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The Walt Disney Company **Q2 FY13 Earnings Conference Call**

MAY 7, 2013

Disney Speakers:

Bob Iger

Chairman and Chief Executive Officer

Jay Rasulo

Senior Executive Vice President and Chief Financial Officer

Moderated by,

Lowell Singer

Senior Vice President, Investor Relations

PRESENTATION

Operator

Hello and welcome to the Q2 2013 Walt Disney Company earnings conference call. My name is Myesha, and I will be your operator for today's call. At this time all participants are in a listen-only mode. Later we will conduct a question-and-answer session. (Operator Instructions). Please note this conference is being recorded. I will now turn the call over to Lowell Singer, Senior Vice President of Investor Relations. Lowell, you may begin.



Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank you. Good afternoon, everyone and welcome to The Walt Disney Company's second-quarter 2013 earnings call. We issued our press release about 45 minutes ago. It's available on our website at www.disney.com/investors. Today's call is being webcast, and we will post a transcript to our website after the call.

Joining me in New York for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer; and Jay Rasulo, Senior Executive Vice President and Chief Financial Officer. Bob will make some comments followed by Jay, and then we will be happy to take some questions.

So with that, let me turn the call over to Bob.

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

Thank you very much Lowell, and good afternoon everyone.

We had a strong second quarter, with earnings per share up 36% over last year, when adjusted for comparability, driven primarily by Studio, Parks and Resorts and Media Networks. We are pleased with our overall performance, confident in our strategy, and thrilled with a stock price that keeps reaching new record highs.

Of course it's great to announce such a strong earnings just after we are rolling out another Marvel blockbuster, *Iron Man 3*, which had an incredible domestic opening with almost \$175 million. That makes it the second biggest opening weekend of all time, surpassed only by *The Avengers*.

Internationally, *Iron Man 3* has set new opening weekend box office records in a number of countries, and has already brought in over \$525 million outside the U.S. So to date, the global box office for *Iron Man 3* is more than \$711 million.

We're proud of this movie and thrilled with its performance. *The Avengers* franchise is certainly strong today, but we have a lot more to come, with *Thor: The Dark World* in November, *Captain America: The Winter Soldier* next year, and *The Avengers 2* in 2015.

On the animation front, Pixar continues to create great value for our company, too, and we're very excited about *Monsters University* which opens next month. Pixar's slate of films for the next five years includes fantastic original stories as well as some great sequels to their previous hits. And as we recently announced, we're in production on one of those sequels, *Finding Dory*, featuring Ellen Degeneres once again as the voice of Dory, one of the most beloved characters from *Finding Nemo* – which is one of the most popular and profitable movies to date.



On to Lucasfilm, our integration is well underway and, based on our success with Pixar and Marvel, we're confident we can drive great value from this acquisition. In addition to the *Star Wars* feature films that we've already talked about, we're also working on opportunities for television and our parks. It's still very early in the process, and we'll announce details as these developments evolve.

In the meantime, with great tent-pole features like *Iron Man [3]* and *Monsters University*, followed by Johnny Depp as Tonto in *The Lone Ranger* in July, our studio has delivered an incredibly strong slate of movies and we have a lot more to look forward to.

As I mentioned earlier, Parks and Resorts contributed significantly to our results this quarter, as the investments we've made in our domestic and international parks over the last several years begin to drive growth. We've completed the phenomenal transformation of Disney California Adventure, added two spectacular new cruise ships, and we're well into our historic expansion of Fantasyland at Walt Disney World. And later this month, we will complete our recent expansion of Hong Kong Disneyland with the opening of another new land.

In Q2, Walt Disney World and the Disneyland Resort both set new attendance records for the quarter. Attendance in our Disneyland Resort is now more evenly split between Disneyland and California Adventure – a strategic goal of our investment in that expansion. And in Hong Kong Disneyland, the addition of new lands and attractions also continue to drive strong performance

Cable networks were another important contributor to our results this quarter. As I mentioned on our last call, with 30,000 hours of sports programming across all platforms every year, and long-term rights to the marquee events, ESPN is still the must-have brand for sports fans.

And we just announced a 20-year agreement between ESPN and the Southeastern Conference to create and operate a national multiplatform network airing SEC content 24/7. ESPN has been covering the SEC since 1982, and this new network will provide an unparalleled SEC fan experience with live sports coverage as well as studio shows and original programming. The new network launches in August 2014, and will serve SEC fans as well as multi-channel distributors and advertisers who want to reach them.

Our kids television portfolio is also doing extremely well, and Disney Channel continues to be our biggest and most effective global brand builder and content engine, bringing Disney directly into hundreds of millions of homes around the world. We leveraged that strength to successfully launch Disney XD in multiple new markets, and more recently to launch Disney Junior, which now reaches almost 400 million homes in 166 countries.

Here in the U.S., Disney Junior is now a 24-hour channel reaching nearly 60 million homes. Anchored by hit preschool series like *Sofia the First*, *Jake and the Neverland Pirates*, *Doc*



Mcstuffins, and *Mickey Mouse Clubhouse* – Disney Junior is beating Nick Jr.’s ratings by double digits in almost every category, and beating Sprout’s ratings by triple digits across the board.

As an emerging franchise driver for our company, the success of Disney Junior goes far beyond television. Disney Junior-branded products have a strong and rapidly growing presence in the preschool retail space, with retail sales expected to increase by 80%, to \$1.5 billion in the current fiscal year.

Finally, turning to Disney Interactive -- yesterday we announced a new gaming agreement with Electronic Arts to deliver and publish several new games based on the epic *Star Wars* franchise. As you know, EA is one of the world’s premier developers of mobile, tablet, console, and PC games, and this multi-year, multi-title, and multi-platform agreement will allow us to bring great new *Star Wars* game experiences to the core gaming audience. We’re already planning the first titles from this agreement, and we look forward to announcing them with EA soon. And as part of this deal, Disney retains certain rights to develop new titles within mobile, social, tablet, and online gaming categories, as well as the rights to develop new titles for the Asian gaming market.

So, overall we feel great about what we achieved in Q2. We have an effective strategy and we’re looking forward to what’s ahead. It’s an exciting time at Disney – driven by high quality creative content and our unparalleled ability to leverage it for continued long-term growth.

I’m now going to ask Jay to review the details of our performance and then we’ll take your questions. Jay?

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Thank you, Bob and good afternoon everyone. We delivered another quarter of excellent financial performance with segment operating income up 29% on revenue growth of 10%. Earnings per share, excluding items affecting comparability, were up an impressive 36%. These results demonstrate the ongoing successful execution of our strategy, and our ability to monetize our assets, and the performance of recent investments in our Parks and Resorts business.

Let me spend a few minutes discussing our second quarter in more detail and then I’ll highlight some factors that may influence our performance for the third quarter.

Growth at Media Networks was due to increased operating income from our Cable Networks, partially offset by a decline in our Broadcasting business. The performance of our Cable business in the second quarter reflects the benefit of new affiliate agreements, resulting in total cable affiliate revenue growth in the low-teens, or almost 10% when adjusting for the impact of revenue deferral timing at ESPN and foreign exchange rates.



Operating income at Cable increased 15% on revenue growth of 9% primarily due to growth at ESPN. Results at ESPN were driven by increased affiliate and advertising revenue, partially offset by increased programming and production costs. The increase in programming costs were related to contractual rate increases for college football and college basketball rights.

During the second quarter, ESPN deferred \$70 million less in affiliate revenue compared to last year, which benefited reported revenue. In the third quarter, ESPN will recognize \$73 million less in net deferred revenue than in the prior year, which will have an unfavorable impact on Q3 reported revenue. I'll remind you these changes have no impact on full-year results.

ESPN ad revenue was up 4% in the second quarter, primarily due to higher units sold and higher rates. So far this quarter, ESPN's ad sales are pacing up more than 10%.

At Broadcasting, lower operating income in the quarter was due to higher cost write-offs for underperforming shows, an increase in primetime programming costs for acquired programming, and a decline in ad revenue at the ABC Network, partially offset by an increase in ad revenue at our owned stations. The decline in ad revenue at the network was due to lower ratings, partially offset by higher rates and an increase in online advertising.

Ad revenue at the ABC Network was down low single-digits compared to the prior year. Quarter-to-date scatter pricing at the ABC Network is running more than 25% above upfront levels. Ad revenue at the Stations was up 5% during the second quarter, and so far in Q3 TV station ad sales are pacing down single digits versus prior year.

Our Parks and Resorts segment delivered an impressive quarter with revenue up 14% and operating income up 73%. The increase in operating income was primarily due to growth in domestic operations as a result of higher guest spending and attendance at Walt Disney World and the Disneyland Resort, and higher passenger cruise days given a full quarter of operation for the Disney Fantasy. These increases were partially offset by higher costs, which were primarily due to growth initiatives.

For the quarter, attendance at our domestic parks was up 8% and per capita spending was up 10% on higher ticket prices, food and beverage, and merchandise spending. Average per room spending at our domestic hotels was up 7% and occupancy was down two percentage points to 80% due to an increase in available room nights at Walt Disney World.

So far this quarter, domestic resort reservations are pacing up 7% compared to prior year levels, while booked rates are comparable to prior year levels.

Higher operating income at our international operations reflects higher guest spending at Disneyland Paris and increased attendance at Hong Kong Disneyland Resort, partially offset by lower results from Tokyo Disney Resort reflecting the absence of business interruption insurance proceeds that we collected last year.



Total segment margins were up almost 400 basis points in the second quarter compared to the prior year, and were favorably impacted by about two percentage points due to the timing of the New Year's and Easter holidays.

While operating income in the second quarter was aided by a portion of the New Year and Easter holidays falling in Q2 relative to when those holiday periods fell last year, the results also reflected improved attendance and spending throughout the period and the growth investments we've made over the past couple of years are performing well.

Studio Entertainment operating income improved significantly in the quarter due to lower film write-offs compared to prior year, and improvement in our worldwide theatrical results due to the strong performance of *Oz The Great and Powerful* and *Wreck-It Ralph* compared to *John Carter* last year.

At Consumer Products, the increase in operating income resulted from higher performance in merchandise licensing and retail. The increase in Licensing is due to higher revenue from Disney Channel, standard character and Marvel merchandise, partially offset by lower revenue from *Cars* merchandise, as well as the resolution of a licensee audit. On a comparable basis, earned licensing revenue was up low single digits versus last year. The performance of our retail business was driven by higher comp store sales in North America and Japan, as well as higher online sales in North America.

Results at our Interactive business improved this quarter due to higher operating income from our Japan mobile business, increased sales of mobile games, and lower purchase accounting impact at our social games business.

As we look to the third quarter, I'd like to highlight a few factors that will impact our results, most of which are timing related.

At Parks and Resorts, the timing of the Easter holiday will adversely impact our Q3 results, as only one week of the two-week holiday fell in Q3, whereas the entire holiday period fell in Q3 last year. We estimate the adverse impact of the Easter holiday shift on Q3 to be about \$35 million.

Our Studio results in the third quarter will be impacted by the timing of pre-release marketing expenses for *The Lone Ranger*, which will be released domestically and in some international markets very early in fiscal Q4.

At Interactive, we expect an operating loss in Q3 that is comparable to the loss in the second quarter due primarily to the shifting of the release date of our Infinity game from Q3 to Q4.



And at Broadcasting, programming expenses are expected to be about \$40 million higher due to an increase in hours of original programming compared to last year. We also face a difficult syndication comparison due to the sale of shows, including *Castle*, in the prior year, as well as lower sales of library shows this year, which we expect to have a total adverse impact of about \$40 million in Q3.

We continued to repurchase our stock during the second quarter by buying back 15.8 million shares for about \$850 million dollars. Fiscal year to date, we have repurchased 38 million shares for \$2 billion dollars.

We feel great about the results this quarter and for the first half of the fiscal year. We remain incredibly well positioned strategically and financially, which enables us to continue to create value for our shareholders.

And with that, I'll now turn the call over to Lowell for questions.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank you, Jay. Operator, we are ready for the first question.

Q&A

Operator

(Operator Instructions). Michael Nathanson, Nomura.

Michael Nathanson — *Analyst, Nomura*

A quick housekeeping for Jay, then one for Bob. Jay, thanks for giving us the organic affiliate fee number. You made Lowell's life a little easier tonight.

The question I have for you is for the rest of the year, what's the right rate, thinking about the kind of like-for-like growth on affiliate fees? Is there anything unusual about this quarter, or will low teens kind of be consistent for rest of the next couple of quarters?

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

I think in general, you can look for high single digits, low teens moving forward for the rest of the year. Nothing extraordinary about this quarter.



Michael Nathanson — *Analyst, Nomura*

Okay. And then, Bob, for you, Jay just laid out kind of the big picture story on all of your drivers kind of kicking in the next couple of years. You have spent the past few years investing in franchises, investing in your parks, and a lot of your competitors have focused on buying back stock. Looking at the next couple of years, your drivers are all unknown to you. So do you consider at this point increasing the capital returns levels, dividends, buybacks? Are you adding some incremental debt to the company? How do you think about that knowing all you've done is kind of now paying dividends?

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

Well, we feel good about our ability to deliver more free cash flow. And don't have much to say specifically about how we'll allocate it, except that as you look back, we obviously made three pretty important and large acquisitions in Pixar, Marvel, and Lucasfilm, which we think delivered great -- has already delivered and will continue to deliver great growth and value to our shareholders.

But I'm not sure that we, as we see ahead, we see opportunities that are of like size. Not to preclude that from occurring completely, but we just -- it is just not obvious to us. That will then leave us with the opportunity, if we continue to grow our cash flow, to increase our dividend or buy back more shares. But we've not made that decision yet; I think it will be a good problem for us to have.

Michael Nathanson — *Analyst, Nomura*

Thanks.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

I think, Michael, in terms of the capital allocation -- almost because it's a given Bob didn't mention that first and foremost we look for internal opportunities to invest our capital in projects like you have seen us do over the last five years in addition to acquisitions. You know, the work we have done in parks and resorts, the joint ventures on free-to-air **television stations** -- I mean, we constantly look for ways that we can get superior returns through investment in organic growth. And we continue to want to grow the company organically. What's left after that, Bob just handled.



Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

We've also never really been a hoarder of cash. So I think you can expect that philosophy to continue. And we've been pleased with our credit rating, and I doubt you'll see us going to the market in the way that would necessarily -- that would impact our rating. For more debt, that is.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank you, Michael. Operator, next question, please.

Operator

Ben Swinburne, Morgan Stanley.

Ben Swinburne — *Analyst, Morgan Stanley*

Thanks, good afternoon. Just to clarify, Jay, I wanted to ask you -- the almost 10% growth in affiliate rev, that was organic ex-currency and ex-deferrals. Was that ESPN or overall cable? I realize we are kind of splitting hairs here.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

That was the overall cable number. I can tell you that if you back those two factors out, Ben, you are looking at 12.5% growth this year in affiliate revenues. If you back out -- this quarter, I'm sorry -- if you back out the deferral and the FX impacts.

Ben Swinburne — *Analyst, Morgan Stanley*

At cable?

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes.

Ben Swinburne — *Analyst, Morgan Stanley*

Okay, thank you. And then is there any particular reason -- would parks' margins be better because of the calendar shift? I realize it benefits attendance, etc., but I would -- obviously incremental expenses from the extra.



Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes. But of course, with the flow-through you have on incremental business, in our business when you're taking on that kind of incremental revenue in a single quarter, if you think about, for instance, around the holiday period, we're already fully staffed. So we have very strong flow-through. So yes, we think that of the 400 basis points, about 2% was due to the shift in the front end and the back end of that quarter in terms of impact on margins.

Ben Swinburne — *Analyst, Morgan Stanley*

Okay, thanks. And then lastly, Bob, could you just talk about your outlook for the studio segment? You've put a lot of capital to work with Lucas and Marvel, and clearly the titles are clicking on all cylinders.

You know, when you look back a few years ago, this was a billion-dollar plus profit pool. And I know the DVD market has changed, but you've also made some headcount changes. How do you think about the potential here for that line over the next several years as you roll out all these franchise films?

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

Well, I think you'll see more and more focus on big tentpole films and less on non-franchise, non-branded smaller films. You have to -- when you consider that strategy and that investment, you also have to consider the impact that that investment and those films have across the company. So, obviously consumer products, to some extent, Interactive. Certainly there are opportunities on the theme park front.

But we feel good about the slate ahead from all sectors of the company. Disney Animation, which has, we think, an excellent Christmas film in *Frozen*. Pixar, I mentioned on the call with a blend of sequels like *Monsters*, as a for instance and *Nemo*, with some real good original shows -- original movies, rather. I mentioned Marvel, which is very, very rich; *Star Wars* in 2015; and then some Disney live-action films that we feel quite good about in terms of our ability to basically drive decent returns on them.

It is definitely a more challenged business in terms of what I'll call physical sales or the physical home entertainment side of the business -- that is sell-through and rental of physical goods. But it's been growing nicely on the digital front. And I think that bodes well for the future.

Ben Swinburne — *Analyst, Morgan Stanley*

Thank you.



Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Ok, thanks Ben. Operator, next question, please.

Operator

Doug Mitchelson, Deutsche Bank.

Doug Mitchelson — *Analyst, Deutsche Bank*

For Bob and one for Jay. Bob, if you could talk about the timing of the rollout of My Magic Plus. Is there any way to give us a sense of the potential impact from that initiative? It's not the easiest thing for us to model.

And for Jay, hotel bookings up 7% against flat room rates? Is there a discounting strategy driving -- to drive hotel market share? Are those both in organic outcome, you know, as you look at it right now?

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

I'll start, Doug. On hotel bookings I would say it's an organic outcome. We have, in California, because of the strength of the demand that has accompanied Disney's California Adventure, we have really rolled out a lot of the discounting that's taken place on that property and feel very good about demand holding up despite that, and the overall both strategic and financial impact that product is having.

But of course, when you're looking at average booked rates across the domestic business, it is heavily weighted towards Walt Disney World. We have brought on a lot more inventory with that new value hotel that we've opened, and I think that we feel pretty strongly that you're seeing the demand numbers.

And remember, when you bring on a big value hotel, the very mix of the pricing that you have across the inventory of rooms will continue to push your rate down a little bit. But there's no promotional pricing that's taking place to push volume right now in that business. We're really at a point, as we said we would be, where we are yielding the volume returns and pricing returns on the ticket side that accompanied the investment we've made in that product. And I think you'll continue to see that as Fantasyland fully opens, and then as My Magic Plus is fully implemented, which Bob is going to speak to right now in terms of timing.



Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

The goal is for us to roll out My Magic Plus at some point this year. It's at various levels of beta testing right now. We want to be very careful that it is working absolutely right before we roll it out to the general public. There's no reason for us to rush it to market.

In terms of what we can expect from it return-wise, you're right; it's somewhat -- although we've modeled it -- it's somewhat difficult to be specific about. You can expect that it will create a better experience, and with that we believe people will spend more time at our parks and ultimately deliver more business per guest.

We also know that it will deliver some up-sell opportunities in terms of the array of products the basically digital technology will allow, and we also think it's going to give us somewhat of a competitive advantage. I think you have to look at all of those things. Basically new products to sell, better experience that should obviously keep people coming back for more or staying longer, and then the competitive advantage would be the way to do it. But I can't get specific with you, Doug, in terms of how to model that.

Doug Mitchelson — *Analyst, Deutsche Bank*

Perhaps then, Bob, just in terms of timeframe, would that be something where by fiscal 2014 you would think we start to see some impact?

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

Yes. I think -- well, I definitely believe we'll see some impact in fiscal 2014. That is certainly our plan. You were going to mention something --

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes, Doug, just in terms of how to think about this. We have known for a really long time that getting our visitors to Walt Disney World to make decisions about where they spend their time before they leave home is a powerful driver of visits per guest. When they get into the Orlando market and their time isn't yet planned, they can be subject to everything you see down there, which is a lot of in-city marketing for all the many products that people have put there to basically bleed off the feed that we fundamentally motivate.

So if we can get people to plan their vacation before they leave home, we know that we get more time with them. We get a bigger share of their wallet. So that's one thing for you guys to think about.



And the second thing is what happens to purchases when they become much more convenient, and you don't spend time queuing up for a transaction, queuing up to get in the park, and you actually have more time to enjoy the entertainment and, subsequently, spend more money doing things that -- other than standing in line, which, of course, you can't spend any money while you're doing that.

So those are the components. Bob spoke to the enhanced product and competitive advantages and so on, sort of on the more strategic level. But on components, to think about how to model that financially, you might think through some of those.

Doug Mitchelson – *Analyst, Deutsche Bank*

Thank you very much.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

Lowell Singer – *Senior Vice President, Investor Relations, The Walt Disney Company*

Operator, next question, please.

Operator

Next question is Jessica Reif Cohen with Bank of America Merrill Lynch.

Jessica Reif Cohen – *Analyst, Bank of America Merrill Lynch*

Thank you. I have one for Bob and one for Jay. Bob, I'll start with you. The company is obviously hitting on all cylinders, basically -- the parks; film, as you mentioned; and consumer products, cable networks, etc.

With the really strong multi-year outlook, there's one exception, which is the television business, meaning not just the broadcast network, but also your TV production is not at the levels of some of your peers. How much of a focus is it for you? And can you give us some specifics about what you're thinking about doing in terms of turning that around?

Bob Iger – *Chairman and Chief Executive Officer, The Walt Disney Company*

Well, I think the network and particularly in this quarter, the stations, too, have had somewhat of a tough run these last few months. Station business has been generally soft, by the way. And



even though our stations are performing well in their markets, and actually in some markets growing share nicely, the markets themselves are basically compressing or getting smaller, and that is obviously an issue.

On the network front we would like a stronger primetime schedule. Particularly one that is populated with more programming that we own. It's hard to look at that year over year in terms of the product that we own, because we tend to look more long-term at these investments than short-term.

So from a short-term perspective, you'd have to say that *Scandal* is certainly -- a program that we own -- has great potential in terms of delivering on our investment, but we would like more of them. So what you really end up doing there is you hope that your team in place, which is a great team, comes up with the kind of shows that not only drive higher ratings and more advertising revenue, but ultimately includes a number of shows that we own that drive more revenue in general.

That's basically -- there's no real secret to it, Jessica, as you know. You've been following us for a long time. But we could use a few more new hits, and certainly hits that we own. It's that simple.

Paul Lee is hard at work with his team on that, as you know, as we speak. I've seen the pilots. I'm reasonably encouraged by what I've seen -- actually, more than reasonably encouraged. I'm very encouraged by what I've seen and hopeful that the year ahead will deliver more value for us than the year prior.

Jessica Reif Cohen — *Analyst, Bank of America Merrill Lynch*

Okay, thanks. And then on the parks, for Jay. I have a couple of really short questions. But can you break out what percent of the costs are variable at this point, what your mix is of international and domestic visitors? Obviously spending has come down quite a bit, but if you could give us -- kind of update your thoughts on where margins -- you have said that you expect to get to peak margins at least in the US, which we can't see yet. How do you feel about margins kind of over the next few years?

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay, let me try to take a couple of those. So in terms of the international domestic mix, this quarter is the same exact mix as last quarter. I told you that in general, we run between 18% and 22%. We're at the low end in Q2 of that, but our strength has been from Brazil and the UK. A little bit of weakness from Canada in the second quarter.



But I would say there's not a big story there. Although we'd love to see our business from Brazil continue to grow; it's been a real driver for us. And it's nice to see growth back from the UK. You know, in past quarters a lot of our international attendance growth has been from Canada. So, anyway, I think the story there is within the range, and we are pretty happy with it. With the overall increase in volume, international has kept its pace.

In terms of margins, you know, the story there is going to be one of improving margins as we put behind us the launch costs and ramp up lower margins of new business initiatives that have been affecting us since we started on our big parks capital program. Sort of every quarter or every other quarter, we've been launching a business. There's been substantial preopening costs that are associated with those, of course, with no revenue. And even in the following quarter, when the revenue starts, it's usually not at full tilt.

So that should be contributing to our overall margins. We're pretty happy, frankly, with what we see in the base business margins. If you back out the things that we backed out, I think this has been a quarter that has evidenced very, very strong fundamental growth in margins in that business.

And even though there have been a lot of structural changes that have occurred since we used to talk about 20% margins, i.e. the consolidation of businesses overseas into the park segment that were not consolidated before; recognizing incentive comp in the parks margins, which was not done before. When you take those things out, we really do believe that we can get back on a steady-state basis to the kinds of margins we had pre-downturn.

So I think the story is good there. I'm sorry I can't give you a whole bunch more detail. In terms of the variable percentage, you know, it varies through the course of the year. Obviously you are in periods where more of a -- down periods in the year, when more of the costs are fixed. When you go through the holidays like New Year's and Easter, you have a much larger variable component. But I can't really give you too much more insight beyond that.

Jessica Reif Cohen – *Analyst, Bank of America Merrill Lynch*

Okay, thank you.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

Lowell Singer – *Senior Vice President, Investor Relations, The Walt Disney Company*

Operator, next question, please.



Operator

Alexia Quadrani, JPMorgan.

Alexia Quadrani – *Analyst, JP Morgan*

Thank you. Just staying on the parks for a minute. Given your experience at Cars Land and the real impressive attendance growth that has followed that opening, could you give us a bit of color on how we should think about Fantasyland renovation? How significant can it be in terms of driving growth going forward at Disney World?

And any sense of how much that might have already -- I know part of it already was renovated and opened, but a lot of it is still ahead of us. Any sense on sort of the timing when we might see sort of the marketing push behind or we might see more of a notable impact on that renovation?

Bob Iger – *Chairman and Chief Executive Officer, The Walt Disney Company*

Well, as you may or may not know, the Magic Kingdom park in Orlando is the number one park down there. It's actually the number one park in the world. And we hadn't really done much to Fantasyland in the many, many years since we opened.

So this was significant both from our perspective, but also from a guest perspective. The only thing I can tell you that may give you some sense is that the Magic Kingdom broke an all-time single-day record for attendance during the Easter holiday, and we believe that was a direct result of the investment that we made in Fantasyland.

Obviously the summer will tell us a lot more. We do know from a guest satisfaction perspective that the numbers that we're seeing from the Magic Kingdom, specifically from Fantasyland, are way up. We have more to open, as you cited Alexia, but what we've opened is really being well received.

Alexia Quadrani – *Analyst, JP Morgan*

And in terms of the expenses or sort of for the launch costs, I'm guessing it sort of is straight line as far as you open it? Or is there a bigger component of it that comes later on that we'll see a bit more of cost pressure around?



Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

I wouldn't expect to see significant cost pressure. Unlike -- when you think about the magnitude of Fantasyland, extraordinarily important for us to do that in the Magic Kingdom, because of all the reasons Bob just discussed. But if you look at the impact of that on the overall cost base at Walt Disney World, it is nothing like Disney's California Adventure expansion, which was substantive relative to the base of the Disneyland Resort.

So I wouldn't look very hard for a whole bunch of costs associated with its launch. And I think that you can see -- certainly in 2014 you will start to see reasonably good contribution from that. I wouldn't look for a cost degradation there.

Alexia Quadrani — *Analyst, JP Morgan*

Alright, thank you very much.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thanks, Alexia. Operator, next question, please.

Operator

Todd Juenger, Sanford Bernstein.

Todd Juenger — *Analyst, Bernstein*

Hi, good afternoon. I have just what is probably a handful of questions that are disguised as one question. So I'll just limit myself to that.

I'm interested in your international television business. So particularly as a network operator or other cases where you are a de facto operator by licensing large blocks of content, and really just interested in any commentary you'd share on how fast is that part of your business growing in both affiliate fees and advertising? How much is that contributing to your media segment growth of those line items? What are the margin trends? I told you this was several questions disguised as one. How big will that sort of be as we look out and it compounds over the next couple of years? And are there any opportunities for investment there, either organically or even through M&A, to increase that portion of your business? Thank you for indulging all that.



Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

I'm not sure that we can give you much detail, except to say that our international television business, which is largely Disney-branded -- Disney channels; Disney XD; Disney Junior, as I mentioned on my call, 166 countries. We do have, as you mentioned, we have program blocks that that we have licensed to third-party distributors in a variety of places in the world.

And obviously, we distribute the other content that the company owns, notably our movies and our TV shows. All of that has grown very nicely over the years, and we think that it will continue to grow.

We've also continued to make investments in new channels in new markets. So we will be launching a free over-the-air Disney Channel in Germany. We launched in Russia; we launched in Turkey. We're looking for some other opportunities there as well. But to give you some perspective on -- I just don't have the details in terms of a growth trajectory or what it looks like from a margin perspective.

We also look at it as brand-building opportunity, too. Because as I mentioned a number of times, the Disney Channel has become one of the most important drivers of, basically, brand value for the company. The impact that it has not only with the programs that it puts on, but essentially supporting all the other content that the company has, particularly our movies, is pretty substantial around the world. And there's value there that we don't necessarily put specifics against.

But it's been a great growth engine for the company, and we believe it will continue to be. Particularly, again, as some of these markets that we have only launched recently mature. Russia a good example of that.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes. I mean, what you're seeing right now in the numbers, Todd, are dilutive to our earnings in each of those. They're still all in the launch stage -- Germany, Turkey, Russia, and our Japan D-life project. We're still in investment mode in all of those new ones. And needless to say, we wouldn't invest in those if they're not going to turn around and be accretive to our earnings down the road. So, as Bob said, we can't get too much into the details of how the margins relate to our domestic business, but we are investing in growth in the international television business.

Todd Juenger — *Analyst, Bernstein*



Okay, I had to give it a try. I appreciate it. Can I just say, is it material to the affiliate fee growth rate, when we look at sort of low teens 10%-ish organic? Is the international contribution, which I assume those things are growing maybe faster than that -- it is it material? Or is it -- should we not even think about it as we think about how that grows over for years and pops up or aids the acceleration of that growth? And then I'll leave you alone. Thank you.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

It was not material in Q2, Todd.

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

But what I will say, I think what you can say just as you think of the future is we have been very, very aggressive over the last five years at launching new channels in many, many places. So I think while we'll continue to look for opportunities to launch new channels in new markets, as I mentioned, there will be fewer new launches in the future than there have been in the past five years. And obviously, as they mature and we move out of the investment phase and basically into the real growth phase, then you will start to see an impact on the bottom line, both from advertising and from affiliate fees.

Todd Juenger — *Analyst, Bernstein*

Fair enough. Thank you guys.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank you, Todd. Operator, next question, please.

Operator

Anthony DiClemente, Barclays.

Anthony DiClemente — *Analyst, Barclays*

Just one question, turning to ESPN and your sports franchises. I think if I have this correct, I think in the Spring of next year, your new MLB deal takes effect. And then in the Fall of 2014, your new NFL deal and presumably new SEC network agreement kicks in.

I want to ask about the NBA deal, which you share with TNT. Is that -- I think goes until 2015 and 2016. And I'm just wondering how core the NBA is to your sports franchises? There are other national sports networks out there. Fox Sports, one; NBC Sports. They will presumably be



hungry for sports content when that deal comes up. So I just want to get your thoughts on that. And the other question there is, do your current affiliate renewals with the MSOs contemplate a renewal of your NBA deal in those contracts? Thank you.

Bob Iger – *Chairman and Chief Executive Officer, The Walt Disney Company*

The NBA deal that we currently have goes through 2016. So you're off a little bit, Anthony, in your timing there. If you look at ESPN, they have locked down rights, other than to the NBA, to virtually every other important sports franchise that they have for a long time. They've also concluded a number of very long-term affiliate agreements.

So if you think about our businesses going forward, there is probably more certainty as it relates to ESPN than almost any other business that we're in, which I think generally speaking is a good thing. Now there are some opportunities to buy some other events, and we obviously have the NBA, which is important programming to us coming up.

And we have a few new affiliate deals to do, but not many. But I think generally speaking, ESPN is in great shape. As we look at the timing of when new contracts kick in, as you mentioned, Major League Baseball and the SEC, we don't look at it in a vacuum. We look at it against the timing of when new distribution deals kick in.

As we talked about it I think more in the last quarter as it related to Comcast and new rates, as a for instance. So we think that ESPN's future in terms of its growth trajectory is actually quite good, and we know a lot about what it is likely to be. And I can't comment as to whether there are affiliate deals that are in any way tied to a renewal of the NBA.

Lowell Singer – *Senior Vice President, Investor Relations, The Walt Disney Company*

Ok. Thanks, Anthony. Operator, next question, please.

Operator

David Bank, RBC Capital Markets.

David Bank – *Analyst, RBC Capital*

Thanks very much. Two questions. The first is, Bob, can you talk about as viewership of premium video over time, both ESPN and ABC, migrates incrementally over, kind of online, how do you view the optimal monetization for ad inventory on kind of a Nielsen OCR demo sold basis versus sort of a gross impression? How do you think that inventory is maximized most, and why?



And then, second, as you think about rolling out the FastPass Plus and all of those new technological elements, do you think it's a better strategy to kind of bifurcate them by offering them to resort guests or something only at first to drive higher occupancy? Or do you go wide for everybody with that stuff? Thanks very much.

Bob Iger – *Chairman and Chief Executive Officer, The Walt Disney Company*

I'll answer the second question, because it's easier to answer. We have for years had in place products that are available only to hotel guests. And actually, one thing that I think Jay alluded to, didn't say specifically, is the My Magic Plus will definitely encourage people to stay more on-property than off-property. Jay was talking about essentially by being able to plan ahead, people will basically have more plans with us, and that will in effect discourage them from doing other things. I think it will also encourage them to stay more in our hotels. And so I think you have to look at that as an additional value to My Magic Plus.

I'm not 100% sure I understand your question, the first part, but let me give it a shot. I don't know that you're going to see more viewing -- migrating online, necessarily. I think you'll see more online viewing of product, both scripted traditional entertainment and sports. We look at that as essentially a real opportunity, because we think we are giving consumers, particularly consumers who have already bought the basic -- or the expanded basic bundle an opportunity to choose the screen that makes most sense for us.

What we obviously need to happen at the same time is we need for either Nielsen or some measurement system to kick in that adequately compensates us for the increased consumption on new devices. What we have done is we've created selling tools and a selling structure across our businesses -- including at the network, by the way -- that is essentially kind of selling to -- in fact, we're already talking as it relates to ABC and the upfront, selling packages to advertisers that go across all media, which we've been doing for a while at ESPN and we're doing much more aggressively at ABC and the other networks.

We think that will also add value. But I think the key is for us to get a measurement system in place that enables us to monetize, because I'm convinced that there's a lot of consumption going on there.

David Bank – *Analyst, RBC Capital*

Thank you very much.

Lowell Singer – *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank you, David. Operator, next question, please.



Operator

Alan Gould, Evercore Partners.

Alan Gould – *Analyst, Evercore Partners*

Thank you. A couple of park-related questions. They're quick, though. When could you conceivably get the rights back to the Marvel characters and attractions at the parks? Second, could you give us the international park revenue and operating income, which I think comes in the Q? And then, thirdly, the Interactive division. Do you still think it will hit breakeven with the pushback of Infinity to till August?

Bob Iger – *Chairman and Chief Executive Officer, The Walt Disney Company*

The last question -- with the pushback of Infinity to August, it's doubtful that [we're] going to get breakeven this year because of when Infinity will street, which is essentially in our fourth quarter. So it essentially pushes that back.

We believe in Infinity. It's actually been very well received by the gaming community and by consumers. And we're pleased with what we see in the product. That also -- retail has had really great buy-in for it, as well. So we think it will be a great product and it's going to help drive profitability for fiscal 2014. But by pushing it back, it's going to make it harder to achieve profitability or breakeven this year at that division, even though the division will deliver results this year that are substantially improved from last year.

Had Infinity not pushed back and Infinity done what we expect it will do, then achieving breakeven this year was very, very doable.

I can't really say much about Marvel right to the parks other than to say the rights to the Marvel properties, particularly in Florida, are not ours at this point. And I'm not going to even speculate as to not only when we'll get them back, but whether we'll ever get them back. We have plenty of opportunity, though, for Marvel in our parks, and we're hard at work developing Marvel presence, particularly in our international parks, notably in Hong Kong.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Alan, in terms of the revenue of our international parks, it will be -- it was \$543 million this quarter. We saw growth in Paris and Hong Kong, as I mentioned. Because in the prior quarter we had business interruption insurance payments in Tokyo, our revenue there was down a little bit. But the fundamentals at Tokyo Disney Resort are quite strong.



Alan Gould — *Analyst, Evercore Partners*

And the operating income for the international parks, Jay?

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

We'll wait for the Q for that number.

Alan Gould — *Analyst, Evercore Partners*

Okay, thank you.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Thank, Alan. Operator, next question, please.

Operator

Michael Senno, Credit Suisse.

Michael Senno — *Analyst, Credit Suisse*

Good afternoon. Just wondering if you guys could quantify, as you have done in the past, the margin impact at parks from new initiatives in this quarter, and if we could expect to see that continue to decelerate as the year goes on? And then second question, just in regard to the strong per-cap spending. I understand that there were ticket price increases, but it seemed to accelerate this quarter, and I just wanted to see if there are any other particular drivers you are seeing at the parks that are resulting in that? Thanks.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay. On the margin impact on new initiatives. So they're a little lumpy. This quarter they happened to be marginally accretive to the overall margins, but just modestly, to be honest with you. As I said, they are lumpy, and I think next year as everything moves into fuller stride, you'll start to see those be more positive drivers to margins.

Your second question on spending for the quarter across categories -- of course our caps were helped by the holiday business that Bob mentioned, particularly Easter, but there was nothing unusual about any of the categories. They were all up across the board.



Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Ok, thank you Michael. Operator, next question, please?

Operator

David Miller, B. Riley & Co.

David Miller, — *Analyst, B. Riley Caris*

Hey guys, good call being in New York, because it's raining here in Los Angeles. Jay, just following up on -- I think it was Ben Swinburne's question, I think the third question in.

Going back to my -- I have followed you guys for a long time, and I'm going back to my models here actually in the spreadsheet all the way back to 2001, and I don't see any example of a Q2, which is your March quarter -- usually your weakest quarter, ironically enough, for the parks -- where your margins for this high, 11.6%. I know what you're going to say. You're going to talk about the timing shift; you're going to talk about the demand curve moving to the right.

I believe there were some Phase III shutdown sequences that occurred in late March. But was there anything else going on on costs that you're willing to elaborate on? Because these are truly outstanding margins, and I believe -- correct me if I'm wrong -- a record for Q2. And then within that, do you guys still have a fuel hedge for the boats, or has that been unwound? Thanks very much.

Bob Iger — *Chairman and Chief Executive Officer, The Walt Disney Company*

You know, David, Jay mentioned that obviously some of the impact in Q2 at the parks, both on the margin side and on the bottom line, had to do with the shift in timing of both Christmas and Easter. But let's call it what it was. It was a great quarter for the parks -- a great quarter.

There was nothing on the expense side to really note in this case. Continued diligence in that regard for the parks. I think they've done a good job of managing their expenses, particularly when they've continued to invest to grow.

But this was a quarter that I think stood out because the product that we recently put online really worked, like California Adventure, and Fantasyland, and the ships, as we talked about. And the product that we have had online for years and years has, has I think in many respects, just never looked better to the consumer. And in an economy that is I think seeing some slight improvement, you get results like results that we got.



I think it bodes very well for our future. As we mentioned earlier, there will be a little lumpiness in terms of margin expansion. The cost, for instance, of the My Magic Plus you'll see in the next quarter, as a for instance. A little bit more on Fantasyland. But generally speaking, we have a great parks story to tell.

Just as an aside, and we've talked a lot about California Adventure. Before we redid California Adventure, at a typical day at the Disneyland Resort, you would see about 75% of attendance going to Disneyland and 25% going to California Adventure. That's now in most days more like 55%/45%.

That's an incredible change. And it enables us to drive real bottom-line growth, because you have got a better experience at Disneyland. We are getting pricing out of California Adventure that is substantially above what we were able to drive before. We have increased food and merch spending there, as a for instance. That obviously contributes nicely to the margins. I think -- I'm not sure there's any other way to categorize or characterize the quarter for the company in Parks and Resorts except to say it was a tremendous quarter.

David Miller, — *Analyst, B. Riley Caris*

Fair enough. Thank you very much.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

On your fuel hedging question, we generally hedge our fuel out of Port Canaveral. It accounts for about a third of what we will be using in terms of fuel for the cruise line this year.

David Miller, — *Analyst, B. Riley Caris*

Thank you.

Lowell Singer — *Senior Vice President, Investor Relations, The Walt Disney Company*

Operator, we have time for one more question.

Operator

Jason Bazinet, Citi.



Jason Bazinet – Analyst, Citigroup

I just have a question for Mr. Iger. One of the things that always struck me as unusual about your financials on a trailing basis is how much of the growth came from media nets relative to the other divisions, even though if you asked a man on the street what they thought of Disney, they wouldn't necessarily think of ESPN.

Now that you've sort of made all of the investments in parks and made all of the investments in IP, are we just in harvest mode now, and the investments that you've made you're just going to sort of execute and let the strategy play out? Is that the right way to think about it, or is there another pivot that you see sort of on the horizon over the next three years?

Bob Iger – Chairman and Chief Executive Officer, The Walt Disney Company

That's a bit of a tricky question there, Jason. I don't want to in any way say there's something big afoot when I answer your question by saying we're never in harvest mode, per se. There are always opportunities to harvest what we've invested in, but we're in extremely dynamic businesses in a very dynamic global marketplace, and there are always going to be opportunities for us, particularly given the strength of these assets: ESPN, Disney, Pixar, Marvel, and Star Wars. There are going to always be opportunities for us to invest in those to grow in a marketplace that generally is pretty robust.

So we talked about the fact that we believe we'll be able to grow free cash flow nicely. I guess in a way that is a form of harvesting. But I get a little bit concerned about using the word harvest, because sometimes it suggests a status quo approach. And I don't think status quo in as dynamic a marketplace as we operate in is a good strategy.

Jason Bazinet – Analyst, Citigroup

Well let me recast it. Is it fair to say that the Lucas acquisition was the capstone of a fairly significant strategic pivot for the firm?

Bob Iger – Chairman and Chief Executive Officer, The Walt Disney Company

I've said it before, it's kind of -- if you're asking me today as we look ahead at whether there's a Pixar, a Lucas, a Marvel on the horizon, I have to say, not likely. We just don't see it. But that doesn't mean one isn't going to crop up and that we won't act opportunistically, as we did on those three, to take advantage of it if we see an acquisition that we believe is going to really deliver long-term value and growth for our shareholders.

We feel really good about Pixar. We feel great about Marvel. Not just because of this week, although we have to admit that it certainly helped. But when we look ahead at what Marvel has



got in the pipeline and the opportunity to monetize those properties not only across our businesses but across the world -- obviously significant.

We feel great about Lucas. It's been very well received. As we look at Lucas, the more we get into it, the more we realize that we've got a property in our hands that is probably more loved and more well-known than almost anything else that we have, which is remarkable. It's remarkable that it was even available for us to buy.

I don't want to say never, meaning that there is -- never again, there isn't one out there. It's just much more difficult as we look ahead to cite one. I certainly wouldn't be able to mention it to you on this call. I will say that on the Marvel and the -- to give you maybe a little more perspective -- on the Marvel and the Star Wars or the Lucasfilm acquisitions, those appeared on, I'll call it, internal lists of things that we thought might make real sense for this company and its shareholders for quite a long time.

We looked at them very carefully. That list is shorter today than it used to be.

Jason Bazinet – *Analyst, Citigroup*

That's very helpful. Thank you very much.

Lowell Singer – *Senior Vice President, Investor Relations, The Walt Disney Company*

Thanks, Jason. Thanks again, everyone, for joining us today.

Note that a reconciliation of non-GAAP measures that were referred to on this call to equivalent GAAP measures can be found on our website. Let me also remind you that certain statements on this call may constitute forward-looking statements under the securities laws. We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them, and we do not undertake any obligation to update these statements.

Forward-looking statements are subject to a number of risks and uncertainties, and actual results may differ materially from the results expressed or implied in light of a variety of factors, including factors contained in our annual report on Form 10-K and in our other filings with the Securities and Exchange Commission. This concludes today's call. Have a good night, everyone.

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Forward-Looking Statements:

Management believes certain statements in this call may constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are made on the basis of management’s views and assumptions regarding future events and business performance as of the time the statements are made. Management does not undertake any obligation to update these statements. Actual results may differ materially from those expressed or implied. Such differences may result from actions taken by the Company, including restructuring or strategic initiatives (including capital investments or asset acquisitions or dispositions), as well as from developments beyond the Company’s control, including:

- adverse weather conditions or natural disasters;
- health concerns;
- international, political, or military developments;
- technological developments; and
- changes in domestic and global economic conditions, competitive conditions and consumer preferences.

Such developments may affect travel and leisure businesses generally and may, among other things, affect:

- the performance of the Company’s theatrical and home entertainment releases;
- the advertising market for broadcast and cable television programming;
- expenses of providing medical and pension benefits;
- demand for our products; and
- performance of some or all company businesses either directly or through their impact on those who distribute our products.

Additional factors are set forth in the Company’s Annual Report on Form 10-K for the year ended September 29, 2012 and in subsequent reports on Form 10-Q under Item 1A, “Risk Factors”.

Reconciliations of non-GAAP measures to closest equivalent GAAP measures can be found at www.disney.com/investors.