



The
WALT DISNEY
Company

Q2 FY19 Earnings Conference Call

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Disney Speakers:

Bob Iger

Chairman and Chief Executive Officer

Christine McCarthy

Senior Executive Vice President and Chief Financial Officer

Moderated by,

Lowell Singer

Senior Vice President, Investor Relations

**PRESENTATION**

Operator

Good day, ladies and gentlemen, and welcome to the Walt Disney Fiscal 2019 Second Quarter Financial Results Conference Call. (Operator Instructions)

As a reminder, this conference call is being recorded. I would now like to introduce your host for today's conference, Lowell Singer, Senior Vice President, Investor Relations. Sir, please go ahead.

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

Good afternoon, and welcome to The Walt Disney Company's Second Quarter 2019 Earnings Call. Our press release was issued about 25 minutes ago, and it's available on our website at www.disney.com/investors. Today's call is being webcast and a transcript will also be available on our website. Joining me for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer and Christine McCarthy, Senior Executive Vice President and Chief Financial Officer. Bob will lead off followed by Christine, and we will then be happy to take your questions. So with that, I will turn the call over to Bob, and we'll get started.

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

Thanks, Lowell and good afternoon, everyone.

We're pleased with our results in Q2, which were impacted by our acquisition of 21st Century Fox in late March as well as our ongoing investment in our direct-to-consumer business....But, I'd like to start by mentioning the phenomenal success of *Avengers: Endgame*, which continues to exceed even our highest expectations.



After delivering the biggest opening of all time, the movie has generated almost \$2.3 billion in worldwide box office to date...making it the second highest grossing film of all time...after just two weeks in theaters.

We've also been extremely pleased with the reaction to our Investor Day presentation – which offered an in-depth look at our DTC plans, including additional information regarding ESPN+ and Hulu as well as a detailed look at the content, interface and pricing for Disney+. And, I'm happy to announce that *Avengers: Endgame* will be available on Disney+ on December 11th, just a month after we launch the service.

While the initial response to our DTC efforts has been gratifying, we're not taking anything for granted and we continue to leverage our creative engines across our company to ensure we deliver a strong value proposition to consumers. We're expanding into the DTC arena with tremendous excitement and optimism -- confident that the indelible connection we've built with billions of people over a century of great storytelling gives us an advantage in the marketplace and provides a strong foundation for success.

This is the first earnings call since our 21st Century Fox acquisition closed, and I'd like to give you a quick summary of our integration and consolidation efforts across the company.

From the beginning, we analyzed this acquisition through the lens of our new strategy. When we first considered the deal, we had just announced our DTC initiative, and we saw tremendous value in the Fox assets in terms of expanding our ambitions and enhancing our potential for success and as you saw on Investor Day, we're already moving forward in that regard.

In addition to Fox's tremendous wealth of content, we now have a deep bench of experienced industry leaders across the entire company, a veritable all-star team of proven management talent who have embraced The Walt Disney Company's strategy and are working in concert to execute it.



In our media business, the senior leadership from Fox are now in place including Peter Rice, who's running The Walt Disney Television Group and Dana Walden, who's running our television studios as well as managing the ABC network and owned stations. John Landgraf at FX is looking for opportunities to increase the production capacity at FX to support our DTC businesses, Uday Shankar is running all of our non-parks businesses in India and Asia Pacific and Jan Koeppen is head of our media and DTC businesses in EMEA.

Last week we elevated Alan Bergman to co-chair of our Studio Entertainment group and he and Alan Horn are focused on integrating and managing the combined studio businesses. Emma Watts from 20th Century Fox is now part of their senior leadership team, focused on making movies for theatrical release as well as for our DTC platforms including tent-pole titles such as *Ford vs. Ferrari*, James Cameron's next *Avatar* films, and Steven Spielberg's *West Side Story*. And Fox Searchlight, run by Nancy Utley and Steve Gilula, is another great creative engine that has defined itself with unique, high quality films.

The further we get into the integration process the more impressed we are with the value of the assets, the quality of the talent, and the opportunities we're able to create. National Geographic is a prime example. We're already working with National Geographic to explore the brand's potential across the company, from creating content for our DTC business to eco-travel adventures and merchandise for our Parks, Experiences, and Products business. There's a strong alignment with our ongoing environmental and conservation efforts as well.

Looking forward, we've got a very busy year ahead including a number of major developments in Parks and Resorts. We're breaking ground on a significant expansion in Tokyo DisneySea on the 21st, which will add new themed areas and attractions to that park. And we're looking forward to the grand opening of *Star Wars: Galaxy's Edge* in our Disneyland Resort on May 31st. The excitement around this new land is unbelievable, and it will only grow once people have a chance to experience it for themselves. As we've said, it's the largest land we've ever built but



the sheer audacity of the creativity and technology is even more impressive than the size. Disney World is getting its own Galaxy's Edge on August 29th.

Turning to our Studio, our incredible film slate for 2019 is now even more ambitious as a result of our 21st Century Fox acquisition. The movies we'll release between now and Christmas include: *Aladdin*, *The Lion King* and *Maleficent: Mistress of Evil* from Disney, Pixar's *Toy Story 4*, *Frozen 2* from Disney Animation and *Star Wars: The Rise of Skywalker* as well as *Dark Phoenix*, *Stuber*, *The Art of Racing in the Rain*, *Ready or Not*, *Ad Astra*, *Woman In the Window*, *Ford Vs. Ferrari*, and *Spies in Disguise* from the Fox Studios.

Needless to say, this is clearly an exciting time for our entire company.

I'm now going to turn the call over to Christine to talk about our quarter, and then we'll take your questions. Christine?

Christine McCarthy – Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company

Thanks Bob, and good afternoon everyone. Excluding certain items affecting comparability, earnings per share for the second quarter were \$1.61. As you know, we closed the acquisition of 21st Century Fox on March 20th, so our Q2 results reflect the consolidation of the Fox assets, including the impact of consolidating Hulu, for the last 11 days of the quarter. Results for 21st Century Fox for the 11 days, which we are reporting as a separate segment, reflect a contribution of 373 million dollars in revenue and 25 million in operating income. We recorded 105 million dollars in purchase price amortization in Q2, which is not included in these results.

At Studio Entertainment, lower worldwide theatrical and home entertainment results were partially offset by higher TV/SVOD distribution results. As we discussed last quarter, we expected the Studio's results this quarter to face a tough comparison given that Q2 last year was the best second quarter in the Studio's history. We were pleased with our worldwide theatrical results in the quarter, especially the strong performance of *Captain Marvel*, however



the year-over-year comparison reflects the outstanding performance of *Black Panther* and the carryover performance of *Star Wars: The Last Jedi* and *Coco* last year. Our home entertainment business also faced a difficult comparison given Q2 titles last year, which included *Star Wars: The Last Jedi*, *Thor: Ragnarok* and *Coco*. In total, our worldwide theatrical and home entertainment results came in modestly better than our previous outlook due primarily to the stronger than anticipated performance from *Captain Marvel*.

At Parks, Experiences and Products, operating income growth was driven by higher results at our theme parks and resorts and cruise line businesses, and growth at Consumer Products. Second quarter Parks and Resorts results reflect an adverse OI impact of about 45 million dollars due to the timing of the Easter holiday period as both weeks of the holiday period fell entirely in Q3 this year, whereas last year one week of the holiday period fell in Q2.

Despite this headwind, we continued to deliver solid growth at our domestic parks and resorts business. In the second quarter, higher operating income was driven by increased guest spending and attendance at the parks and higher occupied room nights at the hotels, partially offset by higher costs.

Attendance at our domestic parks was up 1% in the second quarter and per capita spending was up 4% on higher admissions and food and beverage spending. Per room spending at our domestic hotels was up 1% and occupancy was up three percentage points to 93%. So far this quarter, domestic resort reservations are pacing up 3% compared to prior year, while booked rates are up 2%.

Growth at Disney Cruise Line reflects the impact of a 14-day dry dock of the *Disney Magic* during Q2 last year and higher average ticket prices in Q2 this year. Results at our international operations were higher in the second quarter due primarily to growth at Hong Kong Disneyland Resort.



At Consumer Products, growth in operating income was due to higher results in our games businesses, which benefited from the sale of rights to a video game and the release of a licensed title, *Kingdom Hearts III*. These results were partially offset by a decrease in our merchandise licensing business driven by lower minimum guarantee revenue due to the adoption of the new revenue recognition standard, partially offset by a favorable foreign exchange impact.

Total segment operating income margin was up about 220 basis points compared to Q2 last year. We estimate the timing of the Easter holiday period had an adverse impact on the year-over-year change in operating margin of about 60 basis points. Margins at our domestic Parks and Experiences businesses were up about 140 basis points and were adversely impacted by about 80 basis points due to the timing of the Easter holiday period.

At Media Networks, operating income was modestly lower in the second quarter as a decline in Broadcasting more than offset growth at Cable.

Total Media Networks affiliate revenue was up 4% in the quarter due to growth at both Cable and Broadcasting. The increase in affiliate revenue was driven by seven points of growth due to higher rates, partially offset by a little less than a two-point decline due to a decrease in subscribers, and a one point decline due to the adoption of the new revenue recognition standard.

At Broadcasting, operating income was lower in the quarter as growth in affiliate revenue was more than offset by higher programming costs, lower program sales and a 3% decline in advertising revenue. Quarter-to-date, primetime scatter pricing at the ABC Network is running about 40% above upfront levels. Program sales were lower in the quarter, though they came in better than expected since we were able to recognize the sale of season three of *Jessica Jones* in the quarter.



Domestic Cable results were up in the quarter as higher operating income at ESPN and, to a lesser extent the Disney Channel, were partially offset by a decline at Freeform.

At ESPN, operating income was higher in the second quarter as higher affiliate revenue more than offset higher programming and production costs and lower advertising revenue.

ESPN's programming and production costs were higher in the quarter as lower programming costs due to the timing shift of the College Football semi-final games were more than offset by contractual rate and production cost increases for key sports programming. ESPN aired three of the New Year's six bowl games during the second quarter, similar to last year, however this year the two semi-final games aired during the first quarter.

ESPN's domestic linear advertising revenue was down about 2% in the second quarter, though we estimate it was up mid-to-high single digits when adjusted for the adverse impact of the shift in the timing of the College Football semi-final games. So far this quarter, ESPN's domestic cash ad sales are pacing up compared to last year, driven, in part, by scatter CPMs that are up nicely above upfront levels.

Turning to Direct-to-Consumer and International, growth at our international channels, which was due to higher affiliate rates and lower sports programming costs, was more than offset by lower results from our Direct-to-Consumer businesses, which reflect ongoing investment at ESPN+ and Disney+, and losses from the consolidation of Hulu.

Last quarter I told you we expected the continued ramp up of ESPN+ and ongoing development of our Disney+ service to have an adverse impact on the year-over-year change in operating income for the second quarter of about 200 million dollars, with about two-thirds of that attributable to ESPN+. The actual number came in a little better than the guidance we provided last quarter driven by timing of expenses.



As we look to the third quarter, we expect operating income from our direct-to-consumer businesses to reflect full consolidation of Hulu's results, the continued ramp up of ESPN+, and ongoing investment in Disney+. As such, we expect our direct-to-consumer businesses to have an adverse impact on the year-over-year change in segment operating income of about 460 million dollars.

Overall, we estimate the acquisition of 21st Century Fox to have a dilutive impact on our Q3 earnings per share, before purchase accounting, of about 35 cents. Additionally, we expect about 900 million dollars in purchase accounting charges related to the amortization of intangible assets and the step-up on film and TV assets, which we estimate will impact third quarter GAAP reported earnings per share by about 37 cents.

We expect these purchase accounting charges to total approximately 1.8 billion dollars for fiscal 2019. And as you can see in our reporting of this quarter's results, we are reporting the impact of purchase accounting outside of individual segment results.

I'll now turn the call over to Lowell and we'd be more than happy to take your questions.

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

Okay, Christine, thank you. Operator, we are ready for the first question.

Operator

Our first question comes from Ben Swinburne with Morgan Stanley. Your line is open.

Ben Swinburne – *Morgan Stanley*

Bob, I want to ask you about -- actually Bob and Christine-- about Fox, now that it's closed and the streaming Investor Day is behind us. Bob, can you put this acquisition into context? When



you look at the deals you've done in the past, you've talked a lot about acquiring powerful brands like Pixar, Lucas and Marvel and obviously, we've seen the success there. This is just a little bit different transaction but I'd love to hear from you now that you own the business, what you think the biggest opportunity is running this company and integrating it into Disney or opportunities as you look forward, so we can think about where opportunities and upside might exist. And sort of a similar question, Christine, to you, on both synergies and the balance sheet, which are two areas you've talked about. Now that you own the business, can you update us on your thoughts on synergy timing and any opportunities you see on the debt side, too?

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

Thanks, Ben. To give you some perspective, in the summer of 2017, I think it was during our August earnings call, we announced our intention to purchase the controlling interest in BAMTech and to launch Disney and ESPN direct-to-consumer services. Soon after that, Rupert and I first started engaging in conversation about the possibility of buying 21st Century Fox assets. So that when we began analyzing their value, it was all through the lens of the launch of direct-to-consumer platforms. And we were able to, in analyzing value, really think hard about how we might use our leverage in both the content we are buying -- I'm talking about library, the brands we are buying and the titles -- but also the people at Fox, which is critical to essentially enable us to fulfill our goals as it relates to direct-to-consumer.

I think if you then just resolve almost all the way forward to our Investor Day and think about the fact that Uday Shankar was on stage talking about direct-to-consumer service in India, which is beyond even what we're imagining back in '17, and the fact that National Geographic was well represented, the fact that we announced *The Simpsons* deal, just a few examples -- You can, I think immediately conclude that the vision that we had which is to analyze value through that lens was basically being implemented or showing potential right away.

I can't emphasize enough the importance of people, too. Because as I think we all know, these are ambitious plans, both in terms of managing the technology side and the interface with



consumers, but in particular, ambitious plans when it comes to the creation of our original content. And whether you're looking at the movies-side or the TV-side -- although in the direct-to-consumer front the television-side probably takes the front seat -- we need great people to create all the programming and to supervise all of the talent that will be needed to serve consumers well on these platforms. And what we got -- which was in my prepared remarks earlier -- what we got in this acquisition upfront is just amazing. And so I feel really confident in the plans that we've announced and our ability to execute them, because of what we bought. It's kind of that simple.

I know as I compare these to the Marvel, Pixar and Star Wars acquisitions, there are great similarities and there's some dissimilarities. I'd say Pixar, Marvel and Star Wars were probably more brand-focused, although in Pixar's case, it came with a solution to basically address the problems we'd been having at Disney Animation. Marvel and Star Wars were brands; they're both about people as well, franchises, long-term value. Here we get a little bit of everything. We get some really strong brands, Nat Geo, *Simpsons*, good examples of that, but we also have brands that we can even strengthen by fueling them with more resources to create more product using those brands and to put them front and center of our new platforms. I've talked about a lot of them in the past. And in all cases, I said we got great people. That's very, very evident to us today. And also the other thing that's evident is how quickly we've been able to integrate not only the assets, but the people into our plans. I'd say if I'm pleasantly surprised, the thing I'm most surprised about in a positive sense is how quickly we put people in significant positions of leadership in the company that can not only help manage our businesses today, but manage our businesses into the future.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

So Ben, let me address your questions on synergy and the balance sheet. First of all, in synergy, we're still on track to deliver at least \$2 billion in cost synergies related to the acquisition. We told you initially that you should expect us to realize about half of those benefits by the first full year and the remainder in the second full year. And once again, the \$2 billion in cost synergies



never included anything from the RSNs, so that's immaterial to us achieving this \$2 billion going forward. The other thing I've mentioned, and you'll see it in the press release with more disclosure in the Q, you saw some charges taken for restructuring. That number was \$662 million; we'll continue to take those charges as we continue to achieve those synergies, and you'll be able to follow it quarter-by-quarter.

On the balance sheet side, we did significantly increase our debt portfolio. At the close, we had about \$18 billion of long-term debt. And with the increment of debt and related positions coming from other entities, the balance of the debt portfolio went up to about \$52 billion. That's a number that our treasury group has been managing, too. We did some bond exchanges leading up to the close of the acquisition. So we're aggressively managing that portfolio in the same manner in which we have always managed the balance of short-term and long-term liquidity, and the way we positioned the balance sheet.

You're probably also curious about leverage, and we have not recommenced any share buybacks, because we said we would not be doing that until our leverage ratios came back in line with that of a single A company. So for the time being, you can assume that our share repurchases will be suspended.

Ben Swinburne – *Morgan Stanley*

Thank you both.

Operator

Our next question comes from Jessica Reif Ehrlich from Bank of America Merrill Lynch. Your line is open.



Jessica Reif Ehrlich – *Bank of America Merrill Lynch*

Just returning to the Parks. It seems like there's so many drivers right now especially in front of the Star Wars Lands, plural, openings. So can you give us a color on how you're thinking about pricing, particularly given the past year's price increase -- which had no negative impact that we can see on attendance; the timing of the second major attraction at the Star Wars Lands; and maybe some insight how you're thinking about expanding in China over time? I know attendance has been weak recently.

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

Okay. Multifaceted question. On the first question, on the parks, I'll start with pricing. We have been very strategic in our approach to pricing over the last number of years, and it's really paying off. The results this quarter is certainly evidence of that. And what we're trying to do basically is two things: to price according to demand and in managing demand, try to basically spread out attendance so that we can preserve or improve the guest experience. It's that simple.

The popularity of what we've been building, which I think is tied to both the quality and the scale of what we've been building, but also the fact that we've been building attractions in lands and shows, et cetera, that are tied to some of our best stories and our franchises, I think has created an even greater demand and more popularity, which gives us more flexibility on the pricing side. But it's not just about raising prices; it's about being really smart about it, and it's showing.

We have, as you know, Jessica, a tremendous amount of expansion going on. Star Wars Lands is only one of them - and there are 2 of them, I should say. We're breaking ground on a big project in Tokyo just in 1.5 weeks, for instance. We're building cruise ships, and we've got expansion just about every place that we operate. Specifically in China, where business actually has been quite good lately, we have announced that we're expanding with the *Zootopia* Land. I don't



believe we've announced the date for that yet, but we're continuing to look at expansion. And right now, our plans for expansion there are solely focused on Shanghai. We've not talked about building at another location at this point.

By the way, going back to Galaxy's Edge and Star Wars, the lands which are attractions to themselves have 2 E-ticket attractions. One is the Millennium Falcon experience or ride that I've tried a number of times, and it's fantastic. We're opening with that. The second attraction will open later in the year, but we've not said when. And as I mentioned on my call, the Star Wars Lands or Galaxy's Edge will open in Orlando at the end of August. Did I cover all the aspects of that question?

Jessica Reif Ehrlich – *Bank of America Merrill Lynch*

Yes.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Jessica, I would just add one thing on margins. Since I have been in this role, I think any time a question came up about the growth in the parks margins, it was usually asked in the vein of can this margin improvement continue. And I just want to say that while we don't give any guidance on margins, there's nothing structural that would prevent our margins growing from here. And as Bob articulated, the yield strategy is something that benefits the parks on multiple levels, spreading the demand, improving the guest experience and also driving to the bottom line. We also see further potential for improvement in our international parks businesses and are also managing our cost base effectively by deploying capital and labor efficiently. So I don't think there's a constraint right now that we believe on our parks margins.

Operator

Our next question comes from Alexia Quadrani with JP Morgan.



Alexia Quadrani – *JP Morgan Chase & Co.*

On the studio side, after the fantastic *Endgame*, it's kind of hard to match and there's more to come from Marvel, but I'm sure there is. I guess when do you think you can get an update on the longer term slate there? And then a follow-up question staying on the studio. How much opportunity do you think there is on the film side of Fox, taking their IP and refining it further over the years to the success level more in line with Disney's historical portfolio.

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

In announcing our new slate, I think we announced the 2 or 3, maybe 3 new Marvel titles but didn't say what they were -- Marvel dates rather, but without the titles. We obviously know what they are and there's a lot of speculation online. So Alexia, if you go online you may be able to get some of the answers, but Marvel didn't give me permission to announce it today because they want to announce it. I'm guessing they're going to do so later this summer. If you watched, and I hope you did, *Avengers: Endgame*, there were a lot of clues in that film as to the movies that may be coming. But I'm not at liberty to help you with those either. I guess I'm just a Marvel guy when it comes to protecting their secrets.

There are huge opportunities. We bought Marvel, we started studying their characters, and we got to about 8,000 and we stopped. But there are many, many different directions that we can go. We've obviously laid a lot of pipe in terms of characters and character stories -- even though we came to an end on some of them in this film, there are more possibilities certainly beyond it. And then, of course, on the television side, as we announced when we had our Disney+ presentation, Marvel is going to be making a series for Loki. We're doing *Falcon and Winter Soldier*, we're doing one with Wanda and Vision. And all of these are intricately linked and tied to the storytelling in the films. And so we're now looking at basically telling Marvel stories and being somewhat platform-agnostic. We'll make big films for the obvious reasons, but those films will also live on the Disney+ platform in the stories we tell, in the series that we create. And no one's really doing that right now.



As it relates to Fox, there are a number of different opportunities. Clearly, there are library titles that were never going to be made as sequels or as remakes for theatrical distribution, that we're going to look at for a possible production inclusion in Disney+. But there's also sort of richness of development and storytelling for theatrical release using the Fox brand, and Emma Watts is reporting to Alan Bergman and Alan Horn as we're working to develop those. We inherited a slate of films that are being made, we're bringing them to the system, and we're now working with her to basically determine the slate beyond what's been announced. I'm guessing that it'll be somewhere in the neighborhood of 5 or 6 films a year. But we're not locking ourselves into that, from that end and of course, we have Searchlight, which is going to continue their business as is.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Alexia, before you go, I just want to add one thing on *Avengers: Endgame*. And I said a very similar thing a year ago as it related to *Avengers: Infinity War*. Given the size of the cast involved and anyone who's seen it knows that the cast was extremely large and the cost to produce a film of that scale of magnitude and length, that while we expect the results of this film to be terrific, they will be tempered somewhat by the cost structure. And I said the exact same thing as it relates to *Infinity War*.

Operator

Our next question comes from Michael Nathanson with MoffettNathanson LLC.

Michael Nathanson – *MoffettNathanson LLC*

So one for you Bob, and one for your Christine. Bob, at Investor Day, one thing that didn't come up was China. And I look at the parks you have there and how well Marvel does -- how are we thinking about the OTT opportunities for China? And for Christine, in answering Ben's question, regarding single-A credit, when do you think you have the threshold in the coming years?



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

Michael, right now, there are regulations in China that might limit what we can do from an OTT perspective. Certainly, what we can do on our own. We have to, at this point, if we're going to launch something, we have to be with a local partner with shared ownership. So we're going to have to work our way through that. We certainly believe there are opportunities. Interestingly, if you look at performance of *Avengers: Endgame* -- I was going to mention this as related to Shanghai -- but Marvel has gotten extremely popular in China and I think this film has already done somewhere in the neighborhood of \$600 million in Box Office dollars, in China already. It's just enormously popular. So the idea of bringing the Marvel television shows to China as part of our direct-to-consumer platform or proposition is something that we're very, very interested in. And as it relates specifically to Shanghai, we think we have a huge opportunity for Marvel there.

We built something somewhat temporary in nature, just a tent that features Marvel franchises and characters, because when we began designing the park in Shanghai, it was only soon after really we had purchased Marvel, and we went in early enough to do it. But there are great opportunities long-term given the affinity people have in China for these characters. That's a hint to our Parks and Resorts group. We should be hard at work already designing and developing some Marvel presence in Shanghai. They're listening, I know.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay. Now onto the more exciting leverage question, Michael. Let me just say that our approach to fiscal discipline has not changed, it's just that we're managing more. But we're right now in the middle of our long-range planning process, which will followed by our annual process. We'll work through this over the next few months, and we'll have more clarity on it probably by next earnings release. However, what I would say is that-the rating agencies maintain a very solid working relationship with the company, in particular, the treasury team, and they have all been apprised of the activities around the company, not only on our own, but also with closing and with the integration of Fox. And you can see where they're positioning us now, which is



maintaining us at our current ratings level. We have every intention of bringing that down as quickly as possible, but we're going to balance that with investing in our businesses to create that long-term shareholder value.

Operator

Our next question comes from Marci Ryvicker with Wolfe Research.

Marci Ryvicker – *Wolfe Research, LLC*

Going back to the DTC Analyst Day, I think there was a lot more content available on Disney+ than the Street had been expecting, at least in the first year. So is this just a timing of when the content is flowing in from your contracts? Or did you have to negotiate with third-party distributors to get that content back earlier?

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

We did some deals, Marci, to get some of the content back that had been licensed to third parties. We continue to explore ways that we might be able to get more back. But what we announced at Investor Day included some of the rights that we've managed to buy back or negotiate back from what had been licensed to third parties. And there's still more out there that we're exploring.

Marci Ryvicker – *Wolfe Research, LLC*

Okay. And then what happens with content in the Pay Two window? So if you get content from Netflix, does it go back to them? Or do you keep it for forever?

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

I don't want get too specific on that but there was a window in the Netflix deal that enabled us access to some of the films, since they were films that we were licensing to them. And again, I



don't want to get more specific than that. But when we did the Netflix deal way back, we envisioned -- even though at that point the possibility was far off -- that one day we might want to launch our own service, so we carved out an ability to run some of the films on such a service, and it paid off.

Operator

Our next question comes from Kannan Venkateshwar with Barclays.

Kannan Venkateshwar – *Barclays Bank PLC*

I guess a couple. First on the KPIs for DTC going forward. Just wanted to understand what kind of metrics we should be tracking in order to figure out the progress. I mean Disney+, of course, doesn't launch until later in the year. But would you be helping us with subscribers on the Hulu front or on the ESPN+ front? And the second question is, when we look at film margins for Fox, they're significantly lower than Disney and I know you don't manage studios for margins, but the delta's just very big, and it could be a \$1 billion-plus opportunity over time on the margin front. So just wanted to figure out how you're thinking about margins on the studio side for film.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay, Kannan. Let me take first this sub-question. As you saw in the Investor Day, we have committed to being very transparent as it relates to our strategy and our progress in our direct-to-consumer initiative. As you mentioned, Disney+ has not yet launched, there's nothing to report. But as we get further into the latter part of the calendar year, while we're not going to commit to exactly when, we will be providing sub-numbers going forward at the appropriate time as well as some of the other metrics that we spelled out on the Investor Day. So once again, our commitment is to transparency to allow you to understand the progress that we're making in this business. It's very important to us. And on the theatrical side, we do manage our



studio to margins and returns, more specifically. We look at those returns on a regular basis, we update them when a film is in its early run, but it's very much a return-driven business.

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

And we would hope to bring that same approach, that same discipline to the Fox Studios.

Operator

Our next question comes from Doug Mitchelson of Crédit Suisse.

Doug Mitchelson – *Credit Suisse AG*

So one for Bob, one for Christine. Bob, for Hulu, does the expansion of your non-Disney+ entertainment content require you to own 100% of Hulu if you want to take that internationally? And so if I ask that right, do you need to own all of Hulu to do Hulu international? And pushing that further -- because I imagine you're going to say you don't need to -- Disney+ has numerous advantages, you laid those out at the Analyst Day; how do you think about the Hulu opportunity overseas and how that service would be differentiated? And any timing on that? I imagine it will be a couple years before enough content is available. And for Christine, Bob talked about the Fox Film slate coming down to five or so films a year, ex-Searchlight. Fewer films will reduce cost a lot in the Fox Studios side. Does the \$2 billion of cost synergies include bringing down the number of films at Fox? Or should we think about this more as sort of core SG&A and other OpEx-type items?

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

Doug, first of all, we're bullish about Hulu for a number of reasons, but mostly because as we see it, it's the best consumer television proposition out there because it offers linear channels that include a lot of live news and sports, in-season stacking of network programming, a lot of great original programming and then, of course, a lot of library beyond just the network library



in season that I suggested. With Comcast as basically a 33% owner, any big decisions that are made as it relates to investment or expansion would have to be done with their cooperation. And again, I think we would probably both share a bullish outlook about Hulu, but we can't do it on our own.

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

And Doug, as it relates to the studio and where it factors in with the \$2 billion of synergies, at the time that we announced the transaction, that was the number and it did include the studio. It included a reduction in output, as well as two studios that had a significant amount of overlap. With overlap came redundancies, and that's all part of the cost synergies that we're well on the way of realizing for the studio.

Doug Mitchelson – *Credit Suisse AG*

And Christine, if I could just follow up real quick. The \$0.35 Fox dilution for the fiscal third quarter, I imagine is sort of unusually high. Can you confirm that you're still targeting Fox being accretive by fiscal '21?

Christine McCarthy – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

As I mentioned earlier, we are in the early stage -- well in the middle of, not early stage -- in the middle of our long-range planning which will go out for the next couple of years, probably in greater detail than we would do if we had not done this acquisition. But we're in the middle of doing that. So to the extent to which there's any refinement of the accretion dilution, we'll report it at the right point in time.

Operator

Our next question comes from John Hodulik with UBS.



John Hodulik – *UBS Investment Bank*

Bob, it looks like the NFL is going to move forward with a digital version of the Sunday Ticket. Some questions from that. First of all, is that a set of rights that could possibly be a good fit for ESPN+? Or are you still sort of focused on second and third-tier rights? And two, does that change your view on say, the value of the broadcast NFL packages? And then I guess, just 1 follow-up, Fox just announced an equity stake in Stars Group to pursue sports gambling and to sort of leverage their existing set of sports rights. And I know you've said that's not something that you had on the drawing board, but as you look out and it becomes more mainstream, is it something that you could potentially revisit?

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

Well, on the gambling front, we've said and actually we've already done some things that we would integrate it into our programming, but not to the extent that we would be facilitating gambling as an entity. In other words, we'll provide programming that will, I guess, be designed to enlighten people who are betting on sports. But that's as far as we would go. And I think you'll see more of it integrated in the programming, but we just don't intend to go into the gambling business.

On Sunday Ticket, I'm not going to elaborate much, except that we've done some exploration as to whether there was an opportunity there, but I'm going to leave it at that. And we're very bullish on the NFL. By the way, we got a great schedule this coming year, but we're bullish on the relationship ESPN has with the NFL. And I think we all believe that there are opportunities to strengthen our relationship with them.

Operator

Our next question comes from Tim Nollen with Macquarie.



Tim Nollen – *Macquarie Research*

My question is back on the subject of Hulu, if that's okay. News of AT&T selling out and then some discussion of Comcast considering selling. I just wonder, if you lose any partners, what happens to the content that they are contributing to the platform? Do you still get a lot of that Warner content for a long period of time? Does it fall off? And likewise, if Comcast were to drop off -- I'm assuming the answer is they won't do that -- but if they were to, what would happen to their content in Hulu?

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

Well, obviously Warner has sold their stake to us through AT&T; Time Warner sold their stake to us. And I can't be specific about what was tied to that, but there was some ongoing relationship as it related to their product, including their channels. And as it relates to the other question and maybe going back to the one that was asked earlier, we're 2/3 owner of Hulu. So big decisions that are made, there's a vote that has to occur. But we're going to be mindful of how that's managed knowing that we have a fiduciary responsibility to the third-party owner, which is Comcast, 33%. And I think we've publicly confirmed that there has been dialogue with Comcast about them possibly divesting their stake. And you can expect that if that were to occur, there probably will be some ongoing relationship as a result of programming.

Tim Nollen – *Macquarie Research*

Okay. So even if you have lost AT&T, Warner as a part owner and there is the possibility of Comcast leaving, it still means you have a lot, if not all, of the content that they were providing for some fairly long period of time?

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

I'm not going to get more specific than that, so I can't help you at all in terms of your assumptions, beyond what I just said.

**Operator**

The next question comes from Alan Gould with Loop Capital.

Alan Gould – *Loop Capital Markets, LLC*

Bob, you talked about China possibly expanding a Marvel land. I've never seen a series as successful as Marvel. I believe you have the rights west of the Mississippi. Is there any thought of having a Marvel land in the U.S.?

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

We're building a considerable Marvel presence at Disneyland as we speak. And I don't remember how specific we've gotten about what's in it, but I was there last week, maybe a week and a half ago -- there's a lot of construction going on. I just have to check -- I just don't recall whether we've been specific about what's in it. Actually I saw an image online recently of a design concept, but I don't know whether that was leaked or not. We have said that we already have a *Guardians of the Galaxy* presence since we converted Tower of Terror, and there'll be a *Spider-Man* attraction as part of the expansion that I'm describing. We're also building a *Guardians of the Galaxy* coaster at Epcot in Florida, where there are more restrictions to the question that you asked, than we have in California. And then in China, we don't have any restrictions. So I imagine we're at some point going to get very ambitious about what we do with Marvel at Shanghai Disneyland.

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

Alan, thank you. And thanks, everyone, for joining us today. Please note that a reconciliation of non-GAAP measures that were referred to on this call to GAAP measures can be found on our Investor Relations website. Let me also remind you that certain statements on this call, including financial estimates, 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, quarterly reports on Form 10-Q and in our other filings with the Securities and Exchange Commission. This concludes today's call. Have a great afternoon, everyone.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program, and you may all disconnect. Everyone, have a wonderful day.

**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, including statements such as financial estimates, the anticipated availability or timing of our goods or services, our business plans and other statements that are not historical in nature. 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:

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

Such developments may affect entertainment, 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;
- demand for our products and services;
- expenses of providing medical and pension benefits;
- income tax expense;
- performance of some or all company businesses either directly or through their impact on those who distribute our products; and
- achievement of anticipated benefits of the recent transaction with 21st Century Fox.

Additional factors are set forth in the Company’s Annual Report on Form 10-K for the year ended September 29, 2018 under Item 1A, “Risk Factors,” and subsequent reports.

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