Point of View – December 2011

CLEAR SCOPE PARTNERS

a Rizvi | Traverse company

www.clear-scope.com

Clear Scope Partners is pleased to provide you with this quarterly update focused on the state of the capital markets. We hope that sharing our thoughts with you will promote a healthy dialogue that will result in a mutually beneficial relationship. Please feel free to reach out to us at any time. And please visit our website at www.clear-scope.com. It will keep you updated on our current activities and focus.

OUR VIEW: 2011 in Review – Signs of a Resurgence in Capital Markets

From 2005 through 2008, the entertainment industry was flooded with approximately $16 billion of capital from Wall Street. Capital flow came to a crashing halt in 2009 with no significant deals being done during the year. In 2010 capital flow resumed with $2 billion in financings, and 2011 has seen another $2 billion worth of transactions completed, hopefully signaling stabilization. While this trend is positive and makes us optimistic about the future, the forms of capital that comprise the current total tell an interesting story.

Generally, yesterday's deals were funded using high leverage provided by commercial banks, complemented by plentiful mezzanine debt yielding low double-digit returns, with relatively modest equity checks provided by financial investors anxious to deploy capital. The 2011 deals, however, are largely recapitalizations of companies which have experienced meaningful success (e.g. Legendary, Summit, Miramax) and are debt transactions with excess proceeds providing shareholders with a return of their capital. A significant source of funding for these transactions is from a large volume of relatively inexpensive debt capital sources who lend based upon the "Known Value" (the value of receivables or ultimates for released films) verses the "Anticipated Value" (the anticipated box office and ancillary value of a portfolio of unreleased films). The institutional lenders who have once again stepped into the market are parties who may not be film specialists but make an investment decision often heavily based upon a rating provided by a third party rating agency. The emergence of these lenders is positive news for the industry and for those with Known Value but it has not provided an equal opportunity for all participants seeking capital.

Continued on next page

ABOUT CLEAR SCOPE PARTNERS

Clear Scope Partners was formed in 2009 to provide independent, thoughtful and analytical advice to those investing or operating in the entertainment and media industries. Our principals use their extensive entertainment investing, commercial banking and studio finance experience to evaluate the industry with a tangible, results oriented approach.

Our competitive distinction is that we leverage our industry experience and network of industry thought leaders to incorporate current economics and forward looking trends into investing and strategic business recommendations. Using our intimate knowledge of studios and film finance, Clear Scope Partners has developed a sophisticated proprietary film greenlight and business plan model with granular assumptions that can be tailored to meet the specific needs of each client.

We would love to hear your thoughts! Please visit us on the web or contact us directly:

Clark Hallren, Managing Partner
challren@clear-scope.com
(310) 858-2245

Rob Amir, Managing Director
ramir@clear-scope.com
(310) 858-1584

Carolyn Steinmetz, Associate
csteinmetz@clear-scope.com
(310) 858-2206

Continued: 2011 in Review – Signs of a Resurgence in Capital Markets

Additional positive indications can be observed in commercial banking practices and growth of active industry participants. The number of active lenders, which fell from a high in the mid-40's to a low of 10, is now in the mid-to-high teens as established and knowledgeable bankers have joined new banks to initiate or enhance existing practices. The risk tolerance for a majority of these players is again largely based on Know Value, with some library lending or modest production credits. The flight to conservatism in lending practices has stabilized and pricing continues to tighten and reduce for borrowers as banks address an increasingly competitive environment. However, we think it will be some time before commercial banks are again willing to lend against Anticipated Value, which would benefit new companies or those with increasing production levels.

Mezzanine debt has also reappeared in a few transactions, however expect the cost of this capital (provided mostly by funds) to be 50% higher than the former 10-12% levels. This source of capital can provide equity investors with additional leverage to enhance returns, however at current rates it is often too expensive to appeal to equity investors and there are only a handful of credible providers. A number of parties are utilizing mezzanine debt to fund a senior recoupment position in P&A financing structures as commercial banks are generally staying away from lending P&A against Anticipated Value. Generally, this capital may fund approximately 70% of P&A expenses in exchange for a mid-to-high teens interest rate, with the balance funded by equity and recouping after the repayment of the mezzanine debt. The emergence of some level of P&A funding is another positive industry development, although producers may consider the pricing steep in comparison the underlying risk profile.

Although some equity investors flush with capital are quietly exploring opportunities to secure more favorable structures under which to deploy funds, the investment terms that they are seeking include distribution fees in the low single digits, "reverse" cherry picking and caps on marketing spends. These are terms that generally have been too aggressive for studio co-financing appetites in the past; however given the capital constraints they are facing, studios are increasingly willing to discuss these points. The limited number of equity raises that are being or have been secured in 2011 were either from strategic sources (e.g. Hemisphere, Endgame, Relativity China), benefitted from tax related strategies (e.g. Grosvenor Park, Octopus' Investments), or from wealthy individuals or family offices (e.g. Skydance, Studio Canal). Inbound inquiries from institutions considering investing in the industry continue to increase and while there is a general sentiment that the industry is non-correlated to either general equity or debt markets, the general volatility in the markets has many conservative investors continuing to wait by the sidelines.

In summary, the capital markets are showing some improvement and, barring additional shocks to the system either domestically or abroad, there is a little bit of sunshine in the outlook for the coming year.

We wish you a very prosperous 2012!

Top 5 Trends in Film Financings that Improve Investor Economics

1. *Inclusion of premiere properties* – deals no longer block co-investors from participating in studios' most attractive and least risky tent pole films
2. *Lower distribution fees* – this senior expense in the waterfall more closely tracks actual distribution expenses rather than serving as an additional profit center, enhancing investors' back end profitability
3. *Gross corridors* – some deals are including a priority return to investors prior to certain fees and expenses, reducing potential capital impairment
4. *Caps on overhead and marketing costs* – protect investors from inflated costs prior to return of capital
5. *More robust call and rejection features* – deals increasingly grant co-investors greater control over what projects are included and excluded in the slate