



Analysis of Initial Public Offering Digital Entertainment Network (>en)

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Published in The VIC/e, online newsletter of the
Venice Interactive Community 1999

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>EN filed an S-1 last year to raise \$75,000,000 in equity. At this time there is no pricing set. Operating costs, including production of 13 webcast series, for the first six months of 1999 were approximately \$20,000,000. Zero sales revenue was listed, although they have deals with Microsoft, Ford and Pepsi that will each pay them from \$2,500,000 to \$4,100,000 in cash and trade-outs in the near future. Their proposed NASDAQ symbol is DENX. The site opens with a bumper that says: "Spank Your Mind".

Company Description

>EN is pioneering the production and delivery of Internet-based digital entertainment and information services to redefine the entertainment experience for a new generation. >EN has created a digital media network to provide a single online destination for youth between the ages of 14 and 24 to access original, youth-oriented, interactive entertainment and music, participate in building online communities and purchase consumer goods and services.

>EN seeks to revolutionize youth entertainment by creating a rich hybrid experience that combines the best aspects of television and the Internet.

>EN's network features a new format of original, interactive programming similar in appearance to television, consisting of short-format, linear video content surrounded by related interactive multimedia content and activities. >EN produces programming specifically for online distribution.

>EN intends to distinguish their brand by integrating music, community features and electronic commerce specifically targeted to their youth audience.

Astrological Forecast (from the free report section of Kelli Fox's iVillage astrology.net and chartshop.com)

>EN is a Gemini, born on June 4th, 1996.

General Personality Characteristics

You are, in many ways, an eternal child. Your mind is bright, alert, curious, flexible, playful, and always eager for new experiences - and your attention span is often quite brief. You grasp ideas quickly and once your initial curiosity has been satisfied, you want to go on to something else. You crave frequent change, variety, meeting new situations and people.

It may be hard for you to decide just where your talents and true vocation lies, for you have a multitude of interests and are loathe to limit yourself by concentrating on just one. You are easily distracted by all of the other fascinating possibilities. Your curiosity and restlessness propel you into many different experiences in life, and you are willing to taste or try anything once. Doing the same thing over and over again, even if it is something you do well, is real drudgery for you.

Mental Interests and Abilities

Your mind operates in a very deliberate and methodical manner and you dislike being rushed or forced to give an opinion before you have thoroughly ruminated and digested an idea. You are also difficult to influence once your mind is made up.

Though slower to grasp new concepts or learn new skills, you are patient and persevering and, in fact, often become quite adept at whatever you put your mind and hand to, for you are willing to devote much time and attention to it. You succeed not so much because of your mental brilliance, but because you have the ability to concentrate and follow a project through to its completion. You have an aptitude for singing or drawing.

When I Tried the Site

I use a Pentium II 400 with 168k of RAM, a 10 gig HD, and a 17 inch screen with a Mediaone cable modem and a US Robotics 56k telephone connection.

I spent about fifteen minutes surfing >en with a cable modem on January 30 (and had visited it a half dozen times before), and then switched over to the 56k phone modem on February 2, and the difference was significant.

With a 56k connection, I know I'm in trouble on a site when the sponsor banners are in motion <Pepsi> and YOU STILL HAVE 50 ITEMS REMAINING to download. Therefore, in order to benefit from the production values >en has invested heavily in, you should have high-speed connectivity.

Branding For an Internet Site

Lesson One. Branding an internet site is based on two words: "dot com", and DEN ... is a DOT NET site. This is not a minor detail. I was reading a story about >en: Teen Network Plays In IPO Market

by Phil Harvey, Redherring.com, October 09, 1999, and I clicked through on the link Red Herring has under the Company Profile. Problem is, it hits <http://www.den.com>, The Bear's Den - Where a Bear Feels At Home; The website for short sellers. I'm sure this occurs frequently and explains why when I typed in den.com the first few times, I couldn't get in.

Overall, the production values of >en are magnificent, and the music was pop-catchy enough to keep me on the site. Just to make a quick comparison, I checked out competitors, including Craptv, Atomicfilms, Moviehead, Honkworm, etc., and SHOCKWAVE.com was the only site that came close to >en in delivering the kind of quality I expected from a web-casting production company. So even though videos didn't download well on a 56k connection (but the music worked great), their survey rejected me for the free T-shirt no matter what age I entered, and I'm too old for most of the content, I liked >en because THEY WALK THE TALK; they have a digital entertainment network.

Competition

There's been a lot of buzz lately about new artistic strategic content partnerships including: Tim Burton and Shockwave, Robin Williams and Audible.com, Larry David and Icebox.com, and Artisan and Intertainer. I believe >en's real competition is Fox or MTV.

What They're Going To Do

Entertaining Generation Y with netcast content is the mantra of this company, and they plan to invest \$20,000,000 to capture music market share.

>EN's Strategy

Provide a unique entertainment solution for Generation Y: (with a) One-stop entertainment network, (with) Original interactive programming, Music, Community, Commerce, Access to a broad youth audience, Innovative online advertising solutions, Sponsorships, (and) Commerce.

Management - What a difference a day makes.

Who WAS in charge	Who IS in Charge	Title	Salary (from S-1)	% >en Owned
M.C. Rector	Nope	Former director/founder	Not listed	56.51%
H. James Ritts	Nope	Former Executive	Was \$350,000	1.10%
David Neuman	Yep	President and director	\$1,500,000	3.27%
Edward Winter Jr.	Yep	Chief Marketing Officer	\$1,000,000	2.06%
Bruce Gamache	Nope	Former CFO & COO	Was \$400,000	1.65%
Chad M. Shakley	Uh Uh	Former director/founder	Not listed	10.31%
Brock Pierce	No	Founder and former	Was \$250,000	4.76%
Alan L. Friel	Yea	Chief Administrative & G.C.	\$250,000	>1%
Greg Carpenter	Yes	Was CTO, Now CEO	Was \$375,000	0
Gary Gersh	BIG TIME	Former Enmusic, Now CHAIRMAN	WAS \$600,000 (+\$?)	2.53%
John P. Silva	Yes	President en.music	WAS \$600,000 (+\$?)	2.21%
Mitchell Blutt	Must be	Director	Not listed	8.08%
Robert Doede	Must be	Director	Not listed	>1%
Gilbert Friesen	Must be	Director	Not listed	>1%
Marc Nathanson	Must be	Director	Not listed	0
Murray Neidorf	Must be	Director	Not listed	>1%
Jeffery Sachs	Must be	Director	Not listed	8.09%

Employment agreements run (ran) through 2002 and 2003 depending on the executive. Most executives receive(d) stock options and/or cash bonus' when employed or upon goal attainment.

Production

An estimate of Internet series production costs according to a recent Forbes article is \$20,000 per episode, as opposed to TV at \$2,000,000. >en's average cost is \$90,000 per episode.

Given the quality and obvious commitment to using production values to differentiate itself from other sites, to give you an idea of how many people it takes to give a spanking to a teenage mind these days, the credit list for an episode of the >en series Frat Ratz ran to 100 people, not including "the brothers at Lambda Chi Alpha Fraternity, UCLA."

The Money

To date >EN has raised \$74 million, primarily from the sale of convertible preferred stock to half a dozen parties in the past two years. Recently, they've announced a fresh \$24 million infusion from Chase Capital, NBC, Enron and Intel, among others.

There were 7,489,584 actual shares of common stock outstanding as of the filing date. Pro Forma-ed after the conversions, the S-1 states around 19,000,000 common shares will be out. But now, with an added \$24 million that figure is low. Some other capital was purchased for around \$2 a share, so a rough estimate might be to add another 12 million shares, and then figure in the conversion ratio (18,000,000 to be converted and diluted shares?). That may total 37,000,000 Pro Forma shares outstanding.

A quick overview of production for >en's 13 series would estimate the production costs to date at around \$2,000,000. (Most are 7 episodes, that's around 90 episodes total. At a cost of approximately \$20,000 per episode, that totals \$1,800,000.)

OK, say the cost is \$50,000 per episode, and there are 100 episodes total. That's \$5,000,000.

Reportedly, >en shoots on film, so the S-1 says they spent \$12,470,000, in the first six months, including some salaries. The salaries listed on the chart totaled \$5.3 million, so they spent \$7 million on production of around 91 episodes, making the average cost \$91,000 per, or figuring in the salaries - \$138,000 per episode.

Marketing expenses were \$1.3 million, for the first six months of 1999. They've retained ChiatDay.

Network Operations cost \$1.5 million, for the first six months of 1999.

General and Administrative were \$4.6 million, for the first six months of 1999

Interest expense is negligible, and most of it's due to Msrs. Rector and Shackley.

That totals \$19.8 million cash spent for the first six months of 1999.

Since this article is being written more than six months after the financial statements were created, I assume they haven't had the need to spend much more, maybe a couple of million (in lieu of lowering management expenses) to operate since then. That would put the total cash spent in 1999 at around \$21 million.

In spite of all the management changes and charges, >EN has created a big barrier for any pikers to enter this market of Internet programming solutions, and the bar got a little higher now that Gary Gersh is the chairman, given their plans to punch down 1/3rd of their new equity to develop a record company.

A deal like this, which could end up being as large as \$150,000,000, could earn their cost of capital as an "Internet Play", IF the issue price isn't sky high and leaves enough headroom for the secondary market. But too many shares at a low issue price could dilute the value of their current owners/founders/executives/investors

stock below their acceptable levels. I see a re-filing, more or re-capitalized production costs, and a price like the rest: \$15. The real question is: "Is there enough demand for advertising access to that young audience through the Internet to generate sufficient net income to operate a behemoth like this - long-term?" That'll be harder if they insist on expensing the full production costs including salaries.

Good News: Very little debt, so borrowing more isn't out of the question.

Bad News: >EN could have too much preferred stock waiting to convert at too high a ratio to allow an IPO price in a range high enough to get enough money to grow up as fast as they need to keep up momentum through puberty.

From concept to operation, >en looked well planned, and attracted a strong team from industries ranging from the LPGA, Disney, Channel One, Concentric, and major record and television companies. This gave them more muscle than the other lifters to execute their programming vision. But as bad as the vibes on the founders are, I doubt anyone is walking around >en on a day-to-day basis with the same energy (as the founders had) to promote and energize that >en vision, and that's what got them this far. So with an S-1 that is over four months old, and a huge change over in management; Why didn't this one at least get priced? Bad publicity? I don't think so. My old friend Marty Lishon used to say; "It's not a question of the money. IT'S A QUESTION OF THE MONEY!"

Stockholder's equity as of the filing was \$12,153,000 remaining from the original \$49 million they raised. The new money increases that to \$36 million. But they've spent around \$37 million dollars to date, and could need UPWARDS, way upwards, of \$20 million a year to operate at the rate they've been going.

Qualitative Analysis from the VIC Vision Statement

The VIC Vision	Our Weight	Comments	(Rating 1-10)	Total Score
Comfortably embraces more sophisticated technologies	12%	Compared to the other sites (except Shockwave.com), >en blows them away. But too much hype - from every corner of the site (surveys, sponsors, recipes?), and marginal creative content in the series' makes it come across as an AK-47 loaded with 22's.	6	.72
Facilitates a need for people to communicate and collaborate	13%	Within their market, I doubt anyone's doing it any better, or more originally. But some of the language they're using ain't gonna play real nice in Peoria, where Pepsi reigns supreme. I was wondering why they haven't hooked up with Colin Malone?	6	.78
Nurtures a sense of community	14%	Again, Gen Y: Fabulous.	9	1.26
Channels entrepreneurial energy	10%	Bravo! These guys: Rector and Shackley really did it! They used some of their own dough, and they even sold stock in the start-up to Jim White Lumber Sales, Inc., plus having proven themselves with Concentric, and then attracted all those heavies to the start-up. So what if they're not there right now. Maybe they'll come back.	10	1
Enhances the growth of our industry	15%	I again pose the question: "Is there a high enough demand for this advertising solution on the Internet that would require the amount of capital >en's using?"	3.5	.525
Pioneering in the digital revolution	13%	Oh yea, because they put their money where their mouth is, and did it as well as it could be done.	10	1.3
Encourages development of new personal relationships and business opportunities in the interactive mediums	11%	Deals this big may not have the patience for anything "personal", but this is a MoFo of a business opportunity, even though the revenue model depends on advertisers, but if they hook into a hot series they can license, Hello? Is that Rupert Murdoch calling? And when they get the cash to get the label going, I'll bet they'll take INTERACTIVE to a new high.	8	.88
Visionary thinkers	12%	The true test will not be in the capital markets, it'll be if kids use >en repeatedly. I would bet >en's already figuring out what to do next, and then next. Hopefully ... Because their Y market is really fickle, not as loyal as the older surfers.	6.5	.78
Total Score				7.245