REUTERS

Wall St dumps film deals on Hollywood investors

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By Sue Zeidler - Analysis

LOS ANGELES (Reuters) - The financial crisis is forcing Wall Street banks and hedge funds to pull out of billions of dollars worth of film deals, opening the door for specialty investors to scoop up Hollywood assets at discount prices.

From 2005 to 2008, hedge funds partnered with all the major banks from Merrill Lynch to Lehman Brothers to pump an estimated $15 billion into films, taking on risks formerly absorbed by studios like Sony (6758.T: Quote, Profile, Research, Stock Buzz) Pictures and News Corp's (NWSA.O: Quote, Profile, Research, Stock Buzz) 20th Century Fox in return for a share of profits.

Typically, investors help finance "slates" of as many as a dozen movies and collect their returns after the films are released, or start to generate DVD and television revenue, which could be years from their initial investment.

But after some box office duds, such as Tom Cruise's "Lions for Lambs," and the credit freeze, most banks with the exception of JPMorgan (JPM.N: Quote, Profile, Research, Stock Buzz) have reduced their presence in Hollywood. Some are trying to sell off their positions in slate deals for discounts of 30 percent to 70 percent.

"Because of the credit crisis, banks and hedge funds have been writing down securities, including those backed by film assets, and are willing to sell them at lower prices," said Stephen Prough, founder of Salem Partners, which advises investors on how to maximize film investments.

Prough and others cited strong interest and deep pockets for movie assets at current, reasonable prices from seasoned entertainment investors who specialize in the industry, know it well and take a longer-term view on returns.

For example, Content Partners LLC backed by Mark Cuban and Todd Wagner is a pioneer in acquiring films in the secondary market from hedge funds, private equity firms and banks.

"Not only are we buying from financial sellers but we're also looking at transactions for the first time with studios and networks for participations in TV shows and film profits," said Content Partners President Steven Kram.

"We've already purchased 34 films and over 200 hours of television. We can provide a new source of financing for studios and networks who are being squeezed for every penny."

Another investor swooping in on slates of movie deals in Hollywood is David Molner, managing director of Beverly Hills, California-based Screen Capital International.

"I'm five times as busy as I used to be. We launched a $500 million fund that is financing the acquisition of assets in studio slate deals," said Molner. "We are taking the participants in finance deals out of their capital positions in studio slate deals."

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With these deals, many studios have enough financing to make movies through 2010 and are cutting costs while waiting out the credit freeze to thaw before seeking further funding.

Nonetheless, the number of films released by major studios are expected to continue to decrease to correct an oversupplied market. Less than 200 films are slated to hit theaters in 2009, down from about 219 major studio releases in 2008 and 236 in 2007, according to industry estimates.

"There was too much money and too many films. The market couldn't sustain it and the competition was too great to provide the returns the equity and hedge funds were looking for," said PriceWaterhouseCoopers Managing Director Ron Cushey.

Some studios like The Weinstein Co and DreamWorks Studios, led by Steven Spielberg and Stacey Snider, are seeking financing.

Others like Viacom Inc's (VIAb.N: Quote, Profile, Research, Stock Buzz) Paramount ditched efforts to raise $450 million for a slate of films, and instead will co-finance on a picture-by-picture basis, after many of the big slate deals of recent years did not deliver as expected.

In some cases, investors racked up hundreds of millions of dollars in losses and complained the studios tilted terms to keep sure-fire hit movies out of the slates.

Moody's Investors Services analysts Neil Begley said about $80 million in debt tied to Paramount's so-called Melrose I slate, covering films released from 2003 to 2005, including "Get Rich or Die Tryin,'" may soon default.

"Based on the expected cash flows for the film assets, the Class A notes will not be paid in full by their legal final maturity," said Begley. Paramount declined to comment.

Bankers told Reuters that investors in Paramount's subsequent Melrose II film slate, with titles like "Blades of Glory," are now unloading their stakes.

"There are numerous film securitization deals being shopped around right now," said Ken Schapiro, managing partner at media investment firm Qualia Capital. He declined to say which deals his firm was exploring.

Other studios like Sony Pictures adjusted terms of their revenue-sharing agreements after films in a $600 million slate deal called Gun Hill Road I underperformed.

The next big round of financing for Hollywood will likely come from overseas or via deals that are backed by assets, such as film libraries, to minimize risk, bankers say.

Prough cited one situation where a studio's film assets were worth much less than the $500 million it had raised in a private equity financing. "Eventually, they either have to find new money to keep going or sell the assets to get investors their money back," he said.

Independent film and television studio Lions Gate Entertainment Corp (LGF.N: Quote, Profile, Research, Stock Buzz) has attracted interest from activist investor Carl Icahn, who raised his stake in the company to 14.28 percent even after it reported disappointing earnings and underperforming films.

Molner, Schapiro and Prough all said film assets generate good returns over the long term.

"The good thing about investing in film is that you have an asset that continues to generate revenue on pay TV, free TV and in every country around the world," Schapiro said.

(Reporting by Sue Zeidler, editing by Tiffany Wu, Richard Chang)