



The  
**WALT DISNEY**  
Company

## Q3 FY19 Earnings Conference Call

AUGUST 6, 2019

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 Company's Fiscal Third Quarter 2019 Financial Results Conference Call. (Operator Instructions)

As a reminder, this conference call is being recorded. I would now like to turn the conference over to Lowell Singer, Senior Vice President of Investor Relations. You may begin.

---

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

Good afternoon and welcome to The Walt Disney Company's third quarter 2019 earnings call. Our press release was issued about 25 minutes ago and is available on our website at [www.disney.com/investors](http://www.disney.com/investors). Today's call is also being webcast, and a replay and 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. Following comments from Bob and Christine, we will be happy to take your questions. So with that, I will turn the call over to Bob to get started.

---

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

Thanks, Lowell, and good afternoon everyone.

I've been doing earnings calls for a long time and this is one of our more complicated ones. We certainly have a lot to cover and discuss.

This is our first full quarter since we closed our acquisition of 21st Century Fox in March, and our results reflect our efforts to integrate the assets, businesses, and talent we acquired in order to enhance and advance our strategic transformation.



Implementation of our integration plan is well underway -- a complex process given the magnitude of the endeavor, and we remain confident in our ability to successfully execute our strategy to drive maximum value from the combined company and our appreciation for the long-term value we can create has increased.

I'm going to ask Christine to take you through the numbers....and then I'll be back to provide some additional perspective that should give you greater insight into our bullish view of the future.

---

**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 from continuing operations for the third quarter were \$1.35. Our third quarter results reflect a full quarter of performance of the 21CF businesses we acquired and are still in process of integrating, and full consolidation of Hulu.

Results this quarter include a number of factors we recognize can be challenging to model. In a moment, I'll discuss our Q3 results in greater detail and shed additional light on these factors, and then I'll highlight a few items that will impact our Q4 results. Since we are in the middle of our fiscal 2020 planning process, I expect to have more to say on the key drivers of next year's results during our Q4 call.

The 21CF businesses we acquired, excluding 21CF's stake in Hulu, had a slightly negative impact on third-quarter segment operating income. The total adverse impact on segment operating income, including full consolidation of Hulu and the effect of inter-segment eliminations, was about \$300 million. Overall, we estimate the acquisition of 21CF had a dilutive impact on our Q3 EPS, before purchase accounting, of about \$0.60 compared to the \$0.35 guidance we provided last quarter.



The initial guidance of \$0.35 reflected our assumptions about the business at the time, however there were a couple of 21CF businesses whose results came in significantly lower than our expectations, in particular the 21CF Film Studio and Star.

I want to take a moment to discuss the primary drivers of the underperformance of these businesses, which are reflected in our Studio and Direct-to-Consumer and International segments:

First, the 21CF film Studio had an operating loss in the third quarter of about \$170M, which was driven by the underperformance of theatrical titles, including *Dark Phoenix*, marketing for future releases and development expenses, partially offset by TV/SVOD distribution. While 21CF's performance is not reflected in our prior year results, we estimate that 21CF's film studio generated about \$180 million of operating income in Q3 last year. On the other hand, I'll note that the performance of the Disney film Studio continues to be incredibly strong. This quarter's theatrical slate -- including *Avengers: Endgame*, *Aladdin*, *Toy Story 4*, and the carryover success of *Captain Marvel*, drove higher worldwide theatrical results compared to what was also an outstanding slate of films during the third quarter last year, which included *Avengers: Infinity War*, *Incredibles 2*, and *Black Panther*.

Second, as you know, results at DTCL reflect ongoing investment in our direct-to-consumer businesses, and this quarter also included an operating loss at Star of about \$60 million. We estimate Star generated about \$150 million of operating income in the third quarter last year. Star's results this quarter came in well below our expectations and were driven primarily by a meaningful step-up in rights costs for the quadrennial Cricket World Cup and the Indian Premier League, as revenue growth was more than offset by the incremental rights expense.

There was an additional negative impact to EPS of about \$0.06 as a result of the Hulu agreement we entered into with NBCU in May. The agreement provides us with full operational control of Hulu, and most of the six-cent impact results from NBCU no longer being allocated its



share of Hulu operating losses in our financial reporting. You'll find additional detail on the transaction and the financial impact in our 10-Q.

At Parks, Experiences and Products, growth in operating income was driven by higher results at Consumer Products and Disneyland Paris, partially offset by a decrease at our domestic parks and resorts.

Attendance at our domestic parks was down 3% in the third quarter, but per capita spending was up a healthy 10% on higher admissions, food and beverage and merchandise spending. Per room spending at our domestic hotels was up 3% and occupancy was up two percentage points to 88%.

Despite Domestic Parks achieving record revenue in the third quarter, operating income was down slightly due to the decline in attendance and higher costs. Disneyland Resort had strong underlying attendance fundamentals, with growth in local, domestic and international visitation. We are very pleased with how guests have responded to Galaxy's Edge and *Millennium Falcon: Smuggler's Run* is one of our most popular attractions.

The decline in attendance at the Disneyland Resort was primarily driven by lower annual passholder visitation as we managed demand for the first few weeks after opening *Star Wars: Galaxy's Edge* in order to maintain a high level of guest satisfaction.

And at Walt Disney World, our survey data suggests that guests are deferring visitation until after *Star Wars: Galaxy's Edge* opens, which we believe contributed to the decline in attendance we saw during the third quarter.

Looking ahead, we are excited for the opening of *Star Wars: Galaxy's Edge* at Walt Disney World and the opportunity to introduce guests to the Rise of the Resistance, our most technologically



advanced and immersive attraction, when that attraction opens at Walt Disney World in December and at Disneyland in January.

Our domestic parks incurred incremental operating expenses during the quarter, including wage increases and pre-opening and operational expenses associated with the opening of Galaxy's Edge.

Results at our international operations were higher in the third quarter due primarily to growth at Disneyland Paris.

At Consumer Products, growth in operating income was due to higher results in our merchandise licensing and retail businesses. Growth in merchandise licensing was driven by higher revenue from sales of Toy Story and Avengers merchandise, partially offset by lower sales of Star Wars merchandise. Growth in comp store sales at our brick and mortar stores and higher online revenue drove the increase in retail for the quarter.

Looking ahead to the fourth quarter, we anticipate strong segment operating income growth driven by the benefit from a full quarter of *Star Wars: Galaxy's Edge* at Disneyland and growth at merchandise licensing. So far this quarter, domestic resort reservations are pacing up 4% compared to prior year, while booked rates are up 3%.

At Media Networks, total affiliate revenue was up 20% in the third quarter and reflects the impact of the 21CF acquisition as well as underlying growth at our legacy Media Networks. The increase in affiliate revenue was driven by 16 points of growth from the acquisition of 21CF and eight points from higher rates, partially offset by a two and a half point decline due to a decrease in subscribers.

At Broadcasting, lower programming expenses and higher affiliate revenue were more than offset by the impact of lower program sales and a decline in advertising revenue. Ad revenue



was lower in the quarter as higher network rates were more than offset by lower viewership. Quarter-to-date, primetime scatter pricing at the ABC Network is running 35% above upfront levels.

ABC Studios faced a difficult year-over-year program sales comparison since Q3 results last year reflected the sale of *Luke Cage*, and this quarter we had lower sales of *How to Get Away with Murder* and *Designated Survivor* compared to last year.

Domestic Cable results were up in the quarter due to the consolidation of the 21CF Cable businesses and higher operating income at ESPN, partially offset by a decline at Freeform.

At ESPN, growth in operating income during the third quarter was due to higher advertising and affiliate revenue, partially offset by an increase in programming and production costs driven by contractual rate increases for MLB and NBA programming and new rights.

ESPN's domestic linear advertising revenue was up 13% in the third quarter. ESPN benefitted from two extra NBA Finals games compared to last year. When you adjust for the mix and the total number of playoff games this year compared to last year, we estimate there was about an 8-point benefit to the year-over-year growth in advertising revenue. So far this quarter, ESPN's domestic cash ad sales are pacing down compared to last year.

Results at our Direct-to-Consumer and International segment reflect the consolidation of Hulu, and ongoing investment at ESPN+ and Disney+. Results at our direct-to-consumer businesses had an adverse impact on the year-over-year change in segment operating income of about \$400 million. ESPN+ had a little over 2.4 million paid subscribers at the end of the third quarter and Hulu had approximately 28 million paid subscribers.

Now I'll turn to some thoughts about the fourth quarter. We expect our Direct-to-Consumer and International segment to generate about \$900 million in operating losses for the quarter, which



represents an increase of about \$560 million over the fourth quarter last year. We expect the continued investment in our DTC services, including ESPN+ and Disney+, and the consolidation of Hulu, to drive an adverse impact on the year-over-year change in segment operating income of our direct-to-consumer businesses of approximately \$550 million, which is almost the entirety of the total segment change versus prior year.

At Media Networks, there are a few items I'd like to mention that we believe will cause segment operating income to decline by about 10% in the fourth quarter compared to prior year.

We expect the 21CF television businesses to contribute about \$200 million in operating income in the fourth quarter, with two-thirds of that contribution at Broadcasting and one-third at Cable. We estimate 21CF's television businesses generated operating income of about \$485 million in the fourth quarter last year. The expected year-over-year decline is due to a combination of factors, including lower program sales and higher content development expense, which are both related in part to our ongoing investment in our direct-to-consumer businesses.

At ABC Studios, we expect a difficult program sales comparison given we sold two Marvel series, *Daredevil* and *Iron Fist*, during Q4 last year and we don't expect comparable sales in Q4 this year.

At ESPN, we expect higher programming expenses, driven by contractual rate increases and launch costs for the ACC Network, and lower ad revenue to more than offset growth in affiliate revenue.

In aggregate, we estimate the acquisition of 21<sup>st</sup> Century Fox and the impact of taking full operational control of Hulu will have a dilutive impact on our Q4 earnings per share, before purchase accounting, of about \$0.45 per share.



Despite these headwinds, we remain excited about the acquisition of 21CF and still expect the acquisition to be accretive to EPS, before purchase accounting, for fiscal 2021, and we also remain on track to realize over \$2 billion in cost synergies by fiscal 2021.

And with that, I'll now turn the call back over to Bob.

---

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

Before I discuss our new strategy, I'd like to begin by singling out our studio, which is the envy of the industry. The studio has generated \$8 billion in global box office in 2019 – a new industry record – and we still have five months left in the calendar year, with movies like *Maleficent: Mistress of Evil*, *Frozen II*, and *Star Wars: The Rise of Skywalker* still to come.

So far this year, we've released five of the top six movies – including four that have generated more than a billion dollars in global box office. *Avengers: Endgame* is now the highest grossing film in history, with almost \$2.8 billion worldwide.....*Captain Marvel*, *Aladdin*, and *The Lion King* have each surpassed \$1 billion....and with more than \$960 million in box office to date, *Toy Story 4* will likely cross that threshold in the coming weeks. And all of these movies will be on Disney+ in the first year of launch.

The Studio co-chairs behind this record-setting performance, Alan Horn and Alan Bergman, are now redefining 20th Century Fox Film's strategy for the future – applying the same discipline and creative standards behind the success of Disney, Pixar, Marvel and Lucasfilm. They're taking the Fox studio in a new direction -- all new development slates will focus on a select group of high-quality movies -- for theatrical release as well as for our Hulu and Disney+ platforms. And Fox Searchlight will continue to make the prestige films it's known for, while expanding its high-quality original storytelling into the DTC space.

We see great long-term value in the broad collection of theatrical IP we acquired from Fox, including iconic movie franchises such as *Avatar* and *Planet of the Apes*, as well as Marvel's X-



*Men, The Fantastic Four, and Deadpool*, which are now part of Marvel Studios, under the leadership of Kevin Feige – the architect of the Marvel Cinematic Universe, which now includes 23 movies with a global box office of more than \$22 billion to date.

We're also focused on leveraging Fox's vast library of great titles to further enrich the content mix on our DTC platforms – for example, reimagining *Home Alone*, *Night at the Museum*, *Cheaper by the Dozen*, and *Diary of a Wimpy Kid* for a new generation on Disney+.

As I've said a few times, we analyzed the 21st Century Fox opportunity entirely through the lens of our future business – evaluating the long-term potential, especially related to accelerating our transformation into the DTC space on a global basis.

As a result of the acquisition, we also now have full operational control of Hulu – and a clear path to full ownership – providing another powerful platform for us to produce and distribute great content. Hulu will provide us with an excellent opportunity to leverage the capabilities of our television studios and brands: notably, FX and ABC Television.

The deal also added Star and Hotstar to our portfolio of businesses, giving us a significant presence in India, which will soon become the most populous country in the world. It's a huge market with interesting dynamics -- notably, a rapidly rising middle class with a strong and growing appetite for media, especially sports. To give you an idea of the value of this platform – last quarter Hotstar had more than 300 million average monthly users, served an unprecedented 100 million daily users, and delivered a high quality streaming experience to 25.3 million simultaneous users, which is a new world record. The platform's broad array of premium sports rights will serve it well over the next five years – especially as we expand the service into markets across Southeast Asia.

At Walt Disney Television, the Fox acquisition brought us talented and experienced senior leadership, who are now in place, to produce much of the content we will rely on to implement



our ambitious strategy. Their studio capabilities, production expertise, and valuable relationships with the creative community will be vital to our DTC plans, while also overseeing ABC, ABC News, our owned television stations, FX, Freeform, the Disney Channel, and Nat Geo.

National Geographic brings a strong global brand to our portfolio – along with world-class content for our television and DTC businesses. Disney+ will offer more than 600 hours of premium content from National Geographic at launch, along with almost 300 hours of family entertainment from the Fox Studios library.

Disney+ will ultimately become the exclusive streaming service for our vast library of movies and series, National Geographic content, all upcoming Disney, Pixar, Marvel, and Star Wars movies, and a robust slate of high-quality original programming from the creative engines that drive our entire company.

Regarding our suite of DTC services, I'm pleased to announce that in the United States consumers will be able to subscribe to a bundle of Disney+, ESPN+ and ad-supported Hulu for \$12.99 a month. The bundle will be available on our November 12th launch date.

Before we take your questions, let me reiterate a few things:

Today, much of our focus is on integrating Fox's assets and leveraging them, along with our Disney businesses, to move quickly into the direct-to-consumer space. Nothing is more important to us than getting this right.

We remain confident in our strategy and our ability to successfully execute it, and, as Christine noted, we still expect the acquisition to be accretive to EPS, before purchase accounting, for fiscal 2021.

We're clearly bullish on our future, for good reason.



And on that note, Christine and I will be happy to take your questions.

---

**Operator**

(Operator Instructions) Our first question comes from Alexia Quadrani with JP Morgan.

---

**Alexia Quadrani** – *JP Morgan Chase & Co.*

Hi, thank you very much. Just two questions, if I may. First on the Fox integration. I know it's really early days, and you highlighted some areas of weakness 21CF had in the quarter but you also spoke about the opportunity of Fox and its IP presents longer-term. I guess my question is any color how long it takes before the Disney imprint really impacts these assets? I assume it takes a while for the studio and the other assets-you have to own them for a while before you really see the impact.

And then my follow-up question is on the Parks. Any color on how *Star Wars: Galaxy's Edge* opening in Disneyland did versus your internal expectations? And anything you've learned from it in terms of the opening you can sort of apply to Orlando's opening later this month?

---

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

Sure, Alexia. Thank you. First of all, regarding Fox and the integration, I think in terms of these results, aside from a lot of the ins-and-outs that Christine described - like the cost of cricket in India, et cetera, and so on, and the impact of the Hulu deal - I think one of the biggest issues that we faced in this quarter in terms of the earnings was the Fox Studio performance, which was well below where it had been, and well below where we hoped it would be when we made the acquisition.

Now understand, I've been through a number of these. First of all, I was bought twice. First at Capital Cities by ABC, and then Disney bought ABC. And I know what happens when companies are purchased. Often, decision-making can grind to a halt or certainly slow down. We've



managed to avoid that in the purchases of Pixar, and Marvel, and even Lucasfilm in part because between when we made the deals and when the deals closed, it was relatively short periods of time.

In this case, we announced the deal first in December of '17, and we didn't close the deal until spring of 2019. And that's a long period of time for a business that relies on constant decision-making and constant attention to detail. And while I don't in any way mean to cast dispersions at any individuals at all, it was a very difficult transition for that business.

And what we've done is we put it under our studio, and you know the results there. They've been hard at work working primarily with Emma Watts on the live action side to redirect the efforts of the live action part of that business - first of all, the consolidated cutback in the number of releases and then the focus on the kind of releases that we would hope to come out of that studio. We like some of the movies that are coming up, notably there's one called *Ford vs. Ferrari* which we've all seen, which is great, but it will probably take a good solid year, maybe two years, before we can have an impact - obviously it takes longer on the development side - but an impact on the films that are actually in production. But we're all confident that we're going to be able to turn around the fortunes of Fox Live Action, and you'll see those results in a couple of years.

On the *Star Wars: Galaxy's Edge* front, to give you some color, I think a number of things happened. First of all - helped in part by some of our efforts - there was tremendous concern in the marketplace that there was going to be huge crowding when we opened Galaxy's Edge. And so some people stayed away just because they expected that it would not be a great guest experience. The same time that was going on, all the local hotels in the region - expecting a huge influx in visitation - raised their prices. So it simply got more expensive to come stay in Anaheim.



In addition to that, we raised our prices. We brought our daily price up. So if you think about local visitation, we brought the price of a one-day ticket up substantially from a year ago. And then we opened up Galaxy's Edge with one attraction instead of two - the second attraction is going to open in January. And so all of those factors contributed to attendance that was below what we would have hoped it would be. That said, guest satisfaction, interest in the attractions and the land is extremely high. They're among the most popular thing at the Park.

And so long-term - and look, we build these things for the long-term - we have no concerns whatsoever about them. We're opening Galaxy's Edge in August in Orlando. The second attraction there will open in December, and as I said, the second attraction in Anaheim will open in January. So we feel great about the product that we've created. It's just going to take some time for basically - for things to work themselves out in terms of how the marketplace is reacting.

---

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

Alexia, I just want to put a little more granularity on the Disneyland results for the quarter. As I said, the attendance was down 3%, but the paid attendance was up in the quarter, and that lower attendance was primarily driven by the annual passholder visitation. And when we look at the per cap spend across Disneyland, all categories, they were up significantly year-over-year.

---

**Operator**

Our next question comes from Michael Nathanson with MoffettNathanson.

---

**Michael Nathanson** – *MoffettNathanson LLC*

Thanks, I have one for Bob and one for Christine. Bob, thanks for the update on the Hulu bundle. That's what we would have asked you. Another question on Hulu is, any update on international rollout now that you have full control? That's something that people have been focused on.



And then for Christine, I'm just confused a bit by what surprised you at Star, because those cricket contracts were known. So was this something more about performance of those contracts in terms of the ratings of that contract that surprised you? Anything more on India would be helpful. What disappointed you?

---

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

We're not updating anything regarding Hulu internationally. Kevin Mayer and the team at Hulu are studying opportunities, along with our international team market-by-market. Obviously, we have designs on growing Hulu outside of the United States but no update on that right now.

---

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

And on Star, Michael, it was the quadrennial Cricket World Cup of course - they have their Indian Premier League, which is ongoing but this is once every four years for the World Cup. There were a couple of significant games that were rained out. They have insurance coverage for some of those, but any proceeds would be in future periods. And there was also some weakness in advertising revenue that was related to the local advertising market.

---

**Operator**

Our next question comes from Jessica Reif Ehrlich with Bank of America Merrill Lynch.

---

**Jessica Reif Ehrlich** – *Bank of America Merrill Lynch*

Thank you, just a couple of different questions. But could you talk a little bit about the marketing for Disney+ with the launch less than three months away? You talked at the Analyst Day about having 90%-plus awareness. Can you just -- I haven't seen marketing yet so can you talk about the plan?



Different topic, but with all the stuff that's going on in China as well as in Hong Kong, can you talk a little bit about - or give us some color - on what you're seeing in terms of impact on tourism at the parks, and how it might be affecting pricing and future investment?

And then one last kind of follow-up on the pricing. You did increase prices unusually. I think -- I'm not sure if it's just Disneyland -- can you talk about how you're thinking about pricing going forward at the domestic parks? Thanks.

---

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

Disney+ marketing is going to start to hit in - later this month, later in August. We're actually going to allow members of D23 to be the first to subscribe. I'm actually going through a comprehensive marketing plan with the team next week. Comprehensive probably is an understatement. It's going to be treated as the most important product that the company has launched in -- I don't know, certainly during my tenure in the job, which is quite a long time.

And you will see marketing both in traditional and nontraditional directions, basically digital and analog - also a significant amount of support within the company on basically company platforms. And then of course all of the touch points that the company has, whether it's people staying at our hotels, people that have our co-branded credit card, people that are members of D23, annual pass holders... I could go on and on. But the opportunities are tremendous to market this. And I feel good about some of the creative that I've already seen, but you won't start to see it until later this month.

On the China front, to date, we have not seen any impact at all in Shanghai about the unrest that's going on in Hong Kong, or from the trade issues between our countries. In Hong Kong, we have seen an impact from the protests. Obviously, they are significant in nature. And while the impact is not reflected in the results that we just announced, you can expect that we will feel it in the quarter that we're currently in, and we'll see how long the protests go on. But there's definitely been disruption that has impacted our visitation there.



On the pricing side, as we've said a number of times, our pricing is designed to really accomplish a number of things: one is to reflect the value of the product that we have in the marketplace - that includes the franchises and the popularity of them; and of course, the investments that we've made in these parks and resorts by continuing to build them out, and continuing to create experiences that are better than many of those that we've had in the past.

We also have tried very hard to protect guest experience, and so the pricing has been designed to make it more expensive in peak periods to manage that demand, and less expensive or not as expensive in the non-peak periods to make it more accessible. And for the most part, we've done a good job doing that. We know that demand on our product is so extraordinary in the peak periods that it's just in our better interest to manage crowding because it just affects guest satisfaction.

At the same time that we have taken our prices up, our competition has actually been in the market discounting a little bit more. We've certainly seen that with Universal in Florida. And so the gap between what we did, and where they've been - maybe it's a little greater than it's been and perhaps that has had an impact. We obviously monitor these things very carefully. I tried to explain what some of the pricing impact on *Star Wars: Galaxy's Edge* was, but we do not feel that we have a pricing issue at our domestic parks. And that's reflected in basically not only current business, but a fair amount of research that we've done.

---

**Operator**

Our next question comes from Ben Swinburne with Morgan Stanley.

---

**Ben Swinburne** – *Morgan Stanley*

Thank you. Bob, as you get ready to launch Disney+, I'm wondering if you could update us on sort of the technical platform behind the product, and kind of where that stands versus where it needs to be to scale a big business globally. And also your philosophy on distribution partnerships. You mentioned bundling Hulu and ESPN+ which certainly makes sense. But there's



a lot of companies - as you're well aware of – out there sort of selling in a digital native environment, like Amazon and Apple and others... lots of services like these. I'm just wondering if you could talk about your philosophy on utilizing those versus a pure direct-to-consumer business, because those could certainly impact sort of how fast you get out of the gate.

And then I just wanted to ask, Christine, you didn't mention the 21CF Television Studio, which I believe is in your broadcast segment. That's a business that I think you would acknowledge has been performing quite well for a long time. Any sense for how that's doing or how that impacted the quarter would be appreciated.

---

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

Okay. On the second part of your question first, about basically digital distribution partners. At Investor Day, we announced that we had a few distribution partners. There are others out there, notably Apple and Amazon and Google, for instance, that we've been in discussions with about distribution. You can expect that we will conclude deals with them as distribution partners. We think it's important for us to achieve scale relatively quickly, and they'll be an important part of that. Nothing to announce specifically, except we've had conversations with all of them. They're all interested in distributing the product.

On the tech side, we continue to look very carefully at the tech platform that we have. Obviously we're using that platform for ESPN+. We continue to learn with it. We're most focused on - not how robust it is because we believe we have that already - but we're most focused on the onboarding experience and making sure that people who sign up as subscribers for the service do so with incredible ease. We know how important it is to create a frictionless experience and there's a lot of time being spent on that.

I want to also say even though it wasn't part of your question, that as we're dealing with distribution opportunities, as well as what we just talked about - which is the tech and the sign-



on or the onboarding side – there is a huge amount of work going on on the production front. I just want to touch on some of that.

As you know, we're going to launch with a significant number of movie titles that are from our Studio - that will be well over 300 on launch day and over 400 in Year 1, including the great slate that the Studio has out in the marketplace now.

By the way, those titles are significant in terms of their quality. For instance, they'll be 8 Star Wars titles when we launch, 18 Pixar, 70 Disney Animation, 240 Disney Live Action, 4 Marvel and then followed by 8 more Marvel in Year 1. So a lot of quality. And then over 7,500 episodes of Disney TV.

We're augmenting all of that with a tremendous amount of original live action product. And I've actually screened a fair amount, including the entire series *The Mandalorian* for Season 1, a number of the movies that we made including *Togo* and *Lady and the Tramp* and *Noelle* and *Stargirl*... and I can probably name a few others... and a lot of the other series product that we're making from Marvel, from Pixar, from Disney Channel - *High School Musical* another one - and I've been really impressed with the quality, with the variety and with the volume. So a tremendous amount going on, on that front.

I'm convinced that we're going to launch with a tremendous array of intellectual property, for people who are interested in National Geographic, Marvel, Pixar, Disney and Star Wars. And then on the studio front, Christine could take some of the particulars as it relates to the television side.

---

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

Okay. So 21st Century TV was a contributor in the quarter on an operating income basis. It had a more significant contribution on the cable side than the broadcast side. Although we did



mention that there would be some headwinds in the fourth quarter, it will still be a positive contributor. It'll just be lower than it was year-over-year.

---

**Operator**

Our next question comes from Todd Juenger with Sanford Bernstein.

---

**Todd Juenger** – *Sanford Bernstein*

Picking up a little bit, I guess, on where Michael was. I really appreciate all the different lines of businesses and brands and how you're helping us to understand them. Can I ask a little bit about where Hulu Live fits into all of this in the States generally - and just... we've seen price increases at other places - how you feel about profitability there? Just, the fact that you're in the business now of being an MVPD and what that role... that plays for Disney? That's question one.

And question number two, not completely unrelated... I'm a little confused at how you're thinking about the live television brands like National Geographic and the Disney Kids channels which will also exist on Disney+. Will all the content -- especially the new content that's on the TV networks -- be available to Disney+ subscribers? Is there a windowing philosophy, same way going backwards? How do you manage that so that consumers of both products feel like they're getting the full benefit of those brands?

---

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

Good question. Now we're negotiating with a number of MVPDs right now to extend our linear, or live as you call them, television channels. And these remain important deals to us and important businesses to us as well. And obviously, that includes ABC and Disney Channel, and you mentioned Nat Geo, and Freeform, and FX to name a few. So it is important for us to continue to fuel those channels with enough quality, enough original programming to support the businesses as they exist today.



We also know that if you look at all the disruption in our business, the businesses probably being impacted the most is that live multichannel television product. And so the pivot to the direct-to-consumer business is designed to not only address the opportunity that exists in that space, but to address the challenge that exists on the traditional side of the business, which means that we have our own balancing act to do in terms of fueling both sides - the traditional side and the new side, or the direct-to-consumer business - with enough quality product to succeed in both places.

Obviously, what we also are doing is setting ourselves up in a way that we can be resilient - probably more resilient than any of our competitors - should the traditional side erode so significantly that it's not as viable as it has been as a business. And that will enable us to pivot pretty quickly by moving even more product from the traditional channels over to the non-traditional channels.

So it's, as I said, it's a balancing act. We believe that we're making enough quality product for both sides right now to feel confident about both sides of the business. The windowing strategy essentially is that we're taking a lot of product that we're making for the traditional channels, and ultimately moving it on to the nontraditional. But we're also making, as you know, original product for the new channel - the Disney+ and Hulu - that will not go back on to the other channels but... although in some cases, it might. Just to give you an idea, we'd be making FX shows for Hulu that might premiere on Hulu but ultimately end up on the linear channels, is one example of that. So we're going to look at a variety of different opportunities, and just make sure that there's enough content flowing in both directions for the businesses to be successful.

On the Hulu Live front, we felt it was important to do what we can to grow digital MVPD businesses. We obviously know that there are others in the space that have been good partners to us - YouTube would be one to mention. We like the fact that Hulu is out there with a product that is very unique, and that it gives subscribers an opportunity to buy linear television, digital over the top linear television, to buy off-network programming - because we know the deal of...



the content licensing deals that they have with the network - and to buy original programming. And that combination of all three puts Hulu in a very unique place, in that there's really no one out there that's offering the comprehensive television offering the way Hulu is. And we'll continue to stay at it.

The other thing to note by the way, as Hulu has grown, is it's also developed into a very, very important advertising business. And when you think about advertisers who are looking to reach clients on digital platforms, Hulu offers a great opportunity to do that. To what extent those live channels will enable the opportunity to sell advertising, along with the advertising that is sold in the programming that's made just for Hulu, is another story, but it's a big part and a growing part of that business.

---

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

And one more thing on Hulu Live, the digital platform grew the most of any DMVPD this quarter.

---

**Operator**

Our next question comes from Marci Ryvicker with Wolfe Research.

---

**Marci Ryvicker** – *Wolfe Research, LLC*

I have one for Christine. There's so many moving pieces at the moment. Can you just talk about your leverage target? Has this changed at all in terms of the actual target or when you expect to get there? And then maybe comment on your free cash flow priorities and how should we think about the timing on a return to share repurchases?

---

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

Sure. Our target has not changed, Marci. We're still targeting a mid-single A target. We have an ongoing dialogue with the rating agencies. They understand our strategy, they understand what it takes to get there. And the overall pivot in our strategy has been multi-year, and I would say



it's been capped off with the acquisition of 21st Century assets. And we will be meeting with them.

Our attitude towards share repurchase has always been once we invest in our businesses, and we make any acquisitions as we see fit, we look at our dividend capacity. And if all of those still result in excess cash for us, we will return it to shareholders. I don't think you should anticipate that happening in the near future because we're still in an investment mode as it relates to our direct-to-consumer activities, and that's what we're really focused on right now.

---

**Operator**

Our next question comes from Doug Mitchelson with Credit Suisse.

---

**Doug Mitchelson** – *Credit Suisse AG*

Bob, I guess two questions. First, I think there's a lot of familiarity - you saw with everyone listening on the call - as to the U.S. prospects for the Disney+ service and what marketing you might do in the competitive environment. Is international different? I mean you talked about bundling with Hulu in the U.S. but that's not something you can do overseas. So I would just love to hear how you're approaching international marketing and sort of the early prospects of the service overseas to the extent it's different in the United States. And then I have a second question on content distribution strategy.

---

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

Well, we will launch in international markets very quickly. I think two are actually going to launch when we launch Disney+ or around the same time. And then over the next two to three years, we're going to roll out a number of other markets. So you're right, a number of those markets are different than the United States, but what they do share, which is very, very important, is an interest in Marvel, Pixar, Disney, National Geographic and Star Wars.

---



So the product that's being made for the platform travels globally, and that's a big deal. We will have to augment it in certain markets with local programming to meet quotas that are now being applied to OTT services. And we're also going to enter into discussions on an international basis market-by-market with local distributors as well. We're already in those discussions actually. And so we don't have anything to announce right now in terms of new markets that we're going to launch in, but it's safe to assume that we're going to launch in multiple international markets within two years - certainly within three years of launch in the United States and a couple of other markets.

---

**Doug Mitchelson** – *Credit Suisse AG*

Thanks for that. And I guess on content distribution, you talked about fueling the traditional channels versus fueling your OTT services and obviously a third area is selling programming to third-party SVOD services. And I'm sort of curious overseas - I know Hulu international is off-limit - to the extent you're trying to drive Fox profitability to the point where it's accretive in fiscal '21, do you need to continue to sell programming into SVOD windows overseas? And the reason I obviously asked is I'm wondering if at some point you'll start warehousing content that would go into a Hulu international service.

---

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

I think on the Fox front, meaning we'll call it... non-Disney/Pixar-branded type product, or Star Wars - we'll continue to license to third parties overseas to reap the benefits of the revenue that we could derive from those sales, until such time as we believe a launch in that market is imminent, in which case, we'll pivot and hold product for us. We're even going to do that to a lesser extent, a far lesser extent, with some of the Disney content as well until we're ready to launch in a market. We may license some of that content to third parties, too, to continue to drive revenue.



---

**Doug Mitchelson** – *Credit Suisse AG*

Should we assume then shorter term deals than you might have done historically?

---

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

Yes. Yes. Clearly when we do such deals, we're going to do so to avoid the encumbrances that would make it impossible or difficult for us to put the product on our platform once we launch.

---

**Operator**

Our next question comes from Kannan Venkateshwar with Barclays.

---

**Kannan Venkateshwar** – *Barclays Bank PLC*

So Bob, one question for you on the content front, which is when you think about the balance between quality and quantity, how much content from a volume perspective is enough? How much is too much? I mean how are you thinking about the long-term targets in terms of content volumes? And how do you balance that?

And Christine, from your perspective on the marketing side, I think you mentioned Q3 is where we might see some of this spend coming in, Q3 and Q4. Will this all be expensed upfront? Or will this be amortized over time? Would be great if you could help us with that.

---

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

As we said, Kannan, on Investor Day, we said a few times, given the fact that the Disney+ product is Disney and Pixar and Marvel and Star Wars, Nat Geographic - I've mentioned that 8,000 times - we feel that we can focus more on quality than on quantity. But we obviously know we need enough quantity under each brand umbrella to drive subscribers who are primarily interested in those brands. And so obviously if you compare us to Netflix, we're going to have far less product than they do... but we're relying on the strength of our brands and the



fervor that fans of those brands have for the product that we make under those brand umbrellas.

---

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

And on the marketing side, Kannan, in my comments, I mentioned marketing but that was related to 21CF's Film studio, that they had some marketing in the third quarter for movies that would be released in fourth quarter. But I'm assuming your question really is related to marketing that would go along with the launch of Disney+. And as far as that is concerned, we will be expensing those marketing costs as we incur them.

---

**Operator**

Our last question is from Jason Bazinet with Citi.

---

**Jason Bazinet** – *Citigroup*

Just a question for Mr. Iger. In the fullness of time as your DTC strategy plays out, do you think Hulu will be a more important app or financial driver than Disney+? And the reason I ask is... I understand the elements that Fox brought to the Disney+ app - *The Simpsons*, Nat Geo and some of those Marvel characters. But they seem sort of small in the context of the amount of money that you spent to acquire Fox. So it sort of hints that something bigger is afoot in terms of your overall strategy.

---

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

Well, we obviously, in analyzing the assets from 21st Century Fox that we bought, placed a lot of value on the Hulu stake that we were getting. And that obviously was also reflected in the deal that we did with Comcast, where the value of their stake has been public since we announced that deal. So Hulu will play an important part in our future as a platform for the non-so-called family-like programming that will be on Disney+. And that will be fueled not just by library that



we bought from Fox - and that library is both movie and television library - but by a tremendous amount of television production capabilities.

When you think about what -- our company today and the creative engines, we obviously have a movie studio that includes now Fox Live Action and Fox Searchlight. We have, and along with all the Disney assets, we have a sprawling television business that includes ABC, Disney Channel, FX, Nat Geo, Freeform, et cetera, and so on, and the television business or unit that we created under Peter Rice has now been structured to produce original product for all of the platforms, both the linear platforms, the traditional MVPD channels, as well as the new platforms, notably Hulu. So there will be an increase in production activity of the company under that unit producing products specifically for Hulu.

And so as we see it, our play in the digital OTT space, ultimately globally, but we're going to start as we've said more domestically, is to have general entertainment, we'll call it Hulu, more family-like entertainment, which is Disney+, and Sports. And that bundle that we're creating, that \$12.99 bundle where you can buy all three, offers consumers tremendous volume, tremendous quality and tremendous variety, for a good price.

---

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

Thank you, Jason. Thanks, again, 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 Investor Relations website.

In our remarks, we provided estimates of the performance of certain 21CF assets in periods of the prior year. These estimates are based on an analysis of 21CF records but are nonetheless unaudited estimates and are not precise measures of historical results before the acquisition.

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 conference call. Have a great day everyone.

**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 or performance estimates or expectations, the financial impact of certain items, the anticipated availability, timing or pricing 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, asset acquisitions or dispositions, integration initiatives and timing of synergy realization) or other business decisions, 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, regulatory, political, or military developments;
- technological developments; and
- labor markets and activities.

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;
- construction;
- 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 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](http://www.disney.com/investors).