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THEATRE

M&A &CINEMA

Prompted both by digitisation and the changing global economy, M&A activity is, today, transforming the movie industry's landscape - and not just for Exhibition, of course, but for Cinema as a whole. By way of overview, **EFA Partners**, a boutique financial advisor with cross-industry experience, offers a rationale for recent consolidation developments.

During the past several years we've witnessed unprecedented changes in the world economy, much of it spawned from the Digital Age. Tremendous growth in the Asian markets, the Middle East, and others, have resulted in our economies now truly becoming a single global economy rather than one dominated by a small handful of nations. And, indeed, the Digital Era encourages companies to continue pursuing new technologies that meet the needs of businesses and consumers alike.

Such has affected perhaps most industries throughout the world, as start-ups continue to emerge with new technologies, and mature businesses attempt to transfer their legacy platforms to digital. And adapting to new business models isn't easy. Certain industries, like >

the Music sector, continue into the Digital Age as downloads and streaming - via iTunes, Spotify, and others - become the new norm. The Publishing industry, too, has needed to completely revamp its business model, with newspaper and magazine sales often dwindling as today's consumers – both young and old – increasingly obtain their news online.

THE FILM SPACE

Likewise, the Film industry is experiencing global transformation. For an industry that was once dominated by the big Hollywood studios and the U.S. box office, it, too, is now progressing into a new era. International box office has grown at a record pace, with 2015's international box office of $27.2bn now up from $21bn in 2010, compared to the North American figure of $11.1bn, only modestly up from $10.6 bn for the same years. Of course, we've seen the international screen-count grow tremendously – the same fuelled primarily by Chinese growth that has added in the region of 20,000 screens in the recent years. It is projected that this number of screens in China will almost double over the next few years, and so surpassing North America's 40,000+ screens.

Of course, with the Film industry having entered the Digital Age too, almost all screens in the U.S. are now fully-digitised as are those in most countries worldwide. However, the digital distribution of film isn't the *only* industry sector to have embraced digital technology. The entire film process - or 'film chain' – has digitised concurrently, and includes each of its five component links: Production, Post-Production, Distribution, Exhibition and, of course, the many proliferating downstream windows.

Given these dynamics, it's perhaps little wonder that, internationally, many players have looked to enter the industry via one or more of the above sectors, and this has led to new, as well as changing, industry alliances, to say nothing of considerable M&A activity. Indeed, mega-deals have been recently announced, such as the $85bn AT&T/Time Warner merger, along with Wanda Dalian's announced acquisitions of companies in both Production and Exhibition in transactions totaling almost $10bn. All of this has led to considerable worldwide growth and consolidation – although, as can occur in the M&A world, there can be kinks in the chain, too. Let's first consider the Production sector.

FILM PRODUCTION

In the not so distant past, the familiar 'lights, camera, action' refrain had been limited to the major studios which had enjoyed easy access to internal film-funding as well as external funding-partners. But this has changed over the years, with the mini-majors and independents also emerging with successful movies. The Digital Age has reshaped production in two primary ways by: (a) ensuring that movies can be produced and distributed more cost-effectively using digital equipment, and (b) following the significant number of new release-platforms which have emerged, by the likes of Amazon, Netflix, Hulu *et. al*.

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Internationally, growth in Asia has changed the industry. China's unparalleled screen-growth has been accompanied by a surge in Chinese production-capability. Additionally, movie-producers outside of China have their eye on Chinese audiences, utilising story lines and actors tailored to China's culture. Therefore, with so much industry potential, has come significant M&A activity - Dalian Wanda having been at the forefront of this segment with acquisitions, this year, of Legendary Entertainment for $3.5bn, along with its proposed takeover of Dick Clark Productions for an estimated $1bn. Not to be left trailing, Steven Spielberg recently announced that Alibaba Pictures is to buy a stake in his Amblin Partners, to work together on production, marketing and distribution globally, including in China. However, that doesn't mean that activity is limited to China. For one, Qatar-based beIN recently announced its acquisition of Miramax.

POST-PRODUCTION

Some of the most significant changes in the Film sector have occurred in Post-Production, again in the wake of the shifting digital landscape. Digital editing, special effects, colorisation, titling, animation, and many other aspects, can now be accomplished much more readily and cost-effectively. The upshot is that dominant players, like Deluxe and Technicolor, have digitally-aligned their legacy businesses and equipment through both organic change and acquisition. In certain instances, this has produced downsizing and outsourcing, as per Technicolor's announcements, last year. However, Digital has also caused an influx of new businesses on the back of fewer capital equipment requisites than previously, and with many tasks now readily effected using such everyday equipment as digital workstations and laptops, especially with the cost of software having dramatically dropped. It is also true that the global growth of the Film industry has, in turn, escalated the growth in Post-Production – the availability of more foreign films, especially in Asian markets, necessitating more dubbing, titling and related localisation work associated with overseas features. It means also that certain scenes need editing or other modification to suit different markets. There's also been heightened demand for services following the ever-increasing number of digital distribution channels seeking more and more content to fill programming requirements.

M&A in this link of the film-chain will include groups that have overlapping legacy businesses that may make them ripe for consolidation. Other opportunities could exist with complementary digital businesses which overlap little but have legacy-platforms that could benefit from merger.

And while some entities are growing via acquisition, others continue to form new businesses without the potential issues of the legacy personnel and costs associated with most acquisitions. A good example of this is STX Entertainment, founded just over two years ago, and which has already brought to market several high-profile films and an announcement of a deal with China's Huayi's Bros. to co-finance up to 18 movies, most being in the $20-50m budget-range. Whilst a global strategy makes sense from a high-level perspective, the jury is probably still out as to how these groups will work together – from both a business and cultural perspective – to produce films that will satisfy such diverse tastes.

We're also seeing larger companies seeking to acquire smaller ones with niche expertise in the Post-Production, and examples include Technicolor's acquisition of The

Mill, for its connected devices business; and Deluxe's acquisition of Mediapeers for its B2B movie cloud-service for movies.

So, what international bearing does this have? Well, Digital Domain, as one example of a major industry player, recently announced a strategic investment by Chinese firms, CITIC, Softbank China Venture Capital and Qualcomm. Meanwhile, Digital Domain's post-production business has seen global growth, having also embraced new technologies in related sectors, such as Virtual Reality (VR) and Augmented Reality (AR). But, such pace of growth seems to suggest the tip of the iceberg, as also observes Digital Domain's Executive Director and COO, Amit Chopra when he says: "The demand for digital effects and digital editing continues to grow both in Asia and North America. In addition to this, there is yet tremendous demand for the new areas of VR and AR in the Film and interactive gaming sectors".

The conclusion? That consolidation within Post-Production should almost certainly continue apace as larger companies seek to gain global marketshare while reducing their legacy businesses amid the digital-transformation. It is also expected that there could be increasing opportunities for companies to strategically roll-up newer, smaller, fully-digital Post-Production entities.

Demand for digital-effects and editing continues to grow – both in Asia and in North America – along with tremendous demand for VR and AR in the Film and interactive gaming sectors

AMIT CHOPRA
Executive Director & COO
Digital Domain

DISTRIBUTION

The Exhibition industry's digital-conversion, notwithstanding lengthy delays, has today all but been completed, rendering 35mm film a thing of the past. And, while conversion nears its inevitable completion in Exhibition, it is true that film distributors still operate within a changing environment. As screen-growth continues internationally, and new mediums emerge for movie-viewing, those involved in movie-distribution clearly need to adapt, as indeed they are doing. Indeed, the time-honoured launch-platform for new movies is changing as new platforms from the likes of Amazon and Netflix continue to offer original programming for home-viewing. Given this scenario, industry players are demanding higher quality as digital formats offer higher-resolution and greater content-security requirements.

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From an M&A perspective, the Distribution space employs some of the same dynamics as Post-Production and, in fact, many of the same companies specialising in Post-Production services also hold movie-distribution divisions. Deluxe and Technicolor both engage separate movie-distribution businesses, however, in 2015, formed a joint-venture for digital theatrical movie-distribution, via satellite or hard-drive. It's also of note that Cinedigm, formally a leading digital-distribution company, has since focused primarily on over-the-top (OTT) content demand services.

With the sector having many ancillary products and services, it is true that many have been seeking acquisition opportunities in various related sectors, and includes Webedia which, in 2014, acquired BoxOffice Media and then, in 2015, West World Media, an international provider of theatre showtimes to exhibitors. Similarly, global media measurement and research company, Rentrak, which provides box office data, recently merged with U.S.-based provider of data services, comScore, in a $768m transaction.

To sum up, Distribution's changing landscape dictates that new companies should continue to emerge, also that M&A activity ought to continue internationally as larger companies seek out niche businesses with the necessary expertise and marketshare.

THEATRICAL EXHIBITION

So, while Digital Cinema has already refashioned global Exhibition, and with most major circuits already converted, there is still much change happening within the sector. Digital has enabled 3D, Event Cinema and 4D motion-seating, along with immersive sound and other auditorium activity. In addition to this, the industry is experiencing explosions in the popularity of luxury theatres following the re-equipment of recliner-seating as well as upscale concessions and in-theatre dining roll outs. All the while, new exhibition technologies continue to emerge.

One such example can be seen with The Vista Project, the vision of industry veteran, Bud Mayo, President of Alternative Programming & Distribution at Carmike Cinemas, also founder of Clearview Cinemas,

Digital is providing so many new opportunities for exhibitors, who should embrace it so as to better entice and alter the viewing habits of the next generation of movie-goers... and that while consolidation will continue, content is where the industry focus needs to be

BUD MAYO

President of Alternative Programming & Distribution, Carmike Cinemas

Cinedigm and Digital Cinema Destinations. Mayo has teamed with TimePlay and SMPTE (Society of Motion Picture & Television Engineers) and his concept here is one utilising 'second screen', to merge younger audiences' penchant for hand-held devices and mobile entertainment with new film experiences. Today's digital technology can provide movies and preshow with interactive elements, and The Vista Project endeavours to do just that with plots that can, through audience-voting via their mobiles, change during the movie itself.

Stated Mayo on the changing technology: "The Digital Age is providing so many new opportunities for exhibitors who should embrace it to better entice, as well as alter, the movie-viewing habits of the next generation of movie-goers". He also opines that with the present pace of change, there will continue to be greater industry consolidation as companies seek growth, but the bigger picture is that 'content remains king', and that's where the primary focus needs to be for the industry.

The Exhibition sector has, meanwhile, seen some major consolidations in the U.S., Europe, and in other international markets and, until recently, most have centred upon particular regions in the U.S., or with companies like Odeon and Vue, having made acquisitions across Europe. This dynamic has also altered radically with Dalian Wanda's market entry. Its $2.6bn acquisition of AMC in the U.S., also of Hoyts in Australia ($366m) - as well as the subsequently announced acquisitions of Carmike ($1.2bn) and, most recently, Odeon-UCI (also at $1.2bn) - has already made Wanda-AMC a formidable force within global Exhibition. And, if the above acquisitions *do* close as anticipated, Wanda's presence will span over 13,000 screens in 11 countries, making it Exhibition's global #1.

The motivation of sellers we also observe greatly vary according to the ownership-management teams involved. Smaller, family-operated, exhibitors usually won't have such ready access to the needed capital to upgrade and thus remain competitive in their markets; while older generations of theatre-operations may lack the drive or inclination to go tackle extensive project upgrades because the payback can be that much longer for upgrade investments.

A case in point, here, might include the recent sale of Muller Family Theatres, in Minneapolis, to Michigan-based Northwoods Entertainment. The Mullers had successfully run its theatres for decades; however, the decision was made to sell to an exhibitor with a younger management team with upgrade plans for the theatre chain. Affirmed Jon Goldstein, Managing

Wanda acquisitions across the various sectors and regions

Company	Sector	Region	Estimated Deal Size
AMC Entertainment	Exhibition	U.S.	$2.6 billion
Carmike Cinemas	Exhibition	U.S.	$1.2 billion
Hoyts Cinemas	Exhibition	Australia	$366 million
Odeon/UCI	Exhibition	Western Europe	$1.2 billion
Legendary Entertain-ment	Film Production	Global	$3.5 billion
Dick Clark Productions	Television Production	U.S.	$1 billion
			Total $9.9 billion

Industry mergers at a glance

Companies	Deal Type	Estimated Deal Size
AT&T / Time Warner	Merger	$85 billion
Rentrak / comScore	Merger	$768 million
Apollo / Outerwall (Redbox and other assets)	Acquisition	$1.6 billion
Webedia / West World Media	Acquisition	Undisclosed
Digital Domain / Softbank, CITIC, Qualcomm	Investment	$30.7 million
Fandango / M-GO	Acquisition	Undisclosed
Technicolor / The Mill	Acquisition	Undisclosed
Deluxe / Mediapeers	Acquisition	Undisclosed
STX Entertainment / Huayi Bros.	Co-finance	Undisclosed

"The Muller family had done a wonderful job in managing its theatres over the past several decades and the mission, going forward, is to take the theatres to the next level".

JON GOLDSTEIN
Managing Partner
Northwoods Entertainment

Partner of Northwoods: "The Muller family had done a wonderful job in managing its theatres over the past several decades and the mission, going forward, is to take the theatres to the next level".

However, the reasons to be an active acquirer in this sector do seem to vary considerably. For larger operators, there is the continual search for ways to increase shareholder value through growth – be it from building new theatres, upgrading existing ones, by acquisition, or through some combination thereof. And, whilst organic growth and upgrades can result in significant capital returns in the long term, acquisitions can result in near-term revenue-increases as well as near-term profitability. For example, Wanda-AMC's intended acquisition of Carmike, if closed, will result in AMC quickly gaining marketshare in various U.S. regions in which it had little or no previous presence.

Further, as they seek to expand, larger exhibitors have the advantage as they make acquisitions based upon multiples of theatre-level cash flow without taking into account duplicative corporate overhead. Acquisitions may also take place as an exhibitor ventures into new theatre-platforms and this was demonstrated back in 2013 when Southern Theatres acquired Movie Tavern to dip-its-toes into the, by-now, popular in-theatre dining concept.

International expansion can introduce further dynamics, such as exchange-rate-fluctuations, which can impact acquisition-pricing and timing, and a fitting example of this was seen most recently in Wanda-AMC's purchase of UK #1 operator, Odeon-UCI. When announcing the transaction, AMC's CEO and President, Adam Aron, referenced that a factor in the acquisition's

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timing had been the unusually favourable exchange-rate drop following the unexpected Brexit vote back in June.

As a concluding observation, perhaps, while it's anticipated that consolidation should continue apace, issues can arise as exhibitors maintain their need to grow quickly as fewer theatre circuits remain potentially for sale and could therefore lead to acquirers either overbidding or else moving into regions that could be less-well-suited to their existing circuits.

DOWNSTREAM WINDOWS

The list of downstream windows for movies also continues to grow; and, in addition to Amazon, Netflix and Hulu, movies can now be streamed or downloaded via iTunes, Sling Orange, Playstation Vue, and many, many others, while most cable and satellite services also offer VoD options. While these digital options remain popular everywhere, DVD and Blu-ray also remain prevalent. The newest entrant, however, is VR and movie-producers are experimenting with the technology by making movie-shorts specifically for VR devices.

So, what about M&A activity in this exploding sector? One private equity firm, Apollo Global Management, announced earlier this year its agreement to a $1.6bn acquisition of Outerwall which included its Redbox business, a provider of movies on DVD via store kiosks. It should be noted that it was reported that Apollo was having issues with debt-financing for Redbox as lenders wanted more conservative debt terms given the company's competition from online-streaming.

Also this year, ticketing giant, Fandango, stated its intention to buy movie-streaming-provider, M-GO. And one interesting, if not milestone, development that may foreshadow future business models, was Netflix' announcement to begin showing its original programming at iPic theatres in the U.S. Indeed, Netflix recently announced its intention to release over 1,000 hours of original programming in 2017, compared to the 600 hours in 2016, which equates to a 66% increase.

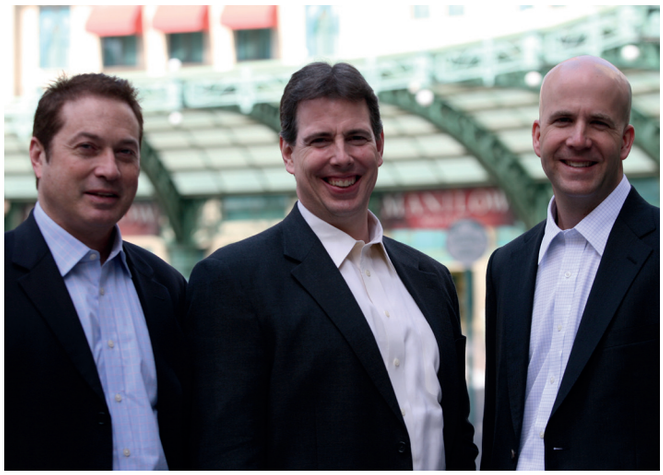
Of course, much of the industry M&A activity we're seeing remains a battle for content and was clearly demonstrated by the recent AT&T-Time Warner 'mega-merger' announcement, above. Significantly, such combines the assets of both, and includes DirectTV, HBO, TNT, MLB, NCAA basketball *et. al.* Following

announcement, AT&T CEO, Randall Stephenson, referenced that we are likely to see many more mergers between content and distribution companies.

Meanwhile, one thing we can be sure of is that this sector will be seeing more emerging companies and technologies, as it would seem that, with the present state of flux, we are merely at the early stages in terms of the evolution of both how and where people want to view movies. M&A activity should also continue as companies seek to invest in other companies with the latest technology and devices. But this can involve some difficult decision-making, and not least because technology that seems 'excellent in concept', isn't always embraced by the public.

CONCLUSION

By way of review, it's perhaps fair to say that the concurrence of increasing digitisation and the ever-evolving global economy, is landing significant opportunities for many throughout the Film sector. Yes, the increasing worldwide screencount along with many new digital-release platforms in the home-market has resulted in many players wanting to enter the film-space. Plus, of course, many view acquisition as the quickest route to gaining marketshare. Moreover, while these trends may decelerate in years to come – as over saturation results in slower screen-growth and lower growth in the downstream sectors – M&A activity could remain particularly prevalent in the foreseeable future.



Increasing global screencount, along with a multitude of new digital-release platforms, has led to many more players entering the film-space via acquisition as the fastest route to marketshare… while these trends may come to decelerate, M&A activity could remain particularly prevalent

EFA PARTNERS

*Amongst others, **EFA Partners** provides investment banking services focused on M&A, and arranging capital for entertainment, media and technology companies.*
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