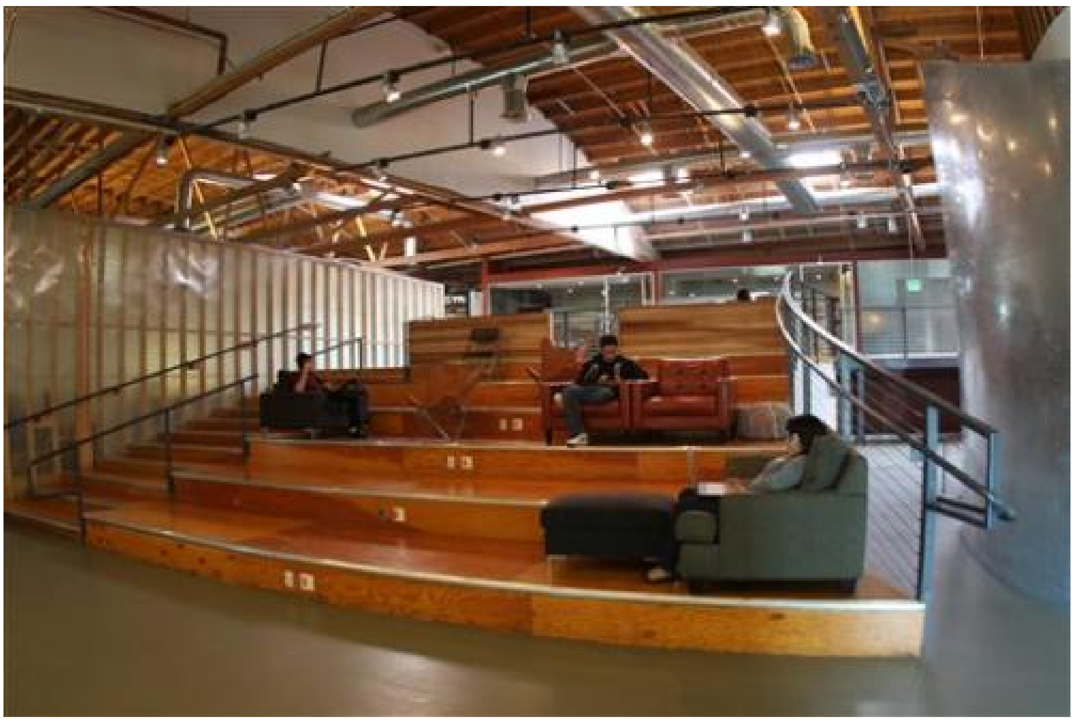
Disney's purchase of Maker a boon for LA startups (Update)

March 25 2014, by Ryan Nakashima



In this May, 8, 2013 photo provided by Maker Studios shows their offices in Culver City, Calif. The Walt Disney Co. announced Monday, March, 24, 2014 a $500 million purchase of YouTube video producer Maker Studios, a sign that Los Angeles-area content and technology startups are coming of age, proving themselves to be as creative and valuable to Hollywood as app makers are to the giants of Silicon Valley. The deal signals Hollywood's new openness to technology, an acknowledgement that the media giants don't have all the answers. (AP Photo/Maker Studios)

Disney's $500 million purchase of YouTube video producer Maker Studios is a sign that the entertainment industry's content and technology startups are coming of age and proving to be as valuable to Hollywood as app makers are to the giants of Silicon Valley.

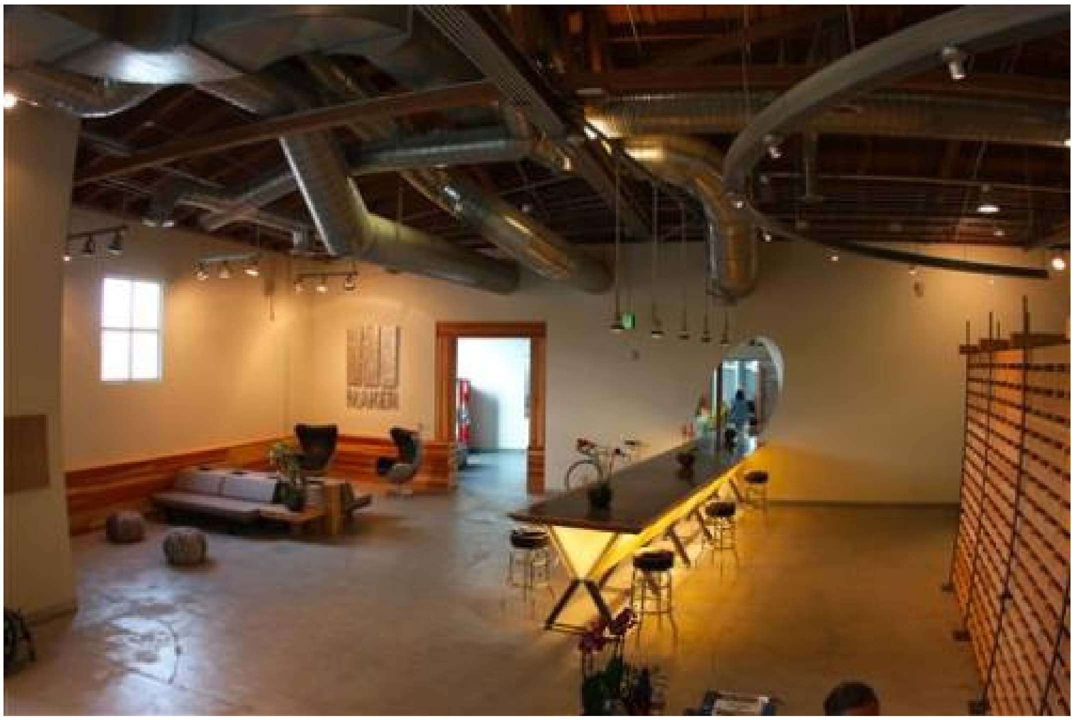
The deal announced Monday also signals Hollywood's new openness to technological innovation, an acknowledgement that media giants don't have all the answers. The acquisition comes a month after The Walt Disney Co. launched a technology startup incubator called Disney Accelerator, which promises to seed 10 companies with $120,000 each to develop ideas that'll have a big impact on entertainment and technology.

Disney's purchase price—which could hit $950 million if Maker hits performance targets—also validates the increasing value of so-called "multichannel networks." Those are the mini media empires that provide funding and support to video creators while taking a cut of ad revenue generated from views on YouTube.

When people subscribe to these channels, they're notified when new videos are available. That helps networks generate regular views on multiple devices, and enables them to deliver video ads on a massive scale.

Only a handful of such networks have reached the size of Maker, which went from startup status in 2009 to a network with 55,000 channels that generate 5.5 billion views a month, the vast majority from people aged 13-34. Other big network players include Machinima, Big Frame and Fullscreen, all based in the Los Angeles area because of its ready supply of actors, directors, camera people and editors who are otherwise struggling to make it onto a big-budget Hollywood movie or TV show.

"I think the big media companies just have a hard time being nimble on their own," says Gerry Laybourne, chairman of Defy Media, operator of YouTube channels including Smosh and Shut Up! Cartoons.



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"They can't take the time to find a Smosh. It's too hard. They can't take the risk of trying to figure out all the angles. They have to rely on the garages for innovation," she says.

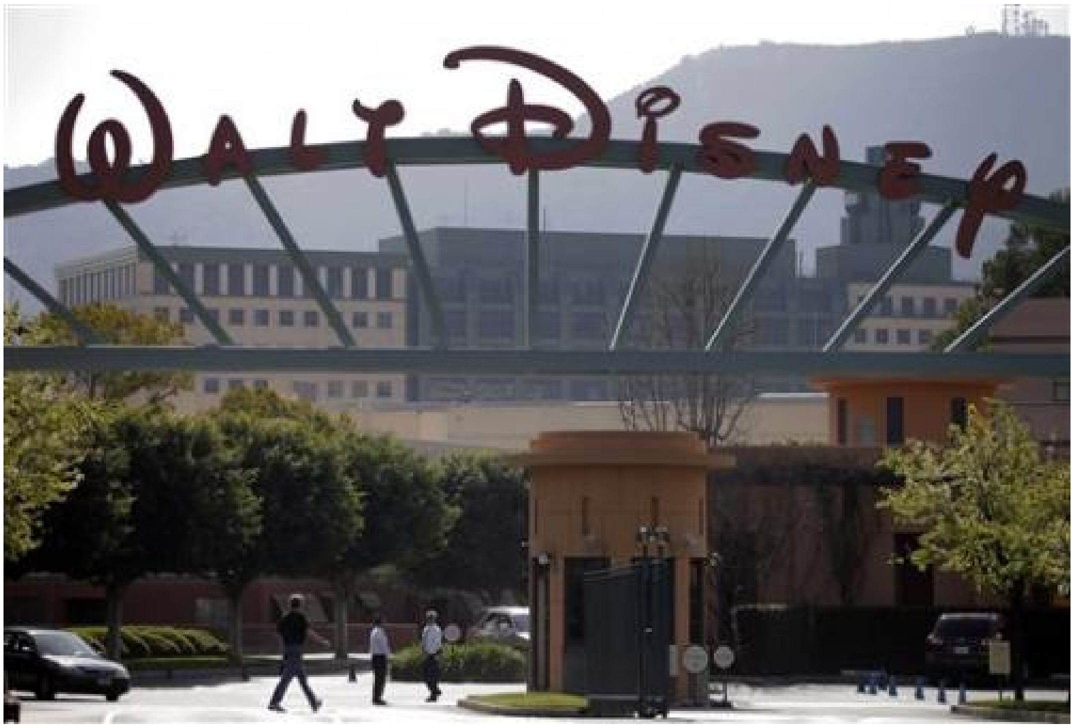
Dana Loberg, cofounder of San Francisco-based digital marketing company MovieLaLa, says the Maker deal provides encouragement to entrepreneurs like herself who are looking to the studios for business and investment.

"To have a buyer in Los Angeles like a studio that can make these big purchases is really big and good for the ecosystem of L.A.," she says. "I'm super happy to see studios are acquiring and paying attention to the digital space."

The purchase price sets a high benchmark for an L.A.-area startup, but it's not the highest.

Facebook Inc. announced its $2 billion purchase of Irvine-based virtual reality headset maker Oculus on Tuesday. Yahoo Inc. bought Burbank-based search marketing firm Overture in 2003 for $1.6 billion. News Corp. bought Beverly Hills-based social network Myspace in 2005 for $580 million. Electronic Arts Inc. paid $680 million for Los Angeles-based mobile game maker Jamdat in 2005 and Sony Corp. bought Aliso Viejo-based streaming game company Gaikai for $380 million in 2012.

Still, it's a high-water mark for a YouTube-focused content creator. The closest comparable deal is DreamWorks Animation SKG Inc.'s $33 million acquisition in May of AwesomenessTV, a West Hollywood-based multichannel network founded by veteran TV and movie producer Brian Robbins.



In this Feb. 8, 2011 file photo, people stand near the entrance to the Walt Disney Studios in Burbank , Calif. Disney said Monday March 24, 2014, that it is buying YouTube channel operator Maker Studios for $500 million as the family entertainment giant aims to stay in front of younger audiences who are increasingly watching short videos online. (AP Photo/Jae C. Hong, File)

According to securities filings, AwesomenessTV made $11.4 million in revenue and $2.4 million in gross profit in the final eight months of last year. But its growth in viewership has been explosive.

DreamWorks CEO Jeffrey Katzenberg told analysts in February that monthly views had skyrocketed in a year from 11.2 million to 374 million while its subscribers had jumped from 3.3 million to 37 million. AwesomenessTV is also on track to meet its performance targets, and the company is now expecting to pay $96.5 million of the maximum $117 million it had promised as incentive pay after the deal closed.

The structure of the so-called "earn-out" pay on the DreamWorks deal suggests "both parents are expecting a lot of growth," according to Mark Zyla, managing director of Acuitas Inc. and an expert on contingency pay in acquisitions.

Given the performance of AwesomenessTV after its acquisition, "$500 million for Maker doesn't sound so crazy," says Howard Morgan, managing partner of venture capital firm First Round Capital.

"You look at the demographics of where the revenue is coming from. You look at, can you grow it dramatically?" Morgan says. "I think we're still in the early stages of all of this."