2013 Deal insights for the Entertainment, Media and Communications industries

2013 Outlook & Analysis of 2012 US deal activity

April 2013

A publication from PwC's Deals practice

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Introduction
Content consumption changes drive M&A activity

During 2012, we saw headline-grabbing, high-profile transactions in the Entertainment, Media & Communications (EMC) industry, and 2013 is shaping up to be no different with the announcement of several billion-dollar deals in the first quarter of 2013. But beyond the headlines, we see fundamental changes happening at companies of all sizes, across several EMC sub-sectors. On the following pages we've identified five key themes that we think will be prevalent for the remainder of 2013.

PwC's extensive knowledge and experience in this evolving sector has helped keep us on the front lines of M&A activity.

Additionally, we're seeing more and more companies continue to assess their portfolios and divest non-core assets as part of their go-forward strategy. Recognizing the challenges inherent with these divestitures, we've provided a brief synopsis highlighting the five critical components of driving divestiture success in a Spotlight Article within this publication.

We hope you find this publication helpful as you evaluate the current and forecasted EMC deal environment. PwC's extensive knowledge and experience in this evolving sector has helped keep us on the front lines of M&A activity. I invite you to contact me, or any of my colleagues listed at the back of this report, with your comments or if you would like to discuss in greater detail any of the topics covered.

Best regards,

Bart Spiegel
Partner,
Entertainment, Media and Communications Deals Practice

2013 Outlook
Five key themes

Today's changing EMC landscape requires market players to make investments to keep up with consumer demand for more bandwidth and new content and delivery models; this is being accomplished through M&A and other partnerships and joint ventures.

Content creators (e.g., film & TV studios, independent production companies) and advertisers are well aware that today's consuming public demands an enriched media experience, regardless of the time of day, device, or physical location. Content aggregators (e.g., broadcast and cable networks), content distributors (e.g., multiple system operators "MSOs"), smart device manufacturers, and their supporting communications companies must be able to meet consumption and broadband demands to remain relevant in today's landscape of immediate, high-quality access and delivery. EMC companies continue to recognize this as part of their broader growth strategy with targeted mergers & acquisitions (M&A), partnerships, and joint ventures serving these criteria.

With the constantly evolving EMC landscape, we believe 2013 deal activity will continue to be active, as evidenced by announced deals to date, and expect M&A strategy to center around the following five themes:

Theme #1: Consumer demand for bandwidth drives need for spectrum

The Communications industry is expected to experience continued consolidation in 2013, primarily driven by the growing consumer demand for bandwidth to support content consumption, social collaboration, location-based services, and other offerings. According to the February 2013 Cisco Visual Networking Index Report, global mobile data traffic is expected to grow 13-fold between 2012 and 2017, which has already resulted in acute spectrum shortages to date. Carriers are searching for additional spectrum to leverage exponential growth in data traffic—much of which is being driven by entertainment and media content consumption. In the United States, both the Federal Communications Commission (FCC) and Congress have been slow in releasing additional spectrum.

Although the FCC has recently decided to provide additional spectrum through incentive actions and spectrum sharing beginning in 2014, the process is expected to take time. In an increasingly saturated US market with limited spectrum options, operators are taking the M&A route to garner additional spectrum, geographical coverage, subscribers, and more robust product and service portfolios. For example, in January 2013, AT&T announced two deals worth more than $2.7 billion in an effort to expand its wireless spectrum holdings to increase its suite of high-speed services.

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Among other issues associated with wireless acquisitions, the valuation of spectrum poses several unique challenges. The unique characteristics of a given spectrum block, as well as the regulatory environment, must be considered in establishing a reasonable price.

Identified business opportunities—Choosing the right acquisition strategy

In order to strengthen competitive positioning, wireless operators should define their long-term spectrum acquisition strategy and quickly begin executing to avoid getting caught between spectrum scarcity and industry consolidation. We have identified four key elements operators should consider in defining this strategy:

1) Intrinsic properties of the target spectrum band, such as population coverage, propagation characteristics, and the state of product ecosystem development

2) Target band's fit with the operator's own strategic plans, including device strategy, network evolution plans, existing spectrum holdings, and outlook for additional spectrum acquisition

3) Long-term technology evolution outlook, including enhancements like carrier aggregation technology that allows 'stitching' of disparate spectrum bands and software-defined antennas that enable handsets to support a much higher number of spectrum bands

4) Regulatory outlook such as build-out requirements and the prognosis for new spectrum auctions and antitrust regime for spectrum holdings. In doing so, operators can create a lasting cost advantage for themselves by balancing these short- and long-term trends in their spectrum acquisition and deployment strategy.

Theme #2: The race for content

The long-standing relationships between content aggregators and distributors have been disrupted by the shift to digital; the availability of content anywhere, anytime (i.e., TV everywhere); and over-the-top (OTT) providers (e.g., Netflix, iTunes). Consumer expectations surrounding ubiquitous viewing experiences require distributors to offer more premium and library content than ever. The race is on to license and/or acquire content and to develop/maintain customer relationships. This shift has EMC companies fighting for consumers' time and money and strategizing on the most efficient way to acquire and monetize content.

The demand for content continues to increase valuations for content creators and companies with established content libraries and intellectual property (IP) rights available for franchising, licensing, and IP expansion (e.g., Disney's recent acquisition of Lucasfilm for approximately $4.1 billion). Even certain OTT providers have come to recognize the value ascribed to successful, original content and have made investments in new content and distribution windows (e.g., releasing all episodes in a season concurrently) on their end, such as Netflix's "House of Cards," which, according to some reports, cost over $100 million for the initial two seasons.

As content creators bring their companies to market, potential buyers are looking for a level of security on prospective cash flows. This may hinge on keeping the existing development team motivated post-transaction to replicate past successes. It's not uncommon for earn-outs, contingent payments, contingent value rights, non-competes, and put/calls to be integrated into the sales terms to help bridge any value gap and retain top talent. Understanding the financial implications and how these structures are reflected in prospective financial results is an important consideration for many companies.

Identified business opportunities—Content management systems

Sophisticated content management systems are critical to organizing, analyzing, and effectively monetizing intellectual property rights. To be competitive in today's fast-changing, global environment, companies need an integrated content rights management system as well as dynamic analytics, not only to operate more effectively but to take advantage of new distribution opportunities. Companies with robust content management systems in place will have the ability to make real-time decisions based on substantiated analytics and are able to grow and/or create incremental revenue or entirely new revenue streams, such as with the second screen (e.g., iPads).

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Theme #3: Looking abroad—Cross-border M&A

The demand for content has fueled M&A activity both domestically and internationally. As US and foreign market players (both content creators and content aggregators) seek to fill the necessary demand for content, they're looking not only in local markets, but also in international markets for quality content to fulfill demand. This was evident in 2012 as several international broadcasters invested in US-based production companies. We expect to see continued inbound interest in US-based content as well as US companies looking overseas for similar assets.

In the broadcasting segment, given that the domestic television and cable broadcasting markets are dominated by established market participants, the international markets are becoming an attractive opportunity for US networks to expand their footprint via M&A or collaborative partnering. We've seen this from Discovery Communications as they completed several international acquisitions in 2012 alone, including Dubai (Takhayal Entertainment) and Scandinavia (SBS Nordic). Although cross-border transactions may prove to be challenging, the appetite for potentially lucrative markets still exists. Those markets with strong GDP and entertainment and media consumption growth forecasts and relatively young populations are likely to be attractive targets (e.g., Turkey, Poland, Russia, and India).

Additionally, for those vertically integrated companies with both content and distribution, this allows another outlet to monetize their library and formats for international consumers.

On the Communications front, cross-border M&A will likely be driven by several factors, including portfolio reshuffling, product portfolio expansion, and geographic market expansion due to the softening global regulatory environments and the opening of emerging markets to foreign investments. We expect inbound M&A interest to continue in 2013 as the US communications industry is among the most advanced

markets in terms of: 1) communication services and profitable subscribers, 2) exponential growth in demand for smartphones and tablets, and 3) high demand for data services. This is drawing the attention of many foreign players who are looking to invest in markets that produce higher subscriber margins. Recent cross-border deals include Softbank's acquisition of Sprint Nextel for over $20 billion.

Identified business opportunities—Key EMC territories poised for growth

In our Global Entertainment and Media Outlook 2015, we forecast investment in emerging markets will in part power global entertainment and media revenue growth which we estimated at 5.7% compounded annual growth rate (CAGR) between 2011 and 2015. For example, entertainment and media spending in the BRIC countries is estimated at 11.7% CAGR (Brazil 11.4%, Russia 11.7%, India 13.0%, and China 11.6%). Other emerging countries, such as Turkey, will also enjoy a healthy five-year growth rate estimated at 13.2% CAGR. To illustrate these trends, we focus on the outlook of three countries:

China will continue to be an attractive market for digital entertainment and media content due in part to an expected surge in online users, estimated at 750 million by 2015. Much of the expected growth is attributable to Internet access growth (wired and mobile) at 12.1%. However, investors should be aware China's population is aging dramatically—18.3% growth in the 45+ age group versus declines in the 6–44 age group. As media usage shifts from print to the Internet, advertising shifts too. PwC expects Internet advertising to grow at 32.1% CAGR in China.

Brazil's political and economic environment will bolster investor confidence in this country's high-performing companies. Brazil's highly stable government gives it a low political risk score that is comparable to mature countries such as the United States, Japan, and France. Entertainment and media spending is forecast at 11.4% CAGR, driven in part by TV subscriptions and Internet access at 16% CAGR, each with more than $10 billion in revenue.

Turkey presents an interesting opportunity for growth with its geographic placement as a gateway to Europe, Asia, or the Middle East. Research shows Turkey's 75 million inhabitants have a per capita income 2x higher than China and 4x higher than India. GDP is expected to grow 5% per annum (2013–2016), and we predict a 13% CAGR on entertainment and media revenue through 2015. Much of this expected growth is attributed to Internet access growth at 22% CAGR and Internet advertising (mobile and wired) at 18% CAGR.

Theme #4: Non-core divestitures

We expect companies to monetize their investments and exit non-core assets as a means to improve liquidity, increase profitability, and allocate capital to those business units that best reflect their go-forward strategy. This scenario is especially prevalent in the publishing sub-sector of EMC, as these companies have been most impacted by the shift to digital consumption. Recent reports of potential divestitures include Time Warner and Tribune, among others. We expect divestitures to be primary contributors to deal value in 2013, especially in the publishing space, with several rumored and reported transactions announced during the first quarter of 2013.

Divestitures are inherently complex to execute, which makes it challenging to preserve value across the lifecycle of a transaction. A key component of the divestiture process is preparing the business for operational separation. This involves considering a multitude of factors, including a detailed divestiture workplan, transition service agreements, stranded costs, separation accounting/discontinued operations, and multi-functional (tax, HR, IT, finance, etc.) separation implications. Satisfactorily addressing these factors in advance of a transaction may require a significant level of investment and commitment by the existing management team at a time when maintaining the ongoing operating results of the business is most significant. Our spotlight article "The five critical components to driving divestiture success" is on page 16.

2013 Outlook *(continued)*
Five key themes

Theme #5: Digital delivery—Blurring the line between Technology and EMC companies

Technology companies continue to change the media landscape and the method by which all content is consumed. This complicates existing business models and offers the possibility of creating new revenue streams such as downloadable content, micro-transactions, and other advertising opportunities. Apple and Google both have made significant investments to change the way we consume content. For example, Apple's iTunes continues to grow and allows consumers immediate access to content that can be consumed on multiple devices.

Efforts are under way to standardize and monetize new metrics, and the industry awaits this great opportunity to generate incremental revenue.

At the same time, many traditional EMC companies are experimenting with new direct-to-consumer digital distribution models. The media landscape is changing rapidly in terms of how content is found, accessed, consumed, and stored. New revenue streams are also being created, such as fees for storing content in the cloud, micro-transactions in online environments, and addressable advertising opportunities. We expect Technology companies to continue to invest in the EMC sector and serve as a catalyst to how we consume content.

With the proliferation of diverse platforms and technologies, measures are more accountable, transparent, and real-time. More digital metrics now exist, and they provide unprecedented visibility. But many companies are just learning to generate real value from big data and are still collecting and mining only the most basic of information. Efforts are under way, however, to standardize and monetize new metrics, and the industry awaits this great opportunity to generate incremental revenue.

2013 Outlook conclusion

As companies search for their position in the digital value chain and how to maximize their digital strategies, they continue to adapt to the accelerated pace of change in consumer behavior. This pace of change and shifting EMC landscape helps drive M&A, partnerships, and joint ventures, which should contribute to continued deal activity in the EMC sector. According to PwC's 16th Annual Global CEO Survey, Communications CEOs are "ahead of the pack" when it comes to M&A—as 53% have entered into a strategic alliance or joint venture in the last 12 months, compared with the overall sample average of just 36%. The survey also highlights that CEOs in entertainment and media, more than any other sector, anticipate bringing new products or services to market—38% versus 25% across all industries—in a combination of organic and acquisition growth domestically and internationally. CEOs are confident about their companies' prospects for growth and will continue doing deals to capture and maximize opportunities in this fast-changing landscape.

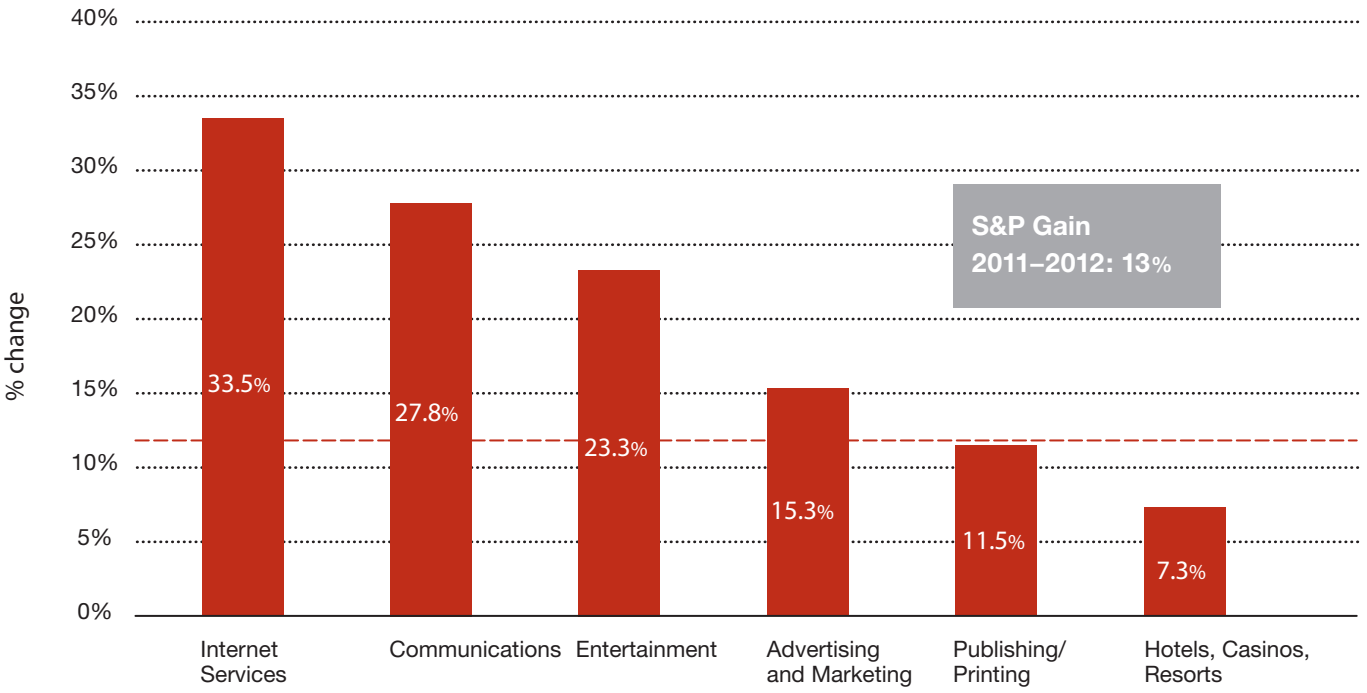
Current capital environment

Strong corporate balance sheets, available credit, and stock performance

With strong corporate balance sheets in terms of both cash reserves and stock appreciation, strategic investors have the necessary capital to seek out attractive vertical or horizontal targets. As of December 31, 2012, the Fortune 500 EMC companies had approximately $110 billion in cash and cash equivalents based on their public filings. At the same time, the availability of attractively priced credit and approximately $1 trillion in capital for private equity has allowed financial players to compete in the current market. Financial buyers have been active across many EMC sectors, including Cable, Broadcasting, and Publishing. If the debt markets remain strong going forward, expect financial buyers to continue to compete with corporate acquirers in sectors with strong growth and/or cash flow generation potential.

In addition to the cash reserves at the Fortune 500 EMC companies, their average stock price growth was 22% from December 2011 to December 2012 compared with a 13% growth for the S&P 500 in the same period.

Fortune 500 EMC Stock Performance 2011–2012



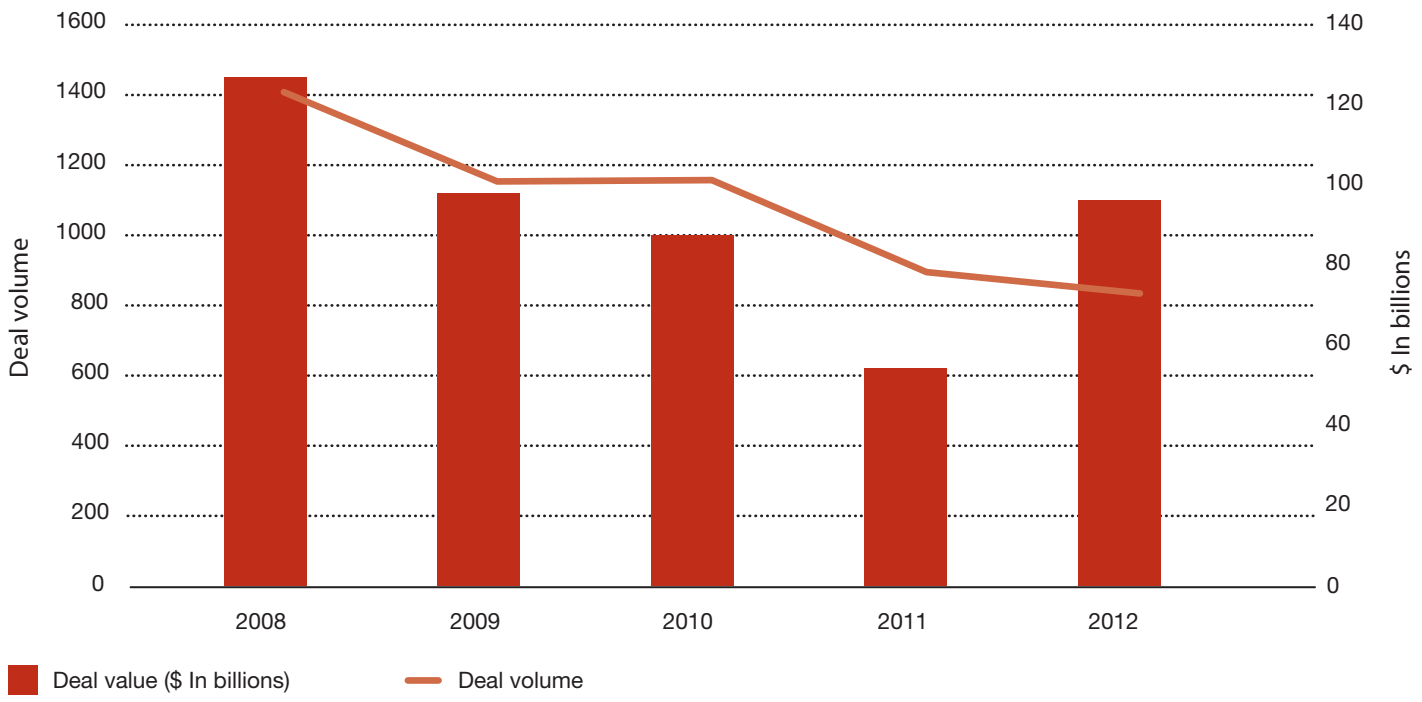
Source: SEC Public Filings

2012 by the numbers
Overall deal activity

After three consecutive years of declining deal values across the EMC sectors, 2012 saw a return to a more robust deal environment.

EMC announced deal volumes declined from 931 to 839 from 2011 to 2012, respectively; however, announced deal value increased from $55.0 billion in 2011 to $96.2 billion in 2012, led by the Softbank/Sprint Nextel deal of $20.1 billion.

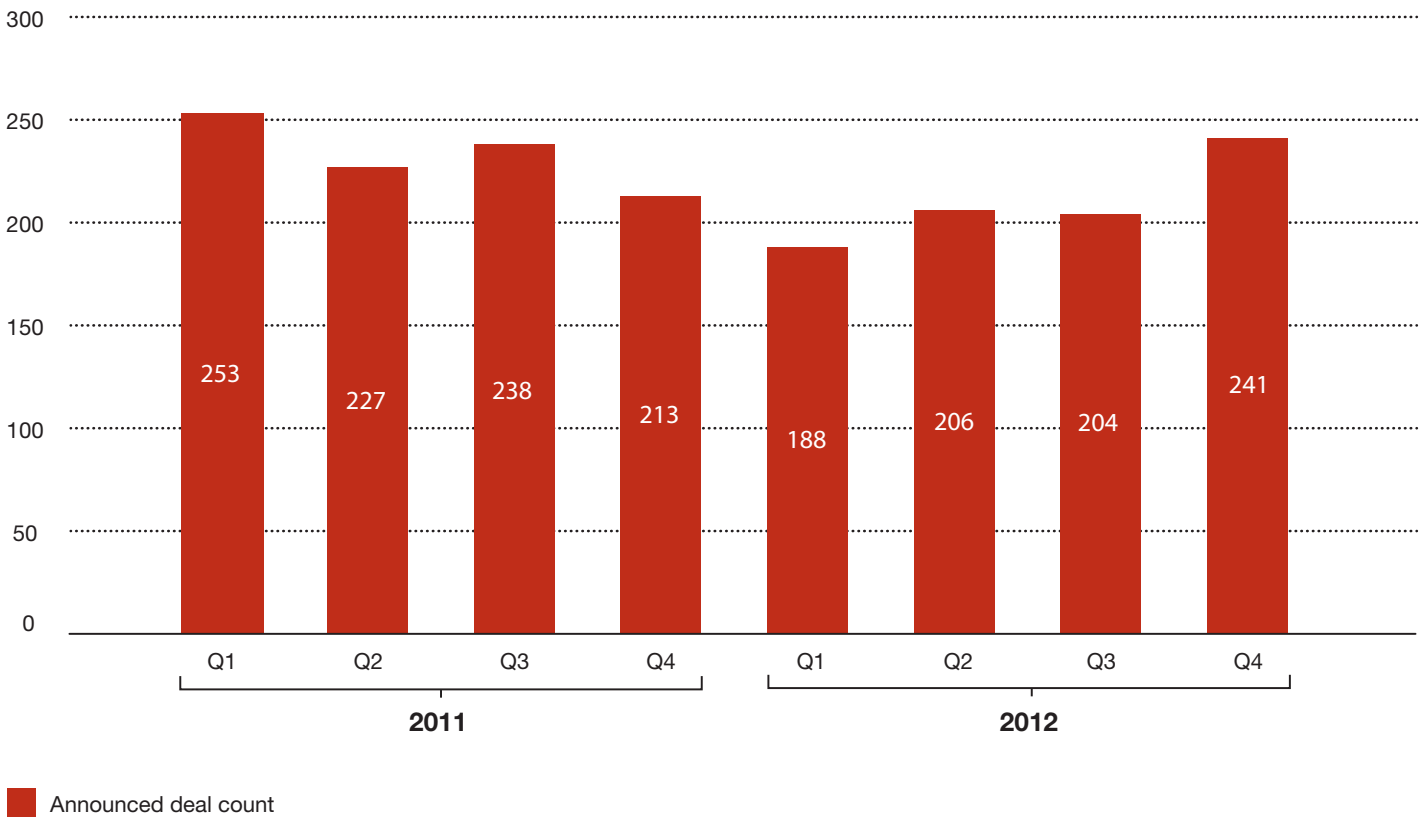
US EMC announced deals



Source: Thomson Reuters

While quarterly volumes declined in 2012 versus the comparable quarters in 2011, Q4 2012 had the highest deal activity compared to the prior six quarters. We believe this was partially driven by uncertainty in the outcome of the recent "fiscal cliff" negotiations with respect to future corporate and personal income tax rates and an attempt to close deals prior to the 2012 year-end.

US EMC announced deals by quarter



Source: Thomson Reuters

2012 by the numbers *(continued)*

Deals by sub-sector

Overall announced EMC deal volumes (with disclosed and undisclosed deal values) declined from 931 announced deals in 2011 to 839 deals in 2012, driven primarily by small middle-market deals in the Internet Software & Services (ISS) and Advertising and Marketing sectors. However, announced deal value increased from $55.0 billion to $96.2 billion for the respective period. Even with the exclusion of the $20.1 billion Softbank/Sprint deal, announced deal value still increased $21.1 billion, or 38% from 2011 to 2012, driven primarily by sports franchise deals in Recreation & Leisure as well as Film/Content deals.

EMC announced deals by sub-sector

	Deal count			Deal value*		
$ In millions	FY11	FY12	Variance	FY11	FY12	Variance
Communications[1]	165	154	(11)	$26,908	$43,497	$16,589
Recreation & Leisure	60	77	17	2,481	10.552	8,071
Internet Software & Services	186	149	(37)	6,030	9,480	3,450
Cable	22	15	(7)	3,366	9,087	5,721
Film/Content[2]	39	40	1	1,125	9,028	7,903
Broadcasting	51	71	20	2,650	5,771	3,121
Publishing	110	117	7	2,872	3,163	291
Advertising & Marketing	246	184	(62)	2,479	2,960	481
Casinos & Gaming	25	19	(6)	2,245	2,540	295
Music	11	7	(4)	3,358	100	(3,258)
Video Games	16	6	(10)	1,434	68	(1,366)
Total	**931**	**839**	**(92)**	**$54,950**	**$96,245**	**$41,295**

[1] Classified as "Telecommunications" within the Thomson Reuters database.
[2] Classified as "Motion Picture/Audio Visual" within the Thomson Reuters database.
* Represents transaction value and not enterprise value
Source: Thomson Reuters

Subsector analysis: Key drivers for growth in 2012 and outlook for 2013

EMC sub-sector deals for 2012 were led by Communications, Recreation & Leisure, ISS, Film/Content, Cable, and Broadcasting which all saw significant increases in disclosed deal value from 2011. Given this level of activity, these sub-sectors are further discussed below:[1]

Communications

Drivers of growth in 2012: Communications deal value increased $16.6 billion, from $26.9 billion in 2011 to $43.5 billion in 2012, led by Softbank's $20.1 billion acquisition of Sprint Nextel, Metro PCS' $3.7 billion acquisition of T-Mobile USA, Crown Castle Communications' $2.4 billion acquisition of tower sites from T-Mobile USA, and SBA Communications' $1.5 billion acquisition of tower sites from TowerCo LLC. Overall deal activity was split fairly evenly between telecom equipment, services, and wireless acquisitions. Ultimately, consumer demand for high-speed mobile connections and devise usage convergence (i.e., smartphones) coupled with a finite broadcast spectrum appeared to be the driver for most of the Communications deals.

2013 Outlook: As Communications companies address growing spectrum needs, some operators are finding M&A the shortest road to a solution for these challenges. Additionally, changing business models that address the need for new products and services, coupled with intense competition are drivers of continued acquisitions. Look for communications companies to expand their service offerings via potential interest in cloud services companies.

Recreation & Leisure

Drivers of growth in 2012: Overall deal value in Recreation & Leisure increased $8.1 billion, from $2.5 billion in 2011 to $10.6 billion in 2012, driven largely by the $2.6 billion acquisition of AMC Entertainment Holdings by Dalian Wanda Group and announced sports team deals of $4.0 billion in total for the Los Angeles Dodgers, Cleveland Browns, and San Diego Padres, reportedly valued at $2.2 billion, $1.0 billion, and $0.8 billion, respectively.

2013 Outlook: We expect this sub-sector will continue to see significant deal activity in 2013 as owners look to monetize these assets given rising deal values in this sub-sector.

Internet Software & Services (ISS)

Drivers of growth in 2012: The majority of deal volume in this space consists of small, middle-market transactions, which explains why disclosed deal volume declined 20% since 2011; however, deal value grew from $6.0 billion in 2011 to $9.5 billion in 2012. In 2012, five deals comprised approximately 71% of the total deal value, which included the acquisition of Taleo Corp for $1.9 billion, Ancestry.com for $1.5 billion, Thomson-Reuters Healthcare Business for $1.3 billion, Instagram for $1.0 billion, and AT&T Inc. Yellowpages.com for $1.0 billion.

2013 Outlook: We anticipate that ISS deal volume will continue to be active throughout 2013 given that the capital requirement to facilitate these investments is not overly burdensome in the middle-market space.

1 Descriptions of sectors provided in italics above and below are provided by Thomson Reuters and are for information purposes only.

Cable

Drivers of growth in 2012: Cable deal value increased $5.7 million, from $3.4 million in 2011 to $9.1 million in 2012, primarily due to the $6.6 billion acquisition of Cequel Communications by an investor group.

2013 Outlook: In 2013, we expect cable companies will continue to explore various strategies to monetize the shift toward increased digital consumption, grow their subscriber base, and improve operational efficiencies. This trend was already seen in Q1'13 with Charter Communications' $1.6 billion purchase of Optimum West (Bresnan Communications) as well as Liberty Media's $2.7 billion investment in Charter. Separately, Liberty Global agreed to acquire UK-based Virgin Media for $23.3 billion in the largest cross-border EMC deal so far in 2013. As more content is consumed digitally, there are increased concerns around bandwidth and the quality of the consumer viewing experience, which has prompted some companies to look for technologies to help deliver an improved digital experience.

Film/Content

Drivers of growth in 2012: Film and Content deal value increased $7.9 billion, from $1.1 billion in 2011 to $9.0 billion in 2012, driven primarily by Disney's acquisition of Lucasfilm for $4.1 billion and a private equity investor group's acquisition of Getty Images for $3.3 billion. Overall deal value of content targets remained strong in 2012 as companies looked to enhance their existing content portfolio and maximize their place in the digital value chain.

2013 Outlook: Given the importance placed on content and overall change in the EMC landscape as discussed in our 2013 outlook, we expect that both corporate and private equity buyers will continue to target content creators as part of their long-term strategic vision. We expect this focus to continue to drive increased valuations for content creators with proven franchises and an ability to turn out reliable, quality programming and monetize their existing intellectual property.

Broadcasting

Drivers of growth in 2012: The 2012 overall deal value of $5.8 billion was driven primarily by NBCU's divestiture of their stake in A&E Television Networks for approximately $3.0 billion. In 2012, the sale of an additional eight Newport Television stations was announced as a part of the divestiture; however, the deal value for these stations was not disclosed. Sources indicate the total deal value of the Newport TV sale was approximately $1.0 billion.[2]

2013 Outlook: Consistent with our discussion in Theme #3, we expect outbound M&A to remain an attractive strategy in 2013 as US companies seek increased audiences to help monetize their content and expand their reach. Also, there has been recent press surrounding alternative technologies which have disrupted the traditional distribution model. It will be interesting to see how the courts rule on this matter and how it impacts the broader broadcast landscape.

Separately, we've already seen one significant transaction in 2013 as Comcast purchased the remaining 49% of NBCU for $16.7 billion.

2 Source: http://www.deadline.com/2012/07/newport-television-to-collect-1b-selling-22-stations-to-nexstar-sinclair-and-cox/

Top 10 deals in 2012

The following chart outlines the top 10 US deals in 2012. These deals are representative of various EMC sub-sectors, with Communications leading the top deals with four of the top 10 deals, followed by Film/Content with two deals.

Top 10 US EMC deals announced in 2012

	Announce date	Target	Target industry	Buyer	Transaction value**
1.	10/15/2012	Sprint Nextel Corp	Communications	SoftBank Corp	20,140
2.	7/18/2012	Cequel Communications LLC	Cable	Investor Group	6,579
3.	10/30/2012	Lucasfilm Ltd	Film/Content	Walt Disney Co	4,050
4.	10/3/2012	T-Mobile USA Inc	Communications	MetroPCS Communications Inc	3,690
5.	8/15/2012	Getty Images Inc	Film/Content	Investor Group	3,300
6.	7/10/2012	A&E Television Networks LLC	Broadcasting	Walt Disney Co & Hearst	3,025
7.	5/20/2012	AMC Entertainment Holdings Inc	Recreation & Leisure	Dalian Wanda Group Corp Ltd	2,600
8.	11/26/2012	McGraw-Hill Education LLC	Publishing	Apollo Global Management LLC	2,500
9.	9/28/2012	T-Mobile USA Inc. towers	Communications	Crown Castle International	2,400
10.	12/19/2012	Motorola Mobility-Set-Top Box	Communications	ARRIS Group Inc	2,350

*US deals is defined as deals where target is located in the US
**Note transaction value may differ from enterprise value
Source: Thomson Reuters, WSJ

Spotlight article

The five critical components to driving divestiture success

Divestitures and divestiture planning activities are on the rise and expected to be primary contributors to deal volumes in the coming year. Divestitures are inherently difficult to execute, which makes it challenging to preserve value across the lifecycle of a transaction. Whether you're the parent company looking to dispose of assets or a buyer acquiring those assets, five separation fundamentals drive alignment between buyers and sellers, enhance the pace of separation activities, and contribute to a successful separation. These five separation fundamentals are:

1. **Establish a Divestiture Management Office (DMO)—** A DMO is the command center for driving the divestiture approach and processes across the separation workstreams, the deal team, and executive decision makers. It is the hub for coordinating activities and resources across functions for both the seller and carve-out business. Having a DMO in place enables rapid decision making; allows for the timely identification and prioritization of issues and dependencies; and helps drive standardization across separation workstreams through the deployment of standards, policies, guidelines, and tools across the divestiture. The DMO assembles, coordinates, tracks, monitors, reports, and distributes key project information across the lifecycle of the separation.

2. **Develop the Target Operating Model—**The Target Operating Model (TOM) defines the "to-be" state of the parent and carve-out business through each phase of the transaction to their respective end states. Common divestiture phases include pre-signing, sign-to-close, close, transition, and, ultimately, complete separation. Sellers and buyers both should focus on core infrastructure elements to understand the degree of change driven by each phase of the transition. At a high level, the core elements of and questions to be answered in order to achieve the TOM include:

- Organization—How does the organization of the parent and carve-out business evolve?

- People—How are employees of the parent and carve-out business impacted?

- Processes—Which processes of the parent/carve-out business are impacted and how do these need to change to support continued operations of the parent and carve-out business?

- Technology and data—Which systems of the parent/carve-out business are impacted? What changes need to be put in place to support continued operations of the parent and carve-out business? What data is needed to support the parent and carve-out business?

- Assets and facilities—How and when will assets, liabilities, and facilities be segregated?

It's critical for both the parent and carve-out business to understand the changes brought with each transaction phase. Developing a TOM helps both the buyer and seller plan and assess the impacts of how they will operate during each phase and will also provide a roadmap for what activities need to be completed by phase.

3. **Define Transition Service Agreements (TSAs)—**TSAs provide a robust definition and costing of services the seller will provide to the carve-out business in order to sustain operations after legal close until it is fully integrated into the buyer or operating on a standalone basis. TSA's offer several advantages to both the seller and buyer:

- Faster close—A TSA can accelerate the negotiation process and financial close by allowing the deal to move forward without waiting for the buyer to assume responsibility for all critical support services.

- Smoother transition—The complexity of a deal often dictates the time between announcement and close. In cases of accelerated timing, the buyer may not have enough time to respond to the separation process, particularly when there factors that cannot be shared until after the deal closes. TSAs can become a vital part of allowing the business to transition or separate quickly.

- Reduced transition costs—Since the seller supports critical services for an agreed-upon duration, the buyer is able to not only spread out, but often reduce transition costs of supporting those services in-house.

- Better end-state solutions—The knowledge transfer process is gradual, giving adequate time to the buyer's employees to take over the services.

- Reduced risk—TSAs are a legally binding obligation for the seller to complete the separation post-close and after the purchase price has been paid, thereby minimizing legal and commercial exposure.

4. **Establish a robust financial model—**A detailed financial model not only captures GAAP and deal information, but also fully considers stranded costs, transition costs, and one-time separation costs. While carve-out financial statements are critical for providing a true picture of the business being sold, it is equally important for the seller to understand the true nature of the costs required to separate and to stand up the carve-out business as an independently operating entity. Savvy buyers will develop their own models during diligence and pressure test the seller's assumptions. Establishing a logical, data-driven point of view will help bring quicker alignment between the seller and buyer.

   It is also important for the seller to understand any stranded costs associated with the carve-out that will remain upon expiration of TSAs.

5. **Develop a change management and communication plan—**Having a change management and communication plan in place for key stakeholders pre-announcement and then for each transaction phase is critical to overall transaction success. Considerations include:

- Employees—Messaging for employees who are part of the carve-out business as well as those remaining with the parent is important. Often, an element of value is associated with retaining employees, and having proper messaging in place will help to keep people in their seats. Be prepared to address labor issues and any collective bargaining agreements.

- Vendors/suppliers—Be prepared to work with vendors/suppliers to duplicate or assign contracts required by the carve-out business. Have a plan in place to address the likelihood that vendors will use this as an opportunity to obtain more favorable pricing or terms.

- Customers—Articulating the value and impact of the transaction to customers is critical, particularly for the customers of the carve-out business. Customers will want to understand how service levels, quality, future product development, and overall support will be impacted. Not having a robust plan in place can lead to lost revenue with existing customers and can impact in-flight deals or the acquisition of new customers.

Conclusion

Together, these five components help make sellers more agile and informed, enabling them to bring their perspective to the buyer, highlighting sources of value, and demonstrating that they thought through risk associated with the transition. Buyers will engage more effectively with a prepared seller, which will lead to a more constructive separation process. Ultimately, the transaction timeline will be accelerated through alignment around key transaction elements and will result in enhanced value for both parties.

Author: Paul Hollinger, M&A Advisory
408.817.8295, paul.j.hollinger@us.pwc.com

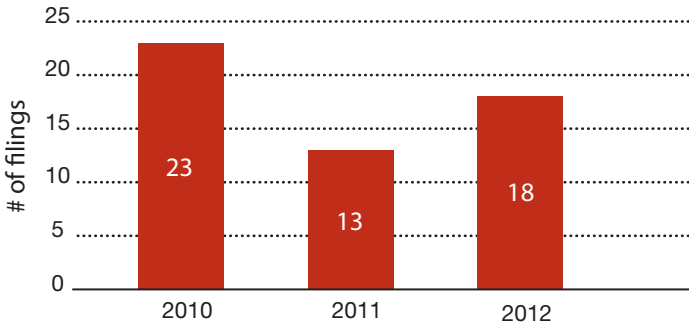
Bankrupt and distressed company analysis
Looking ahead at credit risk and debt maturation, pockets of financial distress remain

Despite sustained fiscal and macroeconomic uncertainty, heavy inflows of capital into the US credit markets and historically low interest rates have led to a heavy volume of refinancings across all US industries. While many expect these trends to continue into 2013, this liquidity could recede fairly quickly should economic growth fall short of GDP growth expectations of 1% to 2%. According to Fitch Ratings, the immediate 2013 maturity schedule for EMC companies is expected to be manageable. Many EMC companies opportunistically accessed the capital markets in 2012, not out of necessity, but to take advantage of low funding costs to strengthen balance sheets and shore up their capital structure. As such, the aforementioned "maturity wall" that most expected has morphed into a "maturity wave" of sorts.

That being said, the EMC sector remains subject to heightened credit risk in 2013 and beyond. Based on the number of weakest links[3], the media and entertainment sector is most vulnerable to default. This sector also has the greatest number of weakest links, with 41 entities (25.9% of the total), followed by the oil and gas exploration sector, with 12 entities (7.6%). Many of these S&P 'B-' rated and lower-rated E&M companies were under continuous debt maturity pressure in 2012 because of high leverage or imminent covenant step-downs, or have delayed refinancing because borrowing is likely to come at a higher cost than they currently enjoy. Given these market indicators and continuing expectations of economic uncertainty, overleveraged EMC sector companies, particularly those in the middle market, deserve close watch in 2013.

Another continuing trend we saw in 2012 is the prevalence of 363 asset sales and pre-arranged/pre-packaged reorganization plans as vehicles for emergence. Of the 18 EMC companies that filed for bankruptcy in 2012, four have already emerged as of the date of this report via reorganization plans with existing lenders and seven are currently pursuing a 363 asset sale strategy.

US EMC bankruptcy filings



Source: TheDeal, S&P Capital IQ, MergerMarket, Debtwire

3 Defined by S&P as issuers rated 'B-' and lower with either negative rating outlooks or ratings on CreditWatch with negative implications. Source: 'Global Weakest Links and Default Rates: The Weakest Links Count Increases to 158' Standard & Poor's Financial Services, LLC, December 26, 2012.

About the data
Defining Entertainment, Media and Communications

Our analysis highlights the ongoing changes in the EMC industry due to technology advances, the convergence of traditional and new media, and ever-shifting consumer preferences. For purposes of our publication, we have focused on the following sectors:

- Communications
- Recreation & Leisure
- Film/Content
- Cable
- Broadcasting
- Internet Software & Services
- Publishing
- Advertising & Marketing
- Casinos & Gaming
- Music
- Video Games

Our analysis was based primarily on individual EMC sectors as defined by ThomsonReuters, with the exception of Telecommunications and Motion Picture/Audio Visual, which we have renamed as Communications and Film/Content, respectively, for the purpose of our analysis. In addition, all deal values disclosed, unless otherwise noted, were determined using transaction value. While in certain cases, enterprise value may exceed transaction value, it has not been considered in our analysis.

Thomson Reuters Sub-sector descriptions:

1. Communications—includes wireless telecommunication carriers, radio and television broadcasting communications equipment, wireless equipment, wired telecommunication carriers, telecommunication resellers, satellite telecommunications, and all other telecommunications.

2. Recreation & Leisure—sport teams and clubs; event and sport facilities including racetracks, bowling alleys, and skiing; other spectator sports; fitness and recreational centers, golf courses, and country clubs; amusement and theme parks; amusement arcades; movie theatres; performing arts and dance companies; recreational goods rentals; nature parks and zoos; museums; historical sites; and all other amusement and recreational institutions.

3. Internet Software & Services—information retrieval services and other internet services related to EMC

4. Film/Content—includes photography, sound recording and studios, motion picture and video production and distribution, teleproduction and other post-production services, and video tape and disc rental.

5. Cable—includes cable, subscription programming, and other pay TV services which may include wired telecommunication carriers.

6. Broadcasting—includes television and radio broadcasting networks.

7. Publishing—Newspaper, periodical, and book publishers both print and internet; database and directory publishers; greeting card publishers; other commercial printing, engraving, bookbinding, and related work; prepress services; and other miscellaneous publishers.

8. Advertising & Marketing—includes advertising and media buying agencies; direct mail advertising; advertising material distribution; display advertising including online, promotion, and public relations; market research; talent agents; and other services related to advertising.

9. Casinos & Gaming—includes casinos, casino hotels, and other gambling industries.

10. Music—includes music publishers, musical groups and artists, record production, prerecorded record reproducing, and record distribution.

11. E-commerce—includes business-to-business electronic markets related to EMC, internet publishing, and web search portals.

We based our findings on research provided by industry-recognized sources—specifically, ThomsonReuters, The Wall Street Journal, Fortune.com, Yahoo Finance, S&P, Debtwire, S&P Capital IQ, The Deal, Mergermarket and Fitch Ratings.

When referencing the EMC sectors of the Fortune 500, we include Telecommunication, Advertising & Marketing, Entertainment, Internet Services & Retailing, Publishing & Printing, and Hotels, Casinos & Resorts. See http://money.cnn.com/magazines/fortune/fortune500/2012/industries for a listing of respective companies.

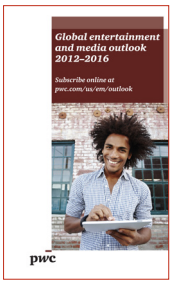
We define US EMC transaction activity as acquisitions, mergers, consolidation of minority interests, shareholder spin-offs, divestitures and restructurings. Acquisition targets are defined as US companies acquired by either domestic or foreign acquirers (both corporate and private equity); and deal value is transaction value as reported. Private equity transactions are defined as acquisitions of initial platform companies only. Subsequent add-on acquisitions by private-equity-controlled platform companies are herein classified as corporate transactions.

As has been the case over each of the past several years due to undisclosed deal activity, 2012's disclosed deal volume was significantly lower than total EMC deal volume. While transactions with disclosed deal values are indicative of overall EMC sector trends, the high volume of undisclosed deal activity is also indicative of growing middle-market deal activity in the space.

Of further interest

Read PwC's other publications

Global E&M Outlook: 2012–2016 - Created by top minds from PwC's Entertainment, Media, and Communications practice, in conjunction with economic forecasters, the Outlook provides in-depth coverage of the market in 13 segments across 48 countries. The next edition will be released on June 5, 2013. Explore the data online at http://www.pwc.com/us/em/outlook.



Consumer Intelligence Series - Through PwC's ongoing consumer research program, we gain directional insights on consumer attitudes and behaviors in the rapidly changing media landscape. Our series explores digital transformation in the entertainment, media, and communications industries. Recent topics include mobile wallets, consumer privacy and customer loyalty. Visit www.pwc.com/consumerintelligenceseries.

Communications Review - As quarterly journal for telecom, cable, satellite, and Internet executives, Communications Review showcases some of the best global practices, leading-edge thinking, and executive interviews, addressing management and financial issues in the Communications industry. Visit www.pwc.com/communicationsreview.

2013 Global CEO Survey - PwC's Annual Global CEO Survey, now in its sixteenth year, aims to inform and stimulate the debate on how businesses are facing today's challenges. Over the years, thousands of CEOs around the world have taken the time to share their views with us. For this issue, we conducted 1,330 CEO interviews in 68 countries. Visit www.pwc.com/ceosurvey to explore responses by sector and location.

The cord-cutting debate and the role of second screen in TV, advertising, and content distribution - Television viewing trends are changing, which impacts business models for companies across the entertainment and media ecosystem. In this report we explore how partnerships, new capabilities, and a strategy incorporating second screen technologies can be an important engine for growth. Visit www.pwc.com/us/em.

Dynamic analytics for enhanced business decision making in the entertainment industry - Companies who extensively use analytics are more likely to outperform their competitors. This publication looks at analytical techniques available today, presents a proposed structure for an analytics project, and illustrates how simulation modeling can be used to address E&M macro strategic decisions. Visit www.pwc.com/us/em.

Entertainment and media asset valuation in the digital age - As consumer trends continue to evolve, measuring and reporting the value of intangible assets has become increasingly complex. Traditional methods employed to value intangible E&M assets may ultimately need to evolve in the interest of improved reporting. Download this publication www.pwc.com/us/valuation.

Webcast replay: Unleashing TV spectrum - A new wave of opportunity for broadcasters and wireless companies : The FCC is coordinating an unprecedented and highly anticipated auction process aimed at freeing up TV spectrum for reuse by mobile operators. The webcast includes the FCC and key industry representatives who help clarify the specifics of the Broadcast Spectrum Incentive Auction process and discuss opportunities for stakeholders. Watch the replay at www.pwc.com/us/comms.

PwC mobile innovations forecast: Making sense of the rapid change in mobile innovation - With the goal of providing business leaders early warnings about coming disruptions and actionable intelligence about new opportunities, PwC introduces its Mobile Innovations Forecast, a four-part framework for analyzing and understanding mobile innovation. Visit www.pwc.com/us/comms.

Technology M&A insights 2013 - While the pace and value of technology sector deals are expected to approximate those of 2012, the outlook for 2013 technology deals will focus on the new core of mobile, social, analytics, and security. To read about the top drivers of technology deals in 2013, visit www.pwc.com/us/deals.

www.pwc.com/us/deals
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Contacts

Authors

Bart Spiegel
EMC Deals
646.471.7085
bart.spiegel@us.pwc.com

Oliver De La Hoz
EMC Deals
646.471.5289
oliver.de.la.hoz@us.pwc.com

PwC Deals

Thomas Rooney
EMC Sector Leader
646.471.7983
thomas.rooney@us.pwc.com

Andreas Ohl
Valuation
646.471.2947
andreas.ohl@us.pwc.com

Richard Veysey
Capital Markets and Accounting Advisory
646.471.7973
richard.veysey@us.pwc.com

Ron Chopoorian
Divestitures
646-471-3491
ronald.chopoorian@us.pwc.com

Michael Kliegman
M&A Tax
646.471.8213
michael.kliegman@us.pwc.com

Perry Mandarino
Business Recovery Services
646.471.7589
perry.mandarino@us.pwc.com

Michael Boro
Human Resources
646.471.0730
michael.boro@us.pwc.com

John Merrigan
Insurance Risk Management
646.471.5847
john.merrigan@us.pwc.com

PwC Entertainment, Media and Communications

Kenneth Sharkey
US Practice Leader
646.471.5114
kenneth.j.sharkey@us.pwc.com

Robert Conklin
US Assurance Leader
646.471.5858
robert.conklin@us.pwc.com

Deborah Bothun
US Advisory Leader
213.217.3302
deborah.k.bothun@us.pwc.com

Peter D'Avanzo
US Tax Leader
646.471.5611
peter.davanzo@us.pwc.com