Northern Alliance

# The Corporate Finance of SMEs in the UK Film Industry.

## A Report for the British Film Institute

## October 2014

## Contents

# 1. Executive summary

The financial performance of individual films is often reported, but less attention tends to be paid to the finances of the companies that make, sell and distribute them. Yet without these businesses those films and the industry that makes them would cease to exist. The overwhelming majority of these companies are small or medium sized[1] ('SMEs').

This BFI-commissioned study examines the financial results of a representative group of production, sales and distribution companies involved with successful UK films, updating an earlier study commissioned by the UK Film Council in 2009.

In the earlier study, Northern Alliance analysed the accounts of 73 companies that produced and distributed the most successful UK films in the years 2006-2008. The accounts analysed covered the period 1 March 2004 until 31 December 2008.

The present study examines the progress of these companies since the end of the previous review period together with a further 35 new companies that subsequently met the criteria for selection. Whilst it has not re-performed the full depth and scale of analysis of the original review, it has examined their latest accounts and other information in the public domain. It has also updated the conclusions of the previous study to the extent they appear, from the latest analysis, to continue to be relevant.

The purpose of the study is to:

- Assess the financial position of the types of film companies in the sectors studied and identify apparent strengths and weaknesses of their business models.
- Identify trends affecting businesses in each sector.
- Inform the development of public policy.
- Assist film businesses that may be considering how to improve their business models and strengthen their balance sheets.

### Findings applicable to all Sectors

A number of conclusions apply to all industry sectors included in the review, in particular:

- Accounting by distributors and producers remains inconsistent and typically falls far short of US accounting requirements.
- There is still a widespread failure to appreciate and accurately value intellectual property created by the UK film industry.
- A statement of recommended accounting practice should be developed for the UK film and television industries, similar in its effect to the standard set for the US industry by the US Financial Accounting Standards Board.

[1] See the glossary for the official definition of an SME. A very small number of companies in the sample did not meet the official definition.

- There are few instances of private investment in film businesses and the ‘equity gap’ in the UK film industry appears as wide as it was during the original review.
- There continues to be an almost systemic reliance on dilatory payment of creditors with some companies continuing to take over six months to settle debts.
- With one exception, issues of shares via the London Stock Exchange appear to have been of very limited use to those film businesses whose shares are publicly traded.
- Public sector investment in film businesses, as opposed to film projects, continues to be nugatory.
- Almost half of the businesses originally identified as producing, selling or distributing the best British films have subsequently ceased trading or appear to be in decline.

**Production Sector**

Independent Stand Alone Production Companies:

- The previous study found that, excluding studio-backed companies, films produced by the Independent sub-sector tend to be the most popular amongst cinema audiences.
- Of the 14 companies originally classified as Independent, three have migrated to an integrated model, three have ceased to make films and two more appear to be struggling to continue.
- The half-dozen remaining account for several of the most popular British films produced in recent years, but typically continue with weak, illiquid balance sheets, often reporting retained losses at their last balance sheet date.
- 12 new entrants met the selection criteria during 2009-2013, however only one was founded by someone who hadn’t been an executive of a film business before 2009.

Production Companies with Talent Attached[2]:

- Companies are thinly capitalised and generally operate on relatively low turnover.
- The sub-sector’s films typically generate relatively low box office.
- Of the ten companies originally classified as Talent Attached:
    - Two have developed non-film production activity, with one of those apparently ceasing to produce films
    - One is operating at a reduced level
    - Two have completely ceased trading
    - The remaining five have continued to be relatively stable marriages of talent and business
- Ten additional companies met the criteria for inclusion in the current review.

[2] i.e. with a writer or director co-owning the business.

   - Six had been established before 2009, but had not produced films that met the selection criteria.
   - Four were established after 2009, three of these appear to be struggling but one appears to be thriving as a result of developing a ‘franchise’.

Studio Backed Production Companies:

- This sub-sector makes the most popular films, and employs the most working capital.
- The most successful companies tend to produce ‘franchise’ films and are highly profitable.
- The remaining companies often generate significant losses.
- Of the nine original Studio Backed companies:
   - Two have ceased activity.
   - Two appear to have looser ties to their Studio and, perhaps as a result, have not produced films that meet the criteria for selection in the latest review period.
   - The remaining five continue to successfully produce commercially successful and award winning films with the support of their sponsoring Studio.
- Studio Backed production companies have the lowest churn rate, with the other categories experiencing churn rates four times higher.
- No new Studio Backed companies were responsible for any of the films that met the criteria for inclusion during the new study period.

Hybrid, Horizontally and Vertically Integrated Production Companies:

- The original study noted this sub-sector had the highest average turnover and above average profitability.
- The Film+TV model still appears to be the most successful (from a film point of view).
- In terms of filmmaking, half of the original Integrated businesses have had mixed results since the original review.
- The remainder have reported significant growth and experienced success both in their film and non-film activities.
- The Integrated model appears resilient in comparison with other production business models:
   - All of the companies originally allocated to this category continued to trade.
   - None chose to adopt different types of business model.
   - The incidence of growth was significantly higher than amongst other categories.
- Nine new Integrated production businesses met the criteria for inclusion in the study.
- Three companies originally categorised as ‘Independent’ have become successful ‘Integrated’ businesses since the end of the original review.

- Integrated business models have replaced Independent Stand Alone businesses as the most frequent type of company responsible for producing the most commercially successful British films.

**Sales Sector**

- The original study found that there appears to be a minimum threshold of around £2 million per annum. in turnover in order for a sales agency to prosper, though exceptions exist.
- The number of UK sales companies that represent the most successful British films has decreased from 13 to 11.
- Whilst all the films in the original study had sales agents attached, four films in the latest review appear to be unrepresented by an agent.
- The attraction of London as a place to locate a sales branch of an overseas company appears to have waned.
- Independent sales companies continue to struggle to operate profitably, typically having limited or no external access to corporate finance.
- Two of the five Independent sales companies have clearly migrated to a vertically integrated business model whilst one was wound up.
- Vertical integration is apparently becoming the most popular business model for a sales company to adopt.
- Vertically integrated companies vary greatly in profitability but had the highest growth in turnover during the original review with most continuing to improve trading subsequently.

**Distribution Sector**

- As with the sales companies, the ‘pool’ of distribution companies that represent the most successful British films has decreased (from 19 to 16).
- In contrast to the consistent pattern of growth noted across all sub-sectors in the previous study, only Mini-Majors appear to have experienced continued growth as a class. Most businesses in the other categories appear to have fallen further behind the Mini-Majors.
- On average, Mini Majors now release more UK ‘hit’ films than MPAA members, with the proportion of the most successful independently produced films released by MPAA members falling from over half to less than 1 in three.
- Of the seven original Vertically Integrated distributors, three appear to be successfully developing their business, one appears to be at a crossroads another is struggling to survive and two have ceased trading.
- The original study concluded that vertical integration appeared to offer little advantage to UK distributors. The mixed results of distributors in this category since the previous review would seem to support the view that vertical integration of itself does not offer any particular advantage, with other factors (such as rigorous cost control) seemingly more important in determining success within vertically integrated distributors.
- All three distributors seen as successfully pursuing a strategy of horizontal integration in the original review appear to have either abandoned their

strategy or have been unable to successfully execute it in the period since the original review.
- All six distributors categorised as Independent in the original study have continued in business since then, but with mixed results and typically with balance sheets that appear vulnerable to downturns in trading.
- The ability of distributors to manage working capital appears to have deteriorated (though typically from a position of great strength). The most delinquent in paying suppliers as noted in the previous study still takes almost seven months on average to settle its liabilities.
- The original study found that cost of sales had typically risen along with turnover, with Mini-Majors' increased costs outstripping their turnover by the highest margin. In contrast the Mini-Majors now appear to have been able to grow revenues faster than direct costs since the end of the previous review, whereas companies in other subcategories that achieved growth in turnover typically saw direct costs increase at a higher rate.
- Whereas there was conflicting evidence in the original review, access to VoD audiences now appears to be emerging as a critical success factor, with two companies attributing their overall growth in profitability directly to widened access to VoD markets.
- During the original review period distributors could, on average, only cover 16% of their liabilities with cash. Although there are individual exceptions, there seems little evidence of any significant improvement in the liquidity of distributors generally since then except for Mini-Majors, which on average have improved both quick and current ratios.

It should be remembered that these 108 companies were selected on the basis that they had made, sold or released the most successful independently produced and distributed British[3] films from 2006 to 2013. This review charts the progress of these businesses and their most recent financial health. In doing so we hope that all UK film businesses may be encouraged to consider how their own business models might be improved and their balance sheets strengthened so they can become more independent as a result.

[3] i.e. officially certified as British under the 1985 Films Act, see over for more information on the basis of selection.

## 2. Introduction

Analysis of the finances of the UK film industry is predominantly focussed on entire sectors of the industry or on individual projects. What analysis of individual businesses exists tends to be uninformed by experience of the finances of the industry, confused by the industry's practices, such as the use of single purpose companies, or is subjective or anecdotal. Better information on the industry's corporate finance could improve the level of debate and understanding amongst executives in the industry, as well as the quality of investment decisions. Such knowledge could also inform policymaking and increase the attention of corporate financiers currently discouraged by the poor quality of analysis.

In order to further these aims the BFI commissioned Northern Alliance to update its analysis of the publicly available financial information on a representative group of 73 companies from across the value chain, originally performed in 2009, and to add to the analysis those companies that subsequently met the selection criteria.

The intention of the 2009 study was to examine those independent businesses that produce[4] and/or distribute the most successful UK films to UK audiences and those independent sales companies that help finance and deliver them to their markets around the world. The sample was therefore drawn from the population of companies associated with the top performing[5] 150 films officially certified as British under the 1985 Films Act and adding to this population films nominated for or in receipt of a BAFTA award for Best Film or Best British Film or an equivalent BIFA award[6] in 2006-2008. Distribution companies owned by MPAA members and special purpose production companies ('SPCos') were excluded[7].

The companies were originally allocated to sub-categories informed by previous analysis by the Research and Statistics Unit of the UK Film Council. Using the annual accounts and relevant contextual information about each company and their films, the UK industry's corporate finance was analysed to identify key trends within and between sub-categories, typical balance sheets were compiled for the various business models and the comparative corporate financial health of those businesses and business models assessed and gaps in access to corporate finance identified.

This review is based on and updates that original report by reviewing the latest filed accounts and other financial and non-financial information in the public domain on those original 73 companies together with a further 35 companies that subsequently met the selection criteria by being associated with similarly qualifying films released

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[4] For the purposes of determining the sample, only one 'leading' production company was associated with each title. New entrants were required to be the main production company behind the development and production of the relevant film, incumbents would only be required to make a significant financial and/or creative contribution to the film. Where an incumbent was associated with a film that met the cultural or creative criteria and made a significant financial and/or creative contribution to the film it was regarded as the 'leading' production company for the purpose of determining the sample.

[5] In terms of UK GBO

[6] All BIFA Best British Independent Film nominees were included in the 2014 review (the 2009 sample only included winners, not nominees) together with those awarded Best Achievement in Production, Best British Documentary and/or The Raindance Award (if these winners aren't also best film nominees). All films with GBO of less than £10,000 were excluded.

[7] Including primarily financing vehicles or companies that have no prior or subsequent track record in film production. It was considered that analysis of these companies would not further the aims of the review in any significant way.

in the period from January 2009 until December 2013. It retained the original categories as there appears to be no reason why the value of those original classifications has depreciated. It has, however, reallocated individual companies between categories where it seems clear that their business model has changed since the original review.

As the analysis is based on the latest accounts filed at Companies House, and as often those accounts are abbreviated, it is often impossible to arrive at firm conclusions about the nature of the corporate finance of particular companies. Public accounts are typically filed many months after the end of a trading period. As a result, the information referred to in this report is all, to some degree, historical. This analysis should therefore not be relied on to make judgements or draw conclusions on the current condition of individual companies and the information has been made anonymous to that end.

It should be emphasised that this study has not attempted to replicate the depth of research and analysis performed during the original review, though it has updated the selection of companies examined with reference to commercial or awards success after 2008. The companies included in this review therefore produced, sold or released the most successful independently produced British films released during the period 2006-2013, as such they represent the backbone of the indigenous UK film industry.

We hope that, by reviewing the financial progress of those companies we can perhaps identify trends, challenges and opportunities for all the companies currently operating in the production, sales and distribution sectors, and gauge the pace and direction of the industry’s finances as a whole.

## Is the UK's Film I.P. fairly valued?

The great majority of companies analysed in the original report and in this review either did not value their Intellectual Property ('IP') or, where they included it in their balance sheets, appeared to undervalue it. Those companies that appear more diligent in valuing their IP, not necessarily in their balance sheet but also by way of note in their accounts, appear to be more successful in raising institutional finance. That is not to say that cause and effect are in that order, it may be the case that improved representation of intellectual property is simply a by-product of raising slabs of corporate finance to build businesses, however there does appear to be a correlation.

For example, the original review noted that the two vertically integrated sales businesses that valued their IP secured institutional finance and reported profits. Their peers, who did not ascribe values to the licences they held, all recorded losses. They seem to have continued to surpass their peers since the end of the original review period, with one in particular not only adding to its IP through on-going trading but also acquiring library assets and entire business units and further strengthening its balance sheet and increasing revenues and profits as a result. It continues to seem that, in terms of IP within the film business, 'you get what you measure'.

US film companies are given detailed guidance on how to compile their accounts by the US Financial Accounting Standards Board; codifying the practice of timing revenue recognition, classifying film costs and facilitating estimates of the future value of transactions. This provides for consistent accounting within the US motion picture industry. In contrast, UK companies adopt a largely incoherent, often idiosyncratic set of policies that Grant Thornton's media team have analysed in detail in successive reports[8]. The first of these appealed for the development of a clear code of accounting practice that could provide the UK with its version of the US guidance:

*"Accounting by distributors and producers in particular is not consistent across the industry and is often poorly disclosed…in our last survey* ***we recommended the development of a statement of recommended practice for the UK film and television industries*** *and still see it as the way forward for the industry based around the well developed US standards..."*[9]

Given the myriad different accounting policies adopted in preparing the accounts of the businesses studied in this review, **the need for improved guidance appears as great as ever**. Whilst adopting a common standard will not immediately transform underlying performance, it could facilitate comparison across industry sub-sectors and allow owners, managers and potential investors to better understand businesses that are often more complex than their modest size implies. Undoubtedly many of the accounting policies adopted by the companies studied are influenced by the desire to avoid paying any more tax than is necessary. It is difficult, however, to avoid the impression that most UK film companies continue to make an almost unconscious decision not to ascribe a value to the intellectual property that is at the core of their businesses. As noted above, the companies in the study were selected because they make, sell or distribute the most commercially successful and critically acclaimed UK films. In aggregate, across the value chain, there seems to be an almost comprehensive failure to reflect the value of those films in their accounts.

[8] GT's UK financial reporting benchmarking survey was first published 2001 'What do we tell the shareholders?' and was followed by "What happened next?" in 2002, and more recently by "Five years on" published in February 2007
[9] "What Happened Next", the use of bold to highlight text has been used in this report, not the original.

# 3. THE PRODUCTION SECTOR

## Summary

41 production companies met the criteria set for the original study. Eight of these have since ceased trading and ten did not produce a film that met the selection criteria during the period 2007-2013. This left 23 companies that produced films that met the commercial and/or cultural criteria during both review periods.

31 new companies met the selection criteria during the latter review period and were added to the study. 23 of these (i.e. 74%), had been established during or before the original review period, but had not produced films that met the criteria for inclusion. Perhaps this illustrates the relative infrequency with which even some of the most established independent production companies produce commercially and or critically successful films.

The majority of the eight companies that started life during the second review period and also managed to meet that study's criteria for inclusion were founded by filmmakers with a track record within the industry that predated the review period. Whether this reflects an industry that is resistant to 'new blood' or simply that there is no substitute for experience in a highly complex area such as film production is beyond the scope of this study, but it appears that in terms of personnel the churn rate of producers within the upper echelons of the UK film industry is fairly low.

All 72 companies were analysed into four categories, though there is a single dividing line in terms of scale with 'Independent' and 'Talent Attached' companies typically eclipsed in terms of turnover and outweighed in terms of the strength of their balance sheets by 'Studio Backed' and 'Integrated' types.

Independent Stand Alone Production Companies:

- The previous study found that, excluding studio-backed companies, films produced by the Independent sub-sector tend to be the most popular amongst cinema audiences.
- Of the 14 companies originally classified as Independent, three have migrated to an integrated model, three have ceased to make films and two more appear to be struggling to continue.
- The half-dozen remaining account for some of the most popular British films produced in this century, but only four were able to produce films that met the criteria for selection during both review periods.
- 12 additional companies met the criteria for inclusion in the current review.
- Eight of these had been established during or before the original review period, but had not produced films that met the criteria for inclusion.
- The remaining four were established after the end of the previous review period (i.e. after 2006), but three of these were founded by executives who had worked in other film businesses during the original review period.

- Companies in this category typically have weak, illiquid balance sheets, often reporting retained losses at their last balance sheet date, though many appear to do so because the owners take out as much cash from their companies as soon as possible.

Production Companies with Talent Attached:

- Companies are typically thinly capitalised and generally operate on relatively low turnover.
- The sub-sector's films typically generate relatively low box office.
- Of the ten companies originally classified as Talent Attached:
    - Two have developed non-film production activity, with one of those apparently ceasing to produce films.
    - One is operating at a reduced level.
    - Two have completely ceased trading.
    - The remaining five have continued to be relatively stable marriages of talent and business, with only one of these unable to produce films that met the criteria for inclusion in both study periods.
- Ten additional companies met the criteria for inclusion in the current review.
- Six of these had been established during or before the original review period, but had not produced films that met the criteria for inclusion
- The remaining four were established after the end of the previous review period (i.e. after 2006), three appear to be struggling financially but one appears to be thriving as a result of developing a 'franchise'.

Studio Backed Production Companies:

- This sub-sector makes the most popular films, and employs the most working capital.
- The most successful companies tend to produce 'franchise' films and are highly profitable.
- The remaining companies often generate significant losses.
- Of the nine original Studio Backed companies
    - Two have ceased activity.
    - Two appear to have looser ties to their Studio and, perhaps as a result, have not produced films that meet the criteria for selection in the latest review period.
    - The remaining five continue to successfully produce commercially successful and award winning films with the support of their sponsoring Studio.
- Perhaps unsurprisingly, Studio Backed production companies have the lowest churn rate, with the other categories experiencing churn rates four times higher.[10]

[10] 44% compared to 157%, 188% and 160% for the independent, Integrated and Talent Attached companies respectively. Please note; the churn rate is calculated on a 'gross' basis (see glossary for more details).

- No new Studio Backed companies were responsible for any of the films that met the criteria for inclusion during the new study period.

Hybrid, Horizontally and Vertically Integrated Production Companies:

- The original study noted this sub-sector had the highest average turnover and above average profitability.
- The Film+TV model still appears to be the most successful (from a film point of view).
- In terms of filmmaking, half of the original Integrated businesses have had mixed results since the original review, with two unable to repeat their success in producing a film that met the criteria for inclusion in the study.
- The remainder have experienced success and reported significant growth both in their film and non-film activities.
- The Integrated model appears resilient in comparison with other production business models:
    - All of the companies originally allocated to this category continued to trade.
    - None chose to adopt different types of business model.
    - The incidence of growth was significantly higher than amongst other categories.[11]
- Perhaps because of the apparent success of the business model, a further nine Integrated production businesses met the criteria for inclusion in the study.
- In addition, three companies originally categorised as ‘Independent’ have become successful ‘Integrated’ businesses since the end of the original review.
- Integrated business models have replaced Independent Stand Alone businesses as the most frequent type of company responsible for producing the most commercially successful British films.

Ostensibly, in contrast to the Sales and Distribution sectors, there appears to have been a broadening of the industrial base from which the most successful British films were made. 41 companies were responsible for the films that met the criteria for inclusion in the original study, whereas 54 production companies produced the films that met the criteria for the later study. However, after adjusting for the respective lengths in the study periods, the opposite appears to be the case[12]; if anything there has been a narrowing of the number of production companies that account for the most successful independent films.

[11] 75% of companies originally allocated to the Integrated category reported results in their latest accounts that appeared to indicate that trading had improved and was continuing to improve since the original review period, whereas there were significantly fewer companies originally allocated to Studio backed (33%), Independent (21%) and Talent Attached (10%) categories that remained in those categories and reported improved trading.

[12] The original study examined films released over a three-year period whereas the second examined films released over a five-year period. As it appears that even the best production companies take several years to make a film that met the selection criteria it is probably the extension of the period rather than any underlying change in the pool of companies that accounts for the overall increase; the ratio of production companies divided by number of years analysed actually fell from 13.7 to 10.8.

What is clear is the length of time that it takes most producers to develop and produce a critical or commercial 'hit' and how difficult it appears to consistently repeat that achievement. Around half of the leading UK production companies identified in the original study were able to do so. Analysing this ability further indicates that the ability to consistently produce films that can be considered to be the 'Best of British' is less common amongst the Talent Attached (46%) and Independent (36%) categories. Studio Backed companies appear to be surprisingly average (56%) however three quarters of those adopting Integrated business models were able to produce films that met the criteria for inclusion in both studies. Although not quantified it would seem that it is the horizontally rather than the vertically integrated production companies that account for this out-performance relative to other types of business models.

As the Film, TV and related industries evolve it appears that horizontally integrated production businesses may be forming a kind of UK 'Media-Mittelstand'[13] that are adept at creating and exploiting content across a range of media and may well represent the bedrock of a UK film industry that is more integrated with the rest of the UK's creative economy in the future.

[13] 'Mittelstand' is an expression typically used to describe the small and medium-sized manufacturing businesses in Germany often credited for its post war economic revival.

## Independent Stand Alone Production Companies

The previous study found that half of the companies in the sub-sector recorded retained losses at their last balance sheet date and would appear to be unable to repay their creditors in full, even if they could successfully call in all of their debts, should they go into liquidation. The current review indicates that this is still likely; the balance sheets of the companies are generally very weak, many still having net liabilities. They also still tend to be infrequent producers of films; the average frequency of one film every 18 months appears to be continuing. Companies continue to show little or no intellectual property on their balance sheets.

Although each business has a unique history, there appear to be three trends for the companies originally allocated to this sub-sector, with companies continuing with varying degrees of success, migrating to an integrated model or ceasing to be active - typically because of the loss of a/the key member of the management or apparent differences between them. For ease of reference the companies have been termed ‘continuing’, ‘migrating’ or ‘ceasing’.

As an example of the continuing type, the two producers at the centre of one company continue to actively produce successful British films, both for itself and for other entities in a freelance capacity. There has been a modest increase in the company’s balance sheet since the end of the original review but the company appears to be one of the most pronounced examples of a corporate wrapper around the services provided by freelance producers.

Another of the longest established and most prolific independent production companies has produced a film every 12-18 months for almost two decades. Its accounts reflect that consistency; although thinly capitalised and almost certainly paying out to its management, rather than retaining, substantially all it generates in terms of profit it has nonetheless expanded its balance sheet by a six-figure amount since the end of the original review.

Despite well established US and European connections, a third company appears to have undergone a period where it struggled to develop and produce films on a par with its earlier successes, though recently appears to have been more active. Whilst its gross assets have quadrupled since the end of the original review period, it recorded significant retained losses during that period.

A fourth company continues to be a regular producer of independent feature films, though the decrease in the strength of its balance sheet across the original review period appears to have continued and the company’s latest accounts show a significant increase in retained losses compared to the six figure positive reserves at the beginning of the original review.

The final example of a ‘continuing’ member of the independent sub group is structured around a long-term partnership of two experienced producers that has continued to develop and produce critically acclaimed and popular films. Its latest accounts are similarly impressive in the context of its peers, with perhaps the strongest balance sheet amongst those that remained in the sub-sector. Despite being ostensibly one of the most successful, like most other production companies its balance sheet fails to ascribe any value to any rights in the films it has developed and produced.

The next two examples are perhaps struggling on the margin between ‘continuing’ and ‘ceasing’; despite the loss of a key member of the management team, the first has continued to produce films, and occasionally TV movies, though not quite at the same frequency as before the end of the original review. Its accounts are perhaps indicative of the changes, with retained losses doubling since the end of the original review period.

Similarly the second company appears to have undergone a relatively quiet period in terms of films released, but currently has several in development, production and awaiting release. There has been a marked deterioration in the company’s balance sheet, with retained losses increasing by a factor of ten since the end of the original review period.

The next example appears, unfortunately, to be more clearly a company that has ceased active production. After producing two very successful films before the end of the original review period it appears to have struggled to continue its initial success with only one further film produced and released to date and that a relative disappointment compared to its earlier productions. Part of this may be attributed to the fragmentation of the creative team associated with the company’s earlier success. Its latest accounts reinforce the impression of a business in search of another successful release, with a frail balance sheet and six-figure retained losses having been generated since the end of the previous review.

Three other companies appear to have clearly ‘ceased’. The first effectively became dormant shortly after the end of the original review once its key executive ceased to produce films. The second hasn’t produced a film since the end of the original review and appears to have effectively become dormant once the management became active in the TV industry (via a separate entity). The third has not produced a film since the end of the original review period and recently became formally dormant.

Three other companies have migrated to become ‘Hybrid / Horizontally / Vertically Integrated Production Companies’ and are considered under that section of this review.

Perhaps one reason why many production companies clearly find operating an independent/stand-alone business a challenge is the extent of competition from other businesses operating similar business models. Of the twelve new entrants to the Independent Stand Alone category in this study, eight had been active during the previous study period but hadn’t met the criteria for selection during the review period (2006-2008). Several of these companies are long established businesses responsible for developing and producing well known, critically acclaimed and commercially successful films in the past and are headed by highly experienced and respected producers.

The first example is led by one such highly experienced and respected producer and, whilst not producing a film which met the criteria for the original review, has been a consistent producer of critically acclaimed and commercially successful British Films for decades. The company did subsequently meet the criteria for selection by producing a hit film. It has perhaps been buoyed by its recent success but seems unlikely to owe its relative balance sheet strength just to that one film. With net assets comfortably into six figures and excellent quick and current ratios the company seems well positioned to add to its distinguished track record.

Although the next company was established before the original review period, it failed to have a film released that met the criteria for selection during it. It has produced two such films since and its most recent accounts reflect its recent success. With cash reserves rising to almost a quarter of a million and retained earnings trebling to a healthy six-figure sum, the company clearly has the resources to fund continued development of high quality films if its experienced and highly successful owner/manager chooses to.

A long established partnership that has been included in the current sample as a result of the awards success of one of its recent films was also associated with a film that met both awards and box office criteria. Its trans-national business model is unusual, as is its policy of valuing its intellectual property on its balance sheet, which rose in its latest accounts along with its cash reserves.

The next new entrant also entered the group of companies by virtue of producing an award winning film. The accounts indicate little has resulted in financial terms from the critical accolade, with negative net assets and losses widening since.

The next three companies also reported relatively weak balance sheets in their most recent accounts, though for varying reasons.

Despite the length of experience of its management, the first remains a modestly capitalised company. After producing a well received and commercially successful film only a couple of years earlier, it had yet to convert a project from development into production up to the end of its most recent accounting period and this fallow period is reflected in its accounts during which it’s balance sheet has shrunk significantly, though it remained solvent and has successfully produced films since.

The second business entered the group by producing a follow up to one of the most popular films in British post war history (long in the making; the original was released before the original review period). Although not making the same impact as the original, the follow up still took over £2.5m at the box office. Much of the dividend has been taken out of the company or paid directly to the producer and, despite the office furniture being valued, no value is on the balance sheet for either the original or its sequel.

The third company is owned and managed by a producer whose experience spans over two decades. Previously collaborating in a number of businesses that successfully produced films, several of which qualified for inclusion in the original or this study, they established their own company shortly before the end of the original review period. Typically producing a film each year, two met the criteria for selection for this review and all have achieved a degree of success. This consistently successful and prolific track record has enabled the owner/manager to pay themselves significant six figure sums, though the company itself had less than £10k of net assets at the end of its most recent accounting period.

The final example of a company established before or during the previous review period which only met the criteria for inclusion afterwards is owned and managed by a former executive of a studio backed production business (which was included in the original review). A producer of popular and widely distributed films, its accounts indicate significant cash-flows, both into the company and out in the form of dividends to its owner.

The remaining four additions to the Independent-Stand Alone category were only established after the end of the previous review period, so were able to find critical or commercial success early in their corporate lives.

The first of these was, like the last example, established by a former manager at a company that had been included in the previous study; in this case by a highly successful former in-house producer at an integrated production business. Their new production business has continued this success with a string of very successful films. The resultant cash flow is evident in the accounts, but virtually all of this has been taken out of the company as remuneration and dividends.

The second new business was established shortly after the end of the original review period with its management moving into production from other sectors of the industry. After producing several films that were poorly received by critics, but with one generating sufficient box office revenue to meet this review's criteria for inclusion, the company's latest accounts indicate the business is struggling to continue and its founder directors have resigned.

The third was established after the end of the previous review period and, after producing a well received TV programme, has made two extremely well received films to date (it met the cultural rather than the commercial criteria for inclusion in this review). Although solvent, it continues to rely in part on capital introduced by tis owner/manager, with its critical success not yet translating into balance sheet strength. Its focus appears to be firmly on film rather than TV and so has been allocated to the Independent rather than the Integrated category.

The final company is both one of the most recently formed and most successful independent producers. Whether its untypical trans-national business model has been part of the reason for its success, it appears to have helped secure the rewards from it, with what appears to be a very effective corporate structure enabling the business to only pay a modest amount of tax whilst distributing seven figure dividends to its offshore parent.

## Is the Stock Market a Useful Source of Finance?

A small number of companies analysed as part of the original review were quoted on the Alternative Investment Market ('AIM'), where investment in shares can attract ostensibly valuable tax relief for investors[14].

Of these only one company's shares are still listed, though the company does not appear to have leveraged its listing to any great effect by, e.g., raising substantial new tranches of capital or acquiring new businesses. Its shares have traded in a wide range and it remains a small company even by the standards of the AIM market (the 'junior index' to the main London stock exchange) with its market capitalisation currently less than 5% of the average AIM-listed company.

Of the remainder, one appears to have ceased trading (though its parent continues) and two have de-listed.

The previous review concluded; *"Taken together these cases seem to illustrate a trend for companies from the film sector to able to list on AIM but not to use that listing to any great effect. The Initial Public Offerings may afford the original owners the opportunity to realise the value of their investment and the stock may initially be attractive to investors, however in general those companies currently listed on AIM appear becalmed. There is a very thin market in their shares and the cost and likely success of new issues appears prohibitive. Compliance with AIM rules appears to increase a company's cost base but the cost of delisting, and the possibility of finding private investors willing to buy out the existing investor base, appears equally prohibitive."*

Given the subsequent experience of the AIM listed companies in the original study, it seems those conclusions remain valid, however one of the new entrants identified as part of the subsequent review is very much an exception. It listed on AIM during that second review period in order to acquire complementary businesses and achieve a level of growth that would almost certainly not have been possible as a privately held company. Its strategy appears to have been successful and it is now significantly larger, solvent and profitable.

It appears that growing film businesses that want to raise finance to continue that growth ought to carefully consider their options before choosing to list on AIM. For companies that are determined to grow by acquiring other companies, and are judicious and/or fortunate in choosing those acquisitions, then an AIM listing may be an effective means of obtaining the currency to make those acquisitions and fund that growth. For others that are not as determinedly acquisitive, AIM may continue to be a costly distraction.

[14] Investments in most shares listed on AIM are eligible for Business Property Relief from Inheritance Tax and in some circumstances Capital Gains Tax on transfers of AIM shares can be deferred. If the shares meet the requirements of the Enterprise Investment Scheme ('EIS') then investors may also enjoy the additional benefits of the EIS (including income tax relief).

## Production Companies with Talent Attached

As with 'Independent' production companies, Talent Attached types of production company generate a fraction of the revenues Studio Backed and Integrated companies generate (around a tenth per the original review).

The sub-sector continues to be very thinly capitalised and also exhibits significant volatility amongst its members' results. Many companies had insolvent balance sheets.

The three types of experience (Continue/Migrate/Cease) observed amongst 'Independent' production companies since the end of the previous review period also seem to be relevant to those that adopted a 'Talent Attached' model.

Two companies have developed their business model since the end of the review period. The first, one of the most prolific UK film businesses, is also now associated with a number of TV projects. The company has been profitable since the end of the previous review period, with revenues doubling since then. Whilst the creative partners remained in a second company, which now has one of the strongest balance sheets amongst all the production companies reviewed, the company appears to have ceased to be active in Film, concentrating instead on commercials and TV work.

Two companies have ceased all activity since the end of the previous review with another operating at a significantly lower level of activity. The principals in the first of these have continued to collaborate with each other and with new partners since the company they owned ceased to be active, but appear to have eschewed the 'Talent Attached' structure for this more recent work. The second hasn't produced a film since the end of the previous review period and the partners recently confirmed their intention to pursue new ventures separately. A third company appears to have become less active, reflecting what appears to be a kind of interregnum in the filmmaking activity of the 'creative' side of the partnership, with its accounts appearing to reflect this subdued level of activity.

Of the remaining five 'Talent Attached' companies, one continues to be the corporate wrapper around a partnership that has produced a number of notable films that have been successful both in the UK and internationally. Its balance sheet fails to reflect the value of the intellectual property it has created, with aggregate retained losses at a similar level to those reported at the end of the previous review period.

Although another company has explored ways in which it can vertically integrate production with distribution, it remains essentially a 'talent attached' producer within the context of this study, with an insubstantial balance sheet which places no value on any underlying copyright or similar intellectual property.

One company continues to epitomise the 'talent attached' model, and has a relatively strong (though modest in absolute terms) balance sheet. The partnership at the heart of another company, a relatively new production business at the time of the original review, has continued to develop and produce films since then, though its balance sheet does not appear to have strengthened as a result.

The final company in this sub-sector survived the loss of one of the partners, but has continued to develop and produce critically acclaimed and commercially successful films with a new partner, though its balance sheet appears significantly weaker and it continues only with the support of key creditors.

Two of the original group of Talent Attached production companies were unable to produce a film the met the criteria for inclusion in the second review period, however ten companies that weren't included in the original study did produce a commercial or award-winning film that met the criteria for the period 2007-13.

Six of these ten companies were established during or before the original review period but didn't produce a film that met its selection criteria during that period.

The first of these is equally at home producing for television or cinema. Co-managed by one of the UK's most successful actors who also often plays a significant role in the production and development of the company's productions, its success on the screen is mirrored in its balance sheet, which is amongst the strongest in its sub-category.

The writer/director behind the second has been one of the most consistent in delivering commercially successful films for over a decade, some of them outright hits, though it remains a small company in financial terms with net assets of less than £100,000 per its latest accounts.

The third has proved a stable and productive business centred on a producer/director collaboration that appears to be growing in strength in terms of both the commercial success of its productions and the financial results that stem from them. Its recent accounts indicate a company that is growing steadily stronger, with increasing net assets and retained profits. Part of this may be attributed to the company's involvement in productions that do not appear to enjoy the involvement of the 'creative' partner, though they clearly remain at the core of other successful films produced by the company.

Although rarely collaborating together on a film produced by their company, the owners and managers of the next company produced films for around a decade before the death of the more creative side of the partnership. Their erstwhile partner subsequently joined a slightly larger team of filmmakers using a different legal entity and whether their original company will continue to be active in making films, with or without their involvement, isn't clear but seems unlikely.

The couple behind the fifth example are partners in life as well as in business, though it is the filmmaking of one of them that the company is focussed on. As a corporate wrapper round their talent it has, perhaps unsurprisingly, a modest but stable balance sheet.

The sixth company is just one of several entities that are connected by being owned/part-owned by a leading British filmmaker who, with others, has built a highly successful diversified media business. As such its modest balance sheet belies the resources at the disposal of its owners, though its continued success including in feature filmmaking does not suggest any imminent need for a capital injection.

The remaining four new additions to the Talent Attached group are all relatively new businesses established during the latest review period.

The first of these was established by a relatively inexperienced producer/director team shortly before the end of the previous review period. Whilst its first production certainly wasn't a failure, its second was a significant hit and appears to becoming a franchise. This success is evident in the latest accounts, with shareholder's funds doubling and a significant amount of undistributed cash at the disposal of the management.

The next is an ambitious production company founded after the end of the original review period by an actor. Whilst initially focusing on one particular genre of films, it has since established other businesses to address other clearly defined audience segments and has now developed a sizeable slate of films that it aims to produce in the near future. Its accounts perhaps reflect the strain, in terms of cash flow, of investing in growth as an independent production company; despite already having a number of films successfully released, it's retained losses have recently widened and both short term and long term creditors have increased.

Another was also founded by an established actor around the same time as the last with ambitious plans to produce both films and TV. Scoring a hit with its first film, its subsequent films have arguably had less impact, though none have flopped. It has recently bolstered its executive team and continues to develop and produce ambitious independent films, though whether it can continue to do so without an injection of working capital would seem to be uncertain; with retained losses, negligible cash and net current assets declining its balance sheet is now one of the weakest of all the companies included in this review.

The fourth and final new talent attached business was established by a producer and director after the latter's highly successful debut. Having itself only a short but successful track record in producing films since being formed, the Company appears to be currently relying on the support of its creditors.

## Venture Capital Investment in UK Film Businesses

Companies finance their business from a variety of sources. The original study noted that on average half[15] of SMEs in London (not just those involved in film) have no external funding whilst the balance typically obtain finance from bank and similar lending or venture capital. The latter can be formal private equity (professionally managed on behalf of institutional investors) or informal investment (ranging from family and friends to organised networks of business angels).

Private investment in individual film projects is quite common. Our own research indicated that around three quarters of films made in the UK on low budgets[16] rely on private investment. Whilst at higher budget levels the incidence is lower[17], it is still a common feature of film finance plans, especially when associated with a tax incentive such as the UK film tax credit and/or an Enterprise Investment Scheme (EIS).

However, on the basis of our original research and this review, there are few instances of venture capital investment in those UK film businesses that make, sell or distribute the most successful UK films.

One distributor, previously noted in the original review as a ‘classic’ venture capital success story, has continued to grow since the end of the review. Another was part of a group backed by a private equity consortium, but the consortium exited when the business was sold to a rival.

Amongst Sales Agents, one was sold shortly after the end of the previous review period by its owner/managers to another film business, the acquisition being funded by a US hedge fund. Another vertically integrated sales business had attracted equity finance for its film development activity and a vertically integrated production business is part of a global production and distribution group majority-owned by a large private equity firm which has continued to support the group and which now has revenues of around £ 0.5 billion and is one of the UK’s top 25 media companies. One of the new entrants to the sector during the latest review period also benefits from the support of private equity finance.

So whilst equity investment by third parties is a factor in the corporate finance of the UK’s film industry, on the basis of our research it appears to continue to be very much an exception not the norm. Those exceptions continue to be largely confined to larger, vertically or horizontally integrated sales or distribution businesses.

Unsurprisingly, given the difficulties many SMEs have experienced in obtaining loans from banks during the post-Lehman era, the low incidence of bank and similar institutional lending to all types of film businesses (as opposed to film projects) noted in the previous report also seems to have continued.

Taken together this seems to indicate that UK film businesses typically still do not have ready access to traditional sources of corporate finance other than their self generated working capital and there remains a wide ‘equity gap’ in the UK film industry.

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[15] London Technology Fund/Company Guides
[16] Low and Micro-Budget Film Production in the UK, June 2008
[17] Based on research undertaken by the UK Film Council

## Studio Backed Production Companies

The original review found that, whilst on a personal level working for a studio might be profitable, at a corporate level, the majority of the companies that enter into long term arrangements with MPAA companies generate significant losses.

However, whilst very few companies in this sub-sector are profitable, those that are profitable typically produce 'franchise' films for the studio to distribute and are highly profitable (before payments to directors are taken into account) with strong balance sheets.

Some companies appear to be operationally relatively independent whilst being fully owned by studios. Others not owned by studios ostensibly retain some independence, but appear to be financially dependent on studio patronage.

At the furthest remove from their studio backers are those companies not owned or attached by long term production financing deals but connected via, e.g. first look deals. Although these companies may be the most independent of all the companies in this sub-sector, they tend to make fewer films.

The sub-sector tends to have relatively high average turnover but thin operating profit margins. On the basis of the accounts, virtually all companies appear not to own the rights in the films they make.

In terms of their experience since the end of the original review, the nine Studio Backed businesses appear to have demonstrated a kind of 'curve' of results that arcs from complete withdrawal of support from their studio to continued success, especially when built around a 'franchise'.

One company appears to have completely ceased to be an active production company, with its key executives leaving the company. A second appears to be essentially dormant following the cessation of the partnership between the producer and his studio backer after changes in the latter's management and, ostensibly from the accounts, the failure to generate profits from films developed and produced by the company. The producer is now using a separate entity to produce films with a range of financing/distribution partners, i.e. has become an Independent 'Stand Alone' producer in the context of this review.

Although it hasn't yet repeated the success of some of its earlier films, and has been slightly less prolific, the third company has continued to produce commercially successful films on, typically, higher than average budgets. With one of the strongest balance sheets in terms of shareholders funds, it appears to have looser ties to its erstwhile studio backer, having some of its films released by other studio and independent distributors.

Despite being one of the least active production companies, with a balance sheet that reflects its modest level of production, the fourth company appears to have extended its first look deal with its studio backer.

Five companies have remained more orthodox 'Studio Backed' companies. The first of these continues to be one of the most prolific UK production companies, with revenues almost doubling compared to those reported during the previous review period. The next company continues to develop and produce large budget 'hi-concept' movies with the support of its studio partner, carrying forward a six-figure surplus of retained earnings whilst distributing surplus cash to its key executive. Another also continues to develop and produce large budget, hi-concept films with its studio partner providing production finance and distribution. Although results have been volatile, the company has continued to be highly profitable and whilst its owners have distributed much of what has been earned its latest accounts show its reserves at their highest since the original review period commenced.

The two remaining companies continue to service their successful franchises, generating significant profits and cash for their employees, directors and owners. Whilst both have developed and produced successful films outside of their 'core' franchises, one has used independent companies and other studios to finance and produce its films whilst continuing to work with its studio partner and its sister company in Los Angeles. Whilst still recording negative retained earnings carried forward, it has shown a modest strengthening of its balance sheet since the end of the review period.

Whilst the UK industry as a whole continues to enjoy what is arguably a very special relationship with Hollywood, no new Studio-Backed production businesses met the criteria for inclusion in the second review period, so whilst this part of the industry is relatively stable, it is so perhaps because it is in a period of managed decline in importance[18]. Together with the decline in the proportion of leading films released by MPAA members[19], including acquisitions from production companies that do not fall in the Studio Backed category, it appears that the MPAA companies have become less engaged with the indigenous[20] UK industry and the indigenous UK industry relies less on their involvement than in the previous review period.

[18] 22% of the leading production companies identified by the original study were backed by MPAA members, the proportion had fallen below 10% during the subsequent review period.

[19] Considered in more detail in the section on distribution below

[20] Changes in the level of inward investment production activity by MPAA members via wholly owned and managed UK subsidiaries is outside the scope of this review.

## Hybrid / Horizontally / Vertically Integrated Production Companies

In the integrated sub-sector the predominant model is of film and television production, though integration with sales and distribution is also evident. The original study found that, though the latter appears to enable more films to be released and distributed, the performance of those films appears to be relatively poor; vertical integration along the film value chain, with no other diversification of interests, does not appear to be the most successful model for a production company.

In general it is the TV and film model that continues to perform best, the more stable and continuous revenue from TV commissions apparently providing an even basis for the more uncertain and irregular returns from film production. On the basis of this review there seems to be no reason to amend that conclusion; for a production business it appears that horizontal integration, including some successful examples of cross border horizontal integration, is more effective than vertical integration, though there are exceptions.

In terms of turnover the hybrid, horizontally and vertically integrated companies continue to have relatively high annual revenues. The integrated companies also tend to be more profitable. Without recourse to management accounts it is not always possible to determine the extent to which turnover and profits accrue from film activities, but integration ostensibly offers an attractive model from the viewpoint of film production.

Perhaps because of this, and as noted above, three companies that originally adopted the ‘Independent’ model have migrated into horizontally-integrated businesses.

The first has built on its earlier success and produced a number of successful films, including in association with other companies. It has also developed a successful TV production arm. Its accounts partially reflect this success, with retained earnings increasing by a six figure sum, but the accounts ascribe no value to the rights, albeit likely to be residual rights, the company almost certainly has in its growing portfolio of film and television productions.

The second has also continued to successfully produce feature films but TV has become equally important to its business, at first producing single dramas then also producing commissioned drama series since the original review. The company’s interest in those productions has not been valued in arriving at a balance sheet that, conversely, indicates a weakening in its overall financial position.

The third ‘migrant’ has only produced a limited number of feature films since the end of the original review, with mixed results. Its owners have, however, diversified to create an eclectic TV, commercials and production services business with access to finance provided by a major European media group that acquired the company. The film business’s most recent accounts reflect the subdued level of filmmaking activity and include aggregate losses of around £ 0.3m generated since the end of the previous review period.

In addition to these three former 'Independent' companies, one of the original Talent Attached companies has branched out into TV production (see that section for details).

Half of the film businesses originally categorised as 'Integrated' in the original study have subsequently had mixed experiences.

One has focussed exclusively on TV since the end of the review period whilst another appears to have been affected by broader issues within the group of companies it belongs to. This appears to have affected both its ability to develop and produce films and its balance sheet, which shows retained losses have doubled since the end of the previous review period.

The third company continues to develop and produce film and television, and also act as a 'servicing producer' for international co-productions, but it appears to have remained a thinly capitalised, insubstantial business. The fourth is part of a small media 'conglomerate' and a long standing, very active and high profile producer of feature films. The film production company remains thinly capitalised and its latest accounts report a balance sheet total of less than £1m and modest retained earnings of less than £100k.

The final four businesses originally included in the Integrated category appear to have gone from strength to strength.

With the support of its TV parent, one company has continued to produce commercially successful films at above average budget levels and has significantly strengthened its balance sheet since the end of the review period.

Another company has experienced continued success on both film and TV since the end of the review period. It has one of the strongest balance sheets amongst all the production companies reviewed, with significant cash balances and 'best in class' current and quick ratios.

The production arm of a production/distribution business has developed and made some very successful films, including a 'franchise', since the end of the previous review period and although it's own balance sheet is similar to that reported at the end of the previous review, its sister company has grown significantly.

The final example is an infrequent but successful producer of films. This TV led company has increased turnover and profits and has a substantial and significantly stronger balance sheet since the end of the previous review period.

All of the nine new additions to the Integrated category were established during or before the original review period, some many years before, though many of them hadn't previously produced films and often were focussed on their complementary business, e.g. producing for TV.

The first two examples are amongst the longest established. One is a long established feature film, TV and commercials production company. Many of its longer-form works have won awards and been commercially successful. Turnover is relatively high and very stable and its latest balance sheet includes several hundred thousand pounds of cash and a current ratio comfortably above 1.0.

The other was formerly one of the most venerable British film companies, but appeared to suffer during several changes of ownership and strategic direction before joining a vertically and horizontally integrated group of companies that includes film production, finance, sales and distribution. The relatively stable period that followed saw the company produce its most successful film for many years, however there has recently been a significant change in the management of the group and the company's auditors make reference to the uncertainty of the company's ability to rely on the support of its parent in its latest accounts, which also show revenue and profits declining significantly.

In contrast, the next two new entrants were included in the study not because they suffered a long interval between 'hits' but because, whilst long established businesses, they are relatively new to feature film production.

The first is a long established producer of factual work, mainly for TV. It qualified for inclusion in the review by virtue of awards success for one of its most recent work, which was acquired and theatrically released by a distributor included in the Independent category below. Though a modest success in box office terms, the company appears to have benefited as a result, with its latest accounts showing increased cash reserves and a shift from negative to positive net assets.

Originally a niche production business, the other now has a range of businesses including feature film production. It also distributes some of its non-film work, but tends to rely on distribution partners for its feature films, including using both independent distributors and US studios. With it's feature film arm in between productions, it generated losses extending into six figures during its latest reporting period but these were tempered by its other activities, which generated profits that increased by almost 10%, and helped it maintain a strong balance sheet that included a significant amount of intangible assets and very healthy reserves of cash. Almost certainly it would not develop and produce feature films of the scale and ambition that it does without the steady and significant contribution from its non-film activities.

The next two additions to the Integrated category were all founded relatively recently.

The first is a relative newcomer to film production and has built out from its foundation in producing commercials and now operates several businesses in parallel. It remains a relatively small company but its latest balance sheet records a modest increase in net assets.

Although established during the previous review period, the next company first produced a TV drama after the end of that period and its first film was then subsequently released to widespread critical acclaim. An offshoot of a production services business operating in a range of creative industries that appears to have made a determined attempt to leverage the strength of its core business into producing content itself, its accounts reflect its initial success and its subsequent hiatus in terms of production. Its latest accounts show costs outstripping growth in turnover and the resulting significant losses have eaten into the reserves it accumulated previously, though it is actively developing both film and TV projects and appears to be able to rely on the continued support of its parent company, which has helped bridge short term cash-flow deficits.

The final three new entrants were arguably so successful that they have now been acquired by larger media businesses.

The first of these was founded shortly after the end of the original review period and since then has produced both films and, mainly, TV drama. With notable success in both media, it attracted the interest of a large international media company that recently acquired the company. Even before its sale the company's success had resulted in it having a very strong balance sheet relative to its peers and this afforded it the ability to pay seven figure dividends to its founding shareholders before the sale of their shares. Whilst its maiden set of accounts as a subsidiary show revenues and profits falling significantly it was still able to generate sizeable profits for its new owner.

The second made a broad range of critically acclaimed television programmes before successfully extending its business into TV drama series and feature film production. The latter includes an eclectic mix of genres, possibly reflecting the untypically large number of experienced figures that comprise the company's management. Perhaps unsurprisingly it appears this team have recently been made an offer they can't refuse by a much larger television business that has now acquired the company, though it's not yet clear whether and to what extent this will constrain its feature filmmaking activity in the future. Its last accounts as an independently owned production company seem to belie its attractiveness to its new parent, with no value placed on its intellectual property beyond the cost of projects currently in development or production.

The third company similarly extended its business model from TV into film production, though in its case the move into feature filmmaking has been focussed on adapting its most successful TV show. It successfully accomplished this and, perhaps as a result, also attracted the attention of a larger television business that recently acquired the company, though not before the original owners reaped the benefit of their success by the payment of significant dividends before their sale of shares. Its maiden accounts as a subsidiary show turnover, profits and cash reserves increasing significantly so it appears that the change of ownership has only increased the forward momentum of the business.

## Public Sector Investment in UK Film Businesses

Every year there is substantial public funding of UK Film, £363 million in 2013[21], significantly higher than the amount typically spent during the original review. Roughly half of this is provided via HM Revenue and Customs, mainly in the form of the UK Film Production tax relief[22], which is paid to companies that produce films certified as British, including the subsidiaries of US Studios and other foreign companies that make films in the UK.

Independently produced films are typically financed from a number of sources that fund Special Purpose Companies (SPCos) established with the single aim of producing an individual film. Whilst these are often subsidiaries of production companies, the production tax relief typically mitigates the risk for investors in the production and reduces the extent of investment required. The tax relief therefore arguably supports investment in film projects rather than the film businesses behind the films.

UK Film businesses can also utilise tax relief intended to support businesses generally, including Venture Capital Funds and Enterprise Investment Schemes. The latter is often used in combination with the specific production tax relief to fund SPCos and further mitigate the risk for investors. We did not, however, observe[23] the use of either Venture Capital Trust or EIS relief in financing any of the film businesses included in the original study or this review.

The BBC and Channel Four invest in and buy broadcast licences from special purpose companies, historically spending around £10-20 million per annum each via their film divisions.[24]The BFI invests in film projects at the development, production and distribution stages. It also supports a range of other activities, either directly or via third parties including film education and film heritage (including the national archive). The direct[25] expenditure of the BFI is currently around £90 million per annum, but it does not make any material investment in film companies per se.

The European Union (EU) also provides assistance to film companies either directly via its MEDIA programme[26] or via other programmes, though again this expenditure is typically directed at individual projects or used to fund training and advice rather than direct investment in businesses.

Taken together, on the evidence of both the original study and this review, we continue to believe that public sector investment in the film businesses that form the spine of the UK's film industry, as opposed to financial support for their films, is nugatory. On average perhaps less than £1 million per annum in total.

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[21] Please see the BFI Statistical Yearbook 2014 for a detailed analysis of expenditure.
[22] The exact amount depends on the value of production spend in any one year.
[23] It may be the case that such relief was utilised and not disclosed in the accounts examined, however the use of the relief would typically be reflected in certain entries in a companies accounts, e.g. the issuance of share capital. Whilst we can't be completely certain, we are confident that any use outside of SPCos is extremely rare.
[24] Please note this excludes amounts paid to acquire licences to broadcast British films after they have been produced.
[25] Excluding grants and expenditure delegated to other public organisations
[26] From 2014 the MEDIA Programme will be replaced by the Creative Europe Programme.

# 4. THE SALES SECTOR

## Summary

The accounts of 15 sales companies were analysed and allocated into three types; 'Independent', 'Vertically Integrated' and 'Branches of Overseas Companies'.

- The original study found that there appears to be a minimum threshold of around £2 million per annum in turnover in order for a sales agency to prosper, though exceptions exist.
- Whilst all the films in the original study had sales agents attached, four films in the latest review appear to be unrepresented by an agent.
- The attraction of London as a place to locate a sales branch of an overseas company appears to have waned. All three previous examples of London based sales branches of companies headquartered overseas have effectively ceased to be UK sales companies.
- Independent sales companies continue to struggle to operate profitably, typically having limited or no external access to corporate finance.
- Two of the five Independent sales companies have migrated to a vertically integrated business model whilst one was wound up.
- The 'pool' of companies that represent the most successful British films has decreased from 13 to 11, with vertically integrated companies in the majority.
- Vertically integrated companies vary greatly in profitability but most of those that remain in the category have seen continued improvements in trading.

Vertically integrated companies exhibited the most growth in turnover during the original review, with Independent companies growing the least. In terms of overall profitability, even adding back payments made to directors, most Independent agents appear to be continuing to struggle to operate successfully.

Four films that met the criteria for inclusion in the recent review do not appear to be represented in the international market by a sales agent. Two of these films met the cultural rather than the commercial criteria for inclusion and could reasonably be described as having a niche or specialised audience. Whilst the other two generated sufficient box office revenues to be included in the review, it is probably fair to say that they were almost certainly always destined to have limited appeal to audiences outside the UK. Whether by choice or necessity it appears that each film's producer is representing the film internationally. Whilst this is worthy of note, given the nature of these particular films, it may be premature to conclude this represents the emergence of an alternative model of international distribution for the most successful independently produced British films.

## Independent Sales Companies

Two of the Independent sales companies have migrated to a vertically integrated business model (and are considered further under that heading) whilst one was wound up after the end of the original review despite being one of the larger sales companies in the Independent sub-category and having a balance sheet stronger than both the mean and median for that category. The company had been profitable throughout the original review period except for the final year, when it reported a significant decline in revenue and substantial losses. The erstwhile CEO subsequently established a radically leaner international sales and financing business with a strong genre focus. Despite what appears to be a determined attempt to limit overheads, this new business' latest accounts reveal a deeply indebted company dependent on the support of its principal creditor, though with several ambitious projects already successfully delivered to the market and more currently in production it may well ultimately prove to have been a successful transition.

The two remaining companies originally allocated to the Independent sub-category were the smallest in the sub-category during the original review. Since then they appear to have continued to be essentially corporate wrappers around small teams of experienced international salesmen and women, though both appear to have considered adapting their business model.

One of these companies appears to have diversified towards vertical integration, establishing a UK associated production company and collaborating with a non-UK producing partner. The early results of this collaboration appear to be encouraging with their first co-production experiencing success at some leading festivals. Production activity appears to be largely undertaken by the production partner, with the agent remaining focussed on bringing the films to market together with other acquisitions, so the company has been kept in the Independent category.

Although the other remaining Independent company has flirted with vertical integration in the past by means of formal collaborations with production and distribution businesses, it remains a 'classic' Independent sales company, and markets itself on that basis (i.e. emphasising its independence).

The aggregate balance sheets of these two remaining Independent sales agents amounts to less than £100k and both have fixed assets of less than £10k each. However, the accounts of both almost certainly understate their value as going concerns; both have modest but valuable portfolios of licensed rights with one company in particular holding sales rights to films that will clearly have a value in the international film market for many years to come.

The original review found that:

> *"UK independent sales companies typically have limited or no access to corporate finance (other than internally generated working capital). …there are fewer staff in independent sales companies and they are paid less,*

> *probably because they generate losses. …in terms of overall profitability, even adding back payments made to directors, UK independent agents appear to be struggling to operate successfully.”*

It appears that subsequent events support those conclusions and the business of being a truly independent sales agent remains a tough one, with previous incumbents either navigating their way towards new types of business model or persevering through being very tightly resourced, low overhead businesses focussed around very small teams of experienced sales executives.

## Vertically Integrated Sales Companies

Of the five original Integrated sales companies, one entered administration shortly after the end of the previous review period and a year later began a creditors voluntary liquidation. The sales side of the business appears to be breaking even in the aftermath of the reorganisation. Another is very much a ‘sales arm’ of its parent production company and continues to be dependent on its owner both for a significant part of its supply of film rights and for on-going financial support. Accumulated losses have quadrupled since the end of the original review period and now represent almost six times turnover.

After the end of the previous review period the third member of this category entered into a joint venture with another UK film company largely operating outside the sectors it had traditionally operated in. The resultant sales company appeared to offer synergies to both partners, but after appearing to suffer a significant downturn in sales activity and accumulating significant losses during the period of joint ownership, the management bought out the majority of the shares held by the partners. It is too early to say whether the revised ownership has resulted in an improvement in fortunes.

The fourth company’s turnover grew throughout the original review period and that trend appears to have continued. Latest reported revenues are almost double those reported at the end of the original review, with continued strong growth evident from the company’s latest accounts. Much of that growth is clearly due to increased production activity, which, along with international TV sales, accounts for the majority of the company’s trade. International film sales continues to represent an important segment of the company’s business however, accounting for less than a fifth of revenues but generating around a quarter of the company’s profits.

As with the previous example, the fifth company appears to have continued to grow steadily, with evidence that growth is continuing. The most recently reported revenues are around half as much again as at the end of the original review. Almost certainly the value of the company has continued to increase, though the full value of the company’s portfolio of film rights does not appear to be included on its balance sheet.

As noted above, two companies were reallocated from the Independent category. Although the first of these businesses had interests outside of international sales at the time of the original review, its core business during the period 2004-2008 appeared to be international sales and it was therefore originally allocated to the ‘Independent’ category. Since then there has been a significant expansion into production services and financing, including an acquisition of a production services company, so it has been re-allocated to the vertically integrated category.

Since the original review, another Independent sales company has floated on AIM, expanded its financing operations (e.g. taking advantage of the EIS scheme to help provide and manage production finance) and more recently has diversified into UK distribution and so has also been re-allocated to the vertically integrated category.

Another company, formed shortly after the end of the original review period, has sold several titles that meet the criteria for inclusion in this study. With the support of associated companies active in other parts of the film value chain and access to private equity finance, the company's latest accounts show turnover increasing, though overheads, which have increased at a faster pace, have reduced its overall profitability. Recent profits have, however, been sufficient to eliminate losses accumulated during its start up phase and it now appears to be well established with an ability to advance minimum guarantees to acquire new films to add to its library of rights. The value of that catalogue of rights is represented in its balance sheet as substantial outstanding advances recoverable over the remainder of the sales term, though it appears that some modest write-offs have already been incurred.

## UK Branches of Sales Companies Headquartered Overseas

The original review found that, except for one company that generated modest average losses of £195k over the period under review, UK sales businesses with owners based outside the UK appeared to have the most robust business model, generating average profits of £3 million (excluding the loss-making business).

Since the end of that review, all the representatives of what appeared to have been a successful business model have ceased to be active, London-based sales agents.

The first was liquidated after the end of the original review as part of the collapse of its parent company.

Whilst retaining a presence in the UK, the entire sales team and many of the staff in related functions of the second company allocated to this category in the original study have been relocated back to the parent organisation and so it would seem unreasonable to continue regarding the business as UK based.

The parent of the third and final company originally allocated to this category merged with a similar international film business and, as part of the merger, its London sales operation was closed with key staff leaving to form a new London-based film sales company with support from a new non-UK film business.

## Trade Credit within the Film Value Chain

Trade credit, the amounts owed by one company to another, plays as important a part in the corporate finance of most UK film businesses as any other source of funds.

The original study found that distributors take the longest to pay their creditors, followed by sales agents, and lastly producers. Average payment practice ranged from extremely efficient: a matter of days in the case of one company, to over nine months for another.

The vast majority of Trade Credit in the UK Film Industry is tied up within the Distribution Sector[27]; over £57 million for the distribution companies analysed as part of the original review.

It appears still to be the case that, given the frailty of their balance sheets, it might be difficult for some distributors to reduce the time taken to pay their creditors as there may simply not be enough money in their business to make a sudden shift in policy, even if they wanted to. There are, however still some stark examples where the businesses are clearly able to pay their creditors more promptly but, ostensibly, choose not to.

A review of the distributors identified as the slowest to settle their liabilities in the original review showed one had further extended the trade credit it extracted from its suppliers, with the latest accounts indicating the average time it took to settle its debts increasing by over a month since the original study. Whilst the distributor previously identified as the most dilatory had shortened the time taken to settle its debts, its latest accounts indicate it still takes almost seven months to pay its creditors.

[27] Distributors may only be enjoying the luxury afforded by the customary terms of trade within the industry whereby accounting is made quarterly. If one assumes that, on average, revenues are received mid quarter, that would give approximately 45 days before the distributor ‘ruled off’, add another month to issue the accounting statement and around 5 days to make the payment and the 69 day average observed during the original study would appear reasonably in line with industry custom and practice.

# 5. THE DISTRIBUTION SECTOR

## Summary

The accounts of 21 distribution companies were analysed and allocated into four categories; ‘Independent’, ‘Vertically Integrated’, ‘Mini Majors’ and ‘Multi Territory’ (i.e. Horizontally Integrated)

- As with the sales companies, the ‘pool’ of distribution companies that represent the most successful British films has decreased (from 19 to 16).
- In contrast to the consistent pattern of growth noted across all sub-sectors in the previous study, only Mini-Majors appear to have experienced continued growth as a class. Most businesses in the other categories appear to have fallen further behind the Mini-Majors.
- Of the seven original Vertically Integrated distributors, three appear to be successfully developing their business, one appears to be at a crossroads another is struggling to survive and two have ceased trading.
- The original study concluded that vertical integration appeared to offer little advantage to UK distributors. The mixed results of distributors in this category since the previous review would seem to support the view that vertical integration of itself does not offer any particular advantage, with other factors (such as rigorous cost control) seemingly more important in determining success within vertically integrated distributors.
- All three distributors seen as successfully pursuing a strategy of horizontal integration in the original review appear to have either abandoned their strategy or have been unable to successfully execute it in the period since the original review.
- All six distributors categorised as Independent in the original study have continued in business since then, but with mixed results and typically with balance sheets that appear vulnerable to downturns in trading.
- The ability of distributors to manage working capital appears to have deteriorated (though typically from a position of great strength). The most delinquent in paying suppliers as noted in the previous study still takes almost seven months on average to settle its liabilities.
- During the original review period distributors could, on average, only cover 16% of their liabilities with cash.[28] Although there are individual exceptions, there seems little evidence of any significant improvement in the liquidity of

[28] Please see the original study for the basis of calculation.

distributors generally since then except for Mini-Majors, which on average have improved both quick and current ratios.

- The original study found that cost of sales had typically risen along with turnover, with Mini-Majors' increased costs outstripping their turnover by the highest margin. In contrast the Mini-Majors now appear to have been able to grow revenues faster than direct costs since the end of the previous review, whereas companies in other subcategories that achieved growth in turnover typically saw direct costs increase at a higher rate.

- Whereas there was conflicting evidence in the original review, access to VoD audiences now appears to be emerging as a critical success factor, with two companies attributing their overall growth in profitability directly to widened access to VoD markets.

- MPAA members released just over half of the films that met the selection criteria during the original review period, but released less than one in three of the films that qualified for inclusion in the second review period.[29]

- It appears that the increased success of the Mini Majors is a principal reason for the decrease in the proportion of the most successful UK films released by MPAA members; on average each Mini Major released more commercial and/or critical UK 'hits' than each MPAA member during the second review period.

[29] Because of differences in the method of analysing the results, the proportion of films released by MPA and/or Mini Majors may not be directly comparable, however the findings should be materially accurate.

## Independent (Stand Alone) Distributors

Of the six companies originally allocated to this category, one company's balance sheet had strengthened since the original study, helped by retained earnings and a share issue, but remained relatively weak (less than £30k of aggregate net assets). Another appears to have been trading more profitably recently, almost eliminating the six-figure deficit on its retained earnings at the end of the previous review period. Much of this improvement is, however, effectively invested in the company's debtors, which have increased more than threefold and now outweigh the cash it holds by a factor of almost 20. With sizeable current liabilities and wafer thin net-equity any significant deterioration in its ability to collect its debt is likely to require its owners to inject funds to continue trading.

A third is similarly very thinly capitalised with the owner/managers apparently taking profits out of the business as they accrue, leaving no free cash in the company, though it appears to have continued to trade very steadily. In contrast, the fourth company, whilst apparently solvent and with relatively healthy reserves of cash, appears to have had to navigate a marked downturn in trading activity. Another suffered a steady decline in gross profits during the review period after the loss of its most important supplier of film rights, though this was offset by significant interest receivable and similar income generated by the very large cash balances it had accumulated (it was previously identified as the best distributor in terms of credit control, but one of the worst in terms of paying its own debts). The latest accounts indicate the decline in profitability has continued, with gross profit during the last two years continuing the pattern of double digit percentage year on year declines evident during the original study. This appears to have taken its toll on its balance sheet, which has lost a quarter of its value. Whilst it still has significant holdings of cash, its former iron-like grip on its debtors has loosened, with the average time taken to collect its trade debt more than trebling since the previous review.

The last distributor in this category experienced an even steeper decline in turnover, losing around four fifths of its business after the loss of a key supplier of rights. Perhaps as a consequence the company's management split, with those remaining in the business facing the challenge of operating at a much reduced level of activity. Previously identified as one of the companies that extracted most trade credit from its suppliers and customers, the business has also seen the time it takes to collect its debts widen significantly. It has, however, passed the bulk of this effect on to its trade creditors who now, on average, have to wait yet another month longer to be paid.

The sole new entrant to the Independent category has gradually built its business by focusing on a particular genre and, whilst still a relatively small company its finances were undoubtedly bolstered by its release of the film that met the 'cultural' criteria for inclusion in this study but was also, in the context of its business to that point, a breakout hit. Its balance sheet strength shows a modest decline according to its latest accounts, but it appears to remain a tightly focussed niche distributor with a modest but growing library of film rights many of which it has been able to advance minimum guarantees to acquire.

## Mini-Majors

All three Mini-Majors increased their turnover throughout the original review.

The only consistently profitable Mini-Major during the original review appears to have continued to grow both revenue and profits. Its balance sheet is enhanced as a result with shareholders funds now over six times the level shown at the end of the previous review and total gross assets trebling over the same period.

The second has also continued to increase annual turnover, with its latest results reporting revenues over seven times higher than at the beginning of the original review. In its latest accounts it reported seeing increasing TV (incl. VoD) revenues more than offsetting declines in Theatrical and DVD during the latest two years. The company is now profitable and has strengthened its balance sheet.

Arguably the third performed so well it became an acquisition target, expanding by acquiring a non-UK distribution business and then itself being merged into a former rival. In its final set of accounts before the merger it reported revenues over three times higher, shareholders funds turning positive and a balance sheet twice the size than at the end of the previous review.

These three original members were joined in this category by a fourth that did not release a film that met the selection criteria during the original review but was the most prolific distributor of leading independently produced UK films in the subsequent review period. Growing organically and by acquisitions, it is now a substantial multi-national business with consolidated revenues and a balance sheet total measured in hundreds of millions of pounds. Perhaps as important as its ability to purchase and integrate complementary businesses is its focus on digital distribution, with over 20p in each pound of income now being generated by the on-line consumption of its titles.

## Multi Territory Distributors

After being acquired by a private equity group, one Multi Territory distributor effectively closed its UK distribution operation and appointed a Mini-Major as a sub-licensee for its UK distribution rights.

A second also withdrew from UK distribution shortly after the end of the previous review period. Although still active in the film industry, it now uses a Hollywood 'Major' as its UK distributor.

The third entered administration and whilst its parent company still survives it is clearly struggling to continue as a going concern.

## Vertically Integrated Distribution Companies

Of the seven companies allocated to this category in the original review, three appear to be successfully operating as part of vertically integrated businesses.

One has steadily grown in size, with its library of film rights now valued at around half as much again as at the end of the previous review period.

Another's turnover had trebled since the end of the previous review period, helped by a successful franchise. Although the financial effects of this sequence of films appear to have begun to decline, sharp reductions in cost of sales and overhead costs have enabled it to increase the operating profits reported in its most recent accounts.

The third example had even more dramatic growth during the previous review period and this appears to have continued into its more recent trading history; in particular a significant new VoD deal struck by the company had trebled revenues under that category.

One company had seen significant growth in revenues during the previous review period and that trend appears to have continued until recently where they declined. This was largely attributed to falling DVD revenues, though the company had increased profits in the face of this by tight control of both direct costs and overheads. The resulting internally generated cash-flow was being used to add to its library of film rights, in particular funding increased co-production activity, enabling the company to secure selected titles earlier in its life-cycle.

The three remaining vertically integrated distribution businesses have clearly not been successful since the original review. One entered administration shortly after the end of the previous review period and a year later began a creditors voluntary liquidation. This saw the creation of new companies into which the group's former businesses were transferred. Unfortunately the new distribution business does not appear to be any more stable, with retained losses widening significantly in its most recent accounts.

Another also ceased active trading shortly after the end of the review period, with its investment in film rights gradually realised since. The third appears to have closed its UK distribution activity.

## Why Are Mini-Majors So Successful?

In parallel to this review, the BFI Research and Statistics Unit (RSU) examined the theatrical release patterns of 558 independently produced UK films released in 2008-2012. In particular the width of the release of films, at the widest point, was analysed and compared to their box office. This shows most narrow-release titles are released by 'Other'[30] distributors and the relative effectiveness of Other distributors when releasing films more widely. Ranking the relative success (based on average box office achieved) of the three categories of distributor used in the RSU review against the bands used to analyse the widest point of release (WPR) gives the following results:

| WPR band | Most Successful | Mid-Successful | Least Successful |
|---|---|---|---|
| 400+ | Other | Mini-Major | Studio |
| 200-399 | Mini-Major | Studio | Other |
| 100-199 | Other | Mini-Major | Studio |
| 50-99 | Studio | Mini-Major | Other |
| 20-49 | Studio | Other | Mini-Major |
| 5-19 | Other | Studio | Mini-Major |
| Under 5 | Other | Studio | Mini-Major |

The limited number[31] of Studio releases in the WPR bands 20-49 and 50-99 would reinforce this presumption in favour of Other distributors. There was, however, only a narrow difference between average box office for films released by Mini-Majors and Others in bands where Others are more successful. In contrast, Mini-Majors eclipse Others in terms of average box office when the former are more successful:

| Average UK box office per film (£k) | | | | |
|---|---|---|---|---|
| WPR band | Mini-Major | Other | Difference | % |
| 400+ | 11,554 | 12,628 | (1,074) | (9.3) |
| 200-399 | 2,436 | 743 | 1,693 | 69.5 |
| 100-199 | 1,010 | 1,015 | (5) | (0.5) |
| 50-99 | 429 | 280 | 149 | 34.7 |
| 20-49 | 104 | 117 | (13) | (12.5) |
| 5-19 | 24 | 26 | (2) | (8.3) |
| Under 5 | 4 | 4 | - | - |
| Total | 2,194 | 263 | 1,931 | 88.0 |

So it would appear that, in general, Mini-Majors have the edge over both the Studios and other categories of distributor in terms of achieving relatively high box-office per print. If they are also able to control their advertising and acquisition costs, as they appear to have done since the end of the previous study, then it is perhaps no surprise that Mini-Majors are becoming stronger and businesses in the other categories examined in this review appear to have fallen further behind the Mini-Majors in terms of their corporate financial strength.

[30] Neither major nor mini-major, i.e., using the terminology of this review, 'Independent' 'Vertically Integrated' and 'Multi Territory'. It was not possible to further analyse the 'Other' category into 'Independent' or 'Vertically Integrated' and there was a difference in the definition of Mini-Majors but this is unlikely to substantially reduce the relevance of the findings.

[31] Only 3 films in these bands were released by Studios. Discounting these would promote 'Other' to 'most successful' in all but two WPR bands.

## Glossary

### Calculations:

Averaging of Results (regarding references to the original study):

Due to the variation in availability of annual accounts for the sample companies, average results for each company were generated from the available information and then averaged again to give sub-sector averages. Sector averages were calculated by taking the average results for each company and averaging them again (i.e. rather than simply totalling the sub-sector averages and dividing by the number of sub-sectors).

Creditor Days: The Creditor Payment Period is an efficiency test that measures how long a company takes to pay its bills.

$$\text{Creditors Collection Period} = \frac{\text{Trade Creditors}}{\text{Cost of Sales}} \text{ x365 = days}$$

Current Ratio: The Current Ratio expresses a company's current assets in relation to its current liabilities; this indicates its ability to meet short term obligations.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} \text{ x100 = \% Ratio}$$

Debtor Days: The Debtor Payment Period is an efficiency test that measures how long on average customers take to settle their bill: ie how long the company takes to get paid.

$$\text{Debtors Collection Period} = \frac{\text{Trade Debtors}}{\text{Turnover}} \text{ x355 = days}$$

Gross Profit Margin: Expresses Gross Profit as a percentage of Turnover, the Operating Profit Margin does the same for Operating Profit.

$$\text{Gross Profit Margin} = \frac{\text{Gross Profit}}{\text{Turnover}} \text{ x100= \% Ratio}$$

$$\text{Operating Profit Margin} = \frac{\text{Operating Profit}}{\text{Turnover}} \text{ x100 = \% Ratio}$$

Quick Ratio: The Quick Ratio (also known as the Acid Test ratio) expresses a company's cash in relation to its current liabilities; this is a more stringent indicator of a company's liquidity.

$$\text{Quick Ratio} = \frac{\text{Cash}}{\text{Current Liabilities}} \times 100 = \%\ \text{Ratio}$$

**Terms:**

Churn Rate:

A measure of the number of items moving into and/or out of a collective group over a specific period of time. Most widely applied in business with respect to a contractual customer base, in this study it refers to the gross change in the number of companies that began in a particular category, i.e. adding the number of new entrants and start up companies to the number that left that category by ceasing trading, changing business model and, in the case of production companies, failing to make a film that met the criteria for inclusion, then dividing that number by the original members in the category. The resultant ratio gives an indication of the dynamism or stability of the category, with higher ratios indicating increased levels of change in membership. N.b. a high ratio may not necessarily have negative implications if, e.g., it is as a result of a relatively large number of new entrants.

Equity Gap:

Many SMEs require much greater funding than that which can be provided by business angels, but do not need the levels of funding venture capitalists would consider (typically > £2m). The gap between these two financing situations is known as "the equity gap".

GBO: Gross Box Office

Hit Film:

For the purposes of this analysis each company's 'hit' film is that which records the highest UK GBO for the period reviewed; a company's best performing feature film in the UK.

Hybrid/Horizontally/Vertically Integrated Company:

A company operating in more than one business sector, eg a vertically integrated film production and film sales company, or a horizontally integrated company operating film and television production businesses.

Independent Company:

A company operating as a single entity rather than being under the control of a larger company or group.

Insolvent Balance Sheet:

A balance sheet exhibiting negative Net Assets, i.e. the company's liabilities exceed its assets. Please note, this does not necessarily mean that the company is insolvent, it may be the case that the company owns assets that are not valued or undervalued in the accounts or that it can rely on the support of a parent company, a shareholder or a third party (eg a Studio) for financial support.

Mini Major:

A distributor operating the same model as an MPAA member (major) studio, with interests in production / financing, sales and distribution, employing economies of scale and distributing mainstream films (albeit on a smaller scale), but without being an MPAA member or matching their scale of operation.

ISA

Individual Savings Account. An account in which a UK taxpayer can invest up to a certain amount each year in a fund through which they can purchase shares and similar investments in qualifying companies and avoid tax on any resulting income and capital gains.

SME

Small or Medium Sized Enterprise. The Companies Act 2006 (Amendment) (Accounts and Reports) Regulations 2008 updated the official definitions used by Companies House and HM Revenue and Customs so a company is "small" if it satisfies at least two of the following criteria:

- a turnover of not more than £6.5 million;
- a balance sheet total of not more than £3.26 million;
- not more than 50 employees

A medium sized company must satisfy at least two of the following criteria:

- a turnover of not more than £25.9 million;
- a balance sheet total of not more than £12.9 million;
- not more than 250 employees

The definitions for small or medium sized groups of companies are similar but slightly more complex. The EU adopts similar definitions in terms of number of employees but its criteria for turnover and balance sheets tend to be significantly higher.

Special Purpose Vehicle Or Single Purpose Company:

A company separate to the permanent production company, set up for the production of an individual film through which the finance for that film flows.

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