Private Equity Money Picks Hollywood as Smart Bet Even in Downturn

Despite fears of a recession, investment firms view star-driven production banners (and major soundstages) as a long-term play in a crowded content marketplace.

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Hollywood executives may be worried about a cooling in content spending, but the smart money doesn't seem to be. Even though companies like Netflix, Warner Bros. Discovery and Disney have indicated that they will be more prudent with their content investments, private equity firms are continuing to invest in entertainment assets at a torrid pace. And while some in the space warn that macroeconomic factors could see things cool down, for now at least, the dealmaking keeps up.

Consider that The North Road Co., Peter Chernin's production roll-up, is being financed by $500million from Providence Equity Partners and $300million in debt from Apollo through its managed affiliates. Chernin tells *The Hollywood Reporter* that he is now in the market for further acquisitions, leveraging the private equity cash to buy "pure-play" companies that focus solely on creating content.

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North Road is just one of many ventures that private financial firms are making plays for in the media and entertainment sector, betting on a long runway for growth. Candle Media, another content roll-up led by former Disney execs Tom Staggs and Kevin Mayer, has a multibillion-dollar war chest from Blackstone. Candle, like North Road, continues to survey the market for buying opportunities. SpringHill, the content venture from LeBron James and Maverick Carter, raised cash in late 2021 from a slate of investors that included RedBird Capital. And in June, Shamrock Capital invested $50million into Religion of Sports, the studio co-founded by Gotham Chopra, Tom Brady and Michael Strahan.

"Unlike TV or cable, today's streaming platforms do not have slots or limitations to how much content that they can hold," Shamrock partner Andy Howard says. "Therefore, content is king, and especially premium content. This is why we, in particular, invested in Religion of Sports and you see other PE firms trying to do the same. Iconic talent and brands that have an embedded following already have a leg up as they will not require the same marketing dollars to get it noticed in a very crowded marketplace."

Chernin says that consolidation has made third-party content providers even more valuable, with Disney, Warner Bros. and Fox either disappearing (in the case of Fox's entertainment assets, now owned by Disney) or increasingly producing only for their own platforms.

"While the world of content spending is increasing, the traditional larger suppliers are going away," Chernin says. "I think it creates more opportunities for us because there is more and more need for this stuff and the number of suppliers is dwindling."

He particularly calls out two needs in the content space: International programming and unscripted, with international a necessity for any service seeking a global presence and unscripted because of its lower cost compared with scripted fare. And while some in Hollywood have expressed concern over there being too much content already, the firms investing in the space clearly disagree. "Obviously, both Apollo and Providence believed in us, too, or they wouldn't have invested behind us," Chernin adds.

Alongside the investment in content, many private equity firms also are buying the infrastructure used in the production of films and TV shows, betting that with more and more projects being developed, the demand for studio space will only increase. And so, investment in the acquisition, construction and expansion of soundstages by private equity is booming.

"Historically, you had more episodic production, which led to more lulls in occupancy," says Peter Rumbold, director of Shadowbox Studios and head of real estate at Commonwealth Asset Management. "Now, with the sort of unbelievably strong secular nature of the demand for new content, that's led to significant increases in the production of that content, which has led to a significant imbalance in the demand for and supply of soundstages in the global productionhub."

After a year that saw investments in commercial properties affected by remote-work chill, private equity turned even more of its attention to Hollywood. In June, private equity firm Silver Lake led a $500million investment to more than double the size of Shadowbox Studios' (formerly Blackhall Studios) Atlanta facility and support development projects in Los Angeles and London. The expansion, part of a $1.5billion capital investment plan, will add 1.2million square feet and 22 new soundstages to the Atlanta location, making it one of the biggest production facilities in Georgia and in the South. Private equity firm Commonwealth in April 2021 purchased Shadowbox, one of Georgia's largest production companies, for $120million.

Additionally, Blackstone and Hudson Pacific Properties revealed in July 2021 plans to invest up to $190million to develop a 240,000-square-foot production studio that would be the first new large-scale production studio facility built in the Los Angeles area in more than 20 years. Hackman Capital, among the largest independent owners of production space, has acquired 19 studio facilities since 2014, including the purchase in January2021 of the Sony Pictures Animation campus for $160million. The firm, which has built up a portfolio of $3.8billion in studio investments in just the past three years, also has roughly 90 stages under construction.

"We're seeing demand so high and supply of infrastructure so low in comparison that you have attention being brought on to studio acquisition, development and expansion," says Jason Hariton, chief real estate officer for the MBS Group, a division of Hackman Capital.

But there are challenges that threaten to slow down dealmaking, even if the rainmakers themselves remain interested in the sector. Sources in the finance space point to two variables of concern: fast-rising interest rates and a potential economic downturn, each of which could throw a wrench into investment plans. The Federal Reserve has been aggressively hiking interest rates this year (in June, it raised rates by 75 basis points, and there are indications that another big hike is coming this month), and that steady rise could cool interest in debt financing, which has become a staple of VC and PE investing in recent years.

Meanwhile, a downturn could force firms to take a close look at their valuations. For companies that don't necessarily need the capital and are selling minority stakes, the lower valuations justified by the current market may not meet expectations, leading some founders to wait things out until conditions improve.

"It takes a while for sellers or potential sellers to recognize the new environment," Liberty Media CEO Greg Maffei told CNBC on July8 from Allen & Co.'s Sun Valley Conference. "Potential buyers are much more quick to say, 'See, things are down.'"

Of course, a downturn also could bring opportunities of its own. Even if private entertainment and production companies get spooked by low valuations, the public markets could provide their own opportunities. Could, for example, Lionsgate be in play once it completes its spinoff of Starz?

"This is the first time in a very long time, five years at least, where there are real opportunities in the public markets," IAC CEO Joey Levin told CNBC on July7 from Sun Valley. "The mathdidn't work for us for a while to buy a growing business with a lot of upside because all the upside was priced in, but the execution wasn't there yet."

For firms spending big to gobble up content and production firms, it could lead to bargains that are hard to pass up.

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