DIGITAL MEDIA

MARKET OVERVIEW | **COVID-19**

Observations

In recent weeks, the coronavirus has sent shockwaves through markets globally. Since mid-February, the outbreak has accelerated and infections have become widespread, resulting in significant market disruptions that could continue for the foreseeable future. Substantial disruption to all business sectors are occurring with wide ranging implications for the media industry.

1. While the environment is still very fluid (and we expect challenges ahead for many across the space), for several leading digital media platforms, whether digital publishers, over-the-top (OTT) platforms, vMPVDs, streaming music services, or digital games companies, we believe "shelter in place" or similar orders will actually provide a catalyst for user growth over the coming weeks; consumers will have extra time to explore and consume digital entertainment alternatives (and will be looking for lower—or no—cost digital media alternatives to traditional/pay-TV platforms). Numerous early reports across our space show user metrics have been surging in recent weeks, suggesting there may be a silver lining for some digital media companies in the near term.
2. It's far from all good news of course. We expect digital media companies that are highly dependent on ad-supported models will face real challenges in the months ahead. While many digital media companies have taken measures (organically and via M&A) to diversify business models and reduce dependency on advertising revenues, many remain vulnerable to softness in advertising. In addition, digital media companies tend to be more dependent on advertising that is tied to shorter spot cycles, which can get cut more quickly during market downturns. If a softness persists for several months, we expect many companies will struggle to maintain profitability and will likely need to pursue strategic M&A/consolidation/distressed M&A in order to ensure survival.
3. We expect that OTT will remain a hot sector to watch. Over the last few years, nearly every major media company has been focused on developing a direct-to-consumer strategy and has now either launched or is racing to launch an OTT platform to compete with Netflix, Disney+, Amazon Prime Video, etc. We believe that the current climate will only serve to highlight the importance of having a robust direct-to-consumer offering. For those media companies that are behind in the OTT streaming wars, we expect to see heighted strategic focus, investment, and further M&A activity in this space (exemplified by Fox's recent acquisition of Tubi, Comcast's acquisition of Xumo, ViacomCBS's acquisition of Pluto, and FaceBank's merger with fuboTV).
4. With content production all but shut down over the near term, those digital media companies that built up robust production capabilities in recent years to satisfy the growing demand for long-form content from large media companies and OTT platforms could be materially impacted by the loss of production revenues. In this climate, social platforms (from Facebook to Snap to Tiktok) and those platforms that specialize in aggregating, producing, and distributing social video (i.e., Jukin Media and Team Whistle) should be better placed to withstand (and potential thrive) in the current downturn.
5. Technological disruption and fundamental changes in consumer behavior (i.e., cord cutting and the generational shift to embrace direct-to-consumer/OTT offerings) have provided a key catalyst for much of the M&A/consolidation that has taken place across the media landscape. Recent M&A activity has been driven by the need to achieve greater scale, increase access to IP, open new revenue streams, reach younger audiences, and enhance direct-to-consumer capabilities. In our view, the current environment does not change these strategic priorities for most media companies (it probably only amplifies the urgency), and as a result, we expect to see continued M&A activity in many of the areas described in this update.

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What Can We Expect to See?

The COVID-19 pandemic is expected to have a significant impact on the media industry. While traffic and engagement increase, advertising revenue is expected to decrease, creating both opportunities and serious challenges across the digital media landscape.

OTT Platforms

- The media industry is at an inflection point as consumers are rapidly abandoning traditional pay TV/cable (cord cutters and cord nevers) and shifting to OTT and vMVPD alternatives. While we believe all forms of home entertainment will benefit from the current environment, the trend toward OTT and vMVPDs is likely to accelerate, particularly with the absence of live sports, as consumers look for more (and reasonably priced) entertainment options to serve the varied needs/interests of their families.
- Nielsen predicts that time spent with streaming services will increase by 60% during the current global coronavirus pandemic.
- We expect to see a surge in demand for leading SVOD services that provide robust, high quality entertainment offerings such Netflix, HBO NOW, and Disney+.
  - HBO Now has seen a 40% spike in overall viewership, led by "The Wire"—one of HBO's all-time classics.
- Similarly leading AVOD services (such as Pluto TV, Crackle, Tubi, etc.) could be significant beneficiaries as consumers look to supplement paid OTT subscriptions.
  - Many ad-supported services provide large libraries of free entertainment options and we hear that leading AVOD platforms are experiencing significant spikes in usage/engagement.
  - However, there are already signs of a decrease in advertising spending which is expected to impact AVOD services as well.

Digital Publishing

- Digital media publishers have been under intense pressure for the past several years—facing existential threats for survival not from COVID-19, but from Facebook and Google—to diversify business models, reduce dependency on social platforms, and achieve greater scale and profitability.
- Well-publicized struggles among several high-profile digital publishers, combined with limited access to growth capital (venture or PE), have provided a catalyst for consolidation across the vertical over the past several years, including multiple well-publicized distressed M&A and stock-for-stock transactions.
  - While many of the largest/best known digital publishers have made considerable progress over the past few years, most are still hovering close to break-even and remain vulnerable in the face of a potential new downturn.
  - There has been some good news, as many digital publishers such as BuzzFeed, Business Insider, and others have been reporting significant spikes in traffic and other key user metrics.
- However, if the pull-back in ad spending and long-form production persists, we believe the negative effects will more than offset the positive user trends, and there will be mounting pressure on many digital publishers (of which many were already facing liquidity constraints before the crisis).
- Further consolidation is likely over the coming 12 months (a continuation of the trend we have been seeing in the space in recent years).

What Can We Expect to See? (Cont.)

Digital Audio

- While audio/music/podcast services must compete for users time and wallet share with all other forms of home entertainment, these services represent “must have” content for many users and are relatively low-cost, if not free, entertainment options. As a result, while a certain amount of belt-tightening is to be expected over the near term (which could impact user churn), overall we expect to see limited impact from the current pandemic in this vertical—in particular for the leading B2C streaming music and podcast platforms. Some of these platforms may actually experience a surge in interest/activity as many consumers have more free time on their hands over the near term.
- B2B music providers, on the other hand, which deliver music curation and streaming services into retail, restaurants, and hospitality environments, will likely face significant headwinds as a large portion of their customer base will be effected by the mandatory business closures around the world.
  - The largest platforms, which operate under long-term contracts, may be somewhat insolated over the near term. Regardless of these contracts, many will need to provide their customers with some relief over the near term (whether by putting the service on pause or by providing a credit while businesses are not operating). As a result, we expect some tough quarters ahead within this segment.

Video Games

- It usually doesn’t take a coronavirus pandemic to force gamers to hunker down inside their homes and self-isolate for hours (or days) at a time. But “shelter in place” orders suddenly mean that the gamer lifestyle is now not only socially acceptable, but actually greatly appreciated by society at large!
- We expect leading digital games developers, publishers, and distributers will benefit from the spike in gameplay/gamer activity over the coming months and from a spike in usage/activity across the board (from casual to competitive/core gamers).
- Early results indicate video games have already seen a significant spike in usage with many people using social video game platforms to socialize and stay in touch.
  - Steam, the worlds largest video game platform is reporting record traffic and Microsoft has indicated unprecedented demand for its Xbox Live service.
  - The latest Call of Duty release, *Warzone*, attracted six million players within 24 hours and passed 30 million players in eight days since its release on March 10.

Social Media

- Social Media is providing the platform to carry much of the social conversation during a time when conventional social interaction is diminished and in many cases even prohibited.
  - Platforms like Facebook, Twitter, and Snapchat have seen significant increases in engagement on their platforms in recent weeks.
- However, the impact of COVID-19 will ripple through the advertising market, and while the large scale platforms like Google and Facebook will be able to withstand a slowdown in advertising spend, other platforms are likely to see a more material impact.
  - For example, data suggests Twitter has had a 20% decline in advertising revenue in March.
  - Platforms that depend more heavily on a specific type of content, in particular live sports (e.g., Twitter), may face even greater headwinds.

Source: Video Games Chronicle

Where Do Companies Go From Here?

Transactions are still getting done and digital media companies that are being impacted by the COVID-19 pandemic have several options to act in this fast-changing and volatile environment.

Significant Transactions Are Still Being Completed

FOX tubi

"Fox Gets Deeper Into Streaming With $440 Million Acquisition of Tubi"

- TechCrunch, March 17, 2020

SCOPELY SEIZE THE PLAY

"Mobile-Games Company Scopely Raises $200 Million"

- Variety, March 19, 2020

fuboTV | FACEBANK

"Facebank Buying fuboTV in Latest Digital Media Merger"

- Deadline, March 23, 2020

Near-Term Strategic Options for Digital Media Companies

Strategic Consolidation/M&A	▪ Strategic M&A activity/consolidation has been robust across the digital media landscape over the past few years, as media companies (large and small) look to gain scale, new (younger) audiences, IP/content, distribution channels, revenue streams, and digital/direct-to-consumer capabilities. ▪ We expect this consolidation to accelerate over the next twelve months. ▪ The current climate should also create some compelling, hard-to-resist opportunities for large, cash-rich media and tech companies to complete transactions with highly strategic companies at more reasonable valuations.
Structured Equity Financing	▪ Digital media companies that need to raise capital in the next twelve months may find the market closed from traditional funding sources, such as growth equity funds, and may need to seek tailor-made structured equity transactions from specialist funds. ▪ Firms looking to deploy capital will be seeking more downside protection while capturing a portion of future upside, utilizing more structured transaction alternatives. ▪ Features of structured equity transactions include items, such as the following: warrants, principal protection, liquidation preferences, derivative structures, anti-dilution clauses, and more.
Distressed M&A Transactions	▪ We also expect to see an increase in distressed M&A as companies start to face liquidity issues over the near term with limited access to rescue capital. ▪ Many companies will need to look for a strategic/merger partner or a white knight to address near-term cash needs and/or help them survive. ▪ Distressed M&A can either happen informally or as part of a more formal Chapter 11 process. ▪ Specialized funds focused on acquiring companies in distressed/special situations can broaden the buyer universe (beyond the typical strategic and financial buyer universe) and expand the number of potential strategic "alternatives."

Outstanding Track Record Executing Digital Media Transactions

Houlihan Lokey professionals have unparalleled experience in advising digital media companies across a wide range of transactions.

FANSIDED
a subsidiary of
meredith
has been acquired by
minute media
Sellside Advisor

Cadence13
has been acquired by
Entercom
Sellside Advisor

Zya
has been acquired by
Google
Sellside Advisor

VERTICAL NETWORKS
has been acquired by
WHISTLE
Sellside Advisor

PARCAST
PODCAST. AUDIO. RADIO. RE-IMAGINED
has been acquired by
Spotify
Sellside Advisor

WHISTLE SPORTS
$28 million financing led by
aser
Financial Advisor

sheknows media
a portfolio company of
Great Hill PARTNERS
has been acquired by
PMC
Penske Media Corporation
Sellside Advisor

GAWKER MEDIA
has sold substantially all its assets, pursuant to Section 363 of the U.S. Bankruptcy Code, to
UNIVISION
Company Advisor

PLAYNETWORK
has been acquired by
TouchTunes
A portfolio company of
SEARCHLIGHT
Sellside Advisor

Slacker RADIO
has been acquired by
LIVEXLIVE
Sellside Advisor

VIANT.
has been acquired by
Time Inc.
Sellside Advisor

WGT MEDIA
has been acquired by
TOPGOLF
Sellside Advisor

How2Media Inc, d/b/a
PANNA
has received financing from
A+E NETWORKS
Financial Advisor*

FanDuel
$275,000,000
Series E Preferred Stock
KKR
Google capital
SHAMROCK
TimeWarner
Placement Agent*

Songza
has been acquired by
Google
Financial Advisor*

VIACOM
has divested its equity stake in
Rhapsody
to
ColumbusNova
Financial Advisor*

Tombstones included herein represent transactions closed from 2014 forward.
*Selected transactions were executed by Houlihan Lokey professionals while at other firms acquired by Houlihan Lokey or by professionals from a Houlihan Lokey joint venture company.

How Houlihan Lokey Can Help

Our firm is extremely well-equipped to help our clients navigate uncertain times. We respond quickly to challenging situations and are constantly helping clients to analyze, structure, negotiate, and execute the best possible solutions from both a strategic and a financial perspective.

What We Offer

Corporate Finance

1 Mergers and Acquisitions

2 Capital Markets

Private Funds Advisory

Board Advisory Services

Financial Restructuring

Company Advisory

Financial Restructuring

3 Distressed M&A

Liability Management

Creditor Advisory

Financial and Valuation Advisory

Portfolio Valuation and Fund Advisory

Transaction Opinions

Corporate Valuation Advisory Services

Transaction Advisory Services

Real Estate Valuation and Advisory

Dispute Resolution Consulting

Mergers and Acquisitions

We are widely recognized as a leading M&A advisor to the middle market in general, and the TMT sector in particular. Our deep expertise across the sector, knowledge of the strategic landscape, and long-standing relationships with all relevant strategic and financial buyers, makes us the M&A advisor of choice for strategic transactions in the digital media industry.

Structured Equity Financing

We have a market leading private capital markets platform focused on the placement of solution-oriented capital for a wide range of financing needs. We have differentiated investor relationships and access to the key decision makers, allowing us to run a bespoke, high-touch, confidential and efficient process.

Distressed M&A

We have the largest, most experienced special situations advisory practice of any investment banking firm and are a recognized leader in achieving M&A transactions for distressed companies. Our group employs an interdisciplinary approach to engagements and is accustomed to evaluating complex, highly leveraged situations in short timeframes.

Why We're Different

- ✓ **Deep Digital Media Industry Expertise**
- ✓ **Strong Relationships With the Most Relevant Buyers**
- ✓ **Solution-Oriented Capital Markets Platform**
- ✓ **Dominant in Special Situations and Restructuring**
- ✓ **Senior-Level Commitment and Dedication**
- ✓ **Superior Work Product/Technical Abilities**
- ✓ **Creativity, Imagination, Tenacity, and Positivity**

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