Q1 FY24 Earnings Conference Call

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Prepared remarks only; Q&A to follow

Disney Speakers:

Bob Iger

Chief Executive Officer

Hugh Johnston

Chief Financial Officer

Moderated by

Alexia Quadrani

Executive Vice President, Investor Relations

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PRESENTATION

Alexia Quadrani – *Executive Vice President, Investor Relations, The Walt Disney Company*

Good afternoon. It's my pleasure to welcome everybody to The Walt Disney Company's First Quarter 2024 Earnings Call. Our press release was issued about 25 minutes ago, and is available on our website at www.disney.com/investors. Today's call is being webcast, and a replay and transcript, as well as the First Quarter Earnings Presentation, will all be made available on our website after the call.

Joining me for today's call are Bob Iger, Disney's Chief Executive Officer, and Hugh Johnston, Senior Executive Vice President, and Chief Financial Officer. Following comments from Bob and Hugh, we will be happy to take some of your questions.

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

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

Thanks, Alexia, and good afternoon, everyone.

Just one year ago, we outlined an ambitious plan to return to a period of sustained growth and shareholder value creation, and our strong performance this past quarter demonstrates we have turned the corner and entered a new era.

As previously noted, we are focused on: transitioning ESPN into the preeminent digital sports platform, building streaming into a profitable growth business, reinvigorating our film studios, and turbocharging growth in our parks and experiences.

Before we dive deeper into our results, let me start by making a number of significant announcements that represent important and exciting steps forward.

First, we announced yesterday the full suite of ESPN's channels will now be available direct to consumer as part of a new joint venture with Fox and Warner Brothers Discovery to create a new streaming sports service, launching this fall. This brings together content from all of these companies' combined assets, including all the major professional sports leagues and college sports.

And in the fall of 2025, we'll be offering ESPN as a stand-alone streaming option with innovative digital features, creating a one-stop sports destination unlike anything available in the marketplace today. ESPN is also adding a sports icon to its lineup, with Coach Nick Saban joining the network as an on-air commentator later this year.

We're excited to share that in November, we will release a feature-length animated sequel to *Moana*, which joins a very robust lineup of upcoming theatrical releases.

We're also thrilled to share that we are entering into an exciting relationship with Epic Games, acquiring a small equity stake and launching a groundbreaking new games and entertainment universe that brings together Disney's beloved brands and franchises with the hugely popular Fortnite.

And I'm pleased to share that Disney's Board has declared an additional dividend, and we will be embarking on a $3 billion stock buyback program in fiscal '24.

Oh, and one more thing: next month Disney+ will become the exclusive streaming home of Taylor Swift's historic concert film, *Taylor Swift: The Eras Tour (Taylor's Version)*.

I'll be sharing more with you about these announcements momentarily, but what's clear is that the important transformation we undertook last year is bearing fruit. And looking at our results this quarter, we can say with confidence our strategy is working.

In Q1, segment operating income increased by 27% and adjusted earnings per share rose 23% compared to prior year.

We've improved our entertainment streaming operating income by a remarkable 86%, year over year, and remain poised to reach profitability in our combined streaming business by the end of fiscal '24, and build on our momentum to deliver significant, sustained profit margins in the future.

Disney's Experiences business generated all-time records in revenue, operating income, and operating margin. And we are on track to meet or exceed $7.5 billion in cost savings, as we continue to look for further efficiency opportunities across the company.

Diving deeper into our announcements, let's first talk about ESPN, which continues to deliver meaningfully for the company and will be a key value driver in the future.

ESPN's domestic sports business continues to grow, and even amid a challenging linear landscape, ESPN increased its overall audience in calendar year 2023, and it continues to break records in ratings. Ultimately, our mission is to make ESPN into the preeminent digital sports brand, reaching as many sports fans as possible and giving them even more ways to access the programming they love, in whatever way best suits their needs.

One way will be through the new streaming sports service coming this fall that we announced yesterday in conjunction with Fox and Warner Brothers Discovery. This service will bring together our collective portfolios of sports channels and direct-to-consumer services – on a non-exclusive basis – providing consumers with more of the sports they want in a single place.

It's important for us to serve the needs of consumers looking for a seamless way to access an aggregated collection of sports-centric content, including capturing fans moving away from the full cable and satellite bundle. And it’s an attractive business proposition for ESPN, allowing us to command per unit economics in line with established market rates for our sports content, just like we do with any streaming or linear service where we offer our programming.

Another exciting option available to sports fans will come in the fall of 2025, when we make the full suite of ESPN’s channels available as a stand-alone and highly interactive digital destination. Not only will consumers be able to stream their favorite live games and studio programming, they’ll also have access to engaging digital integrations like ESPN Bet and fantasy sports, e-commerce features, and a deep array of sports stats, all of which we know will be incredibly compelling to younger sports fans in particular. It will also have very robust personalization features.

ESPN has long prioritized its desire and ability to serve sports fans wherever they are, and these steps will strengthen ESPN’s ability to deliver on that promise. And as you know, we’ve also engaged in productive conversations with potential content and marketing partners for ESPN. We’ve made progress toward securing deals, and we expect to have more to share with you in the near future.

We’re excited to offer a more unified streaming experience, which we expect will deliver strong benefits in terms of higher engagement, lower churn, and greater advertising potential. When

we launch our stand-alone ESPN service, we will also make it available on Disney+ for bundle subscribers, just as we've done for Hulu.

We've already seen an incredible response to the beta launch of Hulu on Disney+, which has far exceeded every metric, and we are looking forward to the full launch next month.

This is all part of the ambitious streaming strategy we've been building. From our acquisition of 21st Century Fox that expanded our vast content library and strong pool of creative talent; to the launch of Disney+ as the home to a century of content; to securing full control of Hulu and expanding our streaming offerings to reach greater audiences; to our significant investments in technology; and now taking significant steps toward ESPN's streaming future.

Disney also has a great advertising story to tell, with unparalleled scale and very strong advertising technology, and our ad-supported Disney+ offering is off to a great start. We successfully expanded outside the U.S. with launches in EMEA and Canada, and grew to over 1,000 global advertisers in the first quarter – that's a 10-fold increase from launch.

More than anything, the success of our streaming services is a testament to the amazing content we create. With 6 of the top 10 most streamed movies across all streaming platforms in the U.S. in 2023, our best-in-class storytelling continues to entertain millions of people.

We received 27 Golden Globe nominations and won top prizes for FX's *The Bear* and Searchlight's *Poor Things*. At this year's Primetime Emmy Awards, we took home 37 wins – more than any other entertainment company – and we lead the industry with 20 nominations heading into the Oscars, which will air on March 10th on ABC.

We're also proud of our recent Disney branded programming successes. *Percy Jackson and the Olympians*, which premiered on both Disney+ and Hulu in December, has become a bona fide hit. Books from the series returned to the #1 slot on *The New York Times* Best Seller list, following the debut of the Disney+ series, and I'm thrilled to share that we just picked up a second season.

And the hit children's animated series *Bluey*, which is exclusive to the Disney Channel and Disney+ in the United States, was recently the #1 most-streamed show across any streaming platform.

Looking ahead, we have an exciting slate of originals coming to Disney+, including *Agatha* from Marvel Studios, *Skeleton Crew* and *The Acolyte* from Lucasfilm, *Win or Lose* from Pixar, and much more.

Additionally, later this month, Hulu will launch FX's highly anticipated saga *Shōgun* in the U.S. And in March, all seasons of *Grey's Anatomy* – our #1 streamed title globally – will join our extensive library of titles on Hulu. When the show returns next month for its 20th season, Hulu will be the only place to see the current and all previous seasons of this truly iconic series.

And speaking of icons, over the past year we've all witnessed the creative genius and sheer power of a true cultural phenomenon — Taylor Swift. When her blockbuster concert film debuts on Disney+ on March 15th, it will feature the concert in its entirety, including the song "cardigan" and four additional acoustic songs which were not in the theatrical or digital purchase release of the film. We know audiences are going to absolutely love the chance to relive the electrifying *Taylor Swift Eras Tour (Taylor's Version)*, whenever they want, on Disney+.

Turning to our film Studios, we have an incredibly robust slate of new releases as we continue revitalizing our creativity. Just consider the lineup of titles we will release through the end of 2026. This year we have *Kingdom of the Planet of the Apes*, *Inside Out 2, Deadpool 3, Alien: Romulus,* and *Mufasa: The Lion King.*

And as I mentioned at the top of the call, this November, we'll release a feature-length animated sequel to *Moana*. This was originally developed as a series, but we were impressed with what we saw, and we knew it deserved a theatrical release. The original *Moana* film from 2016 recently crossed 1 billion hours streamed on Disney+ and was the most streamed movie of 2023 on any platform in the U.S. Along with the live-action version of the original film that's currently in development, Moana remains an incredibly popular franchise, and we can't wait to give you more of Moana and Maui when *Moana 2* comes to theaters this November.

Looking to our 2025 theatrical slate, we're excited to bring audiences *Captain America: Brave New World, Fantastic Four,* Pixar's *Elio, Zootopia 2,* and *Avatar 3*, and we're already looking forward to 2026 and beyond with *Frozen 3*, the first *Toy Story* movie since 2019, and a new Star Wars movie that brings the Mandalorian and Grogu to the big screen for the very first time.

These films will not only reach global audiences in theaters, but as we've consistently demonstrated, they will become important anchors on our global streaming platforms, driving subscriptions and engagement, while also continuing to fuel growth in our Experiences businesses.

After all, one of the things that truly sets Disney apart is our unique ability to turn top quality IP into top quality experiences, leading to significant growth. That was certainly true this quarter. Every one of our Parks was profitable in Q1, giving us an incredibly solid foundation to build upon as we invest significantly to turbocharge growth in this business.

We've had a tremendous response from guests visiting our newly opened World of Frozen at Hong Kong Disneyland as well as our first-ever Zootopia land at Shanghai Disney Resort. And as I've said before, we also have so many untapped stories just waiting to be brought to life in our Parks across the globe as we continue to invest in this extraordinary business.

But it's not just our parks where we're creating new opportunities for consumers to engage with the characters and franchises they love. Our new relationship with Epic Games will create a transformational games and entertainment universe that integrates Disney's world-class storytelling into Epic's cultural phenomenon, Fortnite, enabling consumers to play, watch, create, and shop for both digital and physical goods.

This marks Disney's biggest entry ever into the world of video games and offers significant opportunities for growth and expansion. The new immersive universe will allow fans to unleash their own creativity and experience the Disney stories and worlds that they love in groundbreaking new ways.

Younger audiences, in particular, are huge consumers of video games. In fact, among Millennials, Gen Z, and Gen Alpha, a significant amount of time spent on screen-based platforms is playing video games. This new universe from Disney and Epic provides us with a tremendous opportunity to not only meet more consumers where they are, but to allow more audiences to cultivate a bond with Disney's iconic brands and franchises, including Marvel, Star Wars, and much more.

Looking at the renewed strength of our businesses this quarter – from Sports, to Entertainment, to Experiences – the stage is now set for significant growth and success. In that regard, we see

ample opportunity to increase shareholder returns as our earnings and free cash flow continue to grow.

Our current position of strength, and confidence in our path ahead, already led us to pay a dividend to our shareholders last month, and I'm pleased to share that the Board declared that our next semi-annual dividend, to be paid in July, will be 50% higher versus the last dividend paid in January. The Board has also authorized the company to begin repurchasing shares for the first time since fiscal 2018, and we plan to start by targeting $3 billion this fiscal year. As we continue to invest in our growth businesses and maintain our strong balance sheet, we also expect to prioritize dividend payments and share repurchases in the coming years.

I'm proud of our company's remarkable achievements and I'm grateful to a deep bench of seasoned executives who are helping guide Disney into the future. And that includes Hugh Johnston, our new CFO, who has already proven to be an outstanding addition to the team. We feel very fortunate to have Hugh with us.

And now to take you through more of our results this quarter, I'll turn things over to Hugh.

Hugh Johnston – *Chief Financial Officer, The Walt Disney Company*

Thanks, Bob.

I joined Disney a little over two months ago, and the more I learn about this incredible company, the more excited I am about the opportunities ahead of us. I am looking forward to continuing to partner with Bob and our management team as we execute on our strategy, with the goal of delivering significant, consistent long-term earnings and free cash flow growth.

We are very pleased with this quarter's financial results. Fiscal first quarter diluted earnings per share, excluding certain items, increased by 23% versus the prior year to $1.22, and segment operating margin increased by 350 basis points reflecting both strong pricing and operating expense reductions.

Both revenue and operating income at Direct-to-Consumer, Domestic ESPN and Experiences all increased versus the prior year, and operating income across each of our business segments grew nicely, in part due to the diligent and ongoing cost efficiency work we are driving throughout our businesses, as evidenced by the realization of over $500 million in SG&A and other operating expense savings across the enterprise in the first quarter.

Moving to our results by segment…

At Entertainment, first quarter operating income more than doubled, driven by significant improvement at Direct-to-Consumer.

Entertainment Direct-to-Consumer operating income improved by about $850 million versus the prior year and by nearly $300 million versus Q4. And revenue increased sequentially by over 10%, benefitting from higher subscription and advertising revenue. Operating income in the first quarter was better than the guidance the company gave in the last earnings call, primarily due to expense favorability.

Hulu subscribers increased by 1.2 million from Q4 to Q1, and Disney+ Core subscribers decreased sequentially by 1.3 million, in line with prior guidance, driven by the expected temporary uptick in churn given the recent domestic price increases as well as the end of the global summer promotion. Those impacts were partially offset by strong ad tier net adds, due to domestic growth as well as the launch in certain international markets in the first quarter.

Domestically, we saw continued net additions to our bundled offerings in Q1, which as a reminder have significantly lower churn versus our standalone products.

Disney+ Core ARPU increased by 14 cents versus the prior quarter and by $1.07 versus the prior year, driven primarily by price increases. We expect Disney+ Core ARPU to increase in the second quarter due to the continued benefit of price increases, which should only be partially offset by the impact of adding Charter's Spectrum TV Select subs to the Disney+ ad tier.

I'll note that we are being paid on all entitled Charter subs, which will also be a key driver of accelerated Disney+ Core sub growth in Q2. We expect net adds of between 5.5 and 6 million in the second quarter. Domestic net adds are expected to be in the 7.5 million range, driven by Charter entitlements, net of cannibalization.

And international core subs are expected to decrease modestly, reflecting changes to certain wholesale deals and slightly elevated churn impacts from price increases.

While subscriber growth will vary from quarter to quarter, we are confident in our prospects for ongoing sub growth over the longer term, driven by: the continued global strength of our content slate; advancing our paid sharing efforts; technology advances that are intended to improve our content promotion and discovery capabilities, drive up engagement and lower churn; the impact of making Hulu content available on Disney+ for bundle subs and continued adoption of the bundle domestically, which should both increase engagement and lower churn – a strategy we will repeat in Latin America this summer when we combine Disney+ and Star+; and our continued use of tiering, to provide subscribers with more choices.

As it relates to the opportunity we see on paid sharing, beginning this summer, Disney+ accounts suspected of improper sharing will be presented with new capabilities to allow their borrowers to start their own subscriptions. Later this calendar year, account holders who want to allow access to individuals from outside their household will be able to add them to their accounts for an additional fee.

While we are still in the early days and don’t expect notable benefits from these paid sharing initiatives until the back half of calendar 2024, we want to reach as large an audience as possible with our outstanding content, and we’re looking forward to rolling out this new functionality to improve the overall customer experience and grow our subscriber base.

For Q2, we are expecting revenue at Entertainment DTC to grow sequentially and anticipate that operating losses will be relatively in line with the first quarter. We still expect to reach profitability at our combined streaming businesses in Q4 of fiscal 2024 and have never been more confident about our path to creating a strong and sustainable streaming business – with growing subscribers over the long term and, ultimately, double digit operating margins – a business which we fully expect to be a key earnings growth driver for the company.

Moving on to Entertainment Linear Networks, the decrease in the first quarter operating income versus the prior year was due to lower advertising and affiliate revenues, partially offset by lower programming and production costs.

Lower domestic advertising revenue was driven primarily by lower impressions including from strike-related impacts, in addition to an adverse comparison to the prior year midterm-related political advertising at our owned stations.

Domestic entertainment affiliate revenue decreased by 5% in the first quarter versus the prior year, as a 5-point benefit from higher rates was more than offset by a 10-point decline from fewer subscribers. Adjusted for the non-carriage of certain networks at Charter as a result of our recent deal, the sub decline impact was closer to 7%.

Lower programming and production costs benefitted from strike-related impacts, and we also remain focused on driving ongoing cost efficiencies.

At Content Sales, Licensing and Other, results came in lower versus the prior year, and below the guidance we provided, due to the performance of theatrical titles in the quarter. We do not have any new key theatrical releases in Q2 due to production delays stemming from the strikes, and expect Content Sales, Licensing and Other operating income to come in roughly breakeven for the quarter.

Sports operating income improved versus the prior year due to strength at ESPN, partially offset by lower results at Star India, driven by higher rights costs from airing of the ICC Cricket World Cup.

At domestic ESPN, year over year growth was driven largely by a decrease in programming and production costs from the timing of College Football Playoff games.

Domestic affiliate revenue in Q1 was comparable to the prior year, as an increase of 6% from higher contractual rates was offset by a commensurate decrease from fewer subscribers.

ESPN domestic ad sales in the quarter were down 2% versus the prior year, but up mid-single digits when adjusted for various timing shifts and one-time impacts. The strength we are seeing gives us confidence that leaning into sports will continue to create value for our shareholders.

Second quarter to date, we are seeing continued healthy advertising demand in the sports marketplace, with domestic ESPN cash ad sales pacing up double-digit percentage points versus the prior year. The trend is still solid even when adjusted for the CFP timing shift of an additional game, as well as an extra NFL divisional game in Q2 of this year.

Our Experiences business posted strong Q1 results, with year over year operating income growth of 10% at Parks and Experiences and 4% at Consumer Products. Record setting results this quarter were primarily driven by our performance at Shanghai and Hong Kong theme parks; continued strength at Disney Cruise Line; and the success of *Marvel's Spider-Man 2* at our games business.

And segment margins expanded by over 50 basis points versus the prior year – an achievement delivered despite tough comparisons at Walt Disney World coming off its highly successful 50th anniversary celebration in the prior year, and significant cost pressures driven by wage increases.

We remain optimistic about the segment's continued top line and profit growth, notwithstanding the tough comps domestically in Q2, and we still expect robust OI growth at Experiences for the full year. We plan to invest approximately $60 billion into the business over the next ten years, of which approximately 70% is earmarked for incremental capacity-expanding investments around the globe, which we expect to generate attractive returns.

On a total company basis, as Bob mentioned earlier, we are still on pace to meet or exceed our $7.5 billion annualized cost target by the end of fiscal 2024. I'm pleased with how this is tracking so far; total expenses in Q1 were down 4% versus the prior year, and the efficiencies we've been realizing are a key contributor to that progress.

And we are also still on track to generate about $8 billion in free cash flow this fiscal year.

Putting all this together, we are confident in the progress we are making and the path it puts us on to become a strong cash generator and earnings compounder, starting in fiscal 2024. To that end, we expect full year fiscal 2024 earnings per share excluding certain items to increase by at least 20% versus 2023, to approximately $4.60.

You already heard from Bob about our updated plans for shareholder returns this year, and as he mentioned, we intend to continue investing in our growth businesses, while also maintaining a balanced and disciplined approach to capital allocation.

And with that, we are happy to take your questions.

Q&A transcript to follow

Forward-Looking Statements

Certain statements in this call may constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding our business or financial prospects, trends or outlook; earnings expectations and expected drivers; business plans or opportunities; demand pipeline; financial or performance estimates or expectations (including revenues, operating income, operating results, programming and production costs and cash content spend, capital expenditures and investments, profitability, margins and any guidance); future performance and growth; leadership decisions; plans, expectations or drivers of, as applicable, for direct-to-consumer profitability, advertising, revenue and subscriber growth and levels, pricing, product acceptance and enhancements, expansion, changes to subscription offerings, churn, engagement and margins; estimates of the financial impact of certain items, accounting treatment, events or circumstances; future adjusted EPS and free cash flow and funding sources; anticipated demand, timing, availability, pricing, utilization or nature of our offerings (including experiences and business openings, content within our products and services and content releases and distribution channel); business recovery; shareholder returns and capital allocation, including dividends or share repurchases; consumer and advertiser sentiment, behavior or demand; expected growth and drivers of performance or growth; cost reductions and source; available efficiencies; strategies and strategic priorities and opportunities; expected benefits of new initiatives, including for which definitive agreements have not been signed and may not be consummated or subject to regulatory approval or other conditions, and other strategic transactions; value of our intellectual property, content offerings, businesses and assets, including franchises and brands; and other statements that are not historical in nature. Any information that is not historical in nature included in this call is subject to change. 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, new or expanded business lines or cessation of certain operations), our execution of our business plans (including the content we create and IP we invest in, our pricing decisions, our cost structure and our management and other personnel decisions), our ability to quickly execute on cost rationalization while preserving revenue, the discovery of additional information or other business decisions, as well as from developments beyond the Company's control, including:

- the occurrence of subsequent events;
- deterioration in domestic and global economic conditions or a failure of conditions to improve as anticipated;
- deterioration in or pressures from competitive conditions, including competition to create or acquire content, competition for talent and competition for advertising revenue;
- consumer preferences and acceptance of our content, offerings, pricing model and price increases, and corresponding subscriber additions and churn, and the market for advertising sales on our DTC services and linear networks;
- health concerns and their impact on our businesses and productions;
- international, political or military developments;
- regulatory and legal developments;
- technological developments;
- labor markets and activities, including work stoppages;
- adverse weather conditions or natural disasters; and
- availability of content.

Such developments may further affect entertainment, travel and leisure businesses generally and may, among other things, affect (or further affect, as applicable):

- our operations, business plans or profitability, including direct-to-consumer profitability;
- demand for our products and services;
- the performance of the Company's content;
- our ability to create or obtain desirable content at or under the value we assign the content;
- the advertising market for programming;
- income tax expense; and
- performance of some or all Company businesses either directly or through their impact on those who distribute our products.

Additional factors are set forth in the Company's Annual Report on Form 10-K for the year ended September 30, 2023, including under the captions "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," and "Business," quarterly reports on Form 10-Q, including under the captions "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations," and subsequent filings with the Securities and Exchange Commission. The terms "Company," "we," and "our" are used above and in this call to refer collectively to the parent company and the subsidiaries through which our various businesses are actually conducted.