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Transcript of
Dolphin Entertainment
First Quarter 2020 Earnings Call
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Participants

Mirta A. Negrini – CFO, COO & Director
William O'Dowd – Chairman, President & CEO

Analysts

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James Carbonara – Hayden IR, LLC – Partner of IR Strategy & Operations

Presentation

Operator
Greetings, and welcome to the Dolphin Entertainment First Quarter 2020 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded. It is now my pleasure to introduce your host James Carbonara, Investor Relations. Thank you. Mr. Carbonara, you may begin.

James Carbonara – Hayden IR, LLC – Partner of IR Strategy & Operations
Thank you, and once again, welcome to Dolphin Entertainment's First Quarter 2020 Earnings Call. With me on the call are Bill O'Dowd, Chief Executive Officer; and Mirta Negrini, Chief Financial Officer. I'd like to begin the call by reading the Safe Harbor statement.

This statement is made pursuant to the safe harbor for forward-looking statements described in the Private Securities Litigation Reform Act of 1995. All statements made on this call with the exception of historical facts may be considered forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

Although the company believes that expectations and assumptions reflected in these forward-looking statements are reasonable, it makes no assurances that such expectations will prove to have been correct. Actual results may differ materially from those expressed or implied in the forward-looking statements due to various risks and uncertainties.

For a discussion of such risks and uncertainties, which could cause actual results to differ from those expressed or implied in the forward-looking statements, please see risk factors detailed in the company's annual report on Form 10-K, those contained in subsequent filed quarterly reports on Form 10-Q as well as in other reports that the company files from time to time with the Securities and Exchange Commission.

Any forward-looking statements included in this earnings call are made only as of the date of this call. We do not undertake any obligation to update or supplement any forward-looking statements to reflect subsequent knowledge, events or circumstances.

Now I would like to turn the call over to Bill O'Dowd, Chief Executive Officer of Dolphin Entertainment. Bill, please proceed.

William O'Dowd – Chairman, President & CEO
Thanks, James, and thanks, everyone, for joining today. As usual, I'll arrange my comments as follows: first, I'll highlight our financial results; second, I'll spend some time providing operational updates; and third, I'll turn it over to Mirta to dive deeper into our financial results before having our Q&A. So first up, the financial results.

All members of our PR and Marketing Super Group had a good first quarter, pushing our quarterly revenues to $6,633,800. This represents a 5% year-over-year increase in total revenue, and a 6% year-over-year increase in revenue from our core segment of entertainment publicity, respectively. Furthermore, we are very proud to share net income in the first quarter of $2,073,847, which was $0.08 and $0.01 per basic and diluted share.

Additionally, with respect to our balance sheet, the lender of the Max Steel production loan notified us that the Max Steel VIE that we consolidate does not owe any money under the production loan agreement. As a result, we extinguished approximately $3.3 million of debt, and we subsequently evaluated our status as the primary beneficiary of the VIE and determined that we no longer met the criteria as the primary beneficiary. And consequently, we deconsolidated the Max Steel VIE from our condensed consolidated financial statements.

Cleaning up our balance sheet is a major focus for us in 2020 and specifically our working capital deficit, so let's take a quick look at that. After 4 acquisitions, our working capital deficit at December 31, 2019, was a little over $15.5 million. With the removal of the VIE helping, we reduced our working capital deficit by almost $5 million in Q1 to less than $10.7 million. That is a reduction of more than 30% in 1 quarter. And we're about to do even better. Along with securing capital to make our next acquisition without incurring any additional debt, reducing our working capital deficit was the primary driver for us to take advantage of a market opportunity and to raise $8.3 million in a registered direct offering last month. When we report our Q2 earnings in a few short weeks, we believe we will show an even larger reduction to our working capital deficit. Keep an eye on this metric as we manage ourselves towards the complete elimination of our working capital deficit as quickly as possible.

Furthermore, as long-time investors in our stock know, the puts we provided to the sellers of 42West upon the purchase of that company in March 2017 are almost all finished by December 31 of this year, less than 6 months from now. What started out as nearly an $11 million obligation of Dolphin will be virtually extinguished by year's end, and we expect to complete the puts on schedule in their entirety by the end of Q1 2021.

Turning to operational updates, just like on our 10-K earnings call, I'm sure the questions on the top of everyone's minds are: first, what does the current environment mean for Dolphin Entertainment and its 4 marketing companies, 42West, The Door, Shore Fire Media and Viewpoint Creative? Secondly, what does the current environment mean for Dolphin's M&A strategy? And third, what does the current environment mean for Dolphin's plans to re-enter production? I'll answer those questions one by one. But before I do, I'll mention a few highlights before the business disruptions started to take place at the beginning of March, especially since the start of the first quarter every year gives our PR firms a real chance to shine as the best at what they do in their respective fields.

In January of this year, Shore Fire Media's clients won a collective 11 GRAMMY Awards, including 7 in various Best Album categories. It was our first GRAMMY season together, and we couldn't be more proud of the team at Shore Fire. In February of this year, 42West was involved in various capacities with 13 films that earned a total of 49 Academy Award nominations and won 9 Oscars. Even though it seems like 42West has a fantastic Oscar season every year, we never want to take results like those for granted. Congratulations again this year, 42West.

Also in February, The Door and Shore Fire spearheaded various culinary and music events leading up to Super Bowl 54. For example, The Door handled media relations on behalf of 2 of their clients, the Seminole Hard Rock Hotel and Casino Hollywood and Yellow Tail Wine, which included performances from Pitbull, Diddy and Tiësto. Shore Fire Media on its end handled public relations for the Bud Light Super Bowl Music Fest, which included performances from Guns N' Roses, Maroon 5, DJ Khaled, and James Carbonara's personal favorite, Snoop Dogg. Furthermore, to add icing to the cake and the run-up to the Oscars, Rachel Aberly, Executive Vice President of 42West, won the inaugural Publicist of the Year award at the 2020 Publicists Awards, which feels particularly appropriate since Rachel heads up 42West's work with the Academy Award nominations. Congratulations, Rachel. That's really awesome. The inaugural Publicist of the Year Award. Fantastic.

With such a great start to the year, it's not hard to see why the Observer selected all 3 of our PR companies to be on its prestigious power 50 list this past December. There are over 12,000 PR firms in this country, and we believe we are the only company that owns more than 1 PR firm on the Power 50 list. And of course, all 3 of our PR firms are in the same industry, entertainment. Combining these 3 companies into one family makes us unique, and represents a platform for future growth that no one else has. This is the heart of the investment thesis into Dolphin.

Now back to the overarching questions outlined above. While coming as no surprise, each of our subsidiaries has faced a decline in revenues during the second quarter, some more significant than others. At 42West, we have experienced a drop in revenue from our talent division as television actors temporarily go on hiatus as productions halted for the entire quarter. Also, there were no movies in theaters to promote. However, we have offset a significant amount of that revenue loss by adding a large number of projects from the streaming platforms, almost all of which are our clients. And we expect to build back our revenue loss fairly quickly if productions resume and theaters reopen here in Q3 as expected.

At The Door, April and May were particularly challenging, especially with their core restaurant and hotel clients. Their revenues started to come back in June and again even further in July, allowing us to anticipate a much stronger third quarter. It's during this time that we are most thankful for the investment we made into our Consumer Products division at The Door beginning in January of 2019, shortly after we purchased the company the previous summer. That division, led by Nicole Lowe, has remained strong during this trying time and is helping the company rebound faster than it otherwise would. Of course, when the restaurants and hotels do fully come back, which we anticipate in either Q4 of this year or Q1 of next year, because of the heavy increase in consumer products work, The Door should come out of this period even stronger than when it started. And that is a truly remarkable thing to say for the market's leading hospitality PR agency. And is a true testament to the leadership of Lois O'Neill and Charlie Dougiello.

At Shore Fire, of course, they've lost some revenue from the cancellation of the summer touring season. However, fortunately, as we discussed on our 10-K earnings call I believe, the majority of their work is done online for the promotion of singles and albums. Thus, they've had the smallest percentage of revenue drop of any of our PR firms. With that said, they may not see a full 100% revenue recovery also until Q1 of next year as the fall music touring season is also very much in doubt as we stand here today.

Lastly, at Viewpoint, we've been focused on eliminating unprofitable clients. And I think when we report our Q2 numbers in just a few weeks, we'll have a lot of good things to say about their work during these past few months. Demand for marketing videos that can be used for online campaigns is very strong. And we're excited for the headway that the team has made into the corporate world, which was our priority for Viewpoint going into this year. We recently announced Viewpoint completed the strategic design and full-service production of a branding campaign for a long-time client, Direxion Funds, to introduce a new line-up of strategic weight ETFs. And that's a good example of a great corporate client for Viewpoint. We also recently announced a brand spot that Viewpoint did for CBS News. Those 2 announcements show the balance we'd like to strike between Viewpoint's legacy of best-in-class work for the leading media brands in the industry such as CBS News as well as CNN, HBO, Showtime, Discovery, ESPN with the expansion of that heritage and experience into the corporate world.

Now on the topic that is of strong interest for many of our shareholders, M&A. Let me just say this. We remain highly focused on completing the Super Group. We have never wavered on this path. As I stated above, it is the core investment thesis into Dolphin. And with every acquisition we have made to date, we have only felt validation and enhanced resolve as we see the cross-selling synergies that have already been created. And we want to add to the disciplines we can offer our clients. We will be opportunistic during these times and expect to complete our next 2 acquisitions on schedule this year. And we also believe that one will occur here in the third quarter.

Lastly, on the production side, we acquired feature comedy script Sisters Before Misters. And in Q2, we acquired the rights to action-thriller script Special Delivery. We're excited about those projects. We have directors attached to each and have begun casting each of them as well. Both are female-led movies, and hopefully, we will have lead actresses attached before the start of the film festival circuit in the next few weeks. We were looking forward to taking them out to market and to try and film at least one of them before the end of the year, if possible. And then, of course, COVID hit. Like the rest of the independent production sector, we are waiting for the availability of appropriate production insurance. The studios and the streaming services can underwrite their own risk, but for a large number of independent producers, including Dolphin, starting production without insurance is a gamble that we are not willing to take. So, the industry has to work through that, and we will be patient.

Okay. So to conclude, we're pleased to report a strong first quarter with net income of more than $2 million. Furthermore, we're very happy to have removed the VIE from our balance sheet, and we encourage all of our shareholders to watch our balance sheet carefully for the rest of the year as we work towards completely eliminating our working capital deficit even with our acquisition strategy continuing at full throttle. As you might imagine, we feel very good about our underlying business. We are growing revenues across the board at every one of our companies after the bottom of April and May. And we remain consistent to our core strategy that we shared when we uplisted to NASDAQ at the end of 2017, and we are hyper-focused on acquiring the fifth and sixth companies of our Super Group this year. We look forward to discussing our M&A activities in much more depth on our Q2 earnings call in less than 5 weeks. There is a lot to be excited about at Dolphin.

At this point, I'll now turn it over to Mirta for a more in-depth view of our financials.

Mirta A. Negrini – CFO, COO & Director
Thank you, Bill, and good afternoon. As Bill stated earlier, total Q1 revenue was $6,633,800, which represented an increase of approximately 5% as compared to the same period in prior year, and a 6% increase in revenue from the entertainment publicity and marketing segment as compared to Q1 of 2019. 100% of the revenue for the first quarter of 2020 was derived from our entertainment publicity and marketing segment.

Revenues from our content production segment were $0 in the first quarter of 2020, and $78,990 in the first quarter of 2019. As we have previously discussed, revenues are primarily earned right after the release of a film and the decrease in revenues as part of the normal cycle of a motion picture. Overall, operating expenses in Q1 of 2020 were $7,504,659. Direct costs were $688,977 for the 3 months ended March 31, 2020, as compared to $1,187,419 for the quarter ended March 31, 2019. The decrease in direct cost is primarily related to the decrease in Viewpoint's revenue due to onetime projects completed in the 3 months ended March 31, 2019.

Payroll costs were $4,889,623 for the quarter ended March 31, 2020, as compared to $4,301,413 for the quarter ended March 31, 2019. The change is primarily due to the addition of payroll from the acquisition of Shore Fire on December 3, 2019. Operating loss for the 3 months ended March 31, 2020, of $870,859 includes noncash items and depreciation and amortization of $521,003 as compared to operating loss of $825,161, including noncash items for depreciation and amortization of $481,642 for the quarter ended March 31, 2019.

The net income for the quarter ended March 31, 2020, was $2,073,847, which is $0.08 of basic earnings per share on a weighted average number of shares of 20,498,564, and $0.01 of diluted earnings per share on a weighted average number of shares of 28,384,982. For the quarter ended March 31, 2019, our net income was $122,608, which is $0.01 on basic earnings per share with a weighted average number of shares of 15,944,443 and a diluted loss per share of $0.08, using a weighted average number of shares of 18,690,377 shares.

That concludes my financial remarks. I will now ask the operator to open the phone lines for Q&A. Operator, can you please poll for questions.

Operator
(Operator Instructions)

Our first question comes from Jack Vander Aarde with Maxim Group.

Q: Solid 1Q results despite a challenging environment. So similar to last quarter, you guys did a nice job reviewing your thoughts on potential impact of some of your specific businesses as it relates to COVID. I'm hoping you can provide something similar in more of like a summarized sense for your near-term outlook. And then how you expect that to kind of change. I know that's a very open-ended tough question. How do you expect the near-term outlook impact from COVID to change as we go to, say, the fourth quarter of this year?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Sure. Yes. And hi, Jack. Thank you for the kind words. Yes, we're very, very happy with this quarter. And our businesses are doing well as they ramp up their revenues here in the start of the third quarter. We're starting to get visibility, at least on the drivers for each of them to return to 100% of revenue. 42West, I think will be there if and when movies come back into theaters in the next month or 2 and production resumes. They stayed very strong, as I indicated in the prepared remarks, due to so much business from the streaming services. It's nice to be in a market-leading position, and they certainly are. And our film and TV division is the best in the industry. Shore Fire as well, very strong throughout, with only marginal loss of revenue tied to touring business, but the bulk of their revenue was always in the online singles and albums. The Door is one that, as we said on the 10-K earnings call, took the largest revenue decrease because of their market-leading position with hotels and restaurants. Restaurants will take a little longer to come back than hotels. But the hotels we're starting to see come back already. And I would think in this third quarter, we could have all the hotel business back or the vast majority of it. The fourth quarter -- it will take until the fourth quarter, I think, to have the restaurant business back.

Q: Got it. That's very helpful. And then I think last quarter -- or maybe one of these quarters ago, you guys had spent some time, at least alluding to the recurring revenue aspect of your business. Can you remind me of what components or aspects of your business are recurring revenue? And then if I could follow-up, do you have any informal targets or any additional color you could provide around maybe what you expect for recurring revenue to represent for revenue as in a normalized environment?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Well, the nice part about each of our PR firms is that they have a healthy dose of recurring revenue every month. Project-based revenue does occur in each of them, though. As for recurring revenue -- think of it as we might have certain hotel groups on year-round doing marketing, and I'm thinking of The Door, obviously. But certain restaurants may come on board when they're about to open, and then carry on for several months. That might be more of an example of a project-based fee. So, the recurring revenue stayed steady and allowed us to weather

the second quarter. I think hopefully, much better than people would have anticipated and certainly better than much of our competition because we have steady recurring revenue clients at each of our PR firms. So, the projects, for example, certain feature film releases were pushed on the 42West side. We were blessed, we have some great high-profile movies scheduled for later this year that were originally going to be in the second quarter, like the James Bond movie, I'm very excited for that personally. Top Gun is another we're excited about working on. Both of those pushed out of the second quarter and into the holiday season. So that's also probably worth noting, Jack, that that's not permanently lost revenue. It just shifted from the second quarter to the fourth quarter. And I think you're seeing that with all of our PR firms. And that's what I meant by the comment that speaking about The Door in that case, but as we continue to increase the number of clients of The Door and our consumer products division, and they're going gangbusters really, really strong. Then when the hotel and restaurant business comes back in full, The Door's ahead of where they were when they went into this instead of just trying to get back to the same level. And that's very exciting. And I think we're seeing that with all of our PR firms because of 42West, for example, the increase in the streaming services revenue, we don't expect to -- the genie's out of the bottle, right? HBO Max has launched. Peacock's coming -- or has effectively launched too. And so there will not be less product from the streaming services to promote in Q3, Q4, next summer than there is now. There'll be more. And then when you add the feature films back into the market that, again, 42West is the market leader in both of those verticals. You heard the number of Oscar nominations, that's just one metric for that, right? Then we expect 42West to be stronger than they were going in. So we're looking at that as a nice silver lining that as we get through this coronavirus, we'll have stronger revenue streams at each of our PR firms.

Q: Yes, that's helpful. And I'm happy to hear the James Bond movie and Top Gun, both of my 2 former favorites as a kid are going to be back around, and hopefully, by the holiday season. If I could just sneak one more in there, and I'll jump back in the queue, is you dropped an exciting kind of Easter egg here about your expectations for your completion of your Super Group. And you noted one will be closing sooner than the other. Is there any more color you could provide as to which environment or which vertical that acquisition in the near term will be representing? Or is that going to be a secret until the announcement?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Well, I don't -- I think that the idea -- we've always been -- have long stated that we are excited about adding online marketing to complement our PR firms. We can drive a lot of business into that world from our PR firms. And I think we've stated that, that type of company will certainly be one of the next 2 to complete the Super Group. So certainly, we're excited if and when that time comes, to be able to talk about that vertical. And the cross-selling we can do for online to manage the -- to complement the campaigns that we're doing in PR, that will be very exciting to talk about. And as I said in my prepared remarks, it's hard to believe, but our Q2 earnings call is just 4.5 weeks away. And so we expect to be able to talk a lot more about our M&A activities on that call.

Operator
Our next question comes from Allen Klee with National Securities.

Q: Bill, when you talk to your customers, is there kind of a consensus view of when a movie and TV production will kind of start-up again?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Sure. Hi, Allen. Well, I'll give you -- it depends on which of our 2 types of customers. As for Netflix and HBO Max, and Apple and the studios as examples, right, they're finishing up protocols, and I think all of them would say they expect to be back in production maybe in the next 2 weeks, by the end of this month. There are -- there have been announcements about individual productions and their resumption dates or resuming starting or production -- resuming production or starting production on new projects. Certainly, I think everybody feels like that will occur before Labor Day, which is exciting for us. The independent production producers, so a lot of the independent films that we have as clients, I think one fun fact that we just unearthed again, I think 42West is -- and I'll get this

right, represented either 7 or 8 of the past 15 Best Picture winners, which are historically independent films, right? That's an incredible number, again, holy cow, half of the last 15 years, either way. Independent producers need production insurance. And so that is the hurdle to overcome for them to come back in because they can't underwrite the risk. So $8 million, $10 million, $15 million productions need that to be able to bank the foreign sales that those producers usually require to get the production off the ground. So the industry is working night and day on that. We do expect -- I think the whole industry expects that it won't go past the film festival season in the fall to have an answer for that because the projects are going to be sold. And so they need to start production. So whether that means that heavy independent production will start September, October or right at the 1st of the year is anybody's guess, but I think that's probably what most people are thinking these days.

Q: How do you think about cross-selling synergies across the Super Groups today as business picks up? Is there a way to think of like how much that could add to your typical organic growth rate?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Well, I'll tell you, the best way I can speak about it, Allen, is we're already seeing the effects of Shore Fire. And I think I made a similar type comment maybe on last year's 10-K call that -- take a trip down memory lane with me for a hot second. Two years ago, we had one -- the first company, 42West. And as I like to joke, you can't cross sell with yourself, right? And then we added The Door, and Shore Fire and then last December -- sorry, The Door and Viewpoint. And then last December, Shore Fire. Well, now that you’ve got 4 companies, each company can cross-sell with 3 other distinct type of companies. So you go from -- when you just have 42West and The Door, you had one opportunity to cross-sell between 2 companies. And now, just mathematically speaking, right? You have so many more, you have nine. So it grows exponentially. When we add hypothetically or whenever we are able to add our online marketing expertise, that's 5 companies. Each of our companies cross-selling with them and they with everyone else already. So now you're at 16 different cross-selling opportunities versus one, 2 years ago. And as a practical example, Shore Fire in the music space and 42West in the TV and film space, I don't think it will come as a surprise to anyone on this call. Music-related programming has dominated, has had tremendous success in ratings for almost 20 years now, right? I mean, pick your music-themed programming, right? And whether that's competition series on networks, like American Idol, The Voice, Masked Singer, et cetera, whether that's documentaries, each of the streaming services are having tremendous success with music documentaries. Upcoming ones of major artists have been announced. So we're seeing that. We may even have a nice announcement to make in our Q2 earnings call on that as well. Looking at the first cross-sale of a major endeavor by 42West and Shore Fire coming together. And that was strategically why we wanted the music PR capabilities of Shore Fire because there are just so many cross-selling opportunities. And that's just the 42West-Shore Fire connection. And like we say, sitting here today, we've gone from 1 to 9. But what I don't know that people really appreciate is when we add the next 2 companies, we have all 6 that we want in Phase 1 of our Super Group. That's 25 different cross-selling opportunities. And today we're sitting on 9 and 2 years ago, we were at 1. So we think it's -- it will create exponential growth, and we're seeing it. So that's what's got us excited, Allen.

Q: I have 2 financial questions. One is, if you look at the costs above operating income, all the main cost lines, is there anything unusual in this quarter? Or is this a reasonable run rate, looking at those numbers? And then second, I kind of missed it. I think you said what your diluted share count was for calculating the diluted EPS. I thought I heard something like $50 million, but could you repeat what that was? And then maybe what got added to that. And maybe what the share count was at the end of the quarter.

Mirta A. Negrini *Dolphin Entertainment, Inc. - CFO, COO & Director*
Sure. So at the end of the quarter -- well, let me answer your first question while I look for the answer to the second one. At the end of the quarter -- I mean, as far as the operating expenses, there isn't anything unusual in this quarter on those. And then the share count that was used for the fully diluted was 28,384,982 shares and that's mainly due to having to use the treasury stock method to -- we had to compute how many shares we would

have to sell in order to pay the puts that are due. It's mostly due to the accounting guidance on fully diluted EPS.

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
So that's one other benefit, if I could, that as we eliminate the puts and pay them all down, the fully diluted earnings per share will increase, which is great. Because it's the hypothetical -- that we had to use all of our shares to pay the puts, which isn't true.

Q: My last question, it's kind of vague, but if you're looking long term, I don't know if you've said this before, but is there a way to think of kind of a long-term organic growth rate in margin that you look at as a goal?

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
As much as possible in either case, right? Well, we'll have double-digit -- healthy double-digit revenue growth is in our -- certainly, something we believe we should be able to do and will do. And then the same on the net income basis. When we get through all of the, I guess, puts and convertible notes and all of that, and we get into a true operating income by the end of this year for this company, we'll -- we think we'll take off. And so we're excited because for those investors who have been with us since before we uplisted, that first 3-year plan was to acquire the 6 companies and form the Super Group. And then let the magic of the cross-selling really happen. And we're past the 2.5-year mark. And that's what's got us excited for that double-digit growth, both top line and bottom line, Allen.

Operator
There are no further questions at this time. I'd like to turn the floor back over to management for any closing remarks.

William O'Dowd *Dolphin Entertainment, Inc. - Chairman, President & CEO*
Well, thank you. I appreciate everyone's time, as always. And I know we'll be talking again in a very short number of weeks here. And look forward to elaborate on both the improvements to our balance sheet as well as to our M&A strategy. So talk to everyone then. Thank you all very much.

Operator
Ladies and gentlemen, this concludes today's teleconference. You may now disconnect your lines at this time. Thank you for your participation, and have a great day.