Operational Finance in Entertainment

A Best Practices Guide for Competitive Mid-Level Entertainment Studios

8020 CONSULTING

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It's not easy to compete as a mid-level studio. Entertainment is a competitive and specialized space, with many variables that make it distinct from other industries.

By implementing the practices outlined in this guide, you can make your studio more competitive and more agile, while leveraging data better to improve your decision-making.

As financial consultants to a variety of clients in the entertainment industry, we know it's not always possible to control external factors, such as other studios, technological advances, or international trends — but you can control what happens internally. By addressing how your studio operates, and how it could better function as a whole, you can build a more competitive enterprise.

This guide includes four best practices that mid-sized studios need to follow in order to gain a competitive edge. We've framed them simply, so they're easy to remember:

1. **Define Your Goal**
2. **Pick Your Lane**
3. **Take Advantage of Your Size**
4. **Focus on Communication and Accuracy**

We'll dig into more detail in each of the following chapters. ***Let's get started!***

BEST PRACTICE 1: DEFINE YOUR GOAL

First, start with a clear definition of your organizational goals. Detailing your ideal outcome helps you define the strategies needed to get there. We've found our entertainment clients see the most success when they focus on *one of three primary goals*: Go for Growth, Build for Acquisition, Focus on Efficiency.

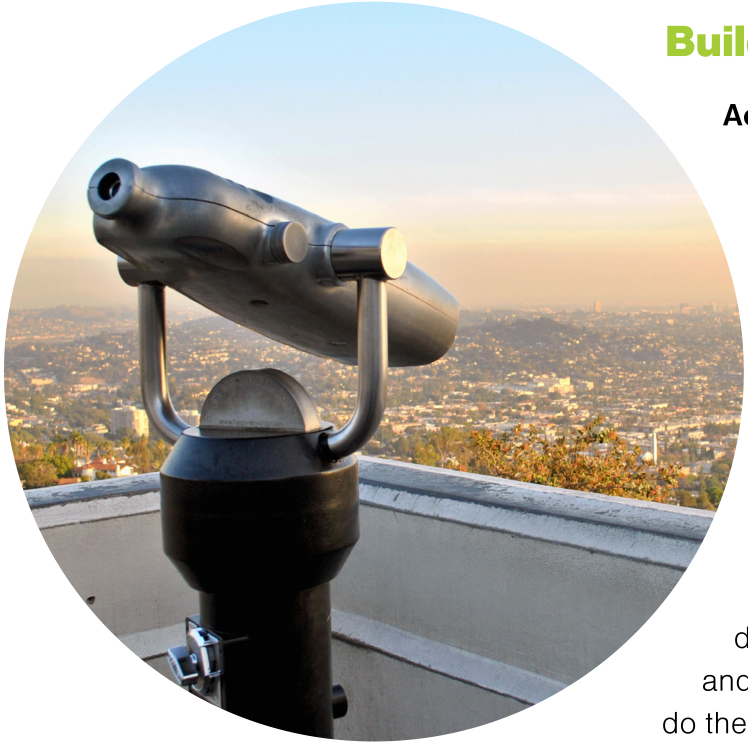
Go for Growth

If you want to grow, you need to present yourself as an expert in a specific space. Some mid-level studios specialize in producing original content, others work as outsourced content partners, and still others focus on distribution. No matter what your specialty, you must build the type of expertise that industry leaders will reference and acknowledge in order to be seen as a growing studio.

In the most basic terms, growth requires team buy-in on the answers to these questions:

- **What do you offer the industry?** What are the studio's strongest capabilities and areas of expertise? It could be that your studio builds portfolios of a type of programming, or the studio is seen as an outsourced resource for a major studio, for example.
- **What sets your studio apart?** Has your studio won international awards at renowned film festivals? Established a strong reputation in trade publications? Define strengths to create an identity that projects a distinct competitive advantage that your studio can "own."
- **How can you capitalize on your studios' competitive advantage?** For a content producer, this could mean putting more boots on the ground at festivals, submitting more films, or taking a more active role in showcasing. For a distributor, it could mean increasing dialogue with sellers and expanding your networks. If you're not sure what to capitalize on, revisit your recent successes. If your properties had big wins or won awards, you might start there. If you secured a big client or on-boarded a big talent, then that might be your focus.

Build for Acquisition



Acquisition can be a viable and lucrative strategy in the fast-moving entertainment industry. Consider these scenarios, each of which could be attractive for a bigger studio considering an acquisition:

- **You produce great content, and you're positioned as a key partner with major studios.** Big studios are more likely to buy than build.

- **You build diverse, engaged audiences in a specific target market.** If you own a target market, like Millennials or women — and can show it — then it's likely a big studio will pay attention. An interested buyer will want to see whether you own a diverse set of properties, how you're reaching the main audience, and, if your content attracts other audiences, what level of engagement do these audiences have with that content.

- **You patented software that delivers content to audiences, or you've created a disruptive distribution model.** Do you have a patent for a particular algorithm? Have you created a system that adds to the quality of production? Have you created a system that improves the value chain or removes manual processes, such as software that can invoice studios directly or an inventory system that monitors quality production? Software licensing and/or acquisition are viable ways to add to your studio's revenue stream.

Focus on Efficiency

Another option is to focus on building a lean and agile studio. Studios with this goal in mind set targets, such as minimizing costs without sacrificing quality, optimizing reporting tools to manage financial resources, or training talent and encouraging innovation. If your studio has creativity down to a science but struggles with financials, it makes sense to bring in operational finance specialists to help minimize spend and maximize decision making.

At **8020 Consulting**, for example, our work impacts every aspect of business operations — extending the reach of finance from compliance fulfillment reporting and incremental budgeting activity to critical analysis of business issues. We can help establish best practices, set benchmarks, and recommend and implement new technologies you might not be aware of.

Once your studio is aligned and focused on the goal, next steps are to set quarterly and annual financial targets for your organization. You should also look to utilize financial models and operations software to quantify key metrics and track progress.

Most importantly, you'll want to effectively communicate the goal internally, so all departments and stakeholders are aligned and on board. Involving the whole team now will improve your ability to make informed decisions later. As you roll out the strategy to achieve your goal, your ability to communicate up and down the chain of command will be critical to your success. (More on that later.)

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If you need help with operational finance, 8020 Consulting can help.
Contact us *for more information.*

BEST PRACTICE 2: PICK YOUR LANE

The digital era has leveled the playing field, so competitive mid-size studios pick a lane and own it to beat the competition. Picking your lane helps you target your customers and exceed their needs, and it makes it much easier to define your studio's points of differentiation.

Picking a lane involves asking a lot of questions, such as:

- **How diverse is our film/TV portfolio?** Great portfolios aren't defined by size as much as by diversity and thoughtfulness. You should have a rhyme and reason to your portfolio, and your properties should complement, not compete with, one another. It's effective to focus on genre and avoid producing every opportunity that arises. Knowing how genres travel is important too. For example:

    - o Drama travels well across the globe.
    - o Comedy is subjective and requires a universal understanding to travel.
    - o TV Series need engaging, intimately relatable characters to succeed internationally.

- **Who are our key domestic and international partnerships?** Look closely at whom you're working with, and what type of exposure they have (i.e., their relationships with studios). Competitive studios keep track of their options and opportunities, so they can take advantage of them when the time is right.

- **How empowered are our key players to make quick business decisions?** At the mid-studio level, agility is a competitive edge. Ideally, your players can place a bid almost immediately at film festivals or other competitive markets. To accomplish that, communication with the finance function is important, both in terms of accessibility and the quality of their financial modeling. How many scenarios can you run through their models, and how accurate are they?

- **Who is our target audience?** Don't cast too big of a net. You must define your portfolio and know exactly how your portfolio will appeal to a specific audience. Say, for example, your audience is moms. Your portfolio might include Cooking (for the moms) and Animation (for their kids) properties. You must be cognizant of how properties complement each other in your portfolio. Big studios often go to a midsized studio, buy its portfolio, and then distribute it (or even co-produce).

- **Is growth or acquisition the main goal?** If so, steer away from niche content, which attracts small audiences and is often timely. (An example might be skateboarding content.) Rather, strive for specialty content, which is focused, but attracts a wider audience with a common interest. (An example might be cooking content.)

  Big studios are looking for partners with universal stories that speak to target demographics in a variety of properties. They're not looking for portfolios that are limited to one small storyline or a niche market such as Westerns (which is usually too localized), Docu-series (unless it's a global name like *Cobain*, or *The Defiant Ones*), or Horror (which doesn't carry well unless you're well-established).

By narrowing their focus, competitive studios build stronger portfolios, hone their expertise, and recruit more effectively. Focusing also empowers better financial modeling. Rather than trying to focus on building a breadth of financial models, competitive studios focus on depth by creating and maintaining a smaller set of robust models with insightful layers they can add or take away to analyze key business decisions.

Some of these layers include marketing comparisons, which can be more robust if you've built a thoughtful, targeted portfolio and collected historical data. How did prior films with similar storylines and similar talent perform? What are your best-case, base-case, and high-case scenarios?

Being able to leverage rational insights is extremely important in the entertainment industry. There's always a margin of error (standard deviation seems somewhere around 20 percent), so having clear and historical insights can dramatically improve your decision-making. The diversity of your portfolio can also help mitigate risk. Diversity will guard against the low-performing blockbuster or mitigate the desperation of looking for a high-performing underdog.

BEST PRACTICE 3: TAKE ADVANTAGE OF YOUR SIZE

Somewhat ironically, mid-size studios have more room to be effective. They can pivot, make decisions quickly, and can outmatch bigger studios in terms of flexibility and speed (like when making a bid at a major film festival). Big studios come with a lot of hierarchy and established structure. They have more silos in which employees juggle the realities of reporting to different levels and needs, and it's common across silos that no one is really speaking the same language.

Size can also result in more flexibility in pursuing properties for your portfolio. The bigger studios are generally limited to franchise productions with very little deviation — they're much more rigid in their approach. Alternatively, mid-size studios can pursue relatable passion projects that capture an audience, like *Slumdog Millionaire* or *Million Dollar Baby* (two big wins for smaller studios).

Big studios may often take up to a week or longer to formally bid on a project. A competitive midsized studio can pull the trigger much more quickly. But there's less cash on hand, so cash flow and net present value (NPV) models can be valuable tools. Your models should be agile, robust, and have assumptions pages that allow your employees to quickly make changes and see adjusted NPV. Having these tools handy can help them move quickly and facilitate bidding by providing instant feedback. It's an immediate safety net for your team.

Some other best practice strategies for midsized studies are:

- **Establish relationships with key vendors to have early insights into upcoming products.** This is a must do, no matter which side of the table you're sitting on. If you're on the distribution side, you might get a sneak peek before the seller comes to the festival, or they might give you the first chance to make a bid. If you're on the production side, you might pair with another producer to co-produce a mutually beneficial property. You should manage your relationships to result in more money and easier cash flow.

- **Partner with other production houses to mitigate financial risks.** Co-producing with smaller shops can help in this regard. If you're not clear on how to mitigate risk, then an operational finance consultant can help. Just make sure to define how much you can risk, your studio's willingness to invest, and what you'll accept in terms of ownership. 8020 often consults with studios to:

    - o Put together the deal analysis or participation schedules.
    - o Put numbers to options, with milestones to increase decision-making confidence.
    - o Create Cash Flow and NPV models that provide instant feedback and facilitate bidding.
    - o Provide low and high best-case mode, i.e., define what would be the different participation payouts, how much should your studio invest to play this game.

BEST PRACTICE 4: FOCUS ON COMMUNICATION AND ACCURACY

Mid-size studios don't have as much rampant hierarchy or siloing as big studios, so they face much less complexity in terms of updating or reining in cross-company communications or processes. By establishing systems and processes now, your studio will be better positioned to achieve its future goals.

For many studios, departments such as marketing, distribution, finance, and corporate operate almost independently, which results in mismatched forecasting approaches and reporting standards. They may even base their assumptions on different datasets or outmoded formulas. (No one should have to use a home vs. international box office returns model that hasn't been updated in five years.) Without a focus on operational consistency, studios will have a difficult time making decisions and scaling.

From a competitive standpoint, communication and accuracy offer a powerful advantage. A midsized studio that communicates effectively, maintains usable data, and reports in a standardized way is positioned to outmatch its competitors in terms of decision-making, flexibility, and growth.

It's important to note that you don't have to figure out best practices on your own. A good operational finance firm like 8020 Consulting can help you establish rules and processes for reporting and build financial presence and understanding across departments.

SUMMARY

To recap, we believe that these four best practices can make you more competitive as a midsized entertainment studio:

1. Define Your Goal
2. Pick Your Lane
3. Take Advantage of Your Size
4. Focus on Communication and Accuracy

While at first glance they seem simple, these best practices center on optimizing how your studio operates. Only then can you make strides toward your goals and improve your position among your competition. If you build a culture centered on operational finance, everyone can work more efficiently, effectively, and purposefully.

If you need help with operational finance, **8020 Consulting** can help. Our entire team is on the ground in Los Angeles, and we have deep knowledge of the entertainment industry.

ABOUT 8020 CONSULTING

While as a firm we are industry agnostic, we have deep experience in entertainment, media, emerging growth and technology, real estate, and consumer products. Some of the services we provide studios are:

- Executive Board Packs and Dashboards (Historical and Future Trend)
- Financial Modeling in Support of New Lines of Business or Optimization of Existing Distribution Outlets
- Sophisticated Green Light Models
- Ultimates Evaluation, Modeling and Enhancements
- Existing Systems Synchronization (Efficient Data Mining)
- Overhead Management Optimization
- Cash Flow Statement Preparation
- Participations, Royalties, and Contract Review and Analysis
- Participation Reports Preparation (What's Paid Out After a Film is Produced)
- Amortization Schedules Preparation With Accounting Principles Updates (e.g., New Revenue Recognition Laws, Incorporation)
- Expert-Level Excel Optimization Support
- Interim FP&A and Accounting Support for Critical Roles During Times of Transition
- Production Finance Support and Modeling

To learn more about our services, you can contact us here.

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Let's Get Started!