

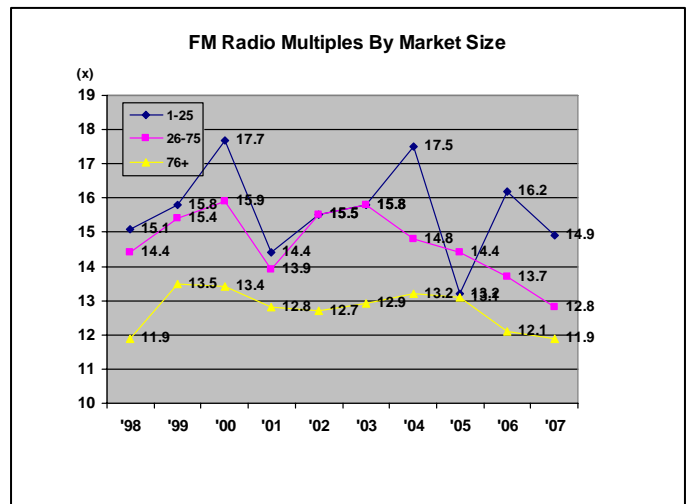
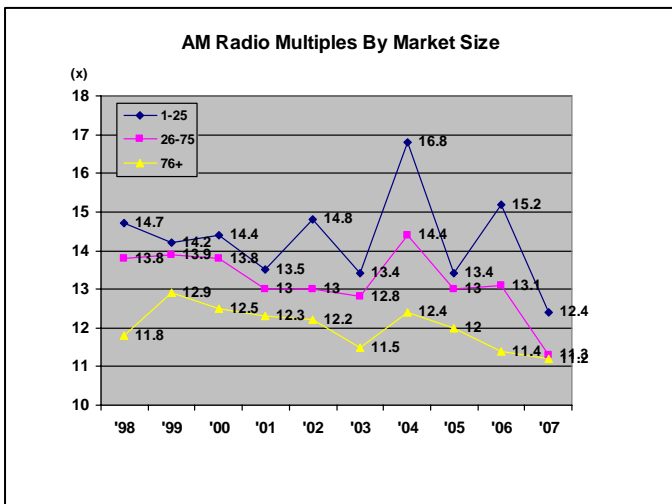
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The year of seller financing....or is it a whole new era?

From our perspective in the broadcast media M&A arena, this could be the year of seller paper or alternative financing (such as LMAs, as will be discussed) in broadcast acquisition transactions, and we may also see this characteristic extend to other segments of the media and telecom industry. Why? The sub-prime meltdown and resulting tightening of credit reigns by banks, in combination with declining valuations for broadcast properties (see table below), are making traditional financing packages less attractive for borrowers and more difficult to obtain ...even for qualified buyers with existing banking relationships.

... for many it seems that relationships with banks are changing...

Additionally, for many of our clients it seems that relationships with banks are changing; while banks for some of these companies used to behave more like partners, this often now seems to no longer be the case, and in some situations the relationships have even turned adversarial. How much of this is due to the sub-prime market meltdown? According to John Zitzmann of Morgan Stanley, "the sub-prime meltdown has sent shockwaves not just in the housing and consumer finance markets but in all markets around the globe. It's going to take several years for this to be re-assimilated into the financial communities worldwide and it is going to make the lending process more arduous even where existing relationships have had wide lane 'bridges of lending'."



Source: Kagan data provided by Media Services Group

...seller financing will bridge the gap on cash-flow multiples between conservative banks and equity providers...

So how will leveraged transactions actually get done? To begin with, seller financing will bridge the gap on cash-flow multiples between conservative banks and equity providers wanting to maximize returns. For example, a broadcast property that would normally be trading at 12x cash-flow, at this time last year one could likely have secured a debt facility at say 6x cash-flow, or half of the capital structure. That same lender might now only consider a loan package at 4x cash-flow, and if the equity source is interested in providing the same 6x cash-flow component (which in the current environment is not a given), there is now a gap of at least another 2x, assuming the same 12x cash flow valuation target. As a seller, moreover, you need to seriously consider this type of structure, or otherwise risk losing the transaction altogether.

With this said, as a seller you are probably going to see a minimum 3-year term on your paper, while the buyer has the opportunity to increase cash flow to a level that would either facilitate a refinancing or an increase of the existing credit facility to allow the seller note to be repaid. As a buyer, therefore, it would be prudent to secure a sufficiently flexible credit facility going into the transaction, to enable you to repay the seller note when the time comes without having to scramble later (and in a potentially still uncertain environment).

... LMA's with the intended seller for a time that allows the buyer to increase the cash flow of the target property to a level that can be financed at a pre-agreed valuation...

Another possible alternative in achieving alternative financing for broadcast buyers is to create a LMA (Local Marketing Agreement) with the intended seller for a period of time that allows the buyer, as a potentially better operator with a different strategy, to increase the cash flow of the target property to a level that can be more easily financed at a pre-agreed valuation (i.e., agreed at the time of the original transaction).. An example to illustrate this alternative may be as follows: Say there is an asking price of \$10 million on a property with \$1 million in cash flow (i.e., at the current time this would be a 10x CF deal). As the LMA/buyer takes over and then increases the property's cash flow to \$1.3 million over 18 months, the total debt financing and equity required to fund the same \$10 million purchase price would in actuality make the cash-flow multiple roughly 7.5x. The seller is happy having received a 'mental-multiple' of 10x on the property's original financial profile, and the buyer is happy having in actuality paid 7.5x and financed a more conservative structure. The bank, by the same token, will have funded a more conservative transaction and, depending on



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the level of cash flow achieved by the time of acquisition, the equity requirement could actually have diminished.

Numerous other industry/commercial buyers and sellers, beyond those in the real estate sector who have been working in this fashion for a long time, seem to be looking at and utilizing these approaches. For those of you who remember the late 1970's and early 1980's, and the record interest rates nearing 20% during the Carter administration, alternative and creative financings were extremely popular, as was seller paper. Such structures became a necessity to survival and to making transactions happen. Although for different reasons this time, are we entering a similar era of seller and alternative financing? Time will tell.

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