Zacks Small-Cap Research

November 2, 2011
Ken Nagy, CFA

www.zacks.com
111 North Canal Street, Chicago, IL 60606

Seven Arts Pictures (SAPX-NASDAQ)

SAPX: Zacks Company Report - OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	10/23/2011
Current Price (11/01/11)	$0.45
Target Price	**$4.00**

OUTLOOK

Seven Arts Entertainment Inc. is an independent motion picture production and distribution company which develops, finances, produces and licenses theatrical motion pictures, with budgets generally ranging from $2 million to $15 million, for exhibition in domestic (United States and Canada) and foreign theatrical markets. Seven Arts strategy is to build their film library up from 33 titles today, to 50 to 75 titles over the next 5 years. While earnings will be up and down and generally difficult to predict the firm should be valued on the monetization of its film library. As distribution changes at a swift pace firms that can continue to monetize creatively will benefit.

SUMMARY DATA

52-Week High	**$5.70**
52-Week Low	**$0.26**
One-Year Return (%)	**-91.61**
Beta	**-1.84**
Average Daily Volume (sh)	**624,397**
Shares Outstanding (mil)	**1**
Market Capitalization ($mil)	**$1**
Short Interest Ratio (days)	**0.02**
Institutional Ownership (%)	**4**
Insider Ownership (%)	**N/A**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**0.7**
P/E using 2012 Estimate	**1.3**
Zacks Rank	**3**

Risk Level	**High**
Type of Stock	**Small-Value**
Industry	**Movie/Tv Pr&Dis**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2009					10.23 A
2010					6.42 A
2011					3.33 A
2012					10.0 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2009					$2.94 A
2010					-$0.34 A
2011					$0.66 A
2012					$0.34 E

© Copyright 2011, Zacks Investment Research. All Rights Reserved.

KEY POINTS

- Distribution of movies and programs is changing dramatically. Video on demand and video over the internet is the new reality of the space.
- The Company has seven motion pictures (Catwalk, The Winter Queen, Mortal Armor: The Legend of Galahad, Romeo Spy, Voodoo Museum, The White Lily and Neuromancer) in development that are expected to be released within the next two to three years.
- Seven Arts controls copyright interests for 21 completed motion pictures and a film library of 14 films, which it anticipates increasing to as many as 50 to 75 pictures over the next five years.
- The number of films produced is shrinking and major studious have cut back on distributing smaller budget pictures and have focused on large budget pictures and franchises.
- Seizing on the opportunity of fewer films produced, Neuromancer could provide significant revenues beyond what is typical of Seven Arts films.

OVERVIEW

Seven Arts Entertainment Inc. is an independent motion picture production and distribution company based out of London, the United Kingdom. The Company develops, finances, produces and licenses theatrical motion pictures, with budgets generally ranging from $2 million to $15 million, for exhibition in domestic (United States and Canada) and foreign theatrical markets.

Seven Arts further provides post theatrical motion picture releases in the media forms of DVD, home video, pay-per-view and free television. Along the same lines, the Company controls copyright interests for 21 completed motion pictures and a film library of 14 films, which it anticipates increasing to as many as 50 to 75 pictures over the next five years.

The Company has recently released the domestic theatrical motion pictures Deal (April 2008), Noise (May 2008), Autopsy (January 2009), The Pool Boys (current release) and Nine Miles Down (current release).

While all of these releases have thus far received limited U.S. theatrical releases (50-300 theaters in the United States) Seven Arts has completed production and is anticipating the release for the theatrical showing of Radio Free Albemuth (United States) and Men Don't Lie (United Kingdom).

The Company has seven motion pictures (Catwalk, The Winter Queen, Mortal Armor: The Legend of Galahad, Romeo Spy, Voodoo Museum, The White Lily and Neuromancer) in development that are expected to be released within the next two to three years.

Additionally, it should be mentioned that in addition to the domestic titles, Seven Arts also released Knife Edge (October 2009) as a United Kingdom DVD premiere and Night of the Demons (September 2010) in the United Kingdom theatrically.

With domestic theatrical box office sales of all films reaching $10.6 billion and worldwide box office reaching as much as $29.9 billion in 2009, many successful independent motion picture companies and major studios

have been reducing the number of pictures that they finance and distribute. Consequently, these large studios and independent motion picture companies have concentrated on a limited number of higher budget films with budgets in the range of $10 million to $100 million or more.

Full-Year Box-office & Attendance Since 1999

Year	Avg. Ticket Price	Total Box-office Gross	Percent change vs. previous year	Tickets Sold	
2009	**$7.46**	**$10,600,000,000**	10.07%	1,420,911,528	5.94%
2008	$7.18	$9,630,000,000	-0.52%	1,341,225,627	-4.67%
2007	$6.88	$9,680,000,000	4.09%	1,406,976,744	-0.91%
2006	$6.55	$9,300,000,000	3.79%	1,419,847,328	1.58%
2005	$6.41	$8,960,000,000	-5.19%	1,397,815,913	-8.14%
2004	$6.21	$9,450,000,000	1.61%	1,521,739,130	-1.33%
2003	$6.03	$9,300,000,000	-0.21%	1,542,288,557	-4.02%
2002	$5.80	$9,320,000,000	11.35%	**1,606,896,552**	8.47%
2001	$5.65	$8,370,000,000	8.00%	1,481,415,929	3.22%
2000	$5.40	$7,750,000,000	3.33%	1,435,185,185	-2.79%
1999	$5.08	$7,500,000,000	7.91%	1,476,377,953	-0.37%

Source: Deadline Hollywood

As a result, Seven Art's business model has turned its primary focus to the distribution in the post-theatrical markets for lower-cost, "genre" motion pictures. The Company's strategy is to produce and distribute two to four $2 million to $15 million motion pictures in house per year.

Seven Arts, also intends to supplement this business strategy by occasionally producing higher cost motion pictures with production budgets in the range of $30 million to $50 million.

Furthermore, each year the Company intends to acquire opportunistic distribution rights to an additional two to five motion pictures that are produced by others. These motion pictures would be distributed by Seven Arts as an agent for a 15 percent to 20 percent fee into the theatrical, video and television markets.

The Changing Landscape of Cinema **(partial source filmmaking.net)**
Just as VHS and DVD once looked threatening to the movie industry, the internet threatens to change distribution once again. The industry is seeing P2P/IP TV as the new TV, download-to-own as the new DVD, and worldwide-synchronous online releases as the new cinema. In the past when the industry viewed new technology as a threat, that very threat ended up increasing sales.

The internet does not only represent a threat (piracy) but rather an opportunity to reach bigger audiences with more product, more quickly for far less cost. Think of the cost benefit of taking DVD's out of the supply chain. Several insiders also point to built-in marketing tools like peer-review and recommendations, and brand new methods for taking advantage of old revenue sources such as advertising.

Desire for Cinema and programs have not changed - just how we choose to access it. And we now have plenty of choices. Download services are re-populating our distribution landscape, giving rise to many

exciting new opportunities. The early pioneers in content delivery are iTunes, Netflix, Amazon.com, Sony Playstation, and Microsoft Xbox.

Universal's Gamble

What Universal is planning is three weeks after its cinema release of Tower Heist, to release the film over a video on demand service. This is a limited trial, with the film being made available over Comcast's VOD service in a limited number of locations (Portland, Oregon, Georgia and Atlanta).

It'll also attract a premium price, costing viewers $60 if they want to see the film this way, this soon. Seems pricey at 5 times what it would sell for normally, but it's a bit like buying a brand new rental copy of a VHS/DVD in the past can be 2 or 3 times more expensive.

In Production

Title	Event	Production
Catwalk	- Principal photography to begin Summer 2011	Summer 2011
Waxworks	- Casting Complete. - Principal photography to begin Fall 2011	Summer 2011
The Winter Queen	- Signed Director Fyodor Bondarchuk (The 9th Company, The Inhabited Island) Milla Jovovich (Resident Evil, The 5th Element) - Production slated for June 2011	June 2011
Mortal Armor: The Legend of Galahad	- Signed Director Jon Amiel (Entrapment, Copycat) - Signed Producer Gale Anne Hurd (Terminator 2, Armageddon) - Currently casting lead	Winter 2011
Romeo Spy	-Signed Director Bronwen Hughes (Harriet the Spy, Stander) -Currently casting lead	Winter 2011
Neuromancer	-Signed Director Vincenzo Natali (Splice, Cube) -Currently rewriting screenplay with William Gibson	Summer 2011

Big Jake

On October 6, 2011 Seven Arts announced its subsidiary has executed a Distribution Services Agreement for digital and physical sound recordings with Entertainment One Distribution, the leading and fastest growing independent record company in the United States. Under the agreement Big Jake Music, will be releasing Seven Arts film soundtracks, along with proprietary recording artists on a national and global basis. The initial soundtrack releases shall be for the Seven Arts films "Night of the Demons" and "The Pool Boys."

Entertainment One Distribution shall receive fees based upon sales generated, and Big Jake Music shall be responsible for production and marketing costs associated with these releases. One Distribution, the largest independent music and video distributor in North America, holds the highest market share of any independent distributor. Through its facilities in New York and Toronto, eOne Distribution manages physical distribution of CD, Blu-ray and DVD inventories and is a leading Internet fulfillment wholesaler of entertainment products through partnerships with the world's largest online retailers. eOne is a leader in digital distribution, aggregating content for multiple partners including iTunes, Netflix, Amazon.com, Sony Playstation, Xbox, eMusic, and Rhapsody.

On August 23, 2011 the firm announced it has executed an agreement for the acquisition of all of the capital stock of Big Jake Music a newly formed record and multi-media entertainment company, for $5,000,000 of

convertible preferred stock, convertible into common stock at a premium to the market price at closing, and which is not subject to conversion for agreed periods of time.

Big Jake Music currently owns $5,000,000 in net value of media credits from News USA, a national media, marketing and publicity firm. Seven Arts expects to be using these media credits to promote its motion pictures.

A typical Deal

Seven Arts receives between 50 and 100 submissions of potential film projects or completed films every year, which generally include a "package" of a screenplay and certain talent elements (such as producer, director and cast). In certain limited cases, Seven Arts will arrange for the creation of a screenplay and the "packaging" of creative elements. Seven Arts commissions independent production budgets of certain projects to evaluate the project's suitability for production or distribution. The pictures produced are selected according to several key criteria formulated to maximize the profit potential of its films, including the potential to license the worldwide distribution rights to the film for an amount greater than the projected production budget (minimum profit margin of at least 20%),

Seven Arts creates a separate finance plan for each motion picture it produces. The sources of the funds for production of each motion picture vary according to each finance plan and is based on state and foreign country tax credits (e.g. Louisiana, United Kingdom and Hungary) and direct subsidies), "mezzanine" or "gap" funds, which are senior to its equity, and senior secured financing with commercial banks or private lenders, together in certain cases with a limited investment from us, which is customarily less than 10% of the production budget.

In 2007, Seven Arts Pictures Louisiana LLC, a subsidiary of SAP Inc., acquired real property in New Orleans, Louisiana, which they are in the process of developing as a production and post production facility for motion pictures in Louisiana. Over the past five years, Louisiana has become a popular destination for the production of motion pictures due to very favorable tax incentives. Since 2005, the Company has produced five motion pictures under the Louisiana Motion Picture Incentive Act (Louisiana Incentives), which provides substantial transferable tax credits for film production activities in Louisiana accredited to a firm whether it produces or acquires a motion picture. The Louisiana Incentives provide generally that the producer will receive both a 25% (increased to 30%) transferable investment tax credit on all film expenditures on Louisiana vendors and a 10% (decreased to 5%) transferable labor tax credit on all expenditures for labor performed in Louisiana by Louisiana residents.

The Company licenses distribution rights for its motion pictures in the United States and in most foreign territories prior to and during the production or upon the acquisition of rights to distribute a picture. The firm shares in the commissions generated by the sales of the pictures. Sale of a license to distribute a motion picture prior to its delivery is termed a “pre-sale” and may occur at any time during the development and production process. In a typical license agreement, the company would license a picture to a distributor before it is produced or completed for an advance from the licensee. This advance is recoverable by the distributor from its share of the revenues generated by the distribution of the picture in the licensee’s territory, after deduction of the distributor’s expenses and distributor fee. The advance usually is in the form of a cash deposit plus a letter of credit or “bank letter” for the balance payable 10-20% on execution and the balance on delivery. The license grants the distributor the right to the post-theatrical release of the picture in all or certain media in their territory for a predetermined time period. After this time, the distribution rights revert back to the Company and they are then free to re-license the picture.

The Film Library

The film library includes 33 films. Twelve films are controlled by Arrowhead Target Fund until the firm recoups its loan. The strategy is to grow the library of films to 50-75 over the next 5 years.

Title	Director	Cast	Production Cost	Title	Director	Cast	Production Cost
Asylum	David MacKenzie	Natasha Richardson	$20,000,000	**Shattered Image**	Raul Ruiz	William Baldwin Anne Parillaud	$7,250,000
Stander	Bronwen Hughes	Thomas Jane Deborah Unger	$14,000,000	**The Hustle**	Stuart Cooper	Bobbie Phillips Robert Wagner	$5,000,000
No Good Deed	Bob Rafelson	Samuel L. Jackson Milla Jovovich	$17,000,000	**Pool Hall Prophets**	Keoni Waxman	Freddie Prinze, Jr. Ving Rhames	$6,000,000
I'll Sleep When I'm Dead	Mike Hodges	Clive Owen Malcolm McDowell	$8,000,000	**Boo**	Anthony C. Ferrante	Trish Cohen Happy Mahaney	$1,000,000
Supercross	Steve Boyum	Sophia Bush Steve Howey	$5,000,000	**Cemetery Gates**	Roy Knyrim	Reggie Bannister	$1,000,000
A Shot At Glory	Michael Corrente	Robert Duvall Michael Keaton	$12,000,000	**Popstar**	Richard Gabai	Aaron Carter Alana Austin	$5,000,000
Johnny Mnemonic	Robert Longo	Keanu Reeves Dolph Lundgren	$24,500,000	**Red Riding Hood**	Randall Kleiser	Lanie Kazan Morgan Thompson	$5,000,000
Never Talk To Strangers	Peter Hall	Antonio Banderas Rebecca DeMornay	$11,700,000	**Back In The Day**	James Hunter	Ving Rhames Ja Rule	$5,000,000

Effective monetization of the film library is critical as technology changes. Seven Arts must continue to find new ways to monetize these assets in order to grow the library with new films.

Title	Director	Cast	Production Cost	Title	Director	Cast	Production Cost
Captivity	Roland Joffe	Elisha Cuthbert	$17,500,000	**Noise aka**	Henry Bean	Tim Robbins William Hurt	$9,000,000
Mirror Wars	Vasily Chiginsky	Armand Assante Malcolm McDowell	$8,000,000	**American Summer**	J.B. Rogers	Matthew Lillard	$15,000,000
Getting' It	Nick Gaitatjis	Jessica Canseco Patrick Censoplano	$2,500,000	**Autopsy**	Adam Gierasch	Robert Patrick	$9,000,000
The Wedding Chest	Nurbek Egen	Natasha Regnier Bolot Tentimyshov	$1,500,000	**Knife Edge**	Anthony Hickox	Joan Plowright Natalie Press	$8,000,000
The Mesmerist	Gil Cates, Jr.	Neil Patrick Harris Jessica Capshaw	$1,000,000	**Nine Miles Down**	Anthony Waller	Adrian Paul Kate Nauta	$17,400,000
A Broken Life	Neil Coombs	Tom Sizemore Ving Rhames	$2,000,000	**Hades**	Gabriel Bologna	Robert Patrick Danielle Harris	$2,500,000
Drunkboat	Bob Meyer	John Malkovich John Goodman	$3,500,000	**Night of the Demons**	Adam Gierasch	Shannon Elizabeth Edward Furlong	$9,000,000
Deal	Gil Cates, Jr.	Burt Reynolds Bret Harrison	$9,000,000				

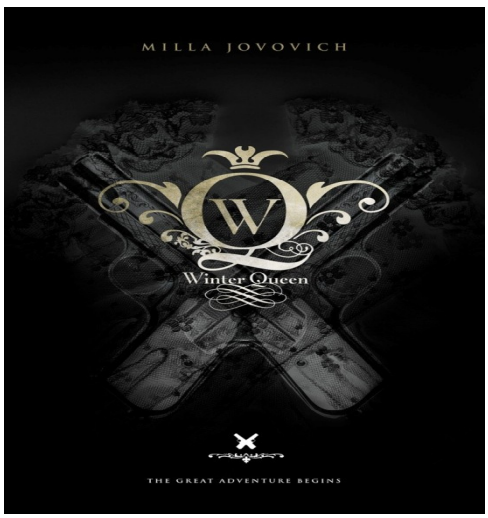
Neuromancer
Poised to take advantage of falling new release films, Neuromancer is the currently in production and projects to have a budget of $60 Million. Beyond the obvious larger potential take at the box office, The opportunity remains for a wider than normal theatrical release along with gaming and franchising rights.

The science fiction film which is based on William Gibson's best selling novel has directors and producers attached. Fees are expected in 2012 followed by a stronger 2013.

The revenue generated could be 3-5 times what the firm usually sees in its smaller budget releases.



Winter Queen is another of the potential bigger revenue films. Set in 1876 the plot surrounds a young investigator with the Moscow police who sets out to solve the apparent suicide of a university student, but soon lands in the middle of a far-reaching international conspiracy. Recognizable talent includes Milla Jovovich (*Resident Evil*, *The Fifth Element*), and Fyodor Bondarchuk (dir.) (*The Inhabited Island*, *The 9th Company*)



Potential Breakdown of Winter Queen

Production Budget	Tax Credits	P & A Spend	Total Cost
$15,000,000	($7,500,000)	$7,000,000	$14,500,000
$15,000,000	($7,500,000)	$10,000,000	$17,500,000
$15,000,000	($7,500,000)	$12,000,000	$19,500,000

Foreign Pre-Sales	US B.O.	U.S. Video, Pay TV, TV	Foreign Overages	Total Revenues
$11,000,000	**$7,000,000**	**$7,000,000**	**0**	**$4,500,000**
$12,000,000	**$15,000,000**	**$10,000,000**	**$2,500,000**	**$12,500,000**
$12,000,000	**$30,000,000**	**$12,500,000**	**$5,000,000**	**$25,000,000**

INDUSTRY OUTLOOK

Media companies suffer from audience fragmentation and limited near-term reinvestment opportunities. Consumers have access to an unprecedented selection of independent media outlets resulting in audience dilution for most traditional media services. An example can be seen in the steep decline in network television ratings largely attributed to audience migration to cable and the Internet. To retain share, large media companies are forced to reinvest in additional media outlets. However, growth is limited by government regulations on media ownership. The changing distribution on films and programs are likely to ignite a new round of industry consolidation. Attractive reinvestment opportunities, nevertheless, remain a challenge. Valuations of attractive acquisition targets have risen in anticipation of further industry consolidation.

Technology remains a wildcard for the industry. It has been both a boon and a bust for media companies. The rapid consumer adoption of DVDs has greatly enhanced returns in the filmed entertainment industry. In direct contrast, rampant file sharing of digital music has significantly impacted sales of recorded music. Personal video recorders (PVRs) represent the most recent emerging technology to affect the media industry. While ad-based media outlets are threatened by the devices' ability to skip commercials, cable and satellite operators stand to benefit from offering the new "time-shifting" devices to attract subscribers and earn incremental revenue from video-on-demand services.

INDUSTRY POSITION

The firm competes against medium and large well capitalized media companies. The number of films produced is shrinking. In 2009 558 films were released compared to 633 the previous year. Major studious have cut back on distributing smaller budget pictures and have focused on large budget pictures and franchises. Several specialty shops have closed such as New Line, Picturehouse and Paramount Vantage all the while sales at the box office have been increasing. This gives Seven Arts a unique opportunity as those who are left in the space have better access to talent and projects.

RECENT NEWS

On October 31, 2011, Seven Arts Entertainment Inc., reported financial results for its fiscal year, ended June 30, 2011.

Seven Arts reported mixed results with a decrease in year over year revenues from $6.417million for the fiscal year ended June 30, 2010 down to $3.328 million during fiscal 2011.The weakness was primarily due to challenges from changes in the Company's new revenue model resulting in reduced production during the fiscal year ended June 30, 2011.

Gross margin during the year dropped sharply, resulting in a gross profit deficit of $120,000 compared to a gross profit of $4.018 million for the fiscal year ended June 30, 2010.Still, Seven Arts' Fiscal year 2011 net income resulted in net income of $1.461 million compared to a net loss of $476,000 during fiscal 2010.

The difference was primarily due to other income from debt settlement of $150,000 which was offset by net interest expense of approximately $1.706 million during fiscal 2010. This compares to the recognized net cancellation of indebtedness revenue of $4.459 million of other income which was offset by $758,000 of interest expense in fiscal 2011.

Based on a weighted average number of basic and diluted common shares of 1.889 million, basic and diluted net income per share resulted in $0.77 per share. This was a year over year increase from a $0.35 basic and diluted net loss per share on a weighted average number of basic and diluted shares of 1.403 million during the fiscal year ended June 30, 2010.

It should be noted that the net cancellation of indebtedness revenue of $4.459 million reflected the Company's continued efforts to reduce indebtedness and increase net shareholder equity.

During the fiscal year, Seven Arts reduced its total loans payable by $5.655 million during the year to $12.646 million from $18.301 million at the end of fiscal 2010, ended June 30 2010.

Similarly, the Company increased net shareholders' equity from $2.200 million as of June 30, 2010 to $7.958 million as of June 30, 2011.

Recently, Seven Arts has completed production and is anticipating the release for the theatrical showing of Radio Free Albemuth (United States) and Men Don't Lie (United Kingdom).

The Company has six motion pictures (Catwalk, Waxwork, Mortal Armor: The Legend of Galahad, Romeo Spy, The Winter Queen and Neuromancer) in development that are expected to be released within the next two to three years.

October 5, 2011, BRG Investments, LLC acquired 250,000 newly issued shares of Seven Arts common stock at a price of $1.00 per share. During the next six months, BRG may purchase an additional 250,000 shares of Seven Arts common stock at the volume weighted average price, but no less than $1.00 or more than $1.50. BRG received a warrant to purchase 100,000 shares of Seven Arts common stock and will receive an additional warrant with the same terms if it purchases the additional 250,000 shares. Seven Arts intends to use the proceeds of this transaction to partially fund its next motion picture production in Louisiana entitled Schism, written and to be directed by Adam Gierasch, the director of Autopsy and Night of the Demons, two recent releases by Seven Arts. Seven Arts and BRG also entered into a mutually acceptable settlement of their dispute relating to their previous investment agreement.

VALUATION

Seven Arts is poised to capture a bigger piece of the entertainment dollar as technology and distribution change. Neuromancer and Winter Queen have the potential to produce three to five times higher revenue than the average Seven Arts picture as well as franchising opportunities.

Through a combination of debt forgiveness, paying down debt, and equity deals Seven Arts reduced its total loans payable by $5.66 million during the year to $12.65 million from $18.30 million at the end of fiscal 2010. Similarly, the Company increased net shareholders' equity from $2.2 million as of June 30, 2010 to $7.96 million. The equity deals add the effect of dilution and investors should be aware of the drag on the shares when lock up periods expire. Over the long-term a film library of 50 to 75 films could produce revenues of between $20-100 million. The firm is nowhere near that yet so we suggest investors look at book value.

The incentive to makes films in Louisiana is significant. The Louisiana Incentives provide generally that the producer will receive both a 25% (increased to 30%) transferable investment tax credit on all film expenditures on Louisiana vendors and a 10% (decreased to 5%) transferable labor tax credit on all expenditures for labor performed in Louisiana by Louisiana residents.

The firm looks undervalued when looking at the price to book and the price to sales metric and fairly valued when looking at the Enterprise Multiple.

Price to book value a ratio used to compare a stock's market value to its book value. It is calculated by dividing the current closing price of the stock by the latest quarter's book value per share. The book value of equity is the difference between the book value of assets (original price – allowable depreciation) and the book value of liabilities. The market value of an asset in contrast to its book value reflects its earnings power and expected cash flows.

$$P/B\,Ratio = \frac{Stock\ Price}{Total\ Assets - Intangible\ Assets\ and\ Liabilities}$$

Metric	Seven Arts	Industry Average
Price/Book Value	0.21	1.91

While not as popular as Price/Earnings or Price/BV, Price/Sales is not influenced by accounting decisions in depreciation, inventory and extraordinary charges. P/S multiples are much less volatile than P/E multiples. However if the problem with the firm lies in cost control the P/S ratio will not reflect this flaw. According to this

Metric	Seven Arts	Industry Average
Price/Sales	0.22	1.76

According to the Price/Book Value and the Price/Sales models the firm appears undervalued compared to the industry.

The enterprise multiple looks at a firm as a potential acquirer would, because it takes debt into account - an item which other multiples like the P/E ratio do not include. Enterprise value is calculated as market cap plus debt, minority interest and preferred shares, minus total cash and cash equivalents. The Firm's Enterprise multiple is 11.35x compared to 6.27x for the industry. According to the enterprise multiple SAPX appears fairly valued to over valued. This metric bears watching since it will improve as EBITDA improves.

$$\text{Enterprise Multiple} = \frac{\text{Enterprise Value}}{\text{EBITDA}}$$

Metric	Seven Arts	Industry Average
EV/EBITDA	11.35	6.27

We see the book value of the stock at approximately $3.00 per share today and feel the intrinsic value of the stock could trade at $4.00 as revenue ramps, further debt is paid down, and the balance sheet is strengthened.

RISKS

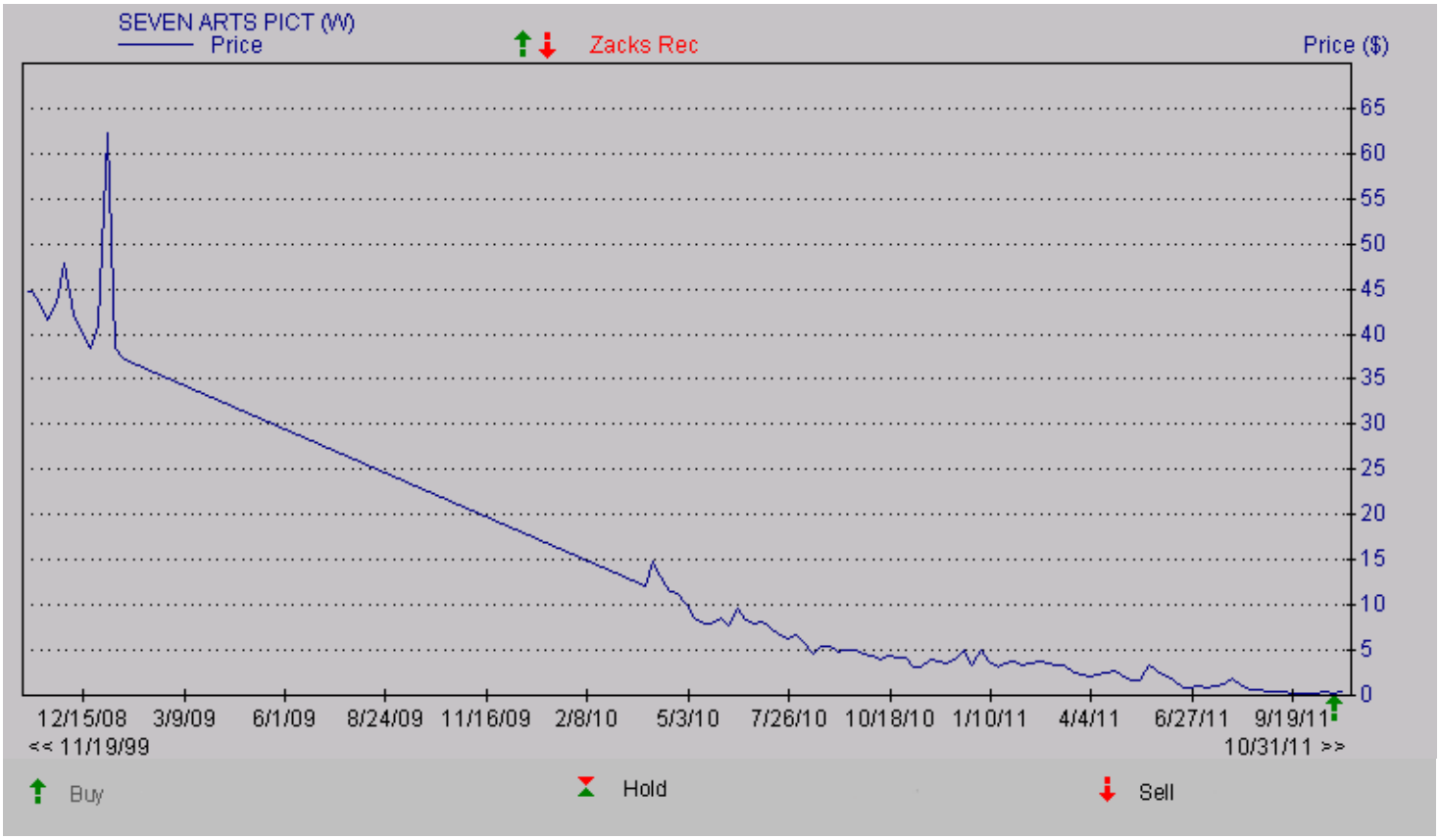
- The production, acquisition and distribution of motion pictures require a significant amount of capital.
- Given the pace of technology, the costs of producing and marketing feature films have steadily increased and may further increase in the future, making it more difficult for a film to generate a profit.
- Seven Arts business model requires the firm be efficient in the production of motion pictures. Actual motion picture production costs often exceed their budgets, sometimes significantly.
- Seven Arts remains highly leveraged and will likely continue to finance its business through dilutive equity deals.

PROJECTED INCOME STATEMENT

INCOME STATEMENT ($ Mil)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012 E
REVENUE					
Film Revenues	**3.265**	**4.22**	**1.97**	**2.76**	**7.00**
Fee Related Revenues	**-**	**6.01**	**4.44**	**0.57**	**3.00**
Total Revenue	**3.27**	**10.23**	**6.42**	**3.33**	**10.00**
Sequential Growth					
OPERATING EXPENSES					
Cost of Revenues	4.09	4.66	2.40	3.45	7.00
% of Revenue					
Gross Profit -	**(0.82)**	**5.57**	**4.02**	**(0.12)**	**3.00**
Proforma Gross Margin	-25.2%	54.4%	62.6%	-3.6%	30.0%
Selling General and Administrative	4.0	3.6	2.6	1.9	2.0
% of Revenue		59.6%	59.0%		
Corp Overhead	-	-	-		
% of Revenue		0.0%	0.0%		
GW Amort, Restructuring, other	-	0.5	0.3	0.2	0.2
% of Revenue					
Total Operating Expenses	4.02	4.12	2.94	2.09	2.23
% of Revenue		68.6%	66.1%	366.1%	74.5%
Operating Income -	**(4.84)**	**1.44**	**1.08**	**(2.21)**	**0.77**
Operating Margin		24%	24%		
NON-OPERATING ITEMS					
Non operating Income/Expense	-0.2	3.3	(1.56)	3.67	-
% of Revenue		54.76%	-35.02%	643.46%	0.00%
Tax Provision	-0.49	0.00	0.00	0.00	0.00
Effective Tax Rate	10%	0%	0%	0%	0%
Net Income -	**(4.56)**	**4.74**	**(0.48)**	**1.46**	**0.77**
Net Income Margin		78.8%	-10.7%	256.4%	25.5%
EARNINGS PER SHARE					
EPS - Basic	-$0.97	$0.78	-$0.07	$0.77	$0.40
EPS - Diluted	-$0.97	$0.58	-$0.07	$0.66	$0.34

Ken Nagy, CFA Zacks Investment Research

HISTORICAL ZACKS RECOMMENDATIONS



DISCLOSURES

The following disclosures relate to relationships between Zacks Investment Research ("ZIR") and Zacks Small-Cap Research ("Zacks SCR") and the issuers covered by the Zacks SCR analysts in the Small-Cap Universe.

ZIR or Zacks SCR Analysts do not hold or trade securities in the issuers which they cover. Each analyst has full discretion on the rating and price target based on their own due diligence. Analysts are paid in part based on the overall profitability of Zacks SCR. Such profitability is derived from a variety of sources and includes payments received from issuers of securities covered by Zacks SCR for non-investment banking services. No part of analyst compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in any report or blog.

ZIR and Zacks SCR do not make a market in any security nor do they act as dealers in securities. Zacks SCR has never received compensation for investment banking services on the small-cap universe. Zacks SCR does not expect received compensation for investment banking services on the small-cap universe. Zacks SCR has received compensation for non-investment banking services on the small-cap universe, and expects to receive additional compensation for non-investment banking services on the small-cap universe, paid by issuers of securities covered by Zacks SCR. Non-investment banking services include investor relations services and software, financial database analysis, advertising services, brokerage services, advisory services, investment research, and investment management.

Additional information is available upon request. Zacks SCR reports are based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Because of individual objectives, the report should not be construed as advice designed to meet the particular investment needs of any investor. Any opinions expressed by Zacks SCR Analysts are subject to change. Reports are not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. Zacks SCR uses the following rating system for the securities it covers. Buy/Outperform: The analyst expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters. Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters. Sell/Underperform: The analyst expects the company will underperform the broader U.S. Equity market over the next one to two quarters.

The current distribution of Zacks Ratings is as follows on the 1025 companies covered: Buy/Outperform- 16.5%, Hold/Neutral- 75.6%, Sell/Underperform – 7.0%. Data is as of midnight on the business day immediately prior to this publication.