



Students are required to choose an organisation in the creative industries and produce a 5000 word report which includes an analysis of the economic environment of the organisation.

Students should then discuss how entrepreneurial business methods and techniques are applied and/or could be applied in the chosen organisation.

Your report is expected to cover the following areas:

A brief history of the chosen organisation, including the major events of the markets, launch of new products and any other strategic changes).

A critical review and discussion of the organisation's business economics including:

- Its products and customer base
- Its major competitors
- Its pricing strategy
- The characteristics of the market that it operates
- The macro environment that it faces
- Students could use a SWOT analysis to help them with this area

A critical review and discussion of the organisation's business finance including;

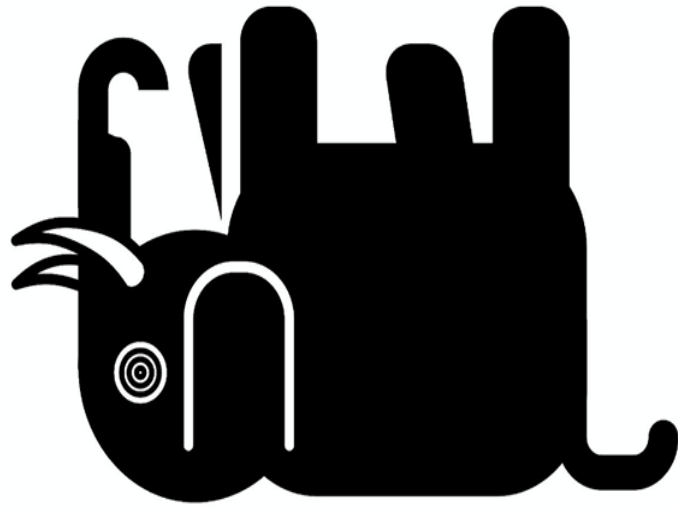
- Its major short term financing
- The current structure of its long term financing
- The recent major financing and investment activities
- A discussion of the pros and cons of alternative ways of financing with respective to the company.
- Students could use a PEST analysis to help them with this area

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HIPGNOSIS

INTRODUCTION

For a firm that is less than five years old, Hipgnosis is having a significant impact on the music industry. Founded by Merck Mercuriadis and Nile Rodgers in 2018 with the intention of providing investors with a pure-play exposure to royalties relating to songs, the fund now ‘owns’ 65,000 songs and is valued at over \$2 billion.



Both founders are well known faces in the global music industry – Nile Rodgers is the co-founder of disco / funk band Chic, who has since produced works by legendary artists such as Diana Ross, Blondie, Mike Jagger and David Bowie. Merck Mercuriadis is not as well known to the public as his co-founder, but has served as manager to such artists as Elton John, The Pet Shop Boys, Morrissey and Beyonce. He was also CEO of the Sanctuary Group for almost twenty years.

Despite this rapid success, Hipgnosis is not a particularly well-known firm, and if we examine their mission statement, we may ascertain why:

“Hipgnosis was created to give the investment community access to extraordinarily successful hit Songs by culturally important artists and to establish Songs as an uncorrelated asset class with attractive returns.

Our ulterior motive is to use the importance of our unparalleled Catalogue and our financial clout as influence to improve the Songwriter’s position in the economic equation.”

(Hipgnosis: About, 2022)

This first part of this statement suggests that Hipgnosis is first and foremost an investment company but utilising the raw materials of the music industry to provide financial returns. Institutional investors, particularly pension funds, are always looking for predictable,

long-term income streams, the kind conventionally provided by equity and bond dividends.

Songs, with their consistent royalty streams, can provide this reliability but it has been difficult to access these streams in the past as they were often bundled in with other assets of a larger group e.g. Sony, where these returns would be compromised by the performance of say, the Playstation. Also, many music publishers are privately owned, and therefore their shares are not available to investors. Warner Music was privately owned between 2011 and 2020, and Universal was a subsidiary of the French multi-media group Vivendi up until 2021.

Whilst Hipgnosis might be considered pioneers in this field, there have been attempts in the past to make song royalties investment grade, the famous ‘Bowie Bonds’. In 1997, David Bowie partnered with the Prudential Insurance Company to issue bonds based on past and future royalties derived from his music. They raised £55 million and paid a coupon of 7.9% for ten years. On maturity in 2007, the rights reverted to David Bowie. (Chen, 2022)

If the first part of the mission statement is aimed at the investor community, the second part is firmly aimed at the music industry. Merck Mercuriadis is very vocal about where the songwriter / composer sits in the current revenue model and is using Hipgnosis as a force for good in attempting to alter the economic equation in their favour.

When asked why they decided to start Hipgnosis, Rogers replied “A song, a single song, should be seen as a commodity – like an emerald or a diamond. The interesting thing with songs are they may fluctuate, but they rarely go down – the economics don’t work like that. Songs stay in the marketplace, stay working for you, and as they get older, they become more valuable.” (Shah, 2019)

TIMELINE

2018

July - formally founded by Merck Mercuriadis and Nile Rogers, raising £202 million by listing on the London Stock Exchange (LSE)

July - acquired their first catalogue from Terius Youngdell Nash (The-Dream) for £19 million, consisting of a 75% interest in 302 songs including Beyonce's "Single Ladies" and Justin Bieber's "Baby" (Reid, 2018)

November - acquired the 214 song catalogue from Jason Boyd (Poo Bear) including Justin Bieber's "What Do You Mean"

November - acquired a 37.5% stake in 290 songs from Chic's co-founder Bernard Edwards, including the hits "Le Freak" and "Good Times"

December - acquired the 121 song catalogue from song-writing and production team TMS including "DNA" by Little Mix

December - acquired the 121 song catalogue from Tricky Stuart including "Touch My Body" by Mariah Carey

2019

January - acquired 182 songs from Giorgio Tuinfort

January - acquired 209 songs from Itaal Shur

March - acquired the 249 song catalogue of Johnita Austin, including "Be Without You" by Mary J Blige

March - acquired 245 songs from Rico Love including "Throwback" by Usher

March - acquired their largest catalogue to date, the 588 strong catalogue from Sean Garrett including "Check On It" by Beyonce

April – raised £146 million from investors

May - acquired Dave Stewart of The Eurythmics' catalogue of 1068 songs, including "Sweet Dreams (Are Made of This)" and "Would I Lie to You". He joins the Advisory Board. (Stassen, 2019)

August – raised £50 million from investors

October – raised £234 million from investors

October - acquired the 108 album catalogue from producer-songwriter-artist Timbaland, featuring hits from 50 Cent, Madonna, Rhianna and Jay-Z (Aswad, 2019)

November – admitted to the Premium Main Market of the LSE

November - acquired four albums from The Kaiser Chiefs

2020

January - acquired the publishing rights of former Blink-182 member Tom DeLonge

March – became a constituent of the FTSE-250 Index

April – acquired 70% of Mark Ronson’s catalogue

July – raised £236 million (target £200 million) with another over-subscribed share placing

August - acquires the catalogue of Barry Manilow, including his fifty Top 40 singles such as “Copacabana”, “Looks Like We Made It” and “Mandy”.

September - in a departure from their previous strategy, Hipgnosis purchases American publishing company Big Deal Music Group, bringing in the catalogues of One Direction, Shawn Mendes and Panic! At The Disco. (Ingham, 2020)

September – raised another £190 million in 72 hours in a share placing

October – acquired the 162 song catalogue of producer LA Reid, with Reid joining the Hipgnosis Advisory Board. Songs included Whitney Houston’s “I’m Your Baby Tonight” and Boyz II Men’s “End of the Road”. (Garner, 2020)

November – in their biggest deal to date, Hipgnosis acquired 33,000 songs from Kobalt Music Group, including songs from 50 Cent, Steve Winwood and The B-52s. The deal cost \$323 million. (Lavin, 2021)

2021

January – acquired the producer royalties of Jimmy Iovine’s 259 recordings as well as his film production rights for “8 Mile” and “Get Rich or Die Tryin”.

January – acquired writer and publisher shares of 161 Lindsey Buckingham of Fleetwood Mac songs

January – acquired all 145 of Shakira’s songs

August - acquired writer and publisher shares of 115 songs by Christine McVie of Fleetwood Mac

October – Blackstone takes an ownership stake in Hipgnosis Songs Management and commits to a \$1 billion investment in the acquisition of rights and catalogues, under the direction of Hipgnosis. (Blackstone, 2021)

2022

July – appointed SACEM to administer and collect their European royalties

July – signed a sub-publisher deal with PeerMusic

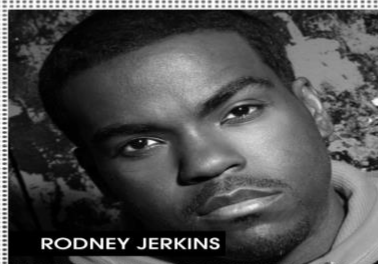
COMPANY STRUCTURE

When we use the name Hipgnosis we are referring to the company which acquires the legacy catalogues of various artists. However, the situation is more complex than this and we should be more specific as to which entity we are referring to.

The company that owns the rights is the Hipgnosis Songs Fund and is a Guernsey-registered investment trust. (An investment trust is a public limited company that is traded on the LSE and whose aim is to generate profit for its shareholders. They may contain a variety of assets, such as bonds, equities, property and in the case of Hipgnosis Songs Fund, the rights deriving from songs.) Appropriately the company's LSE ticker is SONG.

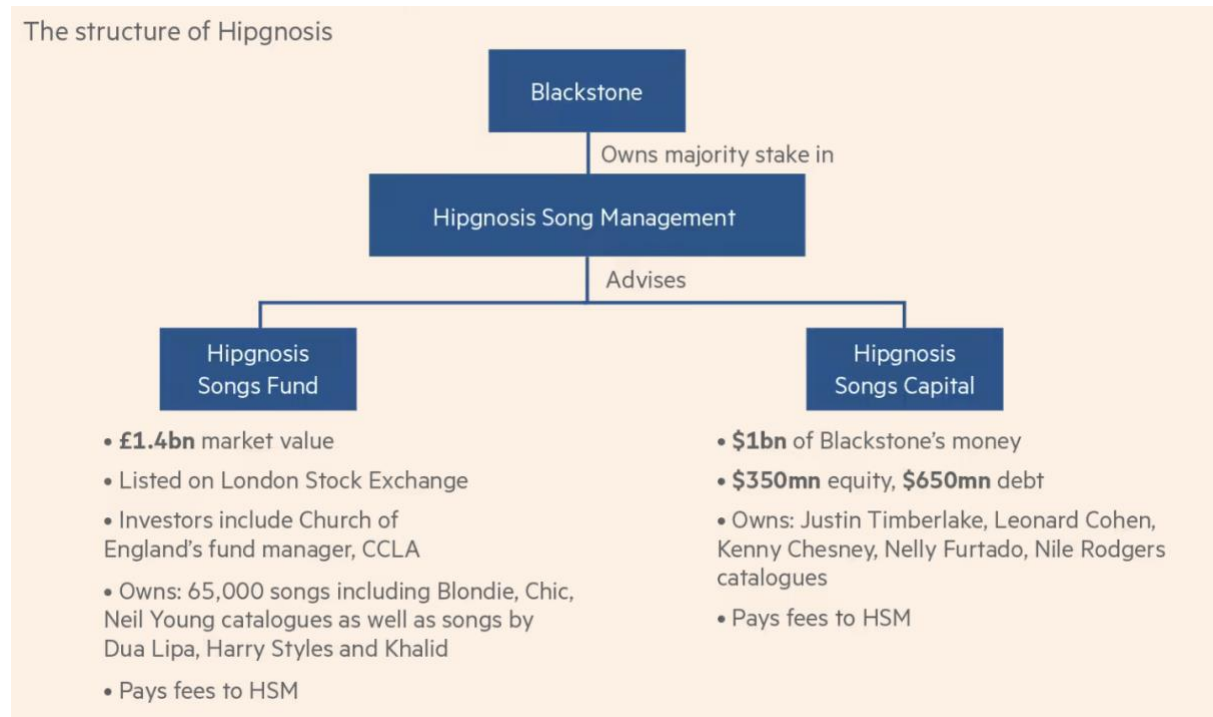
In 2020 the Hipgnosis Song Fund purchased an American publishing company and all its catalogues, Big Deal Music and renamed it Hipgnosis Songs Group. It remains a fully owned subsidiary of the Fund.

All investment decisions as to which catalogues the fund will purchase are taken by the fund's Investment Adviser, which is Hipgnosis Song Management Ltd., a company founded by Merck Mercuriadis (previously known as The Family (Music) Ltd.) To assist and validate the investment decisions, they have appointed an Advisory Board comprising of highly influential figures from within the music industry. It is interesting to note that a number of these Advisory Board members, such as David Stewart, Poo Bear and The-Dream were only appointed to the Board after their catalogues were acquired by the Fund.



(Hipgnosis: Our Team, no date)

This was the picture before Blackstone got involved in 2021. Blackstone is a Wall Street giant, with almost a trillion dollars of assets under management. As well as taking an equity stake in Hipgnosis Song Management, they pledged a billion dollars to set up a fund, named Hipgnosis Song Capital, also advised by Hipgnosis Song Management.



(Wiggins and Nicolaou, 2022)

Since this deal was inked, it has been interesting, though not unexpected to note that major acquisition activity has somewhat switched from Hipgnosis Songs Fund to Hipgnosis Songs Capital. Even though they have the same backers and advisers - Hipgnosis Song Management – the shareholders are of course different, so it could be said that the two funds are actually competitors rather than stablemates.

FINANCING

Most businesses when they are at the start-up phase typically target a variety of financial backing, including Angel investors, government grants, bank loans or even loans/equity investments from friends and family. Given the ambitious nature of what Mercuriadis and Rogers were aiming for with Hipgnosis, these options would have been wholly inadequate.

Teaming up with Singer Capital Markets as their Financial Adviser, they formulated a business plan that survived a punishing schedule of roadshow visits to City institutions, where they were robustly challenged but ultimately won the backing of their audiences. With Singer as the Bookrunner, the IPO was an oversubscribed success, raising £202 million and seeing Hipgnosis Song Fund on the Specialist Fund Segment on the Main Market of the London Stock Exchange in July 2018.
(Singer Capital Markets, 2018)

But this was only the beginning of their successful relationship with the City. Hipgnosis, with their Broker Singer Capital Markets have returned to the markets several times since floating, each time raising millions for their war chest.

2019 April – raised £141.5 million in an oversubscribed share placing at 102p per share (target was £100 million). Issued 138.8 million shares (41% of its enlarged capital)

2019 August - raised £50 million from investors

2019 October - raised £231 million in a 'C' shares issue, placing 231 million new 'C' shares at a price of 100p each.

"This is a demonstration of the financial community recognising the true value of music and proven songs. They are the currency that makes the world go round. They are predictable and reliable and they are better than gold or oil. We have lined up the finest available song catalogues and will be deploying immediately." (Sweney, 2021b)

2020 June – raised £236 million (target £200 million) their biggest equity raise to date (Singer and JP Morgan as joint brokers)

2020 September – raised £190 million in a share placing at 116p per share. Issued 163.8 million ordinary shares. Mercuriadis said: "To raise GBP190 million in 72 hours and GP420 million in two months during a pandemic is the greatest endorsement from the investment community for Hipgnosis and proven songs as an asset class. The uncorrelated returns songs provide have been very important to our shareholders during these difficult times and have only reinforced the belief in our thesis which has now become reality." (Singer Capital Markets, 2021b)

2021 February – raised £75 million through placing, subscription and intermediaries offer. Issued 62 million shares at 121p each

2021 April – raised £11 million from an equity issue. Issued 9 million shares at 119.5p each

2021 July – Raised £156 million (target £150 million) Issued 128 million shares at 121p each. (LSE: Hipgnosis Song Fund, 2023)

“We will now have a portfolio of almost \$2.5 billion of extraordinarily successful and culturally important songs, which offers a massive opportunity for us to add value with our Song Management which manages these songs with bandwidth and responsibility.” (Singer Capital Markets, 2021)

Mercuriadis publicly thanked Singer for their role in the Hipgnosis story, acknowledging their contribution “You have been sensational since day one and we can’t thank you enough for your efforts. Singer Capital Markets have been a major part of our success.” (Singer Capital Markets, 2022)

Bank Loans

Equity raises are an efficient way of raising capital, but they are time-consuming and expensive – typically 5% to 7% of the total raised. So Hipgnosis have also resorted to a revolving credit facility, to allow them to respond to business needs without the efforts and costs of an equity placing.

2023 January – Using interest rate swaps, Hipgnosis hedged its interest payments by fixing \$540 million at 5.7%

2022 October – signed a \$700 million RCF (expiry September 2027) To be used to refinance the company’s existing RCF and for working capital

"Together with the completion of our new revolving credit facility, executing these swaps concludes our refinancing. As debt markets have become increasingly unpredictable during the course of 2022, these new agreements provide long-term certainty and a stable platform to take advantage of the Music industry's tailwinds." (LSE: 2023)

July 2020 – Increased their RCF from £150 million to \$400 million – not only a real increase in value but also a change in currency to USD, given that most of their transactions are conducted in the USA

BUSINESS MODEL

According to their website, the key characteristics of the Hipgnosis business model are:

- “Sustainable earnings, uncorrelated to global capital markets, with sources of income from across the spectrum of music consumption patterns made up of millions of microtransactions such as streaming, physical purchase, downloading, synchronisation, performance, licensing and merchandising.
- A durable and diversified portfolio of high-quality assets founded on the copyright security – 70 years after the death of the last co-composer – of works across a broad range of genres, vintages and geographies of consumer markets. On average our Songs have more than 100 years of copyright protected revenue.
- The benefits of scale on diversification; giving smoother income the larger the fund gets; and the opportunity to drive incremental equity yield over the contracted period through active management and appropriate outsourcing of administration.
- Exposure to structural growth themes in relation to: i) the penetration of technology into everyday life; ii) the growing value of entertainment markets; and iii) the recognition of the real asset value of intellectual property rights.” (Hipgnosis: Our Purpose and Business Models, 2022)

Music is universal and most countries’ legal /social norms acknowledge that music is a resource that should be paid for. Many people are surprised that copyright collecting agencies such as the PRS in the UK and BMI in the USA have been around since 1914 and 1939 respectively. It was only with the development of the mp3 file format and the widescale piracy that occurred in its wake that the concept of ‘free music’ came about. Revenues throughout the music industry decreased sharply and despite many arguments against streaming, it arguably saved the music industry. That is not to say that the streaming model is perfect, far from it, but at least we are now back in a situation where money is being made and consumers are generally happy to pay for the privilege of listening to their favourite artists.

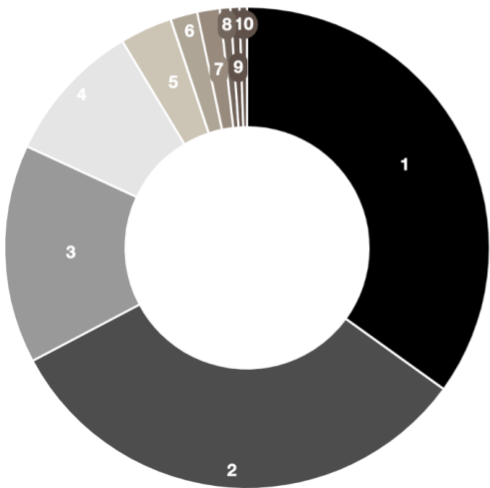
Given this scenario, how is Hipgnosis making money from their portfolio of 65,000 songs? Essentially, they are a music publishing company, even though they would describe themselves as Song Managers, the principle is the same.

Having started out with literally zero songs and with the £200 million proceeds of the IPO as a war chest, Hipgnosis went on the acquisition trail. So rapid was their progress that they were described by MusicBusiness Worldwide as “one of the most aggressive acquisitive parties in the modern music business” (Ingham, 2019). As soon as they burned through the cash, they returned to the capital markets, who were more than happy to enable them with more money to buy even more catalogues. Within three years they had raised almost a billion dollars and spent it all. Their investment strategy

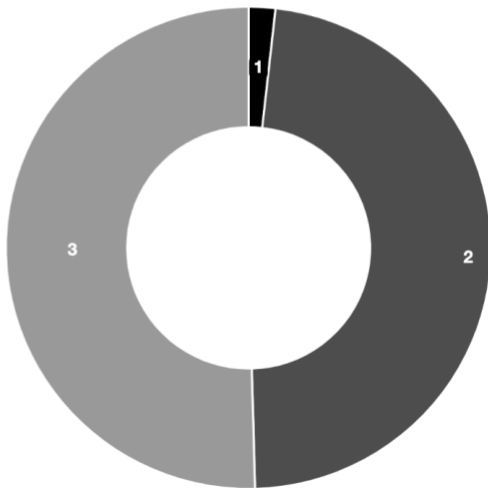
was to build “a diversified Portfolio, acquiring Catalogues that are built around proven hit Songs of cultural importance by some of the most talented Songwriters globally”. By diversified, they mean diverse in terms of genre, age and recording artist as this helps de-risk the portfolio.

All of the Songs in the Portfolio have a proven track record and are diversified by vintage, genre and recording artist. They are represented by some of the most successful original recording artists of all time.

Portfolio Value by Genre (%)



Portfolio Income by Age (%)



Genre	(based on fair value)	31 March 2022
1.	Rock	35.0%
2.	Pop	32.3%
3.	R&B	14.7%
4.	Dance	9.5%
5.	Latin	3.5%
6.	Country	1.8%
7.	Disco	1.5%
8.	Christian	0.6%
9.	Hip-Hop	0.7%
10.	Soul	0.5%

Age	(based on fair value)	31 March 2022
1.	0-3 years	1.7%
2.	3-10 years	45.9%
3.	10+ years	52.4%

(Hipgnosis: Songs Fund, 2022)

As the owner of 65,000 songs it was time to sweat the assets, and Hipgnosis claim that as Song Managers and not a publishing company, the difference is how much extra effort they put into making each song earn money compared to say, Universal Music.

Songs belong to the composers / songwriters who write them. These might be individuals, or collaborators. When a song is written it is automatically the property of the writers and cannot just be used by anyone without permission from the songwriter. Once a song has been released and is being played on some form of media, it would be impossible for the songwriter to administer the song as it could be played anywhere in the world. Most songwriters join the collecting agency that represents their country of residence eg SACEM in France, GEMA in Germany or PRS in the UK. If the song is correctly registered the collection agency should be able to pay the songwriter any royalties due.

A song makes money in one of the following ways:

Performance Royalties - Whenever a song is performed live, on TV, on radio, in a cinema or online

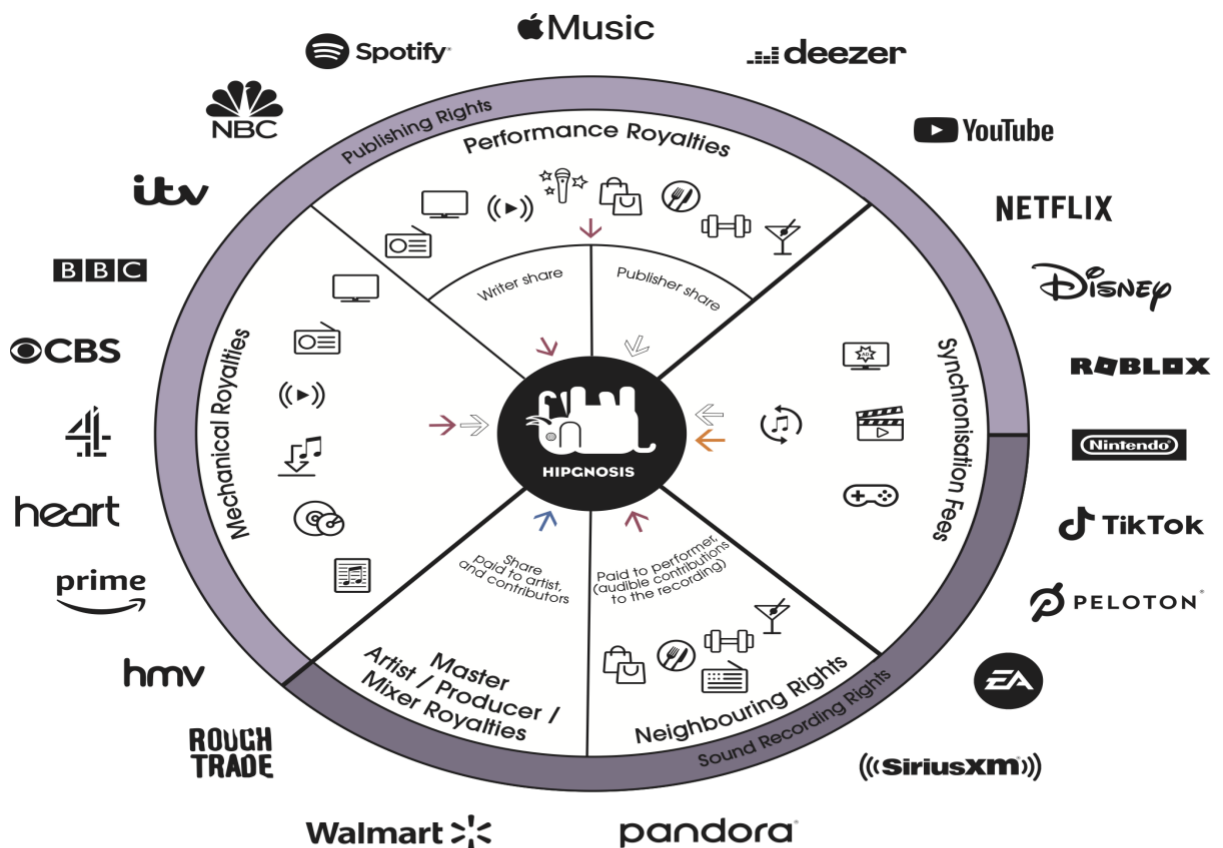
Mechanical Royalties - Whenever a copy of a song is made onto CD, DVD or vinyl, for downloading or streaming, or used to make a TV / radio programme, commercial or film. When used for the latter purpose, it is common to use the term 'synchronisation' but it is just a form of mechanical royalty involving synching the song to moving images.

The other royalty that can be claimed from a song is the Master Recording rights, which is the copyright attached to the recording of a particular song, typically owned by a record label, but may have been bought back by a successful artist. If possible, Hipgnosis likes to acquire the Master Rights to the songs it buys and having the full rights gives it more control over the onward licensing negotiations. But rights these days are very fragmented and it may not be possible to own a song outright.

When songwriters become successful, it is common for them to be offered a publishing contract. The publisher would then take charge of the administration of the writer's portfolio. A good publisher would also be looking to maximise revenue from that portfolio, by seeking out artists to record it and by seeking lucrative synchronisation opportunities, particularly in advertising or television. However, Universal Music has a catalogue of 3 million songs, and obviously is not going to be able to actively manage every song in its portfolio. At the Hipgnosis AGM in October 2019, Mercuriadis argued that the traditional publishing model was broken and that he preferred to call Hipgnosis a Song Management company.

At Hipgnosis, each song is considered its own business with its own Profit and Loss statement (P&L) and each Song Manager has a much smaller roster of songs to manage which means they can give more time and effort to each song.

The diagram below, taken from the Hipgnosis website, illustrates how the different rights streams contribute to the overall revenue, and the complexity of their revenue model. Anyone who uses music is a potential customer – TV companies such as Netflix and the BBC, advertising agencies, the Digital Streaming Platforms, even video game producers.

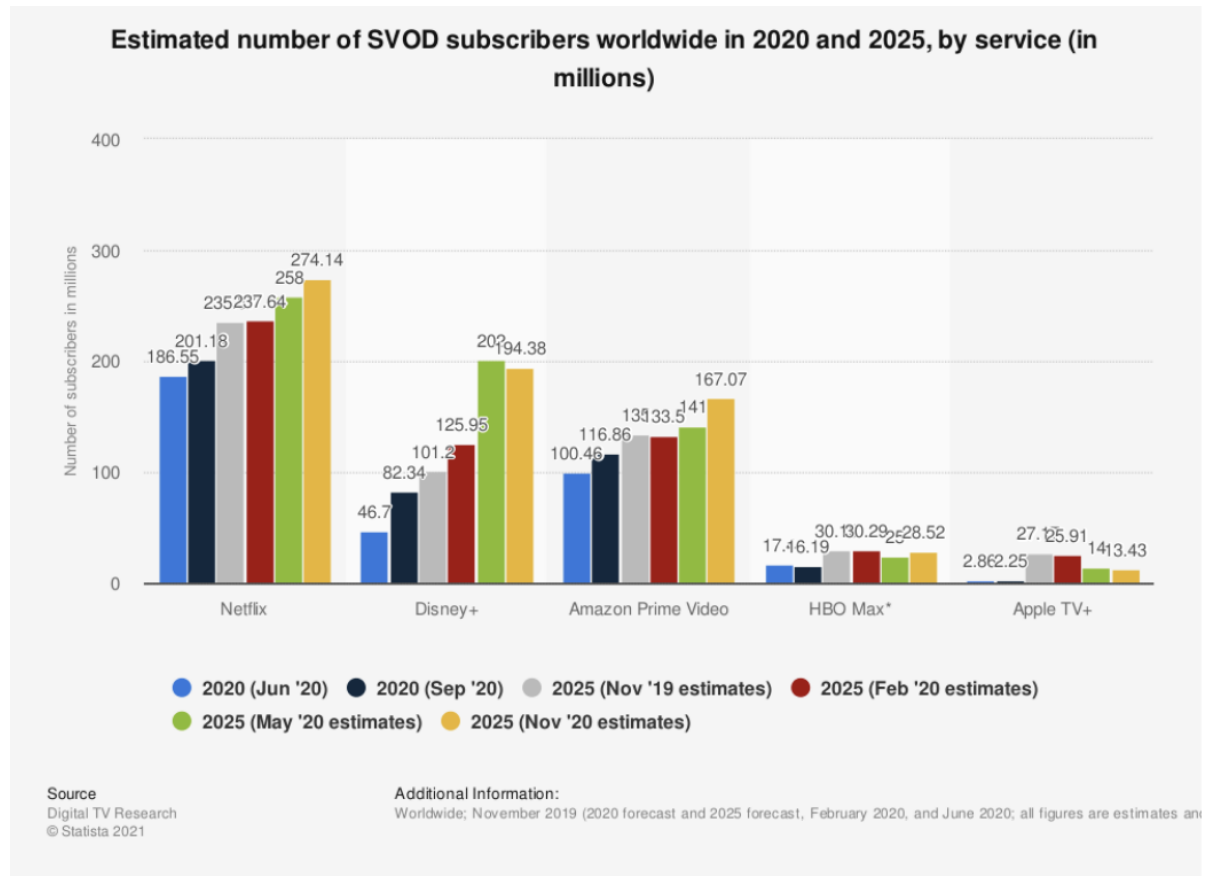


(Hipgnosis: Our Purpose and Business Models, 2022)

It is interesting to note that despite having ownership of these royalty streams, the monies are not paid directly to Hipgnosis, but depending on the rights concerned, through intermediaries such as their catalogue administrators, the record labels and the

collecting agencies. This means that they do not need to run administrative departments which would not be efficient given the relatively small size of their portfolio.

Increasingly over the last five years, synchronisation is becoming the most lucrative business to gain, driven primarily by the growth in the number of TV/movie channels available and the sheer amount on new content being produced, as illustrated below:



(Record-Play, 2021)

A pertinent example is of course ‘Stranger Things’ – each song featured on the show boasts an average of 87 million streams on Spotify and the official playlist boasts a quarter of a million followers. With a budget of \$30 million per episode, getting a track on the show is every synch manager’s dream – it is estimated that ‘Running Up That Hill’ has made Kate Bush \$2.3 million in streaming fees alone since featuring prominently in Season 4 and that’s not including the sync fee that would have been negotiated between the show and Sony Music Publishing. It is no surprise that the TV show Music Supervisor has become the “new big cheese in the music ecosystem” (Hall, 2022).

In a recent article in The Telegraph, Mercuriadis confirmed that Hipgnosis receives around 75 sync requests a day for songs in its catalogues, and that they ask three

questions before deciding whether to give permission or not. Some days it's Yes to all of them, some days it's No.

- 1) Would the songwriter / artist be happy?
- 2) Is the deal financially acceptable? (though he does not disclose what kind of figure he is looking for!)
- 3) Is the use going to generate significant streaming (and therefore additional revenue from the DSPs)?

“Hipgnosis has a digital marketing team that keeps an eye on TikTok, using its own software called Heatseeker to pick up on unusual song activity. Mercuriadis gives Blondie’s Heart of Glass as an example. Not long after Hipgnosis bought the Blondie catalogue in 2020, Gen Z favourite Miley Cyrus performed the 1979 song as an encore at a concert. Hipgnosis saw this as an opportunity to introduce Debbie Harry’s work to a younger generation. So Harry and Cyrus were introduced, “there was a love-fest as you can expect”, and Hipgnosis juxtaposed a 1979 photo of Harry next to a picture of Cyrus in 2020. “That went viral. TikTok really started to explode with Blondie’s version of Heart of Glass and Miley’s version. And now, almost two years later, we have the better part of 400 million streams more on Heart of Glass over and above what the traditional run-rate has been,” Mercuriadis says.” (Hall, 2022)

THE COMPETITION

Despite being unorthodox in its approach to Publishing / Song Management, Hipgnosis is very much in competition with the traditional music publishers.

The Big Three

Sony Music Publishing (including EMI) controls over 5 million songs

Universal Music Publishing Group controls over 4 million titles

Warner Chappell Music controls around 1 million songs

(Ross, 2022)

The Independents – the Music Publishers Association has 200 UK members, including well know names such as ABKCO Music, Carlin Music, Concord and West One.

(MPA, 2023)

As well as the music publishers, Hipgnosis is also competing with other global Song funds, such as Round Hill Music Royalty Fund and the ICM Crescendo Music Royalty Fund. Even private equity is after a slice of the music pie since BlackRock teamed with Warner Music Group and also formed an alliance with private publisher Primary Wave.

(Ingham, 2021c)

There are millions of songs out there and a lot of companies plugging them, therefore the competition is huge, especially for a small company with a repertoire of only 65,000 songs.

However, Hipgnosis does have a number of competitive advantages:

One is their highly selective roster of songs / songwriters – each of its catalogues will have been purchased after a rigorous selection procedure, involving the full (and expensive) expertise of the Advisory Board (consisting of Grammy Award winners, leading industry figures and members of the Songwriters Hall of Fame).

Mercuriadis noted “When compared with the three major song companies, we have achieved between 7% and 12.5% of their revenue on between 0.5% and 0.9% of their number of songs...All of our songs have a proven track record and we do not speculate on new songs regardless of the past performance of the songwriter, producer or artist. These proven hit Songs produce reliable, predictable and uncorrelated cash flows which are highly investible.” (Variety, 2020)

The other competitive advantage which Hipgnosis has is Mercuriadis himself. When Hipgnosis acquires a catalogue, the press announcement inevitably includes a gushing statement from the CEO as to why they chose this particular artist...but the love is most certainly requited:

Jimmy Iovine said: “I’m happy that my work as a producer with so many great artists has found the right home with Merck and Hipgnosis. I am going to use the proceeds from the deal to help Iovine Young Academy’s initiative to build a high school in South LA as part of the Iovine Young Academy at USC and continue our efforts to support education.” (Ingham, 2021)

Richie Sambora said: “I’m very privileged to have had the incredible success I have achieved as a songwriter and artist to date. These songs are very important to me and I feel very strongly that Merck is the only person I could have entrusted my babies to. I believe the work he is doing that has transformed the way that the world looks at the power of great songs and the songwriting community is very special. I look forward to working with him and his Hipgnosis team to deliver more success for all of us.

(Paine, 2020)

Timbaland said: “Merck is a visionary who I know appreciates the value of my musical life work. My music is in great hands.” His manager, Gary Marella, said: “It’s important to all creators that their work is in the right hands. Merck’s respect for music creators is unparalleled. We are pleased to have part of Tim’s iconic catalogue with Merck and Hipgnosis.”

(Aswad, 2019)

“[Merck] sees his company more like a song management company unlike many publishers who act more like a collection agency and wait for the money to pour in,” said Dave Stewart. “I’m excited to be on the advisory board of this forward thinking company.” (Sweeney, 2021)

LA Reid added: “I can’t imagine a better home for my lifetime of music and songs than Hipgnosis. Merck and his dream team truly value artists and their creative vision, and I couldn’t be more thrilled to partner with them for this exciting new chapter.” (Garner, 2020)

THE MARKET / PERFORMANCE

There are many metrics by which we can judge the performance of a company. Given that the raison d'être for the fund is the ability to reward its investors with a reliable income stream, has the fund lived up to expectations?

The fund has always targeted a dividend yield of 5.25% based on the initial share price of 100p, once fully invested. Since Q4 2020, they have indeed been paying a quarterly dividend of 1.3125p per share making exactly 5.25% (given that today's share price is closer to 90p the dividend yield for new investors would be 6%).

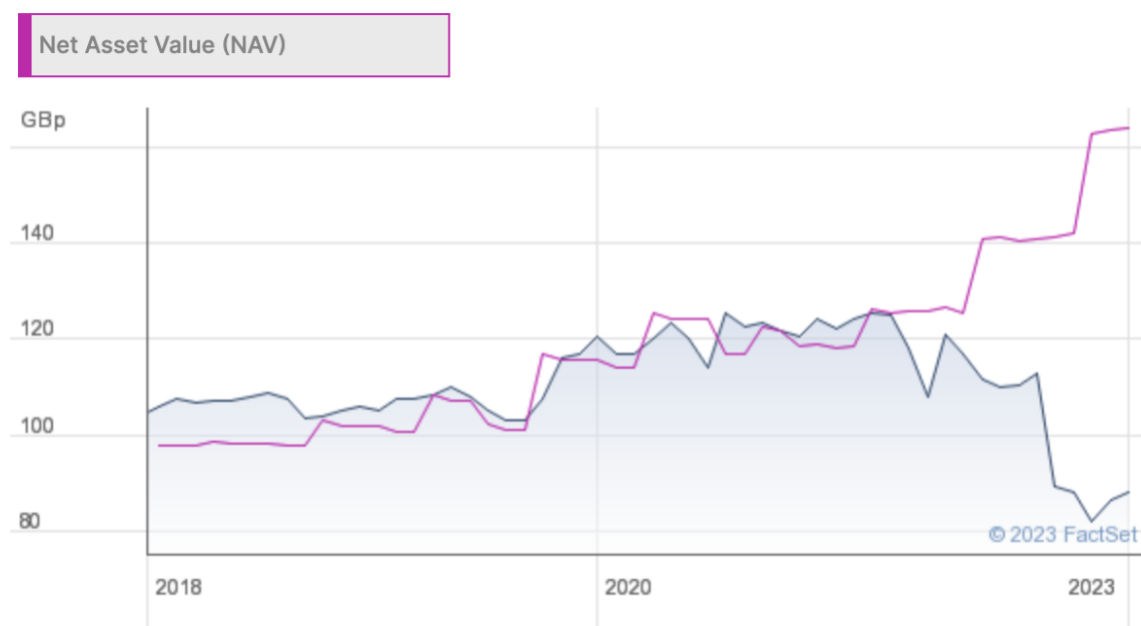
However, Hipgnosis floated in 2018 at 100p per share. The graph below illustrates a pretty steady upwards trend towards 130p until 2022 when there was a downwards lurch to 82p with a small recovery to 90p today.



Long term investors would not be particularly happy with a 10% loss in the value of their portfolio, but with the dividend yield as promised, they would probably keep Holding their portfolio with the expectation of a recovery in the share price, particularly after seeing it hit 130p only a year ago. Later investors who may have been persuaded by the rising share price won't be so happy with an almost 40% drop in the value of their holding, particularly if they bought at that 130p high.

Obviously share price is only one metric to judge a company. If we look at a chart of the Net Asset Value (NAV) of the company, overlaid, we can see that the NAV shows a much rosier picture:

Price



(Hargreaves Lansdowne, 2023)

According to the RNS from the LSE “There are positive tailwinds for the Company due to the decision of the US Copyright Royalty Board to confirm and make retroactive, the CRB III increase in mechanical streaming royalty rates for songwriters and publishers between 2018 and 2022, and the anticipated refinance of the Company’s credit facilities, which is expected to be completed in October 2022. Accordingly the Board continues to target paying an annual dividend of 5.25p per Ordinary share for the financial period to 31 March 2023”. (London Stock Exchange, 2022)

So what caused the share price to drop quite dramatically from 130p to 80p, given that the NAV has been increasing. Having examined a number of Broker reports it seems it was nervousness at Hipgnosis’ exposure to rising interest rates given their Revolving Credit Facility (see the FINANCING section) and the delay in rectifying it:

“While this re-financing is an important development and provides greater security over the company’s ability to service its dividend, investors are entitled to ask just why it has taken so long to execute. Although it has clearly been an error of judgement by the Board and Manager to not fix interest costs earlier, we remain constructive on the asset class and would highlight that the debt fixing provides some comfort over the dividend in the short to medium term. The rating has collapsed in the past year and it is disappointing that SONG has not sought to address this with the same vigour that was previously applied to fund raising, although this again is partly a function of poor balance sheet management. Given the quality of the underlying assets and current discount, we now wonder whether SONG may find itself vulnerable to corporate action”. (Investec: Broker Report on Hipgnosis, 2022)

Pretty scathing – they like what Hipgnosis has done over the last few years but they have made a major financial error which has spooked their investors and made them potentially liable to a hostile takeover.

Interestingly, in 2021, Steve Cooper, the then CEO of Warner Chappell accused Hipgnosis and other companies that were buying catalogues at a rapid rate of knots of financial ill-discipline “When you pay north of a certain multiple, you’re beginning to move into the world of finance that lacks a certain amount of discipline. I praise the people that can figure out how to make money when they pay 25 times [a song’s historical annual royalties]. God bless.” (Nicolaou, 2021)

Whilst the average paid by Hipgnosis is 14.76 times songs’ historic annual income, Mercuriadis has admitted paying 22x for certain un-named catalogues.

CONCLUSION

In a short period of time, Hipgnosis has made a big impact on the music industry. By acquiring (and paying handsomely for) dozens of iconic music catalogues, it is changing the face of the music publishing model. Since they started the trend, others have followed and where such deals were rare only a few years ago, it is now almost a weekly occurrence to hear news of a major catalogue sale – though ironically not to Hipgnosis recently.

Rising interest rates have made raising capital expensive, and competition has grown. Though initially caught unawares, the big three publishing houses have entered the fray and are backed with deep pockets – during the last year or so, whilst Hipgnosis consolidated, it's Universal, Sony and Warner that have been making the headlines – Bob Dylan sold his entire catalogue to Universal for \$400 million, Bruce Springsteen to Sony for \$500 million and David Bowie's estate sold out to Warner Music for \$250 million. (Sweeney, 2022)

Recently JP Morgan issued a research note on Hipgnosis where it maintained its Overweight stance on the stock and said “Given the long-term growth potential of the asset class , and the higher quality (in our view) portfolio relative to [Round Hill Music], we believe SONG offers compelling value”.

As a shareholder in Hipgnosis, I am happy to hold and take my 5.25% annual yield. I am confident that the price will rise again as investors take advantage of the deep discount in the price vs the NAV. With streaming uptake continuing to grow and sync licensing increasing the size of the royalty pie, this is an asset class that looks exciting, particularly in these turbulent economic times.

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