the historical results of Donnelley Financial Solutions and LSC Communications will be presented as discontinued operations.

Business Acquisitions and Dispositions

2015 Acquisition

On June 8, 2015, the Company acquired Courier Corporation ("Courier"), a leader in digital printing and publishing primarily in the United States, specializing in educational, religious and trade books.

2015 Disposition

On April 29, 2015, the Company sold its 50.1% interest in its Venezuelan operating entity.

2014 Acquisitions

On March 25, 2014, the Company acquired substantially all of the North American operations of Esselte Corporation ("Esselte"), a developer and manufacturer of nationally branded and private label office and stationery products. On March 10, 2014, the Company acquired the assets of MultiCorpora R&D Inc. and MultiCorpora International Inc. (together "MultiCorpora"). On January 31, 2014, the Company acquired Consolidated Graphics, Inc. ("Consolidated Graphics"), a provider of digital and commercial printing, fulfillment services, print management and proprietary Internet-based technology solutions, with operations in North America, Europe and Asia.

2014 Dispositions

On August 15, 2014, the Company sold the assets and liabilities of Journalism Online, LLC ("Journalism Online"), a provider of online subscription management services. On August 11, 2014, the Company's subsidiary, RR Donnelley Argentina S.A. ("RRDA"), filed for bankruptcy liquidation in bankruptcy court in Argentina. On February 7, 2014, the Company sold the assets and liabilities of Office Tiger Global Real Estate Services Inc. ("GRES"), its commercial and residential real estate advisory services business.

2013 Disposition

During the fourth quarter of 2013, the Company sold the assets and liabilities of R.R. Donnelley SAS (“MRM France”), its direct mail business located in Cosne sur Loire, France.

For further information on the above acquisitions and dispositions, see Note 2, Acquisitions and Dispositions, to the Consolidated Financial Statements.

Competitive Environment

Technological changes, including the electronic distribution of documents and data, online distribution and hosting of media content, and advances in digital printing, print-on-demand and Internet technologies, continue to impact the market for the Company’s products and services. One of the Company’s competitive strengths is that it offers a wide array of communications products and services, including print, which provide differentiated solutions for its customers. The Company works with its customers to create, manage, deliver and optimize their multi-channel communications strategies. The Company has and will continue to develop and expand its creative and design, content management, digital and print production, supply chain management and distribution services to address its customers’ evolving needs while supporting the strategic objective of becoming a leading global provider of integrated communication services.

The print and related services industry, in general, continues to have excess capacity and remains highly competitive. Despite consolidation in recent years, the industry remains highly fragmented. Across the Company’s range of products and services, competition is based primarily on price in addition to quality and the ability to service the special needs of customers. Management expects that prices for the Company’s products and services will continue to be a focal point for customers in coming years. Therefore, the Company believes it needs to continue to lower its cost structure and continue to differentiate its product and service offerings.

Digital technologies have impacted printed retail inserts, magazines and catalogs as some advertiser spending has moved from print to electronic media. Electronic communication and transaction technology has eliminated or reduced the role of many traditional printed products and has continued to drive electronic substitution in directory and statement printing, in part driven by environmental concerns and cost pressures at key customers. In recent years the trend in e-book substitution has shifted and the publishing industry has experienced growth in consumer print book volume, while sales of e-books have declined. The future impact of technology on the Company’s business is difficult to predict and could result in additional expenditures to restructure impacted operations or develop new technologies. In addition, the Company has made targeted acquisitions and investments to offer customers innovative services and solutions that further secure the Company’s position as a technology leader in the industry.

The acquisitions of Courier, Consolidated Graphics, Esselte and MultiCorpora support the Company’s strategic objective of generating profitable growth and improved cash flow and liquidity through targeted acquisitions. These acquisitions have enhanced the Company’s existing capabilities and ability to serve its customers and have provided cost savings through the combination of best practices, complementary products and manufacturing and distribution capabilities.

The Company has implemented a number of strategic initiatives to reduce its overall cost structure and improve efficiency, including the restructuring, reorganization and integration of operations and streamlining of administrative and support activities. Future cost reduction initiatives could include the reorganization of operations and the consolidation of facilities. Implementing such initiatives might result in future restructuring or impairment charges, which may be substantial. Additionally, to align with its long-term strategic goals, the Company announced that it intends to create three independent public companies and expects the transactions to be effective in October 2016. The proposed spinoff transactions will allow each of the businesses to pursue their own strategies and invest according to the unique dynamics of their respective industries. Refer to Business – Proposed Spinoff Transactions for further details regarding the proposed spinoff transactions.

Seasonality

Advertising and consumer spending trends affect demand in several of the end-markets served by the Company. Historically, demand for printing of magazines, catalogs, retail inserts and books is higher in the second half of the year driven by increased advertising pages within magazines, and holiday volume in catalogs, retail inserts and books. Partially offsetting this pattern, demand for financial print and related services is typically stronger in the first half of the year due to annual compliance requirements. As a result of the acquisition of Consolidated Graphics, which provides significant campaign-related printed products, quarterly and annual results may also be impacted by U.S. election cycles. These typical seasonal patterns can be impacted by overall trends in the U.S. and world economy. The seasonal pattern in 2015 was in line with historical patterns.

Raw Materials

The primary raw materials the Company uses in its print businesses are paper and ink. The Company negotiates with leading suppliers to maximize its purchasing efficiencies and uses a wide variety of paper grades, formats, ink formulations and colors. In addition, a substantial amount of paper used by the Company is supplied directly by customers. Variations in the cost and supply of certain paper grades and ink formulations used in the manufacturing process may affect the Company’s consolidated financial results. Paper prices fluctuated during 2015, and volatility in the future is expected. Generally, customers directly absorb the impact of changing prices on customer-supplied paper. With respect to paper purchased by the Company, the Company has historically passed most changes in price through to its customers. Contractual arrangements and industry practice should support the Company’s continued ability to pass on any future paper price increases, but there is no assurance that market conditions will continue to enable the Company to successfully do so. Management believes that the paper supply is consolidating, and there may be shortfalls in the future in supplies necessary to meet the demands of the entire marketplace. Higher paper prices and tight paper supplies may have an impact on customers’ demand for printed products. The Company has undertaken various strategic initiatives to mitigate any foreseeable supply disruptions with respect to the Company’s ink requirements. The Company also resells waste paper and other print-related by-products and may be impacted by changes in prices for these by-products.

The Company continues to monitor the impact of changes in the price of crude oil and other energy costs, which impact the Company’s ink suppliers, logistics operations and manufacturing costs. Crude oil and energy prices continue to be volatile. The Company believes its logistics operations will continue to be able to pass a substantial portion of any increases in fuel prices directly to its customers in order to offset the impact of related cost increases. Decreases in fuel prices are also passed on to customers which negatively impacts sales. The Company generally cannot pass on to customers the impact of higher energy prices on its manufacturing costs. However, the Company enters into fixed price contracts for a portion of its natural gas purchases to mitigate the impact of changes in energy prices. The Company cannot predict sudden changes in energy prices and the impact that possible future changes in energy prices might have upon either future operating costs or customer demand and the related impact either will have on the Company’s consolidated annual results of operations, financial position or cash flows.

Distribution

The Company’s products are distributed to end-users through the U.S. or foreign postal services, through retail channels, electronically or by direct shipment to customer facilities. Through its logistics operations, the Company manages the distribution of most customer products printed by the Company in the U.S. and Canada to maximize efficiency and reduce costs for customers.

Postal costs are a significant component of many customers’ cost structures and postal rate changes can influence the number of pieces that the Company’s customers are willing to print and mail. Under the 2006 Postal Accountability and Enhancement Act, it had been anticipated that postage would increase annually by an amount equal to or slightly less than the Consumer Price Index (the “CPI”). However, on December 24, 2013, the Postal Regulatory Commission (the “PRC”) approved the United States Postal Service (“USPS”) Board of Governors’ request under the Exigency Provision in the applicable law for price increases of 4.3%. The exigent rate increase was approved as a surcharge in addition to a 1.7% rate increase, equal to the CPI, for total price increases of 6.0%, on average, across all significant mail categories, effective January 26, 2014. On January 15, 2015, the USPS filed for a CPI rate increase of approximately 2.0%, which was approved by the PRC on May 7, 2015, and became effective May 31, 2015. In January 2016, the USPS announced that the 4.3% exigency rate increase is expected to be eliminated in April 2016. As a leading provider of print logistics and among the largest mailers of standard mail in the U.S., the Company works closely with its customers and the USPS to offer innovative products and mail preparation services to minimize postage costs. While the Company does not directly absorb the impact of higher postal rates on its customers’ mailings, demand for products distributed through the U.S. or foreign postal services has been negatively impacted by increases in postal rates. The USPS is continuing to pursue its previously announced plans to restructure its mail delivery network, including the closure of many post office facilities and a possible suspension of Saturday service. The impact to the Company of the USPS's restructuring plans, many of which require legislative action, cannot currently be estimated. Mail delivery services through the USPS accounted for approximately 43% of the Company's logistics revenues during the year ended December 31, 2015.

Customers

For each of the years ended December 31, 2015, 2014 and 2013, no customer accounted for 10% or more of the Company's consolidated net sales.

Technology, Research and Development

The Company has a research facility that supports the development and implementation of new technologies to meet customer needs and improve operating efficiencies. The Company's cost for research and development activities is not material to the Company's consolidated annual results of operations, financial position or cash flows.

Environmental Compliance

It is the Company's policy to conduct its global operations in accordance with all applicable laws, regulations and other requirements. It is not possible to quantify with certainty the potential impact of actions regarding environmental matters, particularly remediation and other compliance efforts that the Company may undertake in the future. However, in the opinion of management, compliance with the present environmental protection laws, before taking into account estimated recoveries from third parties, will not have a material adverse effect on the Company's consolidated annual results of operations, financial position or cash flows.

Employees

As of December 31, 2015, the Company had approximately 68,400 employees.

Available Information

The Company maintains an Internet website at www.rrdonnelley.com where the Company's Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and all amendments to those reports are available without charge, as soon as reasonably practicable following the time they are filed with, or furnished to, the Securities and Exchange Commission ("SEC"). The Principles of Corporate Governance of the Company's Board of Directors, the charters of the Audit, Human Resources and Governance, Responsibility & Technology Committees of the Board of Directors and the Company's Principles of Ethical Business Conduct are also available on the Investor Relations portion of www.rrdonnelley.com, and will be provided, free of charge, to any shareholder who requests a copy. References to the Company'nbsp;

Deposits
21,798 16,460 11,342 5,779 29,400
Federal funds purchased and securities sold under agreements to repurchase
2,472 1,790 1,177 581 2,499
Note Payable
214 167 117 63 38
Other borrowed funds
11 8 6 3 42
Federal Home Loan Bank advances
19,174 14,203 9,308 4,659 15,900
Debentures and capital securities
3,022 2,200 1,466 733 2,933
Total interest expense
46,691 34,828 23,416 11,818 50,812
Net interest income
55,871 41,690 27,873 14,083 56,460
Provision for loan losses
7,610 6,124 5,028 2,173 6,159
Net interest income after provision for loan losses

48,261 35,566 22,845 11,910 50,301
NON-INTEREST INCOME

Mortgage banking revenue
10,194 9,751 10,908 4,358 6,409
Service charges on deposit accounts
6,259 4,631 3,082 1,527 5,823
Trust fees
2,560 1,803 1,172 609 2,715
Trading account losses
0 0 0 0 (20)
Security gains (losses)
4,584 3,617 51 51 592
Gain on sale of banking centers
5,619 5,619 5,619 5,619 0
Other operating income
9,351 6,598 4,130 2,098 7,906
Total non-interest income
38,567 32,019 24,962 14,262 23,425
NON-INTEREST EXPENSE

Salaries and employee benefits
29,583 21,947 15,246 7,604 26,345
Net occupancy
4,740 3,504 2,324 1,199 4,480
Equipment
4,052 3,143 2,098 1,039 3,898
Professional services
3,417 2,612 1,905 767 2,139
Assessment on deposits and other taxes
1,503 1,281 780 392 1,397
Amortization of intangible assets
467 343 230 118 475
Merger costs
0 0 0 0 134
Banking center reconfiguration
0 0 0 0 2,096
Other operating expenses
11,001 7,935 5,106 2,554 8,532
Total non-interest expense
54,763 40,765 27,689 13,673 49,496
Income before federal income taxes
32,065 26,820 20,118 12,499 24,230
Income tax expense
8,910 7,814 6,019 3,838 6,230
Net income
$23,155 $19,006 $14,099 $8,661 $18,000
NET INCOME PER COMMON SHARE:

Basic
$2.43 $1.99 $1.48 $0.90 $1.82

Diluted	$2.41	$1.97	$1.46	$0.89	$1.79
Weighted average common shares outstanding:					
Basic	9,512,324	9,526,125	9,552,149	9,620,401	9,905,832
Diluted	9,623,388	9,631,663	9,644,621	9,714,253	10,040,001
Note: Fully taxable equivalent adjustment	$1,977	$1,486	$1,001	$506	$2,083

Second Bancorp Incorporated and Subsidiaries
Consolidated Balance Sheets
(Dollars in thousands)

	Dec. 31 2003	Sept. 30 2003	June 30 2003	March 31 2003	Dec. 31 2002
ASSETS					
Cash and due from banks	$ 40,773	$ 57,305	$ 42,194	$ 43,334	$ 60,822
Federal funds sold and other temp. investments	6,529	13,128	44,505	29,523	61,449
Securities available-for-sale (at market value)	620,696	602,893	556,434	539,309	523,669
Loans:					
Commercial	631,170	598,762	571,788	558,499	542,693
Consumer	399,137	372,826	339,723	325,819	322,840
Real estate (including loans held for sale)	319,513	330,030	288,119	331,163	302,258
Total loans	1,349,820	1,301,618	1,199,630	1,215,481	1,167,791
Less allowance for loan losses	18,874	18,372	18,030	17,756	17,595
Net loans	1,330,946	1,283,246	1,181,600	1,197,725	1,150,196
Premises and equipment	19,013	17,944	17,048	16,125	16,632
Accrued interest receivable	8,501	8,710	8,289	9,414	8,762
Goodwill and intangible assets	20,047	20,117	20,230	20,343	20,422
Servicing assets	20,936	19,827	14,880	13,743	12,403
Other assets	49,089	51,580	41,053	39,511	40,420
Total assets	$ 2,116,530	$ 2,074,750	$ 1,926,233	$ 1,909,027	$ 1,894,775
LIABILITIES AND SHAREHOLDERS EQUITY					
Deposits:					
Demand - non-interest bearing	$ 170,176	$ 165,242	$ 155,285	$ 155,892	$ 179,714
Demand - interest bearing	142,709	164,186	204,430	147,747	103,583
Savings	346,851	350,231	347,722	363,443	405,437
Time deposits	555,606	485,622	465,379	454,784	506,378
Total deposits	1,215,342	1,165,281	1,172,816	1,121,866	1,195,112
Federal funds purchased and securities sold under agreements to repurchase	216,761	238,047	175,011	206,069	138,796
Note payable	7,750	7,750	7,750	14,000	7,000
Other borrowed funds	1,301	1,579	1,219	155	3,863

Accrued expenses and other liabilities	14,524	17,562	19,612	20,089	17,331
Federal Home Loan Bank advances	492,299	478,198	379,089	379,971	365,844
Debentures	31,537	0	0	0	0
Corporation-obligated mandatorily redeemable capital securities of subsidiary trust	0	30,534	30,521	30,508	30,495
Total liabilities	1,979,514	1,938,951	1,786,018	1,772,658	1,758,441
Shareholders equity:					
Common stock, no par value; 30,000,000 shares authorized;	42,973	42,815	41,750	41,745	41,763
Treasury stock	(36,173)	(36,173)	(34,771)	(33,740)	(27,180)
Other comprehensive income	(834)	457	7,642	6,410	6,656
Retained earnings	131,050	128,700	125,594	121,954	115,095
Total shareholders equity	137,016	135,799	140,215	136,369	136,334
Total liabilities and shareholders equity	$ 2,116,530	$ 2,074,750	$ 1,926,233	$ 1,909,027	$ 1,894,775
Miscellaneous data:					
Common shares issued	10,991,460	10,990,460	10,936,760	10,922,720	11,041,263
Treasury shares	1,520,089	1,520,089	1,468,541	1,426,841	1,279,009
Bank owned life insurance (in other assets)	$ 34,742	$ 34,149	$ 33,769	$ 33,489	$ 33,086
Loans serviced for others	$ 1,750,733	$ 1,692,880	$ 1,631,790	$ 1,463,926	$ 1,320,316
Goodwill	$ 16,700	$ 16,647	$ 16,647	$ 16,647	$ 16,708
Other intangibles	3,347	3,470	3,583	3,696	3,714
Total goodwill and intangible assets	$ 20,047	$ 20,117	$ 20,230	$ 20,343	$ 20,422
Mortgage servicing rights (net of allowance)	$ 20,512	$ 19,378	$ 14,429	$ 13,299	$ 11,967
Other servicing assets	424	449	451	444	436
	$ 20,936	$ 19,827	$ 14,880	$ 13,743	$ 12,403
Valuation allowance for mortgage servicing rights included above	$ (2,393)	$ (2,774)	$ (6,304)	$ (4,783)	$ (3,794)

Second Bancorp Incorporated and Subsidiaries
Consolidated Average Balance Sheets
For the Quarter Ended
(Dollars in Thousands)

ASSETS	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Cash and demand balances due from banks	$ 40,524	$ 43,675	$ 37,686	$ 38,392	$ 35,454
Federal funds sold and other temp. investments	12,219	14,697	50,390	44,849	47,197
Securities:					
Trading	0	0	0	0	0
Available-for-sale	628,310	610,468	541,921	528,434	494,245
Total securities	628,310	610,468	541,921	528,434	494,245
Loans:					
Commercial	613,183	584,553	562,499	551,882	533,996
Consumer	389,303	353,299	336,303	324,729	323,939
Real estate (including loans held for sale)	314,667	308,128	298,498	301,006	313,227
Total loans	1,317,153	1,245,980	1,197,300	1,177,617	1,171,162
Allowance for loan losses	18,463	18,137	17,787	17,566	17,345
Net loans	1,298,690	1,227,843	1,179,513	1,160,051	1,153,817
Premises and equipment	19,020	17,666	16,828	16,508	16,611
Goodwill and intangible assets	20,076	20,166	20,282	20,461	19,676
Servicing assets	20,105	17,377	14,859	13,310	11,832
Other	53,609	52,897	47,499	47,519	46,882
Total assets	$2,092,553	$2,004,789	$1,908,978	$1,869,524	$1,825,714

LIABILITIES AND SHAREHOLDERS EQUITY					
Liabilities:					
Demand deposits (non-interest bearing)	$ 167,689	$ 161,281	$ 159,636	$ 153,223	$ 156,607
Demand deposits (interest bearing)	152,202	187,231	183,323	117,469	100,240
Savings	353,391	346,965	356,281	382,673	411,109
Time deposits	523,107	462,340	460,479	482,316	512,653
Total deposits	1,196,389	1,157,817	1,159,719	1,135,681	1,180,609

Federal funds purchased and securities sold under agreements to repurchase	230,115	208,549	178,618	164,329	165,504
Note payable	7,749	7,750	8,369	9,733	4,107
Borrowed funds	370	563	186	455	1,281
Accrued expenses and other liabilities	15,693	17,626	18,243	17,863	14,306
Federal Home Loan Bank advances	478,044	447,116	374,061	375,710	291,957
Debentures and capital securities	30,540	30,524	30,513	30,499	30,721
Total liabilities	1,958,900	1,869,945	1,769,709	1,734,270	1,688,485
Shareholders equity:					
Common stock	42,839	42,506	41,747	41,757	41,153
Treasury shares	(36,172)	(35,646)	(34,127)	(30,666)	(25,050)
Other comprehensive income	(2,128)	939	7,434	6,778	7,032
Retained earnings	129,114	127,045	124,215	117,385	114,094
Total shareholders equity	133,653	134,844	139,269	135,254	137,229
Total liabilities and shareholders equity	$2,092,553	$2,004,789	$1,908,978	$1,869,524	$1,825,714

Second Bancorp Incorporated and Subsidiaries
Consolidated Average Balance Sheets
For the Year-to-date period ended:
(Dollars in Thousands)

ASSETS	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Cash and demand balances due from banks	$ 40,085	$ 39,937	$ 38,037	$ 38,392	$ 34,606
Federal funds sold	30,406	36,535	47,635	44,849	68,503
Securities:					
Trading	0	0	0	0	40
Available-for-sale	577,648	560,575	535,215	528,434	452,587
Total securities	577,648	560,575	535,215	528,434	452,627
Loans:					
Commercial	578,215	566,431	557,220	551,882	517,185
Consumer	351,092	338,215	330,548	324,729	313,760
Real estate (including loans held for sale)	305,619	302,570	299,745	301,006	290,832
Total loans	1,234,926	1,207,216	1,187,513	1,177,617	1,121,777
Allowance for loan losses	17,991	17,832	17,677	17,566	16,992
Net loans	1,216,935	1,189,384	1,169,836	1,160,051	1,104,785
Premises and equipment	17,513	17,005	16,669	16,508	16,602
Goodwill and intangible assets	20,245	20,302	20,371	20,461	19,018
Servicing assets	16,434	15,197	14,089	13,310	10,520
Other	50,404	49,324	47,508	47,519	47,495
Total assets	$1,969,670	$1,928,259	$1,889,360	$1,869,524	$1,754,156

LIABILITIES AND SHAREHOLDERS EQUITY					
Liabilities:					
Demand deposits (non-interest bearing)	$ 160,499	$ 158,076	$ 156,447	$ 153,223	$ 146,598
Demand deposits (interest bearing)	160,226	162,930	150,578	117,469	101,222
Savings	359,712	361,842	369,404	382,673	374,313
Time deposits	482,118	468,305	471,337	482,316	537,217
Total deposits	1,162,555	1,151,153	1,147,766	1,135,681	1,159,350
Federal funds purchased and	195,619	183,994	171,513	164,329	136,041

securities sold under agreements to repurchase					
Note payable	8,393	8,610	9,047	9,733	1,335
Borrowed funds	394	402	320	455	1,726
Accrued expenses and other liabilities	17,351	17,910	18,054	17,863	12,000
Federal Home Loan Bank advances	419,091	399,224	374,881	375,710	278,998
Debentures and capital securities	30,519	30,512	30,506	30,499	30,528
Total liabilities	1,833,922	1,791,805	1,752,087	1,734,270	1,619,978
Shareholders equity:					
Common stock	42,216	42,006	41,752	41,757	39,177
Treasury shares	(34,172)	(33,498)	(32,406)	(30,666)	(20,590)
Net unrealized holding gains	3,225	5,029	7,108	6,778	5,996
Retained earnings	124,479	122,917	120,819	117,385	109,595
Total shareholders equity	135,748	136,454	137,273	135,254	134,178
Total liabilities and shareholders equity	$1,969,670	$1,928,259	$1,889,360	$1,869,524	$1,754,156

Second Bancorp Incorporated and Subsidiaries
Financial Highlights Non-GAAP Operating Results
Quarterly Data
(Dollars in thousands, except per share data)

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Earnings:					
Net interest income	$14,181	$13,817	$13,790	$14,083	$13,946
Provision for loan losses	1,486	1,096	2,855	2,173	2,350
Non-interest income	5,581	3,491	10,700	8,592	7,314
Security gains (losses)	967	3,566	0	51	(67)
Trading account losses	0	0	0	0	0
Non-interest expense	13,998	13,076	14,016	13,673	12,469
Federal income taxes	1,096	1,795	2,181	1,871	1,577
Net income	**$ 4,149**	**$ 4,907**	**$ 5,438**	**$ 5,009**	**$ 4,797**
Per share:					
Basic earnings	$ 0.44	$ 0.52	$ 0.57	$ 0.52	$ 0.49
Diluted earnings	0.43	0.51	0.57	0.52	0.48
Key ratios: (%)					
Return on average assets (ROA)	0.79	0.98	1.14	1.07	1.05
Return on average shareholders equity (ROE)	12.42	14.56	15.62	14.81	13.98
Net interest margin	3.00	3.06	3.19	3.33	3.38
Net overhead	1.72	2.05	0.74	1.16	1.20
Efficiency ratio	69.12	73.49	56.10	58.98	57.27

Second Bancorp Incorporated and Subsidiaries
Reconciliation of GAAP vs. Non-GAAP Operating Results
Quarterly Data

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Net income	$4,149	$4,907	$5,438	$ 8,661	$3,428
Adjustments to GAAP to reflect Non-GAAP Operating Basis:					
Add non-recurring costs:					
Sale of banking centers	0	0	0	(5,619)	0
Merger costs	0	0	0	0	10
Banking center reconfiguration	0	0	0	0	2,096
Total adjustments	0	0	0	(5,619)	2,106
Federal income taxes (benefit)	0	0	0	(1,967)	737

Net income	$4,149	$4,907	$5,438	$ 5,009	$4,797

Note: Recap of Income from Mortgage Banking Activities

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Gross income from servicing	$ 947	$ 1,052	$ 986	$ 903	$ 764
Amortization of MSRs	(790)	(2,723)	(2,101)	(1,549)	(2,322)
(Excess amortization) / net servicing income	157	(1,671)	(1,115)	(646)	(1,558)
Change in valuation allowance MSRs	381	3,530	(1,522)	(989)	(707)
Net derivative gain (loss) non hedging	(834)	(6,759)	3,035	1,805	(425)
Income (loss) from mortgage servicing	(296)	(4,900)	398	170	(2,690)
Gain on sale of mortgage loans	737	3,743	6,152	4,188	5,348
Net mortgage banking revenue (loss)	$ 441	$(1,157)	$ 6,550	$ 4,358	$ 2,658

Second Bancorp Incorporated and Subsidiaries
Financial Highlights Non-GAAP Operating Results
Year-to-Date Data
(Dollars in thousands, except per share data)

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Earnings:					
Net interest income	$55,871	$41,690	$27,873	$14,083	$56,460
Provision for loan losses	7,610	6,124	5,028	2,173	6,159
Non-interest income	28,364	22,783	19,292	8,592	22,853
Security gains (losses)	4,584	3,617	51	51	592
Trading account losses	0	0	0	0	(20)
Non-interest expense	54,763	40,765	27,689	13,673	47,266
Federal income taxes	6,943	5,847	4,052	1,871	7,011
Net income	**$19,503**	**$15,354**	**$10,447**	**$ 5,009**	**$19,449**
Per share:					
Basic earnings	$ 2.05	$ 1.61	$ 1.09	$ 0.52	$ 1.96
Diluted earnings	2.03	1.59	1.08	0.52	1.94
Key ratios: (%)					
Return on average assets (ROA)	0.99	1.06	1.11	1.07	1.11
Return on average shareholders equity (ROE)	14.37	15.00	15.22	14.81	14.49
Net interest margin	3.14	3.19	3.26	3.33	3.56
Net overhead	1.43	1.33	0.95	1.16	1.49
Efficiency ratio	63.52	61.80	57.49	58.98	58.07

Second Bancorp Incorporated and Subsidiaries
Reconciliation of GAAP vs. Non-GAAP Operating Results
Year-to-Date Data

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Net income	$23,155	$19,006	$14,099	$ 8,661	$18,000
Adjustments to GAAP to reflect Non-GAAP Operating Basis:					
Add non-recurring costs:					
Sale of banking centers	(5,619)	(5,619)	(5,619)	(5,619)	0
Merger costs	0	0	0	0	134
Banking center reconfiguration	0	0	0	0	2,096
Total adjustments	(5,619)	(5,619)	(5,619)	(5,619)	2,230
Federal income taxes (benefit)	(1,967)	(1,967)	(1,967)	(1,967)	781

Net income	$19,503	$15,354	$10,447	$ 5,009	$19,449

Note: Recap of Income from Mortgage Banking Activities

	Dec. 2003	Sept. 2003	June 2003	March 2003	Dec. 2002
Gross income from servicing	$ 3,888	$ 2,941	$ 1,889	$ 903	$ 2,691
Amortization of MSRs	(7,163)	(6,373)	(3,650)	(1,549)	(4,335)
(Excess amortization) / net servicing income	(3,275)	(3,432)	(1,761)	(646)	(1,644)
Change in valuation allowance MSRs	1,400	1,019	(2,511)	(989)	(2,984)
Net derivative gain (loss) non hedging	(2,753)	(1,919)	4,840	1,805	567
Income (loss) from mortgage servicing	(4,628)	(4,332)	568	170	(4,061)
Gain on sale of mortgage loans	14,822	14,083	10,340	4,188	10,470
Net mortgage banking revenue	$10,194	$ 9,751	$10,908	$ 4,358	$ 6,409