



Bluestem Group Inc.
Report as of and for the 13- and 39-weeks ended
November 2, 2018 and November 3, 2017
This report is issued December 12, 2018

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BLUESTEM GROUP INC.
Table of Contents

	<u>Page</u>
Business	1
Management's Commentary on Results of Operations, Liquidity and Capital Resources	2
Condensed Consolidated Financial Statements	
Condensed Consolidated Balance Sheets (Unaudited)	16
Condensed Consolidated Statements of Comprehensive Loss (Unaudited)	17
Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)	18
Condensed Consolidated Statements of Cash Flows (Unaudited)	19
Notes to Condensed Consolidated Financial Statements (Unaudited)	20

FORWARD-LOOKING STATEMENTS

This report contains statements that are “forward-looking statements”. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. All statements contained herein that are not clearly historical in nature are forward-looking. In some cases, you can identify these statements by use of forward-looking words, such as “may,” “will,” “should,” “anticipate,” “estimate,” “expect,” “plan,” “believe,” “predict,” “potential,” “project,” “intend,” “could,” or similar expressions. In particular, statements regarding Bluestem Group Inc. and its consolidated subsidiaries’ plans, strategies, prospects, and expectations regarding its business are forward-looking statements. You should be aware that these statements and any other forward-looking statements in this document only reflect Bluestem Group Inc. and its consolidated subsidiaries’ beliefs, assumptions, and expectations and are not guarantees of future performance. These statements involve risks, uncertainties, and assumptions. Many of these risks, uncertainties, and assumptions are beyond Bluestem Group Inc. and its consolidated subsidiaries’ control and may cause actual results and performance to differ materially from Bluestem Group Inc. and its consolidated subsidiaries’ expectations. Important factors that could cause our actual results to be materially different from our expectations include the risks and uncertainties set forth under “Risk Factors” in the Bluestem Group Inc. and its consolidated subsidiaries’ report as of and for the years ended February 2, 2018 and February 3, 2017 (the “Annual Report”) available at www.bluestem.com.

Forward-looking statements are based on Bluestem Group Inc. and its consolidated subsidiaries’ beliefs, assumptions and expectations of its future performance, taking into account all information currently available to Bluestem Group Inc. and its consolidated subsidiaries. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to Bluestem Group Inc. and its consolidated subsidiaries or are within its control. If a change occurs, Bluestem Group Inc. and its consolidated subsidiaries’ business, financial condition, and liquidity may vary materially from those expressed in its forward-looking statements.

Accordingly, you should not place undue reliance on the forward-looking statements contained in this report. These forward-looking statements are made only as of December 12, 2018, the date of this report. Bluestem Group Inc. and its consolidated subsidiaries undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events, or otherwise.

BUSINESS

As used in this report:

- “BGI,” “we,” “us,” “our,” or “the Company” refers to Bluestem Group Inc. with its consolidated subsidiaries
- “BGI Holding Company” refers to the Bluestem Group Inc. legal entity, excluding its subsidiaries
- “Bluestem” refers to Bluestem Brands, Inc., an indirect subsidiary of BGI which consists of Northstar Portfolio, Orchard Portfolio and PayCheck Direct (which was exited in the first quarter of fiscal 2017)
- “Northstar Portfolio” or “Northstar” refers to the consolidated Fingerhut and Gettington retail brands
- “Orchard Portfolio” or “Orchard” refers to the consolidated Appleseed’s, Bedford Fair, Blair, Draper’s & Damon’s (retail stores were exited during the first quarter of fiscal 2017), Gold Violin, Haband, LinenSource (which was exited in the second quarter of fiscal 2017), Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop, and WinterSilks retail brands
- “Capmark Portfolio” or “Capmark” refers to the commercial real estate finance operations of BGI

The Company

Bluestem Group Inc., a holding company headquartered in Eden Prairie, MN, operates multiple direct to consumer retail brands through its subsidiary Bluestem. The Northstar Portfolio includes Fingerhut and Gettington, both of which are national multi-channel retail brands offering a broad selection of name brand and private label merchandise serving low- to middle-income consumers by offering multiple payment plans through revolving credit lines or installment loans offered by WebBank as the originating bank as described more fully below. The Orchard Portfolio consists of multi-channel brands including Appleseed’s, Bedford Fair, Blair, Draper’s & Damon’s, Gold Violin, Haband, Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop and WinterSilks. These brands offer apparel, accessories, and home products for the boomer and senior demographic, generally considered age 50 and over, and provide customers with the ability to obtain credit through a third-party private label credit card.

By combining proprietary marketing and credit decision-making technologies, Bluestem is able to tailor merchandise and credit offers to existing and prospective customers. Bluestem views merchandising, marketing and credit management within its Northstar Portfolio business model as strategically indivisible. Credit is offered to Northstar Portfolio customers to reasonably assist them in making merchandise purchases while enhancing customer loyalty and driving repeat orders. Bluestem offers a large selection of name-brand, private label, and non-branded merchandise through internet websites and catalogs to customers in the United States of America only. Merchandise is continuously tailored across three key product categories:

- **Home** - including housewares, bed and bath, lawn and garden, home furnishings and hardware
- **Entertainment** - including electronics, video games, toys and sporting goods
- **Fashion** - including apparel, footwear, cosmetics, fragrances and jewelry

Bluestem is a party to a series of transactions with WebBank and Santander Consumer USA Inc. (“SCUSA”) related to revolving Northstar Portfolio customer accounts receivable executed under a set of operating agreements referred to collectively as the “A/R Program Agreements” and the arrangement is referred to as the “Program.” WebBank is the originating bank for Northstar Portfolio customer revolving credit accounts. Bluestem sells all new receivables originated under revolving credit accounts to SCUSA on the same day those receivables are purchased by Bluestem from WebBank. All receivables originated in revolving credit accounts are referred to as “Standard Receivables.” Bluestem services all credit accounts and related receivables as WebBank’s and/or SCUSA’s agent. In consideration of Bluestem’s servicing of the Standard Receivable portfolio owned by SCUSA, SCUSA pays a servicing fee to and shares a portion of the risk adjusted margin (“RAM”) of the portfolio with Bluestem. The Standard Receivables Agreement states if the RAM forecast projects RAM, as a percentage of forecasted average Program receivables, to be less than 5% for the full fiscal year, then Bluestem shall implement a merchant discount on all Standard Receivables to be purchased by SCUSA for the remainder of the fiscal year. SCUSA bears risk of loss due to uncollectibility of the Standard Receivables it purchases without recourse to either Bluestem or WebBank.

Northstar receivables generated in accounts other than revolving credit accounts, are referred to as “Nonstandard Receivables.” Bluestem bears risk of loss due to uncollectibility on Nonstandard Receivables. All Orchard sales are prepaid by the customer or purchased using private labeled or other third-party debit and credit cards.

See Note 5, *Serviced Credit Portfolio*, of the Notes to Condensed Consolidated Financial Statements, for more information on SCUSA-owned and Bluestem-owned accounts receivable.

MANAGEMENT'S COMMENTARY ON RESULTS OF OPERATIONS, LIQUIDITY AND CAPITAL RESOURCES

Our "Management's Commentary on Results of Operations, Liquidity and Capital Resources" is organized as follows:

- *OVERVIEW AND BASIS OF PRESENTATION*: This section provides a discussion of our consolidated company and the presentation of our segment results.
- *RESULTS OF OPERATIONS*: This section presents our consolidated results of operations, segment results, a detailed analysis of each segment's results of operations, and a discussion of information that we believe is meaningful to understand our results of operations.
- *LIQUIDITY AND CAPITAL RESOURCES*: This section provides an analysis of our liquidity and cash flows.

OVERVIEW AND BASIS OF PRESENTATION

Bluestem Group Inc. is a holding company whose businesses include Bluestem, a multi-brand retailer of a broad selection of name-brand and private label general merchandise, and Capmark, which is focused on managing a commercial real estate-related business and existing assets, including monetizing these assets when appropriate.

We present our business results based on the organizational structure we use to evaluate performance and make decisions on allocating resources and assessing performance. Our consolidated business results are presented in three reportable segments (referred to herein as "segments"): Northstar Portfolio, Orchard Portfolio and Corporate and other. Segment merchandise sales and shipping and handling revenue are recorded at the time of shipment to the customer and an adjustment to reduce sales by the estimated amount of orders in-transit to customers is recognized and reported in the Corporate and other segment. The business results for the 13- and 39-weeks ended November 2, 2018 reflect the adoption of the new revenue recognition accounting standard ("Topic 606"). The primary impact of the adoption of Topic 606 was to accelerate the timing of recognizing direct mail catalog advertising costs, which were previously capitalized and amortized over their expected period of future benefit but which are now recognized on the estimated date of first delivery to recipients. Prior year periods were not restated upon adoption of Topic 606.

Northstar Portfolio

The Northstar Portfolio consists of our Fingerhut and Gettington retail brands. These brands are national multi-channel retailers serving low- to middle-income consumers by offering products with multiple payment plans through revolving credit lines or installment loans offered by WebBank as the originating bank. While numerous retailers sell merchandise via the internet and catalogs focusing on low-to middle-income customers, we believe our Northstar Portfolio has created a differentiated business model by utilizing direct-marketing expertise to integrate proprietary credit offerings with broad general merchandise offerings including consumer electronics, domestics, housewares, fashion and home furnishings. The vast majority of sales are on revolving customer credit accounts, originated through WebBank, reflecting Northstar Portfolio's ability to combine relevant merchandise offerings with an attractive consumer credit product aligned with the customer's ability to pay. Fingerhut also offers the FreshStart program, which provides customers with the option of purchasing merchandise on installment credit terms after making an initial down payment.

Important drivers of Northstar Portfolio's business performance include growth in new customer credit accounts, average order size, existing customer repurchase rates, the mix of merchandise sold, the overall performance and credit quality of the customer accounts receivable portfolio, and promotional performance.

Orchard Portfolio

The Orchard Portfolio consists of Appleseed's, Bedford Fair, Blair, Draper's & Damon's (whose retail stores were exited during the first quarter of fiscal 2017), Gold Violin, Haband, LinenSource (which was exited in the second quarter of fiscal 2017), Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop, and WinterSilks retail brands. These brands are national multi-channel retailers offering apparel, accessories, and home products for women and men principally in the boomer and senior demographic, generally considered age 50 and older. Orchard Portfolio offers its product assortments through various platforms including online and direct mail.

Important drivers of Orchard Portfolio's business performance include growth in new customers, average order size, existing customer repurchase rates, the mix of merchandise sold, and promotional performance.

The Orchard Portfolio has an extensive proprietary database of customer information, including customer demographics and purchasing history. The Orchard Portfolio is able to design its marketing programs using this information. Marketing strategies are designed to grow lifetime value with customers by using the strength of its brand portfolio to meet more of its customers' needs. Multiple Orchard Portfolio brand relationships are fostered through circulation strategies, the design of its web universal cart and its use of a third-party private label credit platform across all Orchard brands.

Corporate and other

The Corporate and other segment includes certain costs consisting of indirect general and administrative expenses, amortization and depreciation not included in cost of goods sold, loss on impairment, the elimination of inter-segment activities as well as adjustments to net sales, cost of goods sold, and sales and marketing expenses related to product estimated to be in-transit from shipping point to the customer. In addition, the segment includes Capmark Portfolio and the PayCheck Direct business (which was exited during the first quarter of fiscal 2017). The Capmark Portfolio manages a real estate-related business and existing assets, including monetizing these assets when appropriate. PayCheck Direct was a program that was offered directly through employers or organizations as a voluntary benefit to employees and members. It allowed customers to purchase products with the convenience of paying over 12 months through payroll deductions or automatic bank withdrawals.

RESULTS OF OPERATIONS**Consolidated Results of Operations**

The following table provides our consolidated results of operations (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Net sales and revenue				
Net sales	\$ 407,777	\$ 399,798	\$ 1,211,036	\$ 1,266,314
Commercial real estate revenue, net	514	1,115	1,268	2,522
Total net sales and revenue	408,291	400,913	1,212,304	1,268,836
Costs and expenses				
Cost of goods sold	216,273	208,663	631,499	661,190
Sales and marketing expenses	110,591	107,192	335,843	343,636
Net credit expense	26,674	30,398	80,833	89,821
General and administrative expenses	48,847	46,274	144,034	168,119
Amortization and depreciation not included in cost of goods sold	11,961	13,471	36,308	42,797
Loss on impairment	—	—	—	230
Total costs and expenses	414,346	405,998	1,228,517	1,305,793
Operating loss	(6,055)	(5,085)	(16,213)	(36,957)
Interest expense, net	12,738	12,785	37,853	38,401
Loss before income taxes	(18,793)	(17,870)	(54,066)	(75,358)
Income tax benefit	(4,807)	(1,390)	(6,080)	(1,514)
Net loss	\$ (13,986)	\$ (16,480)	\$ (47,986)	\$ (73,844)
Other comprehensive loss				
Unrealized (gain) loss on interest rate swaps, net of tax	(206)	917	(58)	124
Comprehensive loss	\$ (14,192)	\$ (15,563)	\$ (48,044)	\$ (73,720)

Results of Operations by Segment

The following tables provide selected financial information by segment (in thousands):

	13-Weeks Ended November 2, 2018			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 227,549	\$ 184,332	\$ (4,104)	\$ 407,777
Commercial real estate revenue, net	—	—	514	514
Total net sales and revenue	227,549	184,332	(3,590)	408,291
Costs and expenses				
Cost of goods sold	127,857	91,460	(3,044)	216,273
Sales and marketing expenses	35,393	75,288	(90)	110,591
Net credit expense	26,665	—	9	26,674
General and administrative expenses	7,130	9,350	32,367	48,847
Amortization and depreciation not included in cost of goods sold	—	—	11,961	11,961
Total costs and expenses	197,045	176,098	41,203	414,346
Operating income (loss)	\$ 30,504	\$ 8,234	\$ (44,793)	\$ (6,055)
	13-Weeks Ended November 3, 2017			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 210,115	\$ 201,703	\$ (12,020)	\$ 399,798
Commercial real estate revenue, net	—	—	1,115	1,115
Total net sales and revenue	210,115	201,703	(10,905)	400,913
Costs and expenses				
Cost of goods sold	119,488	96,311	(7,136)	208,663
Sales and marketing expenses	29,490	80,859	(3,157)	107,192
Net credit expense	30,129	—	269	30,398
General and administrative expenses	6,800	9,115	30,359	46,274
Amortization and depreciation not included in cost of goods sold	—	—	13,471	13,471
Total costs and expenses	185,907	186,285	33,806	405,998
Operating income (loss)	\$ 24,208	\$ 15,418	\$ (44,711)	\$ (5,085)

Results of Operations by Segment

The following tables provide selected financial information by segment (in thousands):

	39-Weeks Ended November 2, 2018			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 635,051	\$ 586,888	\$ (10,903)	\$ 1,211,036
Commercial real estate revenue, net	—	—	1,268	1,268
Total net sales and revenue	635,051	586,888	(9,635)	1,212,304
Costs and expenses				
Cost of goods sold	356,169	284,576	(9,246)	631,499
Sales and marketing expenses	94,477	241,506	(140)	335,843
Net credit expense	80,734	—	99	80,833
General and administrative expenses	20,075	27,669	96,290	144,034
Amortization and depreciation not included in cost of goods sold	—	—	36,308	36,308
Total costs and expenses	551,455	553,751	123,311	1,228,517
Operating income (loss)	\$ 83,596	\$ 33,137	\$ (132,946)	\$ (16,213)

	39-Weeks Ended November 3, 2017			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 618,217	\$ 652,408	\$ (4,311)	\$ 1,266,314
Commercial real estate revenue, net	—	—	2,522	2,522
Total net sales and revenue	618,217	652,408	(1,789)	1,268,836
Costs and expenses				
Cost of goods sold	353,678	310,026	(2,514)	661,190
Sales and marketing expenses	92,443	252,766	(1,573)	343,636
Net credit expense	85,436	—	4,385	89,821
General and administrative expenses	19,975	28,699	119,445	168,119
Amortization and depreciation not included in cost of goods sold	—	—	42,797	42,797
Loss on impairment	—	—	230	230
Total costs and expenses	551,532	591,491	162,770	1,305,793
Operating income (loss)	\$ 66,685	\$ 60,917	\$ (164,559)	\$ (36,957)

NORTHSTAR PORTFOLIO

Northstar Portfolio's net sales, costs of goods sold, gross profit, order and new customer data are summarized below (in thousands, except average order size):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Sales by category:				
Home	\$ 95,622	\$ 90,395	\$ 286,042	\$ 284,831
Entertainment	91,002	89,453	243,878	251,260
Fashion	50,184	39,113	127,316	105,056
Total Sales	236,808	218,961	657,236	641,147
Returns and allowances	(13,687)	(13,178)	(35,369)	(36,558)
Commissions and other revenues	4,428	4,332	13,184	13,628
Net sales	227,549	210,115	635,051	618,217
Cost of goods sold	127,857	119,488	356,169	353,678
Gross profit	\$ 99,692	\$ 90,627	\$ 278,882	\$ 264,539
Gross profit percentage	43.8%	43.1%	43.9%	42.8%
Orders filled	1,067	943	2,916	2,761
Average order size	\$ 222	\$ 232	\$ 225	\$ 232
New revolving credit customers	127	104	371	302
New FreshStart customers	52	46	152	142

Net Sales

Net sales of Northstar Portfolio include sales of merchandise, shipping and handling revenue, and commissions earned from third parties that market their products to our customers. Segment merchandise sales and shipping and handling revenue are recorded at the time of shipment to the customer and an adjustment to reduce sales by the estimated amount of orders in-transit to customers is recognized and reported in the Corporate segment. Merchandise sales are reported net of discounts and estimated sales returns, and exclude sales taxes.

Sales to existing customers are driven by our ability to retain customers through our merchandise assortment, marketing campaigns, and credit line account management strategies. New customer accounts are acquired through catalog mailings, digital advertising, and other mass advertising.

Net sales for Northstar Portfolio for the 13- and 39-weeks ended November 2, 2018 increased 8.3% and 2.7%, respectively, compared to the 13- and 39-weeks ended November 3, 2017. Fingerhut net sales increased \$15.0 million during the third quarter and \$16.1 million year-to-date primarily due to marketing efforts targeting inactive account holders to activate or reactivate their accounts and continued acquisition of new customers through external partners. Gettington net sales increased \$2.5 million during the third quarter and \$0.7 million year-to-date due to a repositioning of the brand executed in the second quarter of fiscal 2018 led by new customer acquisition through renewed marketing investment in catalog, digital and third-party partners, partially offset by increased promotional discounts to drive demand.

Cost of Goods Sold

Cost of goods sold of Northstar Portfolio include the cost of merchandise sold (net of vendor rebates, purchase discounts, and estimated returns), shipping and handling costs, inbound freight costs, payroll and benefits for distribution center employees, rent, occupancy costs, depreciation of our distribution center equipment, charges from third-party distribution centers, and estimates of product obsolescence costs.

Gross Profit

Northstar Portfolio's gross profit percentage for the 13- and 39-weeks ended November 2, 2018 increased 70 and 110 basis points, respectively, compared to the 13- and 39-weeks ended November 3, 2017, primarily due to an improved mix of higher margin fashion goods and private label electronics versus lower margin brand name electronics as well as improved margins across all categories.

Sales and Marketing Expenses

The following table presents sales and marketing expenses of Northstar Portfolio, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Catalog direct mail	\$ 22,257	\$ 18,491	\$ 59,120	\$ 56,383
Television and digital marketing	10,496	8,016	28,216	27,472
Order entry and customer service	2,251	2,409	5,650	6,517
Premium (free gift with purchase) and other	389	574	1,491	2,071
Sales and marketing expenses	<u>\$ 35,393</u>	<u>\$ 29,490</u>	<u>\$ 94,477</u>	<u>\$ 92,443</u>
Sales and marketing expenses as a percent of net sales	15.6%	14.0%	14.9%	15.0%

Northstar Portfolio's sales and marketing expenses included an increase of \$3.6 million and \$4.7 million related to changes in timing of the recognition of catalog direct mail costs as a result of the adoption of Topic 606 for the 13- and 39-weeks ended November 2, 2018, respectively. Excluding these timing changes, sales and marketing expense as a percent of net sales was unchanged in the 13-weeks ended November 2, 2018 compared to the 13-weeks ended November 3, 2017, and decreased 90 basis points in the 39-weeks ended November 2, 2018 compared to the 39-weeks ended November 3, 2017 primarily due to improved customer response to marketing, reduced catalog mailings and discontinuation of television advertising in September 2017 as part of our efforts to upgrade the overall credit profile of new customers in our serviced credit portfolio, partially offset by growth in acquisition digital affiliate programs and new Gettington customer acquisition costs.

Net Credit Expense

The following table presents net credit expenses of Northstar Portfolio, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Provision for doubtful accounts:				
Loss on sale of customer accounts receivable	\$ 17,477	\$ 20,950	\$ 54,865	\$ 52,145
Company-owned customer accounts receivable	2,437	1,839	6,578	5,628
Total provision for doubtful accounts	19,914	22,789	61,443	57,773
Credit management costs	15,188	15,882	46,107	50,982
Finance charge and fee income, net	(683)	(361)	(2,149)	(1,763)
Servicing fee income	(6,607)	(6,623)	(20,330)	(20,588)
Gain on servicing right	(1,147)	(1,558)	(4,337)	(968)
Net credit expense	<u>\$ 26,665</u>	<u>\$ 30,129</u>	<u>\$ 80,734</u>	<u>\$ 85,436</u>
Annualized net credit expense as a percent of average customer accounts receivable	7.8%	8.8%	7.7%	8.1%
Average customer accounts receivable	<u>\$ 1,361,839</u>	<u>\$ 1,361,884</u>	<u>\$ 1,394,197</u>	<u>\$ 1,411,524</u>

Net credit expense includes credit management costs on all customer accounts receivable whether such receivables are owned by the Company or SCUSA, a provision for doubtful accounts, finance charge and fee income on Company-owned accounts receivable, servicing fee income and portfolio profit sharing from SCUSA owned accounts receivable and losses (gains) on servicing the portfolio. As of November 2, 2018, total serviced customer accounts receivable was \$1.3 billion, of which \$11.3 million were Company-owned. As of November 3, 2017, total serviced customer accounts receivable was \$1.3 billion, of which \$21.8 million were Company-owned. The decrease in Company-owned accounts receivable is primarily due to the collection of outstanding receivables following the exit of the PayCheck Direct business in the first quarter of fiscal 2017. Credit management costs for the total serviced accounts receivable include statement and payment processing, collections, origination fees paid to WebBank, new account application processing, credit bureau processing costs, and customer service costs. SCUSA bears risk of loss due to uncollectibility of the Standard Receivables it owns. Bluestem bears risk of loss due to uncollectibility on Nonstandard Receivables, and any existing Standard Receivables not purchased by SCUSA.

We maintain an allowance for doubtful accounts at a level intended to absorb probable losses on Nonstandard Receivables as of the balance sheet date and a provision for doubtful accounts needed to reduce the value of accounts receivable purchased from WebBank to the discounted value sold to SCUSA. The Standard Receivables Sale Agreement states that if the Risk Adjusted Margin ("RAM") forecast projects RAM, as a percentage of forecasted average Program receivables, to be less than 5% for the full fiscal year, then Bluestem shall implement a merchant discount rate on all Standard Receivables purchased by SCUSA for the remainder of the fiscal year. Sales of Standard Receivables to SCUSA were made at a discount to par of 7.23% or \$17.5 million and 9.51% or \$21.0 million during the 13-weeks ended November 2, 2018 and November 3, 2017, respectively. Sales of Standard Receivables to SCUSA were made at a discount to par of

8.21% or \$54.9 million and 7.97% or \$52.1 million during the 39-weeks ended November 2, 2018 and November 3, 2017, respectively.

Finance charges are accrued on Company-owned accounts receivable until the account balance is paid or charged off. A late fee is imposed if the customer does not pay at least the minimum payment by the payment due date and continues until the account is over 90 days delinquent for revolving accounts, or until the account initially becomes delinquent for installment accounts.

Northstar receives a servicing fee and shares in a portion of the profits as compensation for servicing customer accounts receivable owned by SCUSA. The Company has determined that the servicing fee received from SCUSA does not allow it to adequately recover the costs of servicing the portfolio nor earn a reasonable level of profit. As a result, the Company records a servicing liability which is adjusted each quarter for changes in its fair value. Northstar recorded non-cash gains of \$1.1 million and \$1.6 million resulting from reductions of the fair value of the servicing liability during the 13-weeks ended November 2, 2018 and November 3, 2017, respectively. Changes in the fair value of the servicing liability resulted in non-cash gains of \$4.3 million and \$1.0 million during the 39-weeks ended November 2, 2018 and November 3, 2017, respectively. Gains recognized in the 13- and 39-weeks ended November 2, 2018 were primarily the result of a reduction of receivables in those periods. See Note 5, *Serviced Credit Portfolio* of the Notes to Condensed Consolidated Financial Statements, for more information.

Credit management costs for the 13- and 39-weeks ended November 2, 2018 compared to the 13- and 39-weeks ended November 3, 2017 decreased by \$0.7 million and \$4.9 million, respectively, driven by operational improvements in collections combined with lower credit bureau cost.

General and Administrative Expenses

The following table presents general and administrative expenses of Northstar Portfolio, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Compensation and benefits	\$ 5,504	\$ 5,486	\$ 15,680	\$ 16,010
Professional fees	1,279	1,001	3,371	3,013
Rents and occupancy costs	136	69	412	207
Other	211	244	612	745
General and administrative expenses	<u>\$ 7,130</u>	<u>\$ 6,800</u>	<u>\$ 20,075</u>	<u>\$ 19,975</u>
General and administrative expenses as a percent of net sales	3.1%	3.2%	3.2%	3.2%

These expenses primarily consist of direct compensation, benefits and other overhead costs for credit, merchandising and marketing management.

General and administrative expenses for the 13- and 39-weeks ended November 2, 2018 were essentially flat compared to the prior year periods.

ORCHARD PORTFOLIO

Orchard Portfolio's net sales, cost of goods sold, gross profit, order and gross customer data are summarized below (in thousands, except average order size):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Sales by category:				
Fashion	\$ 196,224	\$ 205,089	\$ 630,020	\$ 658,451
Home	7,748	12,266	25,631	48,706
Total Sales	203,972	217,355	655,651	707,157
Returns and allowances	(26,323)	(29,630)	(89,538)	(98,631)
Commissions and other revenues	6,683	13,978	20,775	43,882
Net sales	184,332	201,703	586,888	652,408
Cost of goods sold	91,460	96,311	284,576	310,026
Gross profit	\$ 92,872	\$ 105,392	\$ 302,312	\$ 342,382
Gross profit percentage	50.4 %	52.3%	51.5 %	52.5%
Orders filled	2,985	3,225	9,466	10,006
Average order size	\$ 66	\$ 67	\$ 67	\$ 71
Gross new customers ⁽¹⁾	437	494	1,425	1,603
Gross active customers ⁽¹⁾	7,155	7,533	7,155	7,533
Unique new customers ⁽¹⁾	167	167	518	530
Unique active customers ⁽¹⁾	4,327	4,570	4,327	4,570

⁽¹⁾Gross customer data is for individual customers that have made at least one purchase from a particular brand within the Orchard Portfolio and unique customers are unique individuals who have made at least one purchase from the Orchard Portfolio. New customers are individuals who have made a first-time purchase during the period presented. Active customers are individuals who have made at least one purchase in the previous 12-month period.

Net Sales

Net sales of Orchard Portfolio consist of sales of merchandise, shipping and handling revenue, and commissions earned from third parties that market their products to our customers. Orchard Portfolio segment merchandise sales and shipping and handling revenue are recorded at the time of shipment to the customer while an adjustment to reduce sales by the estimated amount of orders in-transit to customers is recognized and reported in the Corporate segment. Merchandise sales are reported net of discounts and estimated sales returns, and exclude sales taxes.

Sales to existing customers are driven by our ability to retain customers through the use of a multi-channel marketing approach, including catalog mailings, digital marketing, site marketing and merchandising. The reactivation of former customers and acquisition of new customers are attained through visibility to our website generated by catalog mailings, space media and digital marketing.

For the 13-weeks ended November 2, 2018, Orchard Portfolio net sales decreased 8.6% compared to the 13-weeks ended November 3, 2017, partially due to the fiscal 2017 exit of the LinenSource brand. Adjusted for exited businesses, net sales decreased 7.9% due to a reduction in catalog circulation as part of our strategy to improve catalog marketing productivity and profitability, increased promotional discounts to drive demand and a reduction in other revenues as a result of decreased enrollments in our loyalty programs.

For the 39-weeks ended November 2, 2018, net sales decreased 10.0% compared to the 39-weeks ended November 3, 2017, in part due to the fiscal 2017 exit of Draper's and Damon's retail stores and the LinenSource brand. Adjusted for exited businesses, net sales decreased 6.7% due to fewer active customers and a reduction in other revenue as a result of decreased enrollments in our loyalty programs.

Cost of Goods Sold

Cost of goods sold of Orchard Portfolio includes the cost of merchandise sold (net of vendor rebates, purchase discounts, and estimated returns), shipping and handling costs, inbound freight costs, payroll and benefits for distribution center employees, depreciation of distribution center facilities and assets and estimates of product obsolescence costs.

Gross Profit

The gross profit percentage for the 13- and 39-weeks ended November 2, 2018 Orchard Portfolio's gross profit percentage decreased 190 basis points and 100 basis points, respectively, compared to the 13- and 39-weeks ended November 3, 2017, primarily due to reductions

in other revenue as a result of decreased enrollments in our loyalty programs, inventory obsolescence costs due to sales trends, and increased promotional discounts to drive demand.

Sales and Marketing Expenses

The following table presents sales and marketing expenses of Orchard Portfolio, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Catalog direct mail	\$ 57,952	\$ 66,182	\$ 190,835	\$ 204,310
Digital marketing	7,244	4,091	19,276	13,406
Order entry and customer service	5,724	6,307	18,268	19,589
Retail Store	48	48	148	2,774
Premium (free gift with purchase) and other	4,320	4,231	12,979	12,687
Sales and marketing expenses	<u>\$ 75,288</u>	<u>\$ 80,859</u>	<u>\$ 241,506</u>	<u>\$ 252,766</u>
Sales and marketing expenses as a percent of net sales	40.8%	40.1%	41.2%	38.7%

Orchard Portfolio's sales and marketing expenses for the 13- and 39-weeks ended November 2, 2018 included net increases of \$1.7 million and \$3.0 million, respectively, related to changes in the timing of the recognition of catalog direct mail costs as a result of the adoption of Topic 606. Excluding this change in expense timing, sales and marketing expense as a percent of net sales decreased 20 basis points and 190 basis points, respectively, primarily due to a reduction in catalog circulation as part of our strategy to improve marketing productivity and profitability, partially offset by increased investment in digital advertising. Catalog direct mail costs for the 13- and 39-weeks ended November 2, 2018, excluding the effects of Topic 606 adjustments, decreased \$9.9 million and \$16.5 million, respectively, compared to the 13- and 39-weeks ended November 3, 2017.

General and Administrative Expenses

The following table presents general and administrative expenses of Orchard Portfolio, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Compensation and benefits	\$ 6,912	\$ 7,040	\$ 20,040	\$ 22,497
Professional fees	1,275	848	4,172	2,307
Rents and occupancy costs	846	853	2,413	2,698
Other	317	374	1,044	1,197
General and administrative expenses	<u>\$ 9,350</u>	<u>\$ 9,115</u>	<u>\$ 27,669</u>	<u>\$ 28,699</u>
General and administrative expenses as a percent of net sales	5.1%	4.5%	4.7%	4.4%

These expenses primarily consist of direct compensation, benefits and other overhead costs for merchandising and marketing management.

Orchard Portfolio's general and administrative expenses as a percent of net sales for the 13- and 39-weeks ended November 2, 2018 increased compared to the 13- and 39-weeks ended November 3, 2017 as a result of increased professional fees related to operational improvement projects and deleveraged costs against lower net sales, partially offset by a decrease in compensation following a workforce reduction completed in March 2017 and a decrease in incentive compensation.

CORPORATE AND OTHER

Corporate and other's net sales, revenues and expenses are summarized below (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Net sales	\$ (4,104)	\$ (12,020)	\$ (10,903)	\$ (4,311)
Commercial real estate revenue, net	514	1,115	1,268	2,522
Net sales and revenues	(3,590)	(10,905)	(9,635)	(1,789)
Cost of goods sold	(3,044)	(7,136)	(9,246)	(2,514)
Sales and marketing expenses	(90)	(3,157)	(140)	(1,573)
Net credit expense	9	269	99	4,385
General and administrative expenses	32,367	30,359	96,290	119,445
Amortization and depreciation not included in cost of goods sold	11,961	13,471	36,308	42,797
Loss on impairment	—	—	—	230
Operating loss	(44,793)	(44,711)	(132,946)	(164,559)
Total interest expense, net	12,738	12,785	37,853	38,401
Income tax benefit	(4,807)	(1,390)	(6,080)	(1,514)
Net loss	\$ (52,724)	\$ (56,106)	\$ (164,719)	\$ (201,446)

Net Sales and Revenues

Corporate net sales consist of adjustments to Bluestem's net sales related to product sales estimated to be in-transit from shipping point to the customer, the elimination of inter-segment activities and the net sales of the PayCheck Direct business (which was exited during the first quarter of fiscal 2017 and which is currently winding down). PayCheck Direct net sales include sales of merchandise (reported net of discounts and estimated sales returns, and exclude sales taxes), shipping and handling revenue, and commissions earned from third parties that market their products to our customers. Commercial real estate revenue includes Capmark's net gains on loans, equity in income of joint venture and partnerships and other gains and losses, net as our equity investments continue to wind down and approach the end of their lives.

Excluding the exited PayCheck Direct business net sales (\$12.2 million during the first quarter of fiscal 2017), the changes in Corporate and other net sales were primarily due to the level and timing of in-transit sales in the 13- and 39-weeks ended November 2, 2018 versus the comparable fiscal 2017 periods.

Cost of Goods Sold

Corporate cost of goods sold consist of adjustments to Bluestem's cost of goods sold related to product sales estimated to be in-transit from shipping point to the customer, the elimination of inter-segment activities and the cost of goods sold of PayCheck Direct. PayCheck Direct cost of goods sold includes the cost of merchandise sold (net of vendor rebates, purchase discounts, and estimated returns), shipping and handling costs, inbound freight costs, payroll and benefits for distribution center employees, rent, occupancy costs, depreciation of our distribution center equipment, charges from third-party distribution centers, and estimates of product obsolescence costs.

Excluding the exited PayCheck Direct business cost of goods sold (\$7.7 million during the first quarter of fiscal 2017), the change in Corporate and other net cost of goods sold was primarily due to the level and timing of in-transit sales in the 13- and 39-weeks ended November 2, 2018 versus the comparable fiscal 2017 periods.

Sales and Marketing Expenses

Corporate and other's sales and marketing expenses for the 13- and 39-weeks ended November 2, 2018 included net increases of \$1.5 million and \$1.6 million, respectively, related to changes in the timing of the recognition of catalog direct mail costs as a result of the adoption of Topic 606. Excluding these timing changes, sales and marketing expenses decreased compared to the 13- and 39-weeks ended November 3, 2017, primarily due to the exit of the PayCheck Direct business and the level of promotional and advertising expenses related to in-transit sales.

Net Credit Benefit

Corporate and other's net credit expense for the 13- and 39-weeks ended November 2, 2018 decreased compared to the 13- and 39-weeks ended November 3, 2017, primarily due to the exit of the PayCheck Direct business.

General and Administrative Expenses

The following table presents general and administrative expenses of Corporate and other, by category (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Compensation and benefits	\$ 18,398	\$ 16,045	\$ 56,758	\$ 64,606
Professional fees and contract labor	4,930	6,971	14,325	24,955
Rents and occupancy costs	6,197	6,231	18,707	23,301
Other	2,842	1,112	6,500	6,583
General and administrative expenses	<u>\$ 32,367</u>	<u>\$ 30,359</u>	<u>\$ 96,290</u>	<u>\$ 119,445</u>

Corporate and other's general and administrative expenses for the 13- and 39-weeks ended November 3, 2017 included restructuring costs of \$0.1 million and \$10.1 million, respectively. Excluding restructuring costs, Corporate and other's general and administrative expenses for the 13-weeks ended November 2, 2018 increased \$2.1 million primarily due to an increase in benefit expense for health and welfare and expense related to the expected settlement of a certain class action lawsuit. See Note 15, *Commitment and Contingent Liabilities* of the Notes to Condensed Consolidated Financial Statements, for more information. Excluding restructuring costs, for the 39-weeks ended November 2, 2018, general and administrative expenses decreased \$13.1 million primarily due to a decrease in compensation as a result of a workforce reduction completed in March 2017, and lower incentive compensation, professional services and other general expenses, partially offset by an increase in benefit expense for health and welfare and expense related to the expected settlement of a certain class action lawsuit. See Note 8, *Restructuring Costs*, of the Notes to Condensed Consolidated Financial Statements, for more information.

Amortization and Depreciation not Included in Costs of Goods Sold

Amortization and depreciation expenses not included in cost of goods sold includes amortization of our customer relationship intangible assets, depreciation of our property and equipment including purchased and internally developed software, computer hardware, machinery and equipment, office furniture, property under capital lease, and leasehold improvements.

Amortization and depreciation expenses not included in cost of goods sold for the 13- and 39-weeks ended November 2, 2018 decreased compared to the 13- and 39-weeks ended November 3, 2017 primarily due to a change in the fair value of finite-lived intangible assets based on updated assumptions that was recorded in the first quarter of 2017 and a decline in capital expenditures.

Loss on Impairment

The overall financial performance for the 39-weeks ended November 2, 2018 of the Orchard Portfolio is below management's expectations. We have experienced a decline in our Orchard customer file due to a decline in rebuy rates and declining new customer acquisition. Management is taking and evaluating actions to improve financial performance by pursuing further enhancements to gross margin, implementing more efficient and profitable marketing strategies and continuing evaluation of under-performing brands. As the financial performance in the third quarter is below management's expectations, we are re-assessing the assumptions in our long term financial plan. This re-assessment has led us to conclude that there is an indicator of possible intangible and long-lived asset impairment relating to the Orchard Portfolio. As of November 2, 2018, the Company has intangible assets relating to the Orchard Portfolio of \$37.1 million in tradenames and \$64.0 million in customer relationships. Due to the significant effort that is required to determine the current fair values of Orchard's intangible and long-lived assets, we are unable to reasonably estimate the amount of impairment, if any, during the third quarter. The Company expects to complete its impairment test in the fourth quarter and the amount of an impairment, if any, that is determined could be material to the Company's consolidated financial statements.

Interest Expense, net

The following table presents interest expense by category, weighted average borrowings outstanding and weighted average interest rates (in thousands except for weighted average interest rates):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Interest on debt	\$ 11,798	\$ 11,237	\$ 34,639	\$ 33,660
Interest on capital lease obligation	9	24	36	103
Interest rate swap net settlements	(414)	176	(859)	592
Amortization of deferred charges	758	758	2,274	2,274
Amortization of original issue discount	593	593	1,779	1,779
Interest income	(6)	(3)	(16)	(7)
Total interest expense, net	<u>\$ 12,738</u>	<u>\$ 12,785</u>	<u>\$ 37,853</u>	<u>\$ 38,401</u>
Weighted average borrowings outstanding	\$ 494,200	\$ 512,003	\$ 487,549	\$ 529,270
Weighted average interest rate	9.5%	7.9%	9.4%	8.0%

The Company's interest expense is primarily related to the outstanding balances of its term loan and asset-backed line of credit. Interest expense for the 13- and 39-weeks ended November 2, 2018 decreased slightly compared to the 13- and 39-weeks ended November 3, 2017, primarily due to the favorable settlement of interest rate swaps that offset the effect of higher market interest rates. See the "Liquidity and Capital Resources" section below for additional information.

Income Tax Benefit

For the 13- and 39-weeks ended November 2, 2018, income tax benefit was recognized on \$18.8 million and \$54.1 million of loss before income taxes, respectively. The tax benefit was primarily related to releases of state unrecognized tax benefit liability and the valuation allowance offset by state and international taxes.

For the 13- and 39-weeks ended November 3, 2017, income tax benefit was recognized on \$17.9 million and \$75.4 million of loss before income taxes, respectively. The tax benefit was primarily related to the release of federal and state tax benefit liabilities and offset by state and international taxes. Based on our historical and cumulative losses, a tax benefit was not recognized for 2017 losses or carryforwards offsetting future years' income.

The Company recognized the income tax effects of the 2017 Tax Cuts and Jobs Act (the "Tax Act") in the February 2, 2018 consolidated financial statements in accordance with Staff Accounting Bulletin No. 118, which provides SEC staff guidance for the application of ASC Topic 740, Income Taxes, and allowed up to one year to complete the required analyses and accounting for the Tax Act. At February 2, 2018 the Company was able to make reasonable estimates of the impact of the Tax Act for among other things reduced the U.S. corporate income tax rate from 35 percent to 21 percent effective January 1, 2018, changed rules related to NOL carryforwards and carrybacks, and added rules that limit the deductibility of interest expense. At February 2, 2018, the Company recorded a provisional income tax benefit of \$24.3 million pursuant to SAB 118. The accounting for the income tax effects of the enactment of the Tax Act is complete as of November 2, 2018. There were no material changes to these provisional estimates during the 39-weeks ended November 2, 2018.

Based on the Company's historical and cumulative losses, a net tax benefit was not recognized for current year pre-tax losses or carryforwards offsetting future year income. Tax benefits from net operating loss carryforwards and other deferred assets are limited to temporary differences expected to generate future taxable income. Tax benefits from carryforwards and other deferred tax assets offsetting additional income beyond the current year may be recognized in the future and could be material.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity and Capital Resources

As of November 2, 2018, we had \$120.7 million in total cash and cash equivalents on hand, of which \$111.5 million was held by BGI Holding Company. Cash is invested approximately 50% in commercial paper and approximately 50% in money market funds. We purchase money market funds that invest in U.S. dollar-denominated money market securities of domestic and foreign issuers rated in the highest categories or in diversified portfolios of high quality, short-term dollar-denominated debt securities issued or guaranteed by the U.S. government or its agencies. BGI Holding Company also held net commercial real estate assets of \$5.7 million (excluding the Irvine Distribution Center discussed below) as of November 2, 2018 and February 2, 2018.

On February 3, 2017, the Board of Directors declared a special cash dividend of \$0.60 per share of the Company's outstanding common stock and Series A Participating Convertible Preferred Stock (the "Special Dividend"). The Special Dividend resulted in an \$80.2 million payment in the 39-weeks ended November 3, 2017.

During fiscal 2017 following the exit of the PayCheck Direct business, Bluestem sold \$43.3 million PayCheck Direct accounts receivable to BGI Holding Company under an arms-length transaction with an 8.6% discount of net book value for proceeds of \$29.8 million in order to accelerate the cash collection of PayCheck Direct receivables to Bluestem. Subsequently \$33.8 million of Paycheck Direct receivables were collected by BGI Holding Company and no Paycheck Direct receivables remain on the balance sheet as of November 2, 2018. BGI Holding Company also paid Bluestem \$2.8 million to service the Paycheck Direct receivables during the run-off period.

On September 1, 2017, Bluestem sold its Irvine Distribution Center in Irvine, PA to BGI Holding Company under an arms-length transaction for net proceeds of \$24.3 million, which has been used as a source of cash to fund Bluestem operations. BGI Holding Company and Bluestem entered into a lease agreement for the Irvine Distribution Center maturing in August 2037. Bluestem's primary sources of liquidity are (1) proceeds from the sales of customer accounts receivables to SCUSA, (2) cash flows from operations, (3) availability under an asset-backed line of credit, (4) cash and cash equivalents on hand, and (5) collections on the Company's owned accounts receivable portfolio.

Bluestem's retail operations require a significant amount of capital to grow and fund operations. Ensuring adequate liquidity is, and will continue to be, at the forefront of Bluestem's business objectives. The primary uses of cash are (1) purchases of inventory, (2) purchases and production of promotional materials, and (3) other general working capital needs. The majority of Northstar Portfolio's sales occur on customer credit accounts issued by WebBank. All eligible Northstar Portfolio revolving customer accounts receivable are sold to SCUSA on the day they are purchased by Bluestem from WebBank. As a result, working capital is improved due to the quicker turn around than if those accounts receivable were held by Bluestem. Orchard offers its customers financing through its private label credit cards, which are issued and managed by a third-party bank. Approximately 29% of Orchard's sales occurred on these cards during the 39-weeks ended November 2, 2018 with the remaining sales primarily occurring on third-party debit and credit cards, resulting in a short-term use of working capital until the receivables are collected. Payable terms are managed with vendors in an effort to achieve a balance between working capital and liquidity.

The Northstar Portfolio's cash requirements are seasonal, with peak needs occurring from September through November as marketing efforts increase and inventory grows in advance of the holiday season. The Orchard Portfolio's cash requirements are also seasonal in nature, peaking in the first and third fiscal quarters due to the purchase of inventory and the production of promotional materials in advance of the Spring and Fall seasons. During these peaks, utilization of the asset-backed line of credit increases. Availability is dependent on eligible collateral for the borrowing base (primarily comprised of inventory and non-customer receivables) and outstanding borrowings.

Additional cash requirements relate to debt service for Bluestem's term loan, capital investments in our business and other general working capital needs. Bluestem's Excess Cash Flow (as defined in the term loan agreement) is used to pay down the term loan, and may also be used to pay down outstanding amounts under the asset-backed line of credit.

Bluestem has interest rate swap agreements under which a fixed rate is paid and a variable rate is received. The notional amounts of the swap agreements are \$100 million, \$75 million, and \$75 million respectively, with maturity dates of April 29, 2019, June 28, 2019, and April 30, 2020, respectively. The swap agreements are designated as cash flow hedges. See Note 12, *Derivative Instruments*, of the Notes to Condensed Consolidated Financial Statements for more information.

Substantially all of the Company's existing debt obligations have been incurred by Bluestem, which is expected to continue to be required to comply with certain financial covenants and ratios contained within the term loan agreement and the asset-backed line of credit agreement ("Lender Requirements"), as well as separate financial covenants and ratios under the A/R Program Agreements ("Program Requirements"). The Lender Requirements are based on Bluestem's standalone financial results excluding unrestricted subsidiaries while the Program Requirements are based on Bluestem's standalone financial results including all subsidiaries. Unrestricted subsidiaries are designated by Bluestem based on qualifications defined by the loan agreements.

Bluestem's performance against covenants as of November 2, 2018 were as follows (net liquidity in thousands):

	Leverage Ratio		Net Liquidity	
	Results	Requirement	Position	Requirement
Term loan agreement and asset-backed line of credit agreement	4.09	< 4.50	\$86,982	> \$ 40,000
Program agreement	4.11	< 5.00	\$87,118	> \$ 40,000

Bluestem's cash flow is highly dependent on the volume of its sales and the credit performance of the receivables sold to SCUSA. Bluestem's reported losses in fiscal 2017 and the 13- and 39-weeks ended November 2, 2018 were driven by decreasing net sales and the merchant discount on receivables sold to SCUSA due to challenging and competitive credit and retail environments. As a result, Bluestem has taken and continues to evaluate actions to improve the performance and stability of the business. To date, actions have included a workforce reduction, exiting certain businesses that were neither accretive nor consistent with our strategic goals, tightening underwriting on the Northstar credit portfolio, eliminating unproductive or unprofitable Orchard marketing spend, investing more in

digital advertising, and eliminating redundant facilities. The Company's performance relative to the financial covenants is expected to be tight for the foreseeable future and there can be no assurance that Bluestem's operating results will improve or that any actions taken will allow Bluestem to remain in compliance with the Lender Requirements or Program Requirements.

Sources and Uses of Cash

The following table represents a comparison of the net cash provided by operating activities, investing activities, and financing activities (in thousands):

	39-Weeks Ended	
	November 2, 2018	November 3, 2017
Net cash provided by operating activities	\$ 30,839	\$ 52,229
Net cash used in investing activities	\$ (68,032)	\$ (57,902)
Net cash provided by (used in) financing activities	\$ 33,452	\$ (76,893)

Operating cash flows resulted primarily from sales of products to our customers offset by cash payments for purchases of inventories, purchases and production of promotional materials, employee compensation, credit management costs, operating leases, interest payments on our debt obligations, and general working capital needs. The decrease in cash provided by operating activities for the 39-weeks ended November 2, 2018 compared to the 39-weeks ended November 3, 2017 was driven by a decrease in net loss.

Investing cash flows for the 39-weeks ended November 2, 2018 resulted primarily from purchases of customer accounts receivable from WebBank and purchases of property and equipment, offset by proceeds from sales of our customer accounts receivable to SCUSA and distributions from equity investments. The increase in cash used in investing activities for the 39-weeks ended November 2, 2018 compared to the 39-weeks ended November 3, 2017 was primarily a result of decreased net proceeds from the sale and purchase of customer accounts receivable due to an increase in the average merchant discount and decreased equity investment distributions due to the wind down of the Capmark's portfolio of commercial real estate assets.

Financing cash flows resulted primarily from net proceeds of borrowings on our asset-backed line of credit offset by payments on the outstanding Term Loan. The decrease in cash provided by financing activities for the 39-weeks ended November 2, 2018 compared to the 39-weeks ended November 3, 2017 was primarily due to the fiscal 2017 Special Dividend and increased net borrowings on the asset-backed line of credit for working capital needs.

Transfers and Servicing of Financial Assets - Customer Accounts Receivable

Information regarding Transfers and Servicing of Financial Assets - Customer Accounts Receivable is included in Management's Commentary on Financial Condition and Results of Operations - "Liquidity and Capital Resources" of our Annual Report. During the 39-weeks ended November 2, 2018, there were no material changes to this previously disclosed information outside of the ordinary course of business.

Debt and Financing Arrangements

Information regarding Debt and Financing Arrangements is included in Management's Commentary on Financial Condition and Results of Operations - "Liquidity and Capital Resources" of our Annual Report. During the 39-weeks ended November 2, 2018, there were no material changes to this previously disclosed information outside of the ordinary course of business.

Contractual Obligations and Commitments

A summary of future Contractual Obligations and Commitments is included in Management's Commentary on Financial Condition and Results of Operations - "Liquidity and Capital Resources" of our Annual Report. During the 39-weeks ended November 2, 2018, there were no material changes to this previously disclosed information outside of the ordinary course of business.

Off Balance Sheet Arrangements

We do not have any guarantee contracts, contingent interest in assets transferred, or variable interest entities that qualify as off-balance sheet arrangements.

BLUESTEM GROUP INC.
Condensed Consolidated Balance Sheets
(in thousands, except share data)
(Unaudited)

	November 2, 2018	February 2, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 120,727	\$ 123,398
Restricted cash	14,579	15,759
Customer accounts receivable, net of allowance of \$5,537 and \$8,233	5,776	9,008
Merchandise inventories	255,085	194,693
Promotional material inventories	22,562	34,660
Other current assets	38,326	28,399
Total current assets	457,055	405,917
Property and equipment, net	93,983	106,246
Intangibles, net	151,926	163,377
Goodwill	36,717	36,717
Other assets	6,707	11,222
Total Assets	\$ 746,388	\$ 723,479
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 205,123	\$ 160,300
Accrued costs and other liabilities	79,499	67,754
Short-term debt	82,022	26,434
Total current liabilities	366,644	254,488
Long-term debt	401,805	420,297
Deferred income taxes	2,541	4,245
Other long-term liabilities	29,215	39,349
Total liabilities	800,205	718,379
Stockholders' equity:		
Series A participating convertible preferred stock, \$0.01 par value, \$5,000 stated value; shares authorized — 10,000,000 at November 2, 2018 and February 2, 2018; shares issued and outstanding — 1,000 at November 2, 2018 and February 2, 2018	5,000	5,000
Common stock, \$0.01 par value, shares authorized - 350,000,000 at November 2, 2018 and February 2, 2018; shares issued - 134,037,321 at November 2, 2018 and 133,208,110 at February 2, 2018; shares outstanding - 134,015,902 at November 2, 2018 and 133,186,691 at February 2, 2018	1,340	1,332
Treasury stock, at cost, 21,419 shares at November 2, 2018 and February 2, 2018	(131)	(131)
Additional paid-in capital	296,852	293,892
Accumulated deficit	(359,151)	(297,324)
Accumulated other comprehensive income, net of tax	2,273	2,331
Total stockholders' equity	(53,817)	5,100
Total Liabilities and Stockholders' Equity	\$ 746,388	\$ 723,479

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements

BLUESTEM GROUP INC.
Condensed Consolidated Statements of Comprehensive Loss
(in thousands, except shares and per share amounts)
(Unaudited)

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Net sales and revenue				
Net sales	\$ 407,777	\$ 399,798	\$ 1,211,036	\$ 1,266,314
Commercial real estate revenue, net	514	1,115	1,268	2,522
Total net sales and revenue	408,291	400,913	1,212,304	1,268,836
Costs and expenses				
Cost of goods sold	216,273	208,663	631,499	661,190
Sales and marketing expenses	110,591	107,192	335,843	343,636
Net credit expense	26,674	30,398	80,833	89,821
General and administrative expenses	48,847	46,274	144,034	168,119
Amortization and depreciation not included in cost of goods sold	11,961	13,471	36,308	42,797
Loss on impairment	—	—	—	230
Total costs and expenses	414,346	405,998	1,228,517	1,305,793
Operating loss	(6,055)	(5,085)	(16,213)	(36,957)
Interest expense, net	12,738	12,785	37,853	38,401
Loss before income taxes	(18,793)	(17,870)	(54,066)	(75,358)
Income tax benefit	(4,807)	(1,390)	(6,080)	(1,514)
Net loss	\$ (13,986)	\$ (16,480)	\$ (47,986)	\$ (73,844)
Other comprehensive loss				
Unrealized (loss) gain on interest rate swaps, net of tax	(206)	917	(58)	124
Comprehensive loss	\$ (14,192)	\$ (15,563)	\$ (48,044)	\$ (73,720)
Loss per share - common stockholders				
Basic and diluted loss per share	\$ (0.11)	\$ (0.12)	\$ (0.36)	\$ (0.56)
Basic and diluted weighted average shares outstanding	133,186,691	132,326,876	132,758,358	132,181,045

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements

BLUESTEM GROUP INC.
Condensed Consolidated Statements of Changes in Stockholders' Equity
(in thousands, except number of shares)
(Unaudited)

	Series A Convertible Preferred Stock		Common Stock		Treasury Stock		Additional Paid-In Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Shares	Amount				
BALANCE - February 3, 2017	1,000	\$ 5,000	132,326,876	\$ 1,323	21,419	\$ (131)	\$ 289,789	\$ (82,867)	\$ 621	\$ 213,735
Net loss	—	—	—	—	—	—	—	(214,310)	—	(214,310)
Total other comprehensive income, net of tax	—	—	—	—	—	—	—	—	1,710	1,710
Stock-based compensation	—	—	—	—	—	—	4,103	—	—	4,103
Reversal of accumulated stock-based compensation forfeitures	—	—	—	—	—	—	—	(147)	—	(147)
Issuance of restricted common stock, net of cancellations	—	—	859,815	9	—	—	—	—	—	9
BALANCE - February 2, 2018	1,000	\$ 5,000	133,186,691	\$ 1,332	21,419	\$ (131)	\$ 293,892	\$ (297,324)	\$ 2,331	\$ 5,100
Balance - February 2, 2018 as previously reported	1,000	5,000	133,186,691	1,332	21,419	(131)	293,892	(297,324)	2,331	5,100
Impact of change in accounting principle*	—	—	—	—	—	—	—	(13,841)	—	(13,841)
Adjusted balance - February 3, 2018	1,000	5,000	133,186,691	1,332	21,419	(131)	293,892	(311,165)	2,331	(8,741)
Net loss	—	—	—	—	—	—	—	(47,986)	—	(47,986)
Total other comprehensive loss, net of tax	—	—	—	—	—	—	—	—	(58)	(58)
Restricted stock award vesting	—	—	—	—	—	—	860	—	—	860
Stock-based compensation	—	—	—	—	—	—	2,100	—	—	2,100
Issuance of restricted common stock, net of cancellations	—	—	829,211	8	—	—	—	—	—	8
BALANCE - November 2, 2018	1,000	\$ 5,000	134,015,902	\$ 1,340	21,419	\$ (131)	\$ 296,852	\$ (359,151)	\$ 2,273	\$ (53,817)

* See Note 3-Significant Accounting Policies and Recently Issued Accounting Standards

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements

BLUESTEM GROUP INC.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(Unaudited)

	39-Weeks Ended	
	November 2, 2018	November 3, 2017
Operating Activities		
Net loss	\$ (47,986)	\$ (73,844)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Amortization and depreciation expense	39,664	46,485
Loss on impairment	—	230
Provision for doubtful accounts	61,362	61,420
Provision for deferred income taxes	(1,718)	794
Gain on servicing right	(4,337)	(968)
Net losses (gains) on loans held-for-sale, investment securities and other	287	(1,614)
Stock-based compensation expense	2,466	3,164
Other, net	3,534	1,738
Net change in assets and liabilities:		
Customer account receivables	(3,562)	26,505
Merchandise inventories	(60,392)	(4,886)
Promotional material inventories	(1,744)	(14,304)
Other assets	(8,586)	7,742
Accounts payable and other liabilities	51,851	(233)
Net cash provided by operating activities	30,839	52,229
Investing Activities		
Purchases of customer accounts receivable	(664,414)	(652,326)
Proceeds from sale of customer accounts receivable	609,846	600,826
Net purchases of property and equipment	(16,430)	(14,604)
Distributions from equity investments	2,966	8,215
Other	—	(13)
Net cash used in investing activities	(68,032)	(57,902)
Financing Activities		
Borrowings of debt	1,802	—
Repayments of debt	(23,402)	(21,601)
Borrowings on asset-backed line of credit	283,069	339,603
Repayments on asset-backed line of credit	(228,017)	(314,694)
Payment of dividends	—	(80,201)
Net cash provided by (used in) financing activities	33,452	(76,893)
Effect of Foreign Exchange Rates on Cash	(110)	59
Net Decrease in Cash, Cash Equivalents and Restricted Cash	(3,851)	(82,507)
Cash, Cash Equivalents and Restricted Cash, Beginning of Period	139,157	228,739
Cash, Cash Equivalents and Restricted Cash, End of Period	\$ 135,306	\$ 146,232
Supplemental Disclosures of Cash Flow Information:		
Interest paid	\$ 33,680	\$ 31,310
Income taxes (refunded) paid	\$ (828)	\$ 495

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Organization and Operations

As used in this report:

- “BGI” or “the Company” refers to Bluestem Group Inc. with its consolidated subsidiaries
- “BGI Holding Company” refers to the Bluestem Group Inc. legal entity, excluding its subsidiaries
- “Bluestem” refers to Bluestem Brands, Inc., an indirect subsidiary of BGI which consists of Northstar Portfolio, Orchard Portfolio and PayCheck Direct (which was exited in the first quarter of fiscal 2017)
- “Northstar Portfolio” or “Northstar” refers to the consolidated Fingerhut and Gettington retail brands
- “Orchard Portfolio” or “Orchard” refers to the consolidated Appleseed’s, Bedford Fair, Blair, Draper’s & Damon’s (retail stores were exited during the first quarter of fiscal 2017), Gold Violin, Haband, LinenSource (which was exited in the second quarter of fiscal 2017), Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop, and WinterSilks retail brands
- “Capmark Portfolio” or “Capmark” refers to the commercial real estate finance operations of BGI

Bluestem Group Inc., a holding company headquartered in Eden Prairie, MN, operates multiple direct to consumer retail brands through its subsidiary Bluestem. The Northstar Portfolio includes Fingerhut and Gettington, both of which are national multi-channel retail brands offering a broad selection of name brand and private label merchandise serving low- to middle-income consumers by offering multiple payment plans through revolving credit lines or installment loans offered by WebBank as the originating bank as described more fully below. The Orchard Portfolio consists of multi-channel brands including Appleseed’s, Bedford Fair, Blair, Draper’s & Damon’s, Gold Violin, Haband, Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop and WinterSilks. These brands offer apparel, accessories, and home products for the boomer and senior demographic, generally considered age 50 and over, and provide customers with the ability to obtain credit through a third-party private label credit card.

By combining proprietary marketing and credit decision-making technologies, Bluestem is able to tailor merchandise and credit offers to prospective as well as existing customers. Bluestem views merchandising, marketing and credit management within its Northstar Portfolio business model as strategically indivisible. Credit is offered to Northstar Portfolio customers to reasonably assist them in making merchandise purchases while enhancing customer loyalty and driving repeat orders. Bluestem offers a large selection of name-brand, private label, and non-branded merchandise through internet websites and catalogs to customers in the United States of America. Merchandise is continuously tailored across three key product categories:

- **Home** - including housewares, bed and bath, lawn and garden, home furnishings and hardware
- **Entertainment** - including electronics, video games, toys and sporting goods
- **Fashion** - including apparel, footwear, cosmetics, fragrances and jewelry

Bluestem is a party to a series of transactions with WebBank and Santander Consumer USA Inc. (“SCUSA”) related to revolving Northstar Portfolio customer accounts receivables executed under a set of operating agreements referred to collectively as the “A/R Program Agreements” and the arrangement is referred to as the “Program.” Except as described in Note 5, *Serviced Credit Portfolio*, of the Notes to Condensed Consolidated Financial Statements, Bluestem sells all new receivables originated under revolving credit accounts to SCUSA on the same day those receivables are purchased by Bluestem from WebBank. Bluestem services the credit accounts and related receivables as WebBank’s and/or SCUSA’s agent. In consideration of Bluestem’s servicing of the portfolio owned by SCUSA, SCUSA pays a servicing fee to and shares a portion of the risk adjusted margin (“RAM”) of the portfolio with Bluestem. See Note 5, *Serviced Credit Portfolio*, of the Notes to Condensed Consolidated Financial Statements for more information. Under the Program, if the forecasted RAM as a percentage of average program receivables is less than 5% for the full fiscal year, Bluestem shall implement a merchant discount on all standard receivables to be purchased by SCUSA for the remainder of the fiscal year.

2. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim reporting. Accordingly, these financial statements do not include all of the information and footnote disclosures required for annual financial reporting. These interim financial statements should be read in conjunction with the financial statements and notes thereto included in the Company’s report as of and for the years ended February 2, 2018 and February 3, 2017 (“Annual Report”), available at www.bluestem.com. The Company’s results for any interim period are not necessarily indicative of results for a full year or any other interim period.

The preparation of the condensed consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported amounts and disclosures of revenues and expenses. Significant estimates made by management include revenue recognition, fiscal year RAM which determines the merchant discount on receivables sold to SCUSA, the allowance for doubtful accounts, reserves for excess and obsolete merchandise inventories, allowances for merchandise returns and customer allowances, income taxes, valuation of stock-based awards, valuation of servicing liability, valuation of goodwill and intangible assets and estimates of the useful

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

lives of long-lived assets. Management bases its estimates on historical corporate and industry experience and various other assumptions it believes are appropriate under the circumstances, including market-based inputs when available. Future changes in credit and market trends and conditions may occur, which could cause actual results to differ materially from the estimates used in preparing the accompanying condensed consolidated financial statements. Certain of the Company's critical accounting estimates require higher degrees of judgment and are more complex than others in their application. For all of these estimates, future events rarely develop exactly as forecasted and, therefore, routinely require adjustment.

The accompanying unaudited condensed consolidated financial statements include financial information for the Company and its consolidated subsidiaries, including wholly-owned and majority owned subsidiaries in which the Company has a controlling financial interest. Intercompany accounts and transactions have been eliminated in consolidation.

In the opinion of management, the condensed consolidated financial statements include all adjustments, consisting of normal recurring accruals, necessary to present fairly the financial position of the Company as of November 2, 2018 and the results of its operations and cash flows for the interim periods presented.

Fiscal Year

Bluestem operates on a fiscal calendar widely used within the retail industry that results in fiscal years consisting of a 52- or 53-week period ending on the Friday closest to January 31 of the following year. In these unaudited condensed consolidated financial statements, including the notes thereto, financial results are for the 13- and 39-weeks ended November 2, 2018 ("fiscal 2018") and November 3, 2017 ("fiscal 2017").

3. Significant Accounting Policies and Recently Issued Accounting Standards

Change in Accounting Policies

The Company's significant accounting policies are described in the notes to the Company's consolidated financial statements included in the 2017 Annual Report. The Company adopted Accounting Standards Update 2014-09 "Revenue from Contracts with Customers" ("Topic 606") with a date of the initial application of February 3, 2018. As a result, the Company has changed its accounting policy for revenue recognition as detailed below. Topic 606 was adopted retrospectively to all uncompleted contracts by recognizing the cumulative effect of initially applying the new guidance as an adjustment to the opening balance of equity at February 3, 2018. Except for the changes below, the Company has consistently applied the accounting policies to all periods presented in these condensed consolidated financial statements.

Revenue Recognition

The Company generates its revenue from the following principal activities, separated by reportable segments:

Northstar Portfolio

The Northstar Portfolio consists of national multi-channel retailers serving low- to middle-income consumers by offering products with customized payment plans through revolving credit lines or installment loans. The contract duration is short term, executed with a purchase order and completed upon delivery of the product, generally within seven to ten days. Contract terms require payment to be made upon receipt of product. Revolving credit is extended directly to Northstar Portfolio customers by WebBank and the customers' accounts receivable are subsequently purchased by SCUSA. Fingerhut customers who are unable to qualify for revolving credit may purchase merchandise with a down payment and installment payment terms of one year or less under its Fresh Start program.

Orchard Portfolio

The Orchard Portfolio consists of national multi-channel retailers offering apparel, accessories, and home products for women and men principally in the boomer and senior demographic, generally considered age 50 and older. Orchard Portfolio offers its product assortments through online and direct mail catalogs. The contract duration is short term, executed with a purchase order and completed upon delivery of the product, generally within seven to ten days. Contract terms require payment to be made upon receipt of product. A third-party bank provides Orchard Portfolio customers the ability to obtain credit through a private label credit card. Orchard does not directly extend any financing terms to its customers.

Under Topic 606, revenue from customers is recognized when the Company's performance obligations under sales contracts are satisfied by transferring control of goods to a customer. Revenue is measured based on consideration specified in contracts with customers, net of discounts, and excludes amounts collected on behalf of third parties. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. When a sales order includes multiple performance obligations, the consideration is allocated between the performance obligations in proportion to their estimated standalone selling prices.

Net sales consist of merchandise sales, shipping and handling revenue, shipping returns fee income and commissions earned from third parties that market their products to the Company's customers. Merchandise sales and shipping and handling revenue are recognized when the customer takes physical possession of the goods upon delivery. Due to the high volume of shipments, the time of delivery to the customer is estimated based on shipping dates, warehouse locations, delivery destinations and historical delivery experience. Payments received in advance of the receipt of merchandise by customers are recorded as deferred revenue. The Company estimates merchandise returns using an expected value method based on historical returns patterns, which are recorded as a reduction of Net sales. Taxes collected from customers and remitted to governmental authorities are excluded from revenue on the net basis of accounting.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Management has evaluated the criteria outlined in ASC 606-10-55, *Principal versus Agent Considerations*, and determined that the Company is the principal in substantially all of its transactions including drop shipments, and the related revenue is recorded on a gross basis.

The Company receives payment for nearly all of its sales at the time of shipment or within a few days of delivery via third-party debit and credit card processors or the revolving customer credit arrangement with WebBank and SCUSA. The Company also offers certain customers the ability to purchase merchandise with a down payment and installment payment terms of one year or less under its Fresh Start program. Under this program, customers are charged interest during the installment payment term at a market rate for customers of similar credit standing.

The Company adopted Topic 606 on a modified retrospective basis in the first quarter of fiscal 2018, which resulted in the following effects on the condensed consolidated financial statements for the 13- and 39-weeks ended November 2, 2018:

- A decrease to opening retained earnings as of February 3, 2018 of approximately \$13.8 million, net of tax, was recorded for the cumulative effect adjustment of adopting Topic 606. The adjustment related to the acceleration in the timing of recognition of direct mail catalog advertising costs, which prior to adoption were capitalized and amortized over their expected period of future benefit and are now expensed on the estimated date of first delivery to recipients.
- Approximately \$4.1 million of estimated value of future product returns was reclassified from Accrued costs and other liabilities to Other current assets.
- No impact to net cash provided by (or used in) operating, financing, or investing activities reported in the Company's Condensed Consolidated Statement of Cash Flows
- Prior period balances were not retrospectively adjusted as a result of adopting Topic 606. Excluding the accounting for direct mail catalog advertising costs, revenue and expense recognition patterns are consistent with prior revenue and expense recognition policies.
- As a result of adopting Topic 606, direct mail catalog advertising expense was higher in the fiscal first and third quarters and lower in the fiscal second quarter compared to how it would have been reported under the old accounting standards. It is anticipated that direct mail catalog advertising expense will be lower in the fiscal fourth quarter compared to the reporting under the old accounting standards, with no material impact on an annual basis.

The following tables summarize the impact of adopting Topic 606 on the Company's Condensed Consolidated Balance Sheet as of November 2, 2018 and the Company's Condensed Consolidated Statement of Comprehensive Income for the 13- and 39-weeks ended November 2, 2018 (in thousands):

	As of November 2, 2018		
	As Reported	Topic 606 Adjustment	Balances Without Adoption of Topic 606
ASSETS			
Promotional material inventories	\$ 22,562	\$ 23,090	\$ 45,652
Other current assets	38,326	(4,117)	34,209
Total current assets	457,055	18,973	476,028
Total assets	\$ 746,388	\$ 18,973	\$ 765,361
LIABILITIES AND STOCKHOLDERS' EQUITY			
Accrued costs and other liabilities	\$ 79,499	\$ (4,117)	\$ 75,382
Total current liabilities	366,644	(4,117)	362,527
Total liabilities	800,205	(4,117)	796,088
Accumulated deficit	(359,151)	23,090	(336,061)
Total stockholders' equity	(53,817)	23,090	(30,727)
Total liabilities and stockholders' equity	\$ 746,388	\$ 18,973	\$ 765,361

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

13-Weeks Ended November 2, 2018

	As Reported	Topic 606 Adjustment	Balances Without Adoption of Topic 606
Sales and marketing expense	\$ 110,591	\$ (6,808)	\$ 103,783
Total costs and expenses	414,346	(6,808)	407,538
Operating loss	(6,055)	6,808	753
Loss before income taxes	(18,793)	6,808	(11,985)
Operating loss	\$ (13,986)	\$ 6,808	\$ (7,178)

39-Weeks Ended November 2, 2018

	As Reported	Topic 606 Adjustment	Balances Without Adoption of Topic 606
Sales and marketing expense	\$ 335,843	\$ (9,249)	\$ 326,594
Total costs and expenses	1,228,517	(9,249)	1,219,268
Operating loss	(16,213)	9,249	(6,964)
Loss before income taxes	(54,066)	9,249	(44,817)
Operating loss	\$ (47,986)	\$ 9,249	\$ (38,737)

Revenue is disaggregated by customer type and merchandise category - see Note 16, *Segment Information*, of the Notes to Condensed Consolidated Financial Statements for more information. Revenue is not disaggregated by the timing of revenue recognition as all revenue is recognized at a point in time, i.e., on estimated date of delivery to the customer. The disaggregation of revenue is consistent with the manner in which management internally disaggregates financial information for the purpose of decision making.

Because all of the Company's revenue is recognized at a point in time, no material contract assets are created. Contract liabilities relate to consideration received in advance of receipt of merchandise by customers, primarily due to the time lag between shipment and delivery of goods sold, refunds due to customers and unredeemed gift certificates. These contract liabilities are recorded as Accrued costs and other liabilities on the Company's Condensed Consolidated Balance Sheet. Significant changes in contract liabilities during the period, which are the result of seasonally low sales during the final days of the fiscal year 2017, are as follows (in thousands):

	Contract Liabilities
Balance, February 2, 2018	\$ 32,287
Reclassification of beginning deferred revenue to revenue, as a result of performance obligations satisfied	(17,413)
Gift certificate redemptions and breakage	(2,898)
Provisions for refunds, net of refunds paid	1,046
Cash received in advance and not recognized as revenue	29,635
Balance, November 2, 2018	<u>\$ 42,657</u>

The Company applies the practical expedient of ASC 606-10-50-14 and does not disclose information about remaining performance obligations that have original expected durations of one year or less. This practical expedient is being applied to prepaid unshipped merchandise sales orders and shipped orders in transit to customers at that time.

Commercial real estate revenue, net includes net interest income and other non-interest income related to the Company's real estate business. Net interest income represents the difference between the amount of interest that the Company earns on its commercial real estate interest-earning assets, primarily loans held-for-sale, and the amount of interest that the Company pays on its commercial real estate interest-bearing liabilities. Other non-interest income primarily includes net realized and unrealized gains and losses on loans held-for-sale and equity investments.

Other Recently Adopted Accounting Standards

In January 2016, the Financial Accounting Standards Board ("FASB") issued *Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* ("ASU 2016-01"), which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The Company adopted this standard in the first quarter of fiscal 2018. The adoption of ASU 2016-01 did not have a significant impact on the Company's results of operations or financial position, and a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption was not required.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

In August 2016, the FASB issued *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* ("ASU 2016-15"), which relates to the classification of certain cash receipts and cash payments on the statement of cash flows. The Company adopted this standard in the first quarter of fiscal 2018 applying a retrospective transition method to each period presented. The adoption of ASU 2016-15 did not have a significant impact on the Company's results of operations or financial position.

In October 2016, the FASB issued *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory* ("ASU 2016-16"), which requires recognition of the income tax consequences of intra-entity transfers of assets (other than inventory) at the transaction date. The Company adopted this standard in the first quarter of fiscal 2018 using modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The adoption of ASU 2016-16 did not have a significant impact on the Company's results of operations or financial position.

In November 2016, the FASB issued *Statement of Cash Flows (Topic 230): Restricted Cash* ("ASU 2016-18"), which requires that the statement of cash flows explain the change during the period in total cash, cash equivalents, and amounts generally described as restricted cash. The Company adopted this standard in the first quarter of fiscal 2018 applying a retrospective transition method to each period presented. The adoption of ASU 2016-18 resulted in a reclassification of changes in restricted cash from cash flow from investing activities to the opening and closing balances of Cash, cash equivalents and restricted cash. The adoption had no impact on the Company's results of operations or financial position.

In May 2017, the FASB issued *Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting* ("ASU 2017-09"), which provides guidance about which changes to the terms and conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The Company adopted this standard in the first quarter of fiscal 2018 and it is being applied prospectively to awards modified on or after the adoption date. The adoption of ASU 2016-18 had no impact on the Company's results of operations or financial position.

Accounting Standards Issued But Not Yet Adopted

In February 2016, the FASB issued *Leases (Topic 842)* ("ASU 2016-02") and in August, 2018 issued *Leases (Topic 842): Targeted Improvements* ("ASU 2018-11") which, for operating leases, requires a lessee to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, on its balance sheet. The standard also requires a lessee to recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term, on a generally straight-line basis. ASU 2016-02 and ASU 2018-11 are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. Management anticipates ASU 2016-02 and ASU 2018-11 will impact the Company's balance sheet but does not believe the ASUs will have a significant impact on the reported results of operations or financial position.

In June 2016, the FASB issued *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13") which amends the impairment model to utilize an expected loss methodology in place of the currently used incurred loss methodology, resulting in the more timely recognition of losses. The new standard applies to financial assets measured at amortized cost basis, including receivables that result from revenue transactions and held-to-maturity debt securities. ASU 2016-13 is effective for interim and annual periods beginning on or after December 15, 2020. Earlier application is permitted for interim and annual periods beginning on or after December 15, 2018. Management does not anticipate that ASU 2016-13 will have a significant impact on the reported results of operations or financial position.

In August 2017, the FASB issued *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* ("ASU 2017-12") which provide for better alignment of an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. ASU 2017-12 is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early application is permitted in any interim period after issuance of the update. Management does not anticipate that ASU 2016-12 will have a significant impact on the reported results of operations or financial position.

In August 2018, the FASB issued *Fair Value Measurement (Topic 820)—Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement* ("ASU 2018-13"), which modify the disclosure requirements on fair value measurements in Topic 820, Fair Value Measurement, primarily by eliminating certain required disclosures. ASU 2018-13 is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early application is permitted. Management does not anticipate that ASU 2018-13 will have a significant impact on the reported results of operations or financial position.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

4. Net Loss Per Share

The table below demonstrates how the Company computed basic and diluted net loss per share (in thousands, except per share amounts):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Net loss	\$ (13,986)	\$ (16,480)	\$ (47,986)	\$ (73,844)
Net loss per share, basic and diluted	\$ (0.11)	\$ (0.12)	\$ (0.36)	\$ (0.56)
Weighted average shares outstanding, basic and diluted	133,187	132,327	132,758	132,181

The following potentially dilutive securities outstanding have been excluded from the computations of diluted earnings per share because such securities have an antidilutive impact (weighted average shares, in thousands):

	39-Weeks Ended	
	November 2, 2018	November 3, 2017
Options ⁽¹⁾	2,421	6,341
Restricted Stock Units ⁽¹⁾	1,150	—
Warrants	9,139	9,139
Preferred Stock	1,341	1,341
Restricted Stock	590	860
Total	14,641	17,681

⁽¹⁾ 9,801 outstanding options were exchanged for 4,721 restricted stock units on July 17, 2018. See Note 14, *Stock-Based Compensation*.

5. Serviced Credit Portfolio

The Company is a party to a series of transactions with WebBank and SCUSA related to revolving Northstar Portfolio customer accounts receivable executed under a set of operating agreements referred to collectively as the "A/R Program Agreements" and the arrangement is referred to as the "Program." Under the Program, the Company markets revolving credit accounts and installment credit accounts to qualifying customers identified by the Company. WebBank extends credit directly to Northstar Portfolio customers. The credit accounts may only be used to purchase goods and services from Northstar Portfolio and certain third parties that market their goods and services to Northstar Portfolio customers. The Company is obligated to purchase and assume ownership of the receivables after a contractual holding period by WebBank of three business days. The purchase price of the receivables from WebBank is at par value and the Company pays applicable interchange fees, origination fees and other product fees along with applicable customer finance charges earned by WebBank during the contractual hold period. SCUSA is obligated to reimburse Bluestem for origination and other product fees.

Except as described below, Bluestem is obligated to sell substantially all new receivables originated under revolving credit accounts to SCUSA on the same day those receivables are purchased by Bluestem from WebBank. All receivables originated in revolving credit accounts are referred to as "Standard Receivables." SCUSA bears risk of loss due to uncollectibility of the Standard Receivables purchased from Bluestem. All receivables generated in accounts other than revolving credit accounts, including Fingerhut FreshStart credit accounts, are referred to as "Nonstandard Receivables." Bluestem retains all Nonstandard Receivables purchased from WebBank, and bears the risk of loss due to uncollectibility.

Net Credit Expense

Net credit expense includes credit management costs on all customer accounts receivable whether such receivables are owned by the Company or SCUSA, a provision for doubtful accounts and finance charge and fee income on Company-owned accounts receivable, a provision for doubtful accounts needed to reduce the value of accounts receivable purchased from WebBank to the discounted value sold to SCUSA (see below for more information on the required merchant discount on receivables sold to SCUSA), servicing fee income, portfolio profit sharing from SCUSA owned accounts receivable and loss on servicing right. An allowance for doubtful accounts is maintained at a level intended to absorb probable losses on Nonstandard Receivables as of the balance sheet date. SCUSA bears risk of loss due to uncollectibility of the Standard Receivables it owns.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Net credit expense is summarized below (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Provision for doubtful accounts:				
Loss on sale of customer accounts receivable	\$ 17,477	\$ 20,950	\$ 54,865	\$ 52,145
Company-owned customer accounts receivable	2,414	1,839	6,497	9,275
Total provision for doubtful accounts	19,891	22,789	61,362	61,420
Credit management costs	15,220	16,151	46,286	51,721
Finance charge and fee income, net	(683)	(361)	(2,149)	(1,763)
Servicing fee income	(6,607)	(6,623)	(20,329)	(20,589)
Gain on servicing right	(1,147)	(1,558)	(4,337)	(968)
Net credit expense	\$ 26,674	\$ 30,398	\$ 80,833	\$ 89,821

The Company is responsible for servicing all accounts (“Serviced Credit Portfolio”) whether the related receivables are owned by the Company or SCUSA. Credit management costs, related to both the Company-owned and SCUSA-owned customer accounts receivable, include statement and payment processing, collections, origination fees paid to WebBank, new account application and credit bureau processing costs, as well as direct customer service costs. The Company receives a fee for servicing the SCUSA owned portfolio of Standard Receivables and shares a portion of the profits from those receivables, as defined in the A/R Program Agreements.

Northstar Serviced Credit Portfolio

Fingerhut customers may be offered one of two credit products, Fingerhut revolving credit or Fingerhut FreshStart installment credit. Fingerhut revolving credit is typically accepted on customary revolving credit terms. The Fingerhut FreshStart installment credit product is offered to customers who do not qualify for a revolving credit account. Gettington revolving credit is accepted on customary revolving credit terms.

Northstar Serviced Credit Portfolio metrics as of the end of the periods are as follows (in thousands, except for average balances outstanding):

November 2, 2018	Revolving ⁽¹⁾	FreshStart ⁽²⁾
Balance active accounts	1,749	108
Average balance outstanding	\$ 756	\$ 99
Customer accounts receivable ⁽³⁾	\$ 1,321,081	\$ 10,731
Balances 30+ days delinquent ⁽⁴⁾	\$ 255,519	\$ 3,285
Balances 30+ days delinquent as a percentage of total customer accounts receivable ⁽⁵⁾	19.3%	30.6%
February 2, 2018	Revolving ⁽¹⁾	FreshStart ⁽²⁾
Balance active accounts	1,792	128
Average balance outstanding	\$ 833	\$ 110
Customer accounts receivable ⁽³⁾	\$ 1,492,172	\$ 14,073
Balances 30+ days delinquent ⁽⁴⁾	\$ 243,467	\$ 3,318
Balances 30+ days delinquent as a percentage of total customer accounts receivable ⁽⁵⁾	16.3%	23.6%

⁽¹⁾ Revolving serviced portfolio includes Northstar Portfolio revolving credit accounts.

⁽²⁾ FreshStart serviced portfolio represents Fingerhut's installment credit accounts.

⁽³⁾ Customer accounts receivable balances as of the customers' statement cycle dates prior to or on fiscal period end.

⁽⁴⁾ Delinquent balances as of the customers' statement cycle dates prior to or on fiscal period end.

⁽⁵⁾ Delinquent balances as of the customers' statement cycle dates prior to or on fiscal period end as a percentage of total customer accounts receivable as of the customers' statement cycle dates prior to or on fiscal period end.

Company-owned Customer Accounts Receivable

Company-owned customer accounts receivable primarily consist of FreshStart installment accounts receivable and PayCheck Direct installment accounts receivable. FreshStart and PayCheck Direct installment accounts receivable are not sold to SCUSA. Finance charge and fee income is recognized on FreshStart accounts receivable according to the contractual provisions of the credit account agreements.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Company-owned customer accounts receivable are as follows (in thousands):

	November 2, 2018	February 2, 2018
FreshStart installment accounts receivable	\$ 11,034	\$ 13,950
PayCheck Direct installment accounts receivable	53	2,884
Other	226	407
Customer accounts receivable - gross	11,313	17,241
Less: allowance for doubtful accounts	(5,537)	(8,233)
Customer accounts receivable - net	<u>\$ 5,776</u>	<u>\$ 9,008</u>

The Company maintains an allowance for doubtful accounts at a level intended to absorb estimated probable losses inherent in Company-owned customer accounts receivable, including accrued finance charges and fees as of the balance sheet date. Upon charge-off, any unpaid principal is applied to the allowance for doubtful accounts and any accrued but unpaid finance charges and fees are netted against finance charge and fee income with an offsetting equivalent reversal of the allowance for doubtful accounts through the provision for doubtful accounts.

The number of days Company-owned customer accounts are past due and their related accounts receivable balances are as follows (in thousands):

	November 2, 2018
Current	\$ 5,903
Days past due:	
1 - 29	2,013
30 - 59	1,233
60 - 89	1,116
90 - 119	1,030
120 - 149	8
150 - 179	9
180+	1
Customer accounts receivable	<u>\$ 11,313</u>

Changes in the allowance for doubtful accounts for the 39-weeks ended November 2, 2018 were as follows (in thousands):

	November 2, 2018
Balance as of February 2, 2018	\$ 8,233
Provision for doubtful accounts ⁽¹⁾	61,362
Principal charge-offs ⁽¹⁾	(64,543)
Recoveries	485
Balance as of November 2, 2018	<u>\$ 5,537</u>

⁽¹⁾ Includes \$54.9 million charge for accounts receivable sold to SCUSA below par (merchant discount).

SCUSA-owned Customer Accounts Receivable

Standard Receivable details are as follows (in thousands except for average merchant discount):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Standard Receivables originated	\$ 241,603	\$ 220,370	\$ 668,673	\$ 654,487
Charge to the provision for doubtful accounts and principal charge-off for the sale below par related to Standard Receivables	17,477	20,950	54,865	52,145
Average merchant discount	7.23%	9.51%	8.21%	7.97%

In consideration of the Company's servicing of the Standard Receivables portfolio owned by SCUSA, SCUSA pays a servicing fee to and shares a portion of the profits of the SCUSA portfolio with the Company. The portfolio profits are based on finance charges, fees and other revenues, less charge-offs of uncollectable receivables, net of recoveries, servicing fees, an agreed upon cost of funds and in certain circumstances a merchant fee.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

A servicing rights liability is recorded when compensation received from SCUSA for services provided are not adequate compared to similar servicing provided in the open market. Servicing rights liabilities are carried at fair value in Other long-term liabilities on the Condensed Consolidated Balance Sheets. The fair value of servicing right was determined using an assumed discount rate of 13% and customer accounts receivable attrition rate of approximately 84% within twelve months. Any servicing asset or liability is initially recognized at fair value. Changes in the balances of servicing liabilities are subsequently measured using the fair value measurement method, and the resulting gains or losses are recorded as part of Net credit expense on the Condensed Consolidated Statements of Comprehensive Loss. See Note 13, *Fair Value of Assets and Liabilities* of the Notes to Condensed Consolidated Financial Statements for more information.

Changes in the fair value of the servicing rights liability for the 39-weeks ended November 2, 2018 were as follows (in thousands):

	Servicing Rights Liability
Fair value as of February 2, 2018	\$ 25,988
Credit origination and fee additions	16,759
Payments and charge-off subtractions	(19,642)
Change in fair value due to updated assumptions	(1,454)
Fair value as of November 2, 2018	<u>\$ 21,651</u>

6. Intangible Assets and Goodwill

Intangibles, net consist of tradenames and customer relationships. The changes in the carrying amount of tradenames were as follows (in thousands):

	Intangible Asset - Tradenames
Balance as of February 3, 2017	\$ 98,480
Impairments	(26,310)
Balance as of February 2, 2018	\$ 72,170
Impairments	—
Balance as of November 2, 2018	<u>\$ 72,170</u>

The Company's intangible assets with finite lives, net consisted of the following (in thousands):

	November 2, 2018	February 2, 2018
Customer relationships	\$ 155,909	\$ 155,909
Less: Accumulated amortization	(76,153)	(64,702)
Intangible assets with finite lives, net	<u>\$ 79,756</u>	<u>\$ 91,207</u>

Intangible assets amortization expense for the 13-weeks ended November 2, 2018 and November 3, 2017 was \$3.9 million and \$4.3 million, respectively. Intangible assets amortization expense for the 39-weeks ended November 2, 2018 and November 3, 2017 was \$11.5 million and \$12.8 million, respectively. As of November 2, 2018, estimated annual amortization expense for finite lived intangible assets for the next five fiscal years and thereafter is as follows (in thousands):

Fiscal Years	
2018	\$ 5,404
2019	16,346
2020	13,024
2021	7,170
2022	6,483
Thereafter	31,329
Total	<u>\$ 79,756</u>

Goodwill is the amount by which the cost of the acquired net assets in a business combination exceeds the fair value of the identifiable net assets on the date of purchase or valuation, respectively. Goodwill is not amortized, but is assessed periodically for impairment at the reporting unit level at least annually, or more frequently when events and circumstances indicate that goodwill may be impaired.

The overall financial performance for the 39-weeks ended November 2, 2018 of the Orchard Portfolio is below management's expectations. We have experienced a decline in our Orchard customer file due to a decline in rebuy rates and declining new customer

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

acquisition. Management is taking and evaluating actions to improve financial performance by pursuing further enhancements to gross margin, implementing more efficient and profitable marketing strategies and continuing evaluation of under-performing brands. As the financial performance in the third quarter is below management's expectations, we are re-assessing the assumptions in our long term financial plan. This re-assessment has led us to conclude that there is an indicator of possible intangible and long-lived asset impairment relating to the Orchard Portfolio. As of November 2, 2018, the Company has intangible assets relating to the Orchard Portfolio of \$37.1 million in tradenames and \$64.0 million in customer relationships. Due to the significant effort that is required to determine the current fair values of Orchard's intangible and long-lived assets, we are unable to reasonably estimate the amount of impairment, if any, during the third quarter. The Company expects to complete its impairment test in the fourth quarter and the amount of an impairment, if any, that is determined could be material to the Company's consolidated financial statements.

The changes in the carrying amount of goodwill were as follows (in thousands):

	<u>Northstar</u>	<u>Orchard</u>	<u>Total</u>
Balance as of February 3, 2017	\$ 36,717	\$ 165,839	\$ 202,556
Impairments	—	(165,839)	(165,839)
Balance as of February 2, 2018	\$ 36,717	\$ —	\$ 36,717
Impairments	—	—	—
Balance as of November 2, 2018	<u>\$ 36,717</u>	<u>\$ —</u>	<u>\$ 36,717</u>

7. Debt and Other Financing

Debt and other financing are included as Short-term debt and Long-term debt on the Condensed Consolidated Balance Sheets as follows (in thousands):

	<u>November 2, 2018</u>	<u>February 2, 2018</u>
Short-term debt		
Term loan - net of discount and financing fees of \$4,859	\$ 23,942	\$ 23,943
Asset-backed line of credit	55,587	—
Capital lease obligation and other	868	1,513
Other notes payable	1,625	978
Short-term debt	<u>\$ 82,022</u>	<u>\$ 26,434</u>
Long-term debt		
Term loan - net of discount and financing fees of \$4,966 and \$8,610	\$ 401,588	\$ 419,545
Capital lease obligation	—	535
Collateralized borrowings	217	217
Long-term debt	<u>\$ 401,805</u>	<u>\$ 420,297</u>

Term Loan

Bluestem has a Term Loan facility with a syndication of investors, which is secured by a first lien on unencumbered Bluestem property and equipment and a second lien on Bluestem's inventory and customer accounts receivable not otherwise pledged or sold. Total borrowings under the facility upon its July 10, 2015 amendment were \$580 million. The Term Loan matures on November 7, 2020.

Asset-Backed Line of Credit

Bluestem has an asset-backed line of credit, as amended on July 10, 2015, which is secured by a first lien on inventory and non-customer accounts receivables and a second lien on other unencumbered assets of Bluestem. The asset-backed line of credit has a maturity date of July 10, 2020, and a total facility size of \$200 million, subject to borrowing capacity. As further amended on October 5, 2018, during Bluestem's seasonal high period running from October through December each year the borrowing capacity is calculated as the lower of 90% of the liquidation value from the latest inventory appraisal or 70% of eligible inventory, plus between 85% and 90% of other eligible receivables (depending on the type of receivable), in each case less any reserves, plus the lesser of \$20 million or the applicable portion of Bluestem's eligible inventory in transit. During the remainder of the year, the borrowing capacity is calculated as before the amendment, i.e., the restriction on eligible inventory is the lower of 90% of the liquidation value from the latest inventory appraisal or 65% of eligible inventory. Bluestem's asset-backed line of credit is subject to the same minimum net liquidity and total leverage ratio financial covenants as the Term Loan.

As of November 2, 2018, the availability on the asset-backed line of credit was \$83.2 million and outstanding borrowings totaled \$55.6 million. Bluestem had \$14.3 million of outstanding letters of credit as of November 2, 2018. Letters of credit are primarily used to support the Company's customs bonds, insurance requirements and other vendor trade requirements. As of November 2, 2018 and November 3, 2017, Bluestem was in compliance with all provisions of the asset-backed line of credit agreement.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Debt Covenants

Bluestem is subject to certain financial covenants. Failure to comply with these financial covenants is an event of default, subject to certain cure rights which absent a cure, could result in an acceleration of the payment obligations for amounts outstanding under such obligation. As of November 2, 2018, Bluestem was in compliance with all financial covenants.

Bluestem's cash flow is highly dependent on the volume of its sales and the credit performance of the receivables sold to SCUSA. Bluestem reported losses in fiscal 2017 and the 13- and 39-weeks ended November 2, 2018 driven by decreasing net sales and an increasing merchant discount on receivables sold to SCUSA due to challenging and competitive credit and retail environments. As a result, Bluestem has taken and continues to evaluate actions to improve the performance and stability of the business. To date, actions have included a workforce reduction, exiting certain businesses that were neither accretive nor consistent with our strategic goals and eliminating redundant facilities. The Company's performance relative to the financial covenants is expected to be tight for the foreseeable future and there can be no assurance that Bluestem's operating results will improve or that any actions taken will allow Bluestem to remain in compliance with the Lender Requirements or Program Requirements.

8. Restructuring Costs

During the first quarter of fiscal 2017, the Company initiated restructuring actions, which included initiatives intended to improve operating performance and reduce costs. These initiatives included workforce reductions intended to increase organizational effectiveness and provide cost savings that can be reinvested in core business initiatives. Additionally, the Company exited its PayCheck Direct and LinenSource businesses, closed its Draper's & Damon's brand retail store channel, consolidated various Orchard Portfolio office locations, and exited a Northstar third-party distribution center.

The Company has separated its restructuring charges into provision for doubtful accounts, employee costs, facility closure and other costs, and impairment and accelerated depreciation for which total restructuring charges related to these initiatives are estimated to be approximately \$2.0 million, \$5.2 million, \$8.7 million and \$3.5 million, respectively. Provision for doubtful accounts charge is related to the exit of its PayCheck Direct business. Employee costs primarily consist of severance costs. Facility closure and other costs primarily consists of lease termination fees, lease liability and professional fees related to restructuring actions.

There were no restructuring charges recorded during the 13-weeks ended November 2, 2018. The following table presents fiscal period and cumulative restructuring charges by related segment (in thousands):

	39-Weeks Ended November 2, 2018			
	Northstar	Orchard	Corporate and other	Total
Employee costs ⁽¹⁾	\$ 12	\$ 14	\$ —	\$ 26
Facility closure and other costs ⁽¹⁾	22	10	—	32
Total restructuring charges	<u>\$ 34</u>	<u>\$ 24</u>	<u>\$ —</u>	<u>\$ 58</u>
	13-Weeks Ended November 3, 2017			
	Northstar	Orchard	Corporate and other	Total
Provision for doubtful accounts ⁽²⁾	\$ —	\$ —	\$ —	\$ —
Employee costs ⁽¹⁾	—	(118)	45	(73)
Facility closure and other costs ⁽¹⁾	65	(215)	17	(133)
Impairment and accelerated depreciation	—	—	—	—
Total restructuring charges	<u>\$ 65</u>	<u>\$ (333)</u>	<u>\$ 62</u>	<u>\$ (206)</u>
	39-Weeks Ended November 3, 2017			
	Northstar	Orchard	Corporate and other	Total
Provision for doubtful accounts ⁽²⁾	\$ —	\$ —	\$ 2,034	\$ 2,034
Employee costs ⁽¹⁾	481	1,785	2,848	5,114
Facility closure and other costs ⁽¹⁾	680	3,840	4,018	8,538
Impairment and accelerated depreciation	212	2,097	1,171	3,480
Total restructuring charges	<u>\$ 1,373</u>	<u>\$ 7,722</u>	<u>\$ 10,071</u>	<u>\$ 19,166</u>

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Cumulative through November 2, 2018

	Northstar	Orchard	Corporate and other	Total
Provision for doubtful accounts ⁽²⁾	\$ —	\$ —	\$ 2,034	\$ 2,034
Employee costs ⁽¹⁾	493	1,788	2,916	5,197
Facility closure and other costs ⁽¹⁾	879	3,791	4,018	8,688
Impairment and accelerated depreciation	212	2,097	1,171	3,480
Total restructuring charges	<u>\$ 1,584</u>	<u>\$ 7,676</u>	<u>\$ 10,139</u>	<u>\$ 19,399</u>

⁽¹⁾ Restructuring charges related to employee costs and facility closure and other costs are recorded as a component of general and administrative expenses on the Condensed Consolidated Statements of Comprehensive Loss.

⁽²⁾ Restructuring charges related to provision for doubtful accounts are recorded as a component of net credit expense on the Condensed Consolidated Statements of Comprehensive Loss and within the Corporate and other segment.

The following table summarizes the restructuring accrual related to employee and facility closure for the 39-weeks ended November 2, 2018 (in thousands):

	39-Weeks Ended November 2, 2018		
	Employee costs	Facility closure and other costs	Total
Balance as of beginning of period	\$ 153	\$ 715	\$ 868
Restructuring charges	26	32	58
Payments and settlements	(179)	(350)	(529)
Balance as of end of period	<u>\$ —</u>	<u>\$ 397</u>	<u>\$ 397</u>

The restructuring accruals are included in accrued liabilities on the Condensed Consolidated Balance Sheets. Approximately \$62 thousand of the accruals will be paid in fiscal 2018, but due to certain long-term lease agreements the remaining liability payments will be made in fiscal years 2019 through 2021.

9. Other Balance Sheet Data

The following table provides additional information concerning selected balance sheet accounts (in thousands):

	November 2, 2018	February 2, 2018
Other Current Assets		
Prepaid expenses and other	\$ 20,995	\$ 14,918
Other accounts receivables	15,852	10,825
Current income tax receivable	1,479	2,656
Total other current assets	<u>\$ 38,326</u>	<u>\$ 28,399</u>
Other Assets		
Equity investments	\$ 4,416	\$ 7,140
Deferred charges and other	2,291	4,040
Loans held-for-sale	—	42
Total other assets	<u>\$ 6,707</u>	<u>\$ 11,222</u>
Accrued Costs and Other Liabilities		
Accrued liabilities	\$ 33,044	\$ 32,683
Deferred revenue	30,443	20,193
Accrued payroll and benefits	16,012	14,878
Total accrued costs and other liabilities	<u>\$ 79,499</u>	<u>\$ 67,754</u>
Other Long-Term Liabilities		
Servicing liability	\$ 21,651	\$ 25,988
Unrecognized tax benefits	1,315	6,069
Other	6,249	7,292
Total other long-term liabilities	<u>\$ 29,215</u>	<u>\$ 39,349</u>

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the statement of financial position that sum to the total of the same such amounts shown in the statement of cash flows (in thousands):

	<u>November 2, 2018</u>	<u>November 3, 2017</u>
Total Cash, Cash Equivalents and Restricted Cash Shown in the Statement of Cash Flows		
Cash and cash equivalents	\$ 120,727	\$ 119,123
Restricted cash	14,579	27,109
Total cash, cash equivalents and restricted cash shown in the statement of cash flows	<u>\$ 135,306</u>	<u>\$ 146,232</u>

10. Variable Interest Entities

The Company is involved with various entities in the normal course of business that may be deemed to be Variable Interest Entities ("VIEs"). The Company holds significant variable interests in VIEs in which it may or may not be the sponsor. The Company consolidates VIEs for which it is determined to be the primary beneficiary.

The Company has investments in real estate partnerships and similar vehicles in the United States and Europe. The investments were generally in the form of limited or membership ownership interests in the United States and share ownership interests in Europe. These real estate partnerships invested in various real estate ventures with local operating partners. The Company's maximum exposure to loss for these entities is limited to the Company's investment in these equity method investees and the contractual commitment to provide additional equity in certain circumstances. The Company ceased making any new investments as part of this business line, but continues to have contractual commitments to make additional investments in certain funds. The remaining commitments are solely for existing assets and to fund operations. As of November 2, 2018, and February 2, 2018, the Company was not the primary beneficiary of any VIEs.

The following table sets forth the total assets and liabilities, and sources of maximum exposure of entities deemed to be VIEs for which the Company is not considered to be the primary beneficiary, and which are not consolidated by the Company, including significant variable interests as well as sponsored entities with a variable interest (in thousands):

	Size of VIEs ⁽¹⁾	Carrying amount of assets ⁽²⁾	Maximum exposure to loss ⁽³⁾		
			Commitments	Loans, equity investments and other investments	Total
As of November 2, 2018					
Equity investments in real estate investment funds and other real estate ventures	\$ 231,367	\$ 4,409	\$ 3,590	\$ 4,409	\$ 7,999
Loans held for sale	—	—	—	—	\$ —
Total	<u>\$ 231,367</u>	<u>\$ 4,409</u>	<u>\$ 3,590</u>	<u>\$ 4,409</u>	<u>\$ 7,999</u>
As of February 2, 2018					
Equity investments in real estate investment funds and other real estate ventures	\$ 349,044	\$ 7,133	\$ 3,937	\$ 7,133	\$ 11,070
Loans held for sale	126	42	—	42	42
Total	<u>\$ 349,170</u>	<u>\$ 7,175</u>	<u>\$ 3,937</u>	<u>\$ 7,175</u>	<u>\$ 11,112</u>

⁽¹⁾ Size of the VIEs represents the amount of the underlying assets held by the VIEs.

⁽²⁾ Amounts represent the carrying amount of the Company's variable interest included in assets on the Company's Condensed Consolidated Balance Sheets. The Company has no variable interest included in liabilities on the Company's Condensed Consolidated Balance Sheets.

⁽³⁾ Maximum exposure to loss is based on the assumption that all of the assets in the VIEs become worthless and incorporates not only potential losses associated with assets included on the Condensed Consolidated Balance Sheets, but also potential losses associated with off-balance sheet commitments, such as unfunded liquidity and/or lending commitments and other contractual arrangements.

11. Income Taxes

For the 39-weeks ended November 2, 2018, \$6.1 million of tax benefit was recognized on \$54.1 million of loss before income taxes. The tax benefit was primarily related to a \$4.8 million state unrecognized tax benefit liability release and a \$1.8 million valuation allowance release, offset by state and international tax expense. For the 39-weeks ended November 3, 2017, \$1.5 million of income tax benefit, consisting primarily of \$1.4 million release of federal unrecognized tax benefits offset by state and international tax expense, was recognized on \$75.4 million of loss before income taxes.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

The Company recognized the income tax effects of the 2017 Tax Cuts and Jobs Act (the "Tax Act") in the February 2, 2018 consolidated financial statements in accordance with Staff Accounting Bulletin No. 118, which provides SEC staff guidance for the application of ASC Topic 740, Income Taxes, and allowed up to one year to complete the required analyses and accounting for the Tax Act. At February 2, 2018 the Company was able to make reasonable estimates of the impact of the Tax Act for among other things reduced the U.S. corporate income tax rate from 35 percent to 21 percent effective January 1, 2018, changed rules related to NOL carryforwards and carrybacks, and added rules that limit the deductibility of interest expense. At February 2, 2018, the Company recorded a provisional income tax benefit of \$24.3 million pursuant to SAB 118. The accounting for the income tax effects of the enactment of the Tax Act is complete as of November 2, 2018. There were no material changes to these provisional estimates during the 39-weeks ended November 2, 2018.

Based on the Company's historical and cumulative losses, a net tax benefit was not recognized for current year pre-tax losses or carryforwards offsetting future year income. Tax benefits from net operating loss carryforwards and other deferred assets are limited to temporary differences expected to generate future taxable income. Tax benefits from carryforwards and other deferred tax assets offsetting additional income beyond the current year may be recognized in the future and could be material.

12. Derivative Instruments

Interest Rate Swaps

The Company has interest rate swap agreements to manage the risk associated with a portion of its floating-rate long-term debt. The Company does not utilize derivative instruments for speculative purposes. The interest rate swaps involve the exchange of fixed-rate and variable-rate payments without the exchange of the underlying notional amount on which the interest payments are calculated.

The notional amounts of the swap agreements are \$100 million, \$75 million, and \$75 million respectively, with maturity dates of April 29, 2019, June 28, 2019, and April 30, 2020, respectively. The Company has designated the swaps as cash flow hedges and has determined that they qualify for hedge accounting treatment. Changes in fair value of cash flow hedges are recorded in other comprehensive income (net of tax) until income or loss from the cash flows of the hedged item is realized. Unrealized gains and losses are reflected in net income attributable to the Company when the related cash flows or hedged transactions occur and offset the related performance of the hedged item. The estimated fair value of the current portion of cash flow hedges is recorded in Other current assets and the long-term portion is recorded in Other assets on the Company's Condensed Consolidated Balance Sheets. See Note 13, *Fair Value of Assets and Liabilities*, of the Notes to Condensed Consolidated Financial Statements for more information on the fair value of the interest rate swaps.

The cash flow hedges were highly effective for the 39-weeks ended November 2, 2018 and November 3, 2017. The occurrence of continued debt repayments and hedged transactions remains probable.

The unrealized gains and losses on financial instruments recorded in other comprehensive loss are summarized below (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Unrealized (loss) gain on interest rate swaps, net of tax	\$ (206)	\$ 917	\$ (58)	\$ 124

The estimated fair value of financial instruments is summarized below (in thousands):

	November 2, 2018	February 2, 2018
Other current assets	\$ 1,117	\$ —
Other assets	\$ 1,155	\$ 2,331

13. Fair Value of Assets and Liabilities

Fair Value Hierarchy

Following is a description of the valuation methodologies used for financial instruments measured at fair value on a recurring basis, as well as the general classification of such instruments pursuant to the three-level fair value hierarchy.

Servicing Rights

Servicing rights are carried at fair value in Other long-term liabilities on the Condensed Consolidated Balance Sheets. The Company recognizes gains or losses on servicing rights for servicing the SCUSA owned portfolio of Standard Receivables when compensation received from SCUSA for services provided are not adequate compared to similar servicing provided in the open market. Servicing rights are valued using a discounted cash flow methodology, and are classified within Level 3. The Company determines fair value of the servicing rights by projecting future cash flows using payment rates and other assumptions, and discounts these cash flows. The servicing rights valuations, as well as the assumptions used, are developed and reviewed by Company management. Risks inherent in servicing rights valuation include higher than expected prepayment rates and/or delayed receipt of cash flows. There is minimal observable market

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

activity for servicing rights on comparable portfolios and, therefore, the determination of fair value requires significant management judgment.

Derivative Instruments

Derivative instruments are accounted for as either assets or liabilities and are carried at fair value. The fair value of interest rate swaps is determined by the counterparty based on interest rate changes. Interest rate swaps are valued based on observable interest rate yield curves for similar instruments and classified within Level 2 of the valuation hierarchy.

Fair value of assets and liabilities measured on a recurring basis

The Company accounts for certain of its assets and liabilities at fair value on a recurring basis or considers fair value in their measurement.

The following tables summarize the assets and liabilities measured at fair value on a recurring basis (in thousands):

November 2, 2018	Quoted Prices In Active Markets For Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Interest rate swaps asset	\$ —	\$ 2,272	\$ —	\$ 2,272
Servicing rights liability	—	—	21,651	21,651
February 2, 2018				
Interest rate swaps asset	\$ —	\$ 2,331	\$ —	\$ 2,331
Servicing rights liability	—	—	25,988	25,988

There were no transfers of assets or liabilities between Level 1 and Level 2 or into or out of Level 3 during the 39-weeks ended November 2, 2018 and November 3, 2017. There were no purchases, issuances, or sales impacting the fair value of the Level 3 assets and liabilities on a recurring basis during the 39-weeks ended November 2, 2018. See Note 5, *Serviced Credit Portfolio* of the Notes to Condensed Consolidated Financial Statements for a reconciliation from the opening balance to the closing balance of the servicing rights measured using significant unobservable inputs (Level 3).

Fair value of assets and liabilities measured on a nonrecurring basis

Certain assets are measured at fair value on a nonrecurring basis, including adjustments to fair value based on the application of lower of cost or fair value accounting and asset impairments. There were no liabilities or Level 1 or Level 2 assets measured at fair value on a nonrecurring basis as of November 2, 2018 and February 2, 2018.

The Company's non-financial assets, which primarily consist of property and equipment, intangible assets and goodwill are not required to be measured at fair value on a recurring basis and are reported at their carrying value. However, on a periodic basis whenever events or changes in circumstances indicate that their carrying value may not be recoverable (and at least annually for goodwill and other indefinite-lived intangible assets), non-financial assets are assessed for impairment and, if applicable, written-down to fair value using significant unobservable inputs (Level 3). See Note 6, *Intangible Assets and Goodwill*, of the Notes to Condensed Consolidated Financial Statements for further information related to impairment.

The following table presents the adjusted basis of non-financial assets measured at fair value on a non-recurring basis in the Condensed Consolidated Balance Sheets (in thousands):

February 2, 2018	Level 1	Level 2	Level 3	Total
Tradenames intangible asset	\$ —	\$ —	\$ 72,170	\$ 72,170

Significant financial assets and liabilities not measured at fair value (in thousands)

The fair value of the Company's Term Loan facility, based on indicative valuations received from a third party financial institution, a Level 2 fair value hierarchy level source, was \$269,920 and \$310,730 as of November 2, 2018 and February 2, 2018, respectively. The Term Loan facility, excluding debt issuance costs, is recorded at carrying value of \$435,355 and \$456,956 on the Condensed Consolidated Balance Sheets as of November 2, 2018 and February 2, 2018, respectively.

The carrying amounts of other current assets, accounts payable, accrued and other current liabilities approximate fair value due to their short-term nature.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

14. Stock-Based Compensation

Stock Option Exchange

On March 22, 2018, the Company's Board approved a stock option exchange program (the "Exchange") pursuant to which eligible employees were able to exchange all or none of their outstanding options, whether vested or unvested, for new restricted stock units ("RSUs"). Partial exchanges were not accepted. One share of the Company's common stock is issuable upon the vesting and settlement of each RSU. The number of RSUs granted in exchange for the options was determined on a grant-by-grant basis and depended on a variety of factors including the employee's position, responsibilities and performance. The Exchange commenced on June 15, 2018 and expired on July 16, 2018. In connection with the Exchange, the Company accepted options to purchase 9,800,881 shares of its common stock and issued a total of 4,721,269 RSUs. All surrendered options were canceled and became available for issuance under the 2014 Incentive plan. There were 65,000 options that were not exchanged.

The Exchange is considered a modification of the original option awards under ASC 718 "Stock-based Compensation." Accordingly, the future RSU compensation cost expected to be recognized was measured as the total of the unrecognized compensation cost of the options surrendered, plus the excess of the fair value of the RSUs issued over the fair value of the options tendered immediately before the exchange, if any.

As described further below, a portion of the RSUs vest subject to a service condition based on the passage of time ("Time Vesting RSUs") and a portion vest upon a combination of time and market conditions ("Performance Vesting RSUs"). The Time Vesting RSUs were valued as of July 17, 2018 (the "Modification Date") using a discounted cash flow model based on historical Company performance, internal financial projections, market performance of peer companies and assumptions regarding general economic and market conditions. The Performance Vesting RSUs were valued using a closed-form solution of a series of "asset-or-nothing" call options assuming a term of 5.55 years, a risk-free rate of 2.76%, volatility of 66.9% and a starting stock price of \$1.01 per share.

As of the Modification Date, the incremental fair value of the RSUs issued in the Exchange was \$1.3 million. The total future compensation cost related to the RSUs issued in the Exchange, including the unrecognized compensation cost of the options surrendered, was \$5.8 million.

Restricted Stock Units

On March 22, 2018, the Board approved the Restricted Stock Unit Plan. Under the Restricted Stock Unit Plan 18.8 million common shares were authorized to be issued as settlement of restricted stock units granted to participants in the plan. Under the terms of the Restricted Stock Unit Plan, with certain exceptions:

- 35% of each RSU award is time vesting and will settle on February 4, 2022 or, if earlier, upon a change in control of the Company, and
- 65% of each RSU award is performance vesting and will vest and settle upon the first to occur of an initial public offering or "up-listing" of the Company's stock on a national exchange, a change in control or February 4, 2024, in an amount dependent upon the fair value of the Company's common stock on the vesting date as follows:
 - a) No performance vesting award shall vest if the fair value is below \$2.54
 - b) 25% of the performance vesting award shall vest if the fair value equals or exceeds \$2.54 but is less than \$3.17;
 - c) 50% of the performance vesting award shall vest if the fair value equals or exceeds \$3.17 but is less than \$3.81;
 - d) 75% of the performance vesting award shall vest if the fair value equals or exceeds \$3.81 but is less than \$4.44; and
 - e) 100% of the performance vesting award shall vest if the fair value equals or exceeds \$4.44.

In addition, an award of 313,272 performance vesting RSUs that vest only if the fair value on the vesting date equals or exceeds \$4.50 was granted to an executive and an award of 685,282 time vesting RSUs was issued to another executive that vested upon issuance. All RSUs are subject to certain vesting acceleration provisions in the event of a termination for reasons other than for cause or a resignation for good reason. Compensation expense will be recognized on a straight-line basis from the Modification date or grant date through February 4, 2022 (time vesting RSUs) or February 4, 2024 (performance vesting RSUs).

The following table summarizes activity related to the RSUs for the 39-weeks ended November 2, 2018:

	Number of Shares		Weighted Average Grant Date Fair Value	
	Performance Vesting RSUs	Time Vesting RSUs	Performance Vesting RSUs	Time Vesting RSUs
Outstanding as of February 2, 2018	—	—	\$ —	\$ —
RSUs granted	3,912,250	1,937,912	0.54	1.01
RSUs issued in the Exchange	2,846,108	1,875,161	1.01	1.56
RSUs vested	—	(701,208)	—	0.26
RSUs forfeited	(82,712)	(31,751)	1.98	3.47
Outstanding as of November 2, 2018	6,675,646	3,080,114	\$ 0.73	\$ 1.49

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Stock Options

A summary of stock option activity for the 39-weeks ended November 2, 2018 is provided below:

	Performance-Based Stock Options			Time-Based Stock Options		
	Number of shares	Weighted average exercise price per share ⁽¹⁾	Weighted average remaining contractual term (years)	Number of shares	Weighted average exercise price per share ⁽¹⁾	Weighted average remaining contractual term (years)
Outstanding as of February 2, 2018	6,229,555	\$ 4.04	7.2	4,138,352	\$ 4.04	7.2
Exchanged	(5,880,529)	4.02	—	(3,920,352)	4.02	—
Forfeited or canceled	(323,746)	9.12	—	(201,146)	8.74	—
Outstanding as of November 2, 2018	25,280	\$ 5.75	—	16,854	\$ 5.75	0.1

⁽¹⁾ The weighted average exercise price was adjusted to reflect the impact of the Special Dividend in fiscal 2017.

Time-based stock options exercisable were 16,854 and 2,115,281 as of November 2, 2018 and February 2, 2018, respectively.

Restricted Stock Awards

Under the 2014 Incentive Plan (“Equity Incentive Plan”) the Company may grant restricted stock awards to non-management members of the Board of Directors of the Company.

The Company issued to the non-management members of the Company’s Board of Directors restricted stock grants totaling 829,211 shares on September 13, 2018 pursuant to the Equity Incentive Plan, which will fully vest on the earlier of June 21, 2019 or the date of the Company’s annual Shareholders’ meeting. Restricted stock awards totaling 859,815 shares were issued on August 24, 2017, which fully vested on June 19, 2018. Stock compensation expense associated with these awards of \$0.2 million and \$0.4 million was recognized for the 13- and 39-weeks ended November 2, 2018, respectively.

These liability-classified awards related to stock-based compensation arrangements for non-vested shares are measured at the fair value of the award at the grant or measurement date and are remeasured at fair value on each subsequent reporting date. The related compensation expense is recognized over the applicable service period. The total fair value of shares that vested during the 39-weeks ended November 2, 2018 was \$0.9 million.

Stock-based Compensation Expense

Stock-based compensation expense recognized for the 13- and 39-weeks ended November 2, 2018 was \$0.8 million and \$2.5 million, respectively. Stock compensation expense recognized for the 13- and 39-weeks ended November 3, 2017 was \$0.6 million and \$3.2 million, respectively.

As of November 2, 2018, there was \$4.7 million and \$4.2 million of unrecognized compensation expense related to the remaining performance vesting RSUs and time vesting RSUs, respectively. The unrecognized compensation expense related to performance vesting RSUs will be amortized on a straight-line basis from the grant date through February 4, 2024. The unrecognized compensation expense related to time vesting RSUs will be amortized on a straight-line basis from the grant date through February 4, 2022. The Company expects to recognize the total compensation expense over a weighted average period of 4.3 years.

15. Commitments and Contingent Liabilities

Litigation

The Company may be subject to potential liability under laws and government regulations and other legal actions that are pending or may be asserted against it. The Company may also be subject to governmental and regulatory examinations, information requests, investigations and proceedings, certain of which may result in settlements, fines, penalties, or other relief. The Company periodically is involved in legal proceedings arising in the ordinary course of business, including, among others, claims relating to collection activities, including claims under the Telephone Consumer Protection Act. As of December 12, 2018, after consultation with counsel and based on current knowledge, it is the opinion of management that potential liability arising from pending litigation is not expected to have a material adverse effect on the Company’s consolidated financial condition, results of operations or cash flows. However, due to the inherent uncertainty with respect to legal proceedings, and since the ultimate resolution of the Company’s litigation, claims, and other legal proceedings are influenced by factors outside of the Company’s control, it is reasonably possible that actual results will differ from management’s estimates, and it is possible that litigation, claims or legal proceedings could have a material adverse effect on its results of operations in any particular period. Legal costs for these matters are expensed as incurred. Selective legal proceedings to which the Company is a party are set forth below.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Bluestem is party to two consolidated putative class action lawsuits filed in federal court in the United States by Jessica Parm and Sara Arce on August 27, 2017 and October 14, 2015, respectively. The lawsuits allege violations of various state and federal laws arising from undisclosed finance charges allegedly included in the price of goods sold under the Fingerhut brand. The named plaintiffs in these cases seek, among other relief, unspecified monetary damages and an order enjoining Bluestem from continuing the allegedly unlawful practices. On August 7, 2018, the United States Court of Appeals for the Eighth Circuit ruled in Bluestem's favor and ordered all claims to individual arbitration. The matters are ongoing and the company does not expect any material loss in connection with these cases. No amount was recorded related to any of these matters as of November 2, 2018.

Bluestem is party to a putative class and collective action lawsuit filed in federal court in the United States by Tina Norris on November 18, 2016. The lawsuit alleges violations of various wage and hour laws. One of the named plaintiffs in the case also alleges a claim for retaliation. Among other things, the plaintiffs seek unspecified money damages and attorneys' fees. The Court granted-in-part the plaintiffs' motion for class certification, and the class opt-in period has closed with 107 total class members. Class action discovery is ongoing.

In January 2016, Bluestem received a Civil Investigative Demand from the Bureau of Consumer Financial Protection (BCFP") (f/k/a Consumer Financial Protection Bureau or (the "CFPB"). The BCFP's investigation has involved the production of documents, answers to written questions and oral testimony related to the offering and providing extensions of credit, debt collection and sales of debt. On September 5, 2017, Bluestem responded to an August 2017 Notice and Opportunity to Respond and Advise ("NORA") letter from the CFPB notifying Bluestem that the BCFP's Office of Enforcement is considering recommending that the BCFP take legal action against Bluestem due to alleged delays between the time when Bluestem received payments on already-sold debt and when it forwarded those payments to debt buyers. On October 4 2018, the BCFP issued a five-year consent order against Bluestem that required Bluestem to pay a \$200,000 civil money penalty and agree to certain injunctive relief in exchange for a release of claims from the BCFP. The consent order and accompanying agreements resolve all pending Civil Investigative Demands by the BCFP against Bluestem.

Bluestem is party to a putative class action lawsuit filed in federal court in the United States by Elizabeth Busch on March 14, 2016. The lawsuit alleges violations of the Telephone Consumer Protection Act ("TCPA"). The named plaintiff in this case seeks \$500 - \$1,500 per call in statutory damages and an injunction prohibiting Bluestem from violating the TCPA. On November 15, 2018, the parties attended mediation and reached a preliminary confidential settlement of all class claims. The proposed settlement remains subject to court approval, and we do not expect this matter to have a material impact on the financial statements.

Bluestem is party to a putative class action lawsuit filed in federal court in the United States by Waddell Williams on August 21, 2017. The lawsuit alleges violations of the TCPA. The named plaintiff in the case seeks up to \$1500 per call in statutory damages and an injunction prohibiting Bluestem from violating the TCPA. On September 25, 2018, the parties attended mediation and reached a preliminary settlement of all class claims for \$1,000,000 plus the cost of class administration. The parties filed a motion of preliminary approval of the settlement with the Court on November 21, 2018 and await the Court's approval.

16. Segment Information

The Company reviews and presents the consolidated business results based on the organizational structure the Company's management uses to evaluate performance and make decisions on allocating resources and assessing performance. The Company's consolidated business results are presented in three reportable segments (referred to herein as "segments"): Northstar Portfolio, Orchard Portfolio and Corporate and other.

The accounting policies of the segments are the same as those described in Note 3, *Significant Accounting Policies and Recently Issued Accounting Standards* of the Notes to Condensed Consolidated Financial Statements, except that disaggregated results have been prepared using a management approach. The disaggregated results are consistent with the basis and manner in which management internally disaggregates financial information for the purpose of the decision-making process. Segment merchandise sales and shipping and handling revenue are recorded at the time of shipment to the customer and an adjustment to reduce sales by the estimated amount of orders in-transit to customers is recognized and reported in the Corporate and other segment. Material inter-segment transactions have been eliminated in consolidation. The Company does not disclose segment level balance sheet information as it is not used internally in the decision-making process.

Northstar Portfolio

The Northstar Portfolio consists of the Fingerhut and Gettington retail brands. These brands are national multi-channel retailers servicing low- to middle-income consumers by offering products with multiple payment plans through revolving credit lines or installment loans offered by WebBank as the originating bank. While numerous retailers sell merchandise via the internet and catalogs focusing on low- to middle-income customers, Northstar Portfolio has created a differentiated business model by utilizing direct-marketing expertise to integrate proprietary credit offerings with broad general merchandise offerings including consumer electronics, domestics, housewares, fashion and home furnishings. The majority of sales are on revolving customer credit accounts, originated through WebBank, reflecting Northstar Portfolio's ability to combine relevant merchandise offerings with an attractive consumer credit product aligned with the customer's ability to pay. Fingerhut also offers the FreshStart program, which provides customers the option of purchasing merchandise on installment credit terms after making a down payment.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Orchard Portfolio

The Orchard Portfolio consists of Appleseed's, Bedford Fair, Blair, Draper's & Damon's (whose retail stores were exited during the first quarter of fiscal 2017), Gold Violin, Haband, LinenSource (which was exited in the second quarter of fiscal 2017), Norm Thompson, Old Pueblo Traders, Sahalie, Tog Shop, and WinterSilks retail brands. These brands are national multi-channel retailers offering apparel, accessories, and home products for women and men principally in the boomer and senior demographic, generally considered age 50 and older. Orchard Portfolio offers its product assortments through various platforms including online and direct mail.

Important drivers of Orchard Portfolio's business performance include growth in new customers, average order size, existing customer repurchase rates, the mix of merchandise sold, and promotional performance.

The Orchard Portfolio has an extensive proprietary database of customer information, including customer demographics and purchasing history. The Orchard Portfolio is able to design its marketing programs using this information. Marketing strategies are designed to grow lifetime value with customers by using the strength of its brand portfolio to meet more of its customers' needs. Multiple Orchard Portfolio brand relationships are fostered through circulation strategies, the design of its web universal cart and its use of a third-party private label credit platform across all brands.

Corporate and Other

The Corporate and Other segment includes certain costs consisting of indirect general and administrative expenses, amortization and depreciation not included in cost of goods sold, loss on impairment, gains on derivatives in the Company's own equity, gain on debt extinguishment, the elimination of inter-segment activities as well as adjustments to net sales, cost of goods sold, selling and marketing expenses related to product estimated to be in-transit from shipping point to the customer. In addition, the segment includes the PayCheck Direct business (which was exited during the first quarter of fiscal 2017), and Capmark Portfolio. PayCheck Direct was a program that was offered directly through employers or organizations as a voluntary benefit to employees and members. It allowed customers to purchase products with the convenience of paying over 12 months through payroll deductions or automatic bank withdrawals. Capmark Portfolio is focused on managing a real estate-related business and existing assets, including monetizing these assets when appropriate. Capmark's net gains on loans, equity in income of joint venture and partnerships and other (losses) gains, net as our equity investments continue to wind down and approach the end of their lives.

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

The following tables summarize the results of operations through Operating income by segment for the 13- and 39-weeks ended November 2, 2018 and the 13- and 39-weeks ended November 3, 2017:

	13-Weeks Ended November 2, 2018			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 227,549	\$ 184,332	\$ (4,104)	\$ 407,777
Commercial real estate revenue, net	—	—	514	514
Total net sales and revenue	227,549	184,332	(3,590)	408,291
Costs and expenses				
Cost of goods sold	127,857	91,460	(3,044)	216,273
Sales and marketing expenses	35,393	75,288	(90)	110,591
Net credit expense	26,665	—	9	26,674
General and administrative expenses	7,130	9,350	32,367	48,847
Amortization and depreciation not included in cost of goods sold	—	—	11,961	11,961
Total costs and expenses	197,045	176,098	41,203	414,346
Operating income (loss)	\$ 30,504	\$ 8,234	\$ (44,793)	\$ (6,055)
	13-Weeks Ended November 3, 2017			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 210,115	\$ 201,703	\$ (12,020)	\$ 399,798
Commercial real estate revenue, net	—	—	1,115	1,115
Total net sales and revenue	210,115	201,703	(10,905)	400,913
Costs and expenses				
Cost of goods sold	119,488	96,311	(7,136)	208,663
Sales and marketing expenses	29,490	80,859	(3,157)	107,192
Net credit expense	30,129	—	269	30,398
General and administrative expenses	6,800	9,115	30,359	46,274
Amortization and depreciation not included in cost of goods sold	—	—	13,471	13,471
Total costs and expenses	185,907	186,285	33,806	405,998
Operating income (loss)	\$ 24,208	\$ 15,418	\$ (44,711)	\$ (5,085)

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

	39-weeks ended November 2, 2018			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 635,051	\$ 586,888	\$ (10,903)	\$ 1,211,036
Commercial real estate revenue, net	—	—	1,268	1,268
Total net sales and revenue	635,051	586,888	(9,635)	1,212,304
Costs and expenses				
Cost of goods sold	356,169	284,576	(9,246)	631,499
Sales and marketing expenses	94,477	241,506	(140)	335,843
Net credit expense	80,734	—	99	80,833
General and administrative expenses	20,075	27,669	96,290	144,034
Amortization and depreciation not included in cost of goods sold	—	—	36,308	36,308
Total costs and expenses	551,455	553,751	123,311	1,228,517
Operating income (loss)	\$ 83,596	\$ 33,137	\$ (132,946)	\$ (16,213)

	39-weeks ended November 3, 2017			
	Northstar Portfolio	Orchard Portfolio	Corporate and other	Total
Net sales and revenue				
Net sales	\$ 618,217	\$ 652,408	\$ (4,311)	\$ 1,266,314
Commercial real estate revenue, net	—	—	2,522	2,522
Total net sales and revenue	618,217	652,408	(1,789)	1,268,836
Costs and expenses				
Cost of goods sold	353,678	310,026	(2,514)	661,190
Sales and marketing expenses	92,443	252,766	(1,573)	343,636
Net credit expense	85,436	—	4,385	89,821
General and administrative expenses	19,975	28,699	119,445	168,119
Amortization and depreciation not included in cost of goods sold	—	—	42,797	42,797
Loss on impairment	—	—	230	230
Total costs and expenses	551,532	591,491	162,770	1,305,793
Operating income (loss)	\$ 66,685	\$ 60,917	\$ (164,559)	\$ (36,957)

BLUESTEM GROUP INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

The following table summarizes total net sales by merchandise category for the 13- and 39-weeks ended November 2, 2018 and November 3, 2017 (in thousands):

	13-Weeks Ended		39-Weeks Ended	
	November 2, 2018	November 3, 2017	November 2, 2018	November 3, 2017
Net sales				
Home	\$ 103,370	\$ 102,661	\$ 311,673	\$ 333,537
Entertainment	91,002	89,453	243,878	251,260
Fashion	246,408	244,202	757,336	763,507
Total merchandise sales⁽¹⁾	440,780	436,316	1,312,887	1,348,304
Corporate and other ⁽²⁾	(4,104)	(12,020)	(10,903)	(4,311)
Returns and allowances	(40,010)	(42,808)	(124,907)	(135,189)
Commissions and other revenues	11,111	18,310	33,959	57,510
Net sales	\$ 407,777	\$ 399,798	\$ 1,211,036	\$ 1,266,314

⁽¹⁾ Includes shipping and handling revenue and is net of sales discounts

⁽²⁾ Consists of adjustments to Bluestem's net sales related to in-transit product sales from shipping point to estimated time of delivery, net of sales of PayCheck Direct and the elimination of inter-segment activities.

17. Subsequent Events

These financial statements include consideration of subsequent events through December 12, 2018, the date the condensed consolidated financial statements were issued.