4th Annual MoffettNathanson Media & Communications Summit

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Disney Speaker:

Christine McCarthy

Senior Executive Vice President and Chief Financial Officer

PRESENTATION

Michael Nathanson – *Analyst, MoffettNathanson*

Thanks for being here. This is the kickoff of our 4th Annual Media & Communications Summit, and thank you all for the great support you've given us to start our business.

Today, I want to thank Christine McCarthy, the CFO and Executive Vice President of The Walt Disney Company. We really appreciate Christine being here, kicking it off as Disney did last year as well, so thanks for being here. We appreciate it.

Given next week's opening of *Pandora – The World of Avatar*, let's start with Theme Parks. You're about to open this new attraction at Orlando's Animal Kingdom and then two years later you're going to open two new Star Wars attractions in California and Florida. What have you seen historically when you add new attractions or lands?

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

Thanks, Michael. We couldn't be more excited about the opening of *Pandora – The World of Avatar*. It opens next week down in Orlando and it's been a project that's been in the works for a while and it's something we very much are looking forward to. One of the things that we look at is, every time we do a park expansion or a project in a park, it tends to be unique and driven by different things. Some of the elements of the things that we look for are pretty consistent: We look to make our park destinations must see destinations; we also look for projects that we believe can not only drive new attendance, but can drive increased attendance through repeat visitation; we also look at improving guest spending, and you'll see that in things like per caps; we also look at extending length of stay; and most importantly, we look at improving the guest experience because that's really key to getting repeat visitation for our consumers and guests to want to come back again and again.

So when we look at all of those, we believe that *Pandora*, which is a ten acre immersive land, and when I say immersive, you go in and you feel like you're in the world of *Pandora*. There are a couple of key E type ticket attractions, but in addition to that, you have dining, retail, entertainment, and merchandise that's themed to the land. So all of that comes together to make a very, very attractive and compelling experience.

Michael Nathanson – *Analyst, MoffettNathanson*

And then Star Wars?

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

Oh, and Star Wars and the other thing I'd like to mention on *Pandora,* so if you're looking for what does it do, and I think sometimes you look in the past and you say, what experience is analogous to it? And the one that's most analogous to it is in 2012, when we opened *Cars Land* at Disney California Adventure, very similar type of immersive experience. It went into a park and uplifted the park. We had an immediate increase in attendance and a lot of that attendance was very sustainable. What it also did in California Adventure is it balanced more of our load, our guest visitation, across the two parks. And we expect that same kind of phenomenon to be apparent with Disney's Animal Kingdom, that this will draw more people into Animal Kingdom and will better balance the load throughout Walt Disney World.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay.

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

So Star Wars lands, we also have those coming coming soon. In the Star Wars lands, we have two: there will be one in Anaheim, one in Orlando. They're 14 acres, and at 14 acres, they will be the largest, single themed additions to any park we've ever had. They, too, will be immersive and you will feel like you are in Star Wars. Once again, the same array of dining, retail, entertainment, merchandise, and also a lot of characters that'll be walking around so you will really feel like you're there. And there are a couple of attractions and there probably these two I'd like to mention because I think there's probably some Star Wars fans in the room. One of the attractions allows people to take control of the Millennium Falcon and the other puts you into a battle between the First Order and the Resistance. So these are things that people who love the Star Wars universe are really going to find compelling.

We believe that these will also drive significant increased attendance that we believe will be sustainable in both Hollywood Studios, where the Orlando Star Wars is going, as well as in Disneyland, where the Anaheim Star Wars is located.

Michael Nathanson – *Analyst, MoffettNathanson*

Is there an analogy? You gave us the analogy of the *Cars Land* analogy, which is really great for *Avatar*. Is there an analogy for the Star Wars expansion? Can you think of something that big that's been added?

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

I think you could think of it as that on steroids. Because the fan base is so significant and so loyal to the Star Wars universe, there will be people who probably have never been to one of our parks that this will bring them in.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. So a year ago, when Bob was here, he shared a pre opening video of the Shanghai Disney Resort. Now that's open, how's the park performed versus initial expectations?

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

Yes, I don't know how many of you were here last year and saw Bob's video, but if you did or if you've been to our park in Shanghai, I think you'll note that what we call authentically Disney and distinctly Chinese and the translation of that is you know that you're in a Disney park, but you also know that you're in China. So there are things about that park that are very unique to the park, but it also incorporates a lot of our Disney IP. When we look at how the park has performed to date, we couldn't be happier. It's performed above expectations and I think a lot of people in this room probably want to think about profitability, and two of the last three quarters so it would be our fiscal fourth quarter as well as its most recent quarter were profitable. And you'll see some seasonality for attendance in China that's related to just their school holidays and Chinese New Year. So fourth quarter, you'll have the peak holiday season and in second quarter you'll have Chinese New Year. So those will be the two highest attendance quarters.

When we think about some of the learnings and some of the things that we expected or surprised us, I wouldn't say there's anything that's a big there was nothing that was a big surprise, but one of the things was where the attendance was coming from so far. We had thought it would be more of a local Shanghainese population that would be visiting, and so far, two thirds of the visitors have been from outside of Shanghai. So we find that very encouraging because it makes the park not just a local Shanghai park, but something that's much more national in scope and desire to visit. That's also driven a very high occupancy level at our hotels, and in those hotels, we've been able to get above expectation ADRs and revenue. So those are all good things.

Michael Nathanson – *Analyst, MoffettNathanson*

Right. One of the questions we asked last year, and I think it was too early to find out, was how would the park leverage other parts of Disney's franchises? So what type of benefits you're seeing to maybe films Disney films in China? And CP sales in China due to the Parks business?

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

Yes, this is being in the park presence is significant in that it allows us to once again keep some of our franchises fresh in the minds of consumers. One film I just would like to point out that was released in China and did extremely well was *Zootopia*. It did $235 million at the Chinese box office. Those furry characters are extremely popular in China, and when you see our parades, they're very prominent. So this is something that really resonates with the Chinese guest. And that's just one example of understanding what they really like and what appeals to them and really making it alive and relevant.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Let me take you to something more near term, which is your last earnings call. You said on the last call that you expect Q3 Parks costs to increase meaningfully. Can you help us quantify the increase and discuss the drivers of what's happening in the current third quarter?

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

Sure. So in our Parks business, I think you've seen that we've made a lot of investments to drive growth and we've also been managing our expense growth. You've seen the combination of those two in the strong margin improvement the last few quarters. So when you look at the third quarter specifically, we do have both increases in underlying volume and new attractions that are coming online. With new attractions, we have expenses. Those expenses will be pre opening, operational, sales, and marketing. And three that are in this quarter are *Pandora*, as we've talked about. Also *Guardians of the Galaxy – Mission: BREAKOUT!,* which is in Anaheim. It's at Disney California Adventure, it is a totally reimagined *Tower of Terror* If you've been to Disneyland or DCA, you know that we have *Tower of Terror* it doesn't look like that anymore. It is a *Guardians of the Galaxy* attraction and it's coming very close to the opening of our *Guardians* movie, and this is another thing that we think will draw new guests in and have repeat visitation. The third new attraction that opened earlier this quarter was *Explorers Lodge* and that is our third hotel in Hong Kong, that's a 750 key themed hotel and that, too, came online so you have some expenses associated with that.

The third thing that is going to impact this quarter's growth is a full year of operation in Shanghai. So this is the first third quarter where you have a full quarter of operating expense.

And the last one I'd like to mention is we have an 18 day dry dock of the *Disney Fantasy*. *Disney Fantasy* was launched in 2012, so this is the first time it's going into dry dock.

So when you take all of those together, the growth year over year we expect to be high single digits to possibly low double digits in expense growth. I'd also note that some of the quite a few of these expenses are related to new attractions coming online, but you'll also have some things that will be recurring and that will be things like Shanghai, because Shanghai is up and operating.

Michael Nathanson – *Analyst, MoffettNathanson*

Right, okay. Thank you so let's turn to we're going through all the divisions, next is Studio. Over the past 3 years, Disney's film Studio, based on our math, sourced 60%, 6 0 percent, of the film industry's profitability. It's amazing. And the question that we have is it's a business that's always been historically known as risky, you can't guarantee success. So how have you been able to continue that success over three years in a tough industry? And how have you been able to make that happen both financially and creatively? So what's different about your past three year process maybe other people are not realizing?

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

Thank you for that question. Our Studio has been on a great run for the last three years, both creatively and financially. So there's a couple of things that distinguish our Studio from others and they are great IP and a sound strategy.

So some of the things I'd like to call out, when you look at our acquisitions that have been in the IP space and how they've impacted our Studio business. First was Pixar and all of these acquisitions I'm going to talk about, they are similar in many ways, but they also have some unique elements. The similarities are great IP; really good, creative talent; as well as strong management. But when we look at Pixar, we all know Pixar's track record, it's been great. And one of the things that we were able to get with that acquisition was also a really strong, creative management team in John Lasseter and Ed Catmull. And at the time we did the Pixar acquisition, our Disney Animation Disney Feature Animation wasn't performing up to the expectations that we had. So what we did was Ed Catmull and John Lasseter, in addition to running Pixar, also worked with the Disney Animation team and really reinvigorated their process. And over their period of time, they had increasing successes with their animated films and I'll just point to two recent ones and I think you'll agree that it has been successful: *Frozen* and I am drawing a blank *Zootopia*. *Frozen* and *Zootopia*, two extraordinarily successful movies and they're also Oscar winners. So when you look at the Pixar acquisition, it really, really, not just Pixar, but also reinvigorated our Disney Animation.

Touching for a moment on Marvel. Marvel's IP, we know that the library of characters is extraordinarily deep and many people know those characters through our films in the Marvel Cinematic Universe. And those are things that appeal to a wide they're four quadrant films, so they're not only male skewing, they also appeal to women and children and people of all ages and sizes. So that's another one.

And Lucas. Lucas, I think we can all agree, had what is probably one of the most iconic brands in film history in the Star Wars universe. And since we have acquired Lucasfilm, we've released two films: *The Force Awakens* back in December 2015, did extraordinarily well. I think it was the third all time best box office global on a global basis. And this past December, we released *Rogue One*. Coming December of 2017, we have *The Last Jedi*, which will be *Episode VIII*, and following that, we'll have *Han Solo*. So you'll see a series of Star Wars movies that'll work through our film release slate for many, many years to come.
So when you look at the acquisitions and the impact it's had on us, since the Pixar acquisition, we're including Pixar, Marvel, Lucas, and also the reinvigorated Disney Animation, we've released 33 films that have averaged $800 million in global box office. So when you look at it, that's what it's really done for our Studio.

Michael Nathanson – *Analyst, MoffettNathanson*

With also a low degree of failure rate because what blows you up in any given quarter is a bomb, right? And you've not had, from that catalog, very many problems getting your movies to a certain threshold in the box office.

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

Well, that's a good point. But no, we believe our strategy is very sound, but we also know that no studio is immune to a miss. So I don't want to say we're perfect, but we certainly try to be, but you just never know. We do our best. The strategy we have of creating branded, franchise films that are tentpoles is very important. And we've also reduced the number of films on an annual basis that we release. On average, it'll be about ten. So some years, it'll be more, some years it'll be less. This year, fiscal 2017, we have seven movies. In fiscal 2018, we plan to release 11 movies. So if you look at what is that ten movies composed of? In general, you'll see one to two Star Wars, two to three animated movies and they could be from both Pixar and Feature Animation, two to four Marvel movies. We do have four next year that are being released. And the balance will be filled in by Disney live action.

Now let me touch on Disney live action for a moment. Since 2014, we also changed our strategy for Disney live action and we're getting more and more towards reimagining Disney IP in the live action format. The first we've done seven[1] movies. The first one in 2014 was *Maleficent* and the most recent was *Beauty and the Beast*. And if you look at those films, they averaged $650 million at the box office, so that strategy of reimagining IP in a live action format has also worked very well for us.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Can you talk a bit this is a current debate that we have all the time. Can you talk about how you monetize your films through the various windows and discuss your thoughts on premium video on demand and whether or not it's going to happen?

[1] Should be six

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

Yes, there's been a lot of talk recently about premium video on demand, but let's just talk for a moment about the windows. The windows that we have are very similar to any studio. After release, the home entertainment window is typically first, and that'll be both physical as well as digital distribution of the film, followed on by VOD, and typically next is the pay TV window, followed by free TV. And in the free TV window, you also have sales to basic cable. So that's the kind of sequencing of the windows that's followed for most movies.

As it relates to premium VOD, because our strategy is releasing films that are tentpoles, they're branded, four quadrant tentpoles, many of our movies are seen as events. There's a lot of social media leading up to the releases, a lot of people get invested in the characters through our trailers, some of our trailers have been the most downloaded trailers, you've seen all those kinds of statistics recently. But when we release, we believe, and I believe our consumers believe, that our movies are best seen on a big screen. Definitely initially, and we'd like them to see it on the big screen two or three times. But because of that, we don't feel that we should be moving our movies off of the big screen any sooner than they currently are. So while premium VOD is probably a strategy that does work for other studios given their films and genres, for the kinds of films that we do, we don't believe we're not engaged in conversations on premium.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Turning to Consumer Products. Can you talk a bit about profit performance in the first half of the year and what do you expect for the rest of the year? So it's been a bit of a lagging category, I know. Even in the past three quarters or so, it has not been as consistent as it was, let's say, 2013 to 2015 or 2016. So what's happened and what do you expect for the rest of the year?

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

Sure. Great question, and I'd like a moment to step back and just talk about our Consumer Products business to put things in perspective. So if we go back to a four year period, 2013 to 2016, our Consumer Products business has doubled in operating income, talking from about $1 billion to $2 billion over that four year period. So I just want to this is a business that has grown very, very has had very strong growth over a four year period.

In the first half of this year, back in November, we said that our Consumer Products business was going to have a very, very tough comp to first quarter of 2016, the reason being we still had strong *Frozen* merchandise sales and we had the first Star Wars release that hit in the first quarter of 2016. In addition to Star Wars merchandise, we also had a licensed game by the name of *Battlefront*, so all of that was in our Consumer Products number. The first quarter of this year compared to first quarter of 2016, we were down 25% and we pretty much said we were going to be down over 20%.

So the first half comp has been very difficult and the growth for the year would be if it was year over year growth, it would be driven by the second half. Now while we expect very good, strong growth meaningful growth in both the third and the fourth quarter, that will come from merchandise sales related to two upcoming films *Cars 3*, which we'll release in June, and *Spider Man* in July. So right now, we're about, I don't know, six, seven weeks into the third quarter and where we are now I would say that we don't if we're just saying we don't believe that we could that second half, including the third and fourth quarter will it may not be sufficient to have growth for the full year so it's just that the first half was tough. Second quarter half will be good with strong growth in three and four, but it may not be sufficient for full year growth.

Michael Nathanson – *Analyst, MoffettNathanson*

And on that point, how important are new film releases to driving growth in CP in any given year? Given what you have coming in 2018 and 2019, what should we take away from the pipeline? And how important is that to the overall growth of CP?

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

Well, film releases are they have been important to the growth especially when you look at some of the content that has come through acquisitions with Marvel and with Lucas, with Star Wars. Any given year can be impacted by a film release, but our underlying franchises, we have eleven franchises that generate over $1 billion in retail sales, and among the strongest, the largest are actually Mickey and Disney standard characters. So this is a business that has a very strong base of IP, and on top of that, we have film releases, which add to the franchises. And when you look at these franchises, Disney has a unique way of monetizing and distributing our content throughout our company across the world and we're able to keep these franchises alive for a long period of time, and that's unique to Disney.

Michael Nathanson – *Analyst, MoffettNathanson*

And you know what, it's funny, *Frozen* was a surprise in terms of *Frozen* was I remember when *Frozen* came and all of a sudden the CP followed. So *Frozen* is coming in 2019. It's going to need a different it has to be a different sequence this time around because people anticipate *Frozen* at retail.

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

Sure. *Frozen* there are a couple of things that are upcoming for *Frozen*. First, *Frozen* is one of those franchises that is very appealing to young children. They love the music, and if any of you have children, you have probably heard those songs many, many times. But we have a stage play coming in 2018 to Broadway, and in 2019 there will be a sequel to *Frozen*.

So people are anticipating that, but we can keep *Frozen* alive in our Theme Parks, not only the stories and not only at retail, but in our Theme Parks, on our channels. And when the movie comes in the movie comes out, people haven't forgotten about it, so and that'll be a six year window between the original and the sequel.

Michael Nathanson – *Analyst, MoffettNathanson*

And movie's in the fourth the calendar fourth quarter, it's a Christmas quarter?

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

Yes.

Michael Nathanson – *Analyst, MoffettNathanson*

I have more, but I have to remind everyone, we do take questions and Tracy in about 10 minutes will collect 15 minutes will collect questions from the audience and I'll ask Christine a question, so if people want to write questions in 10 to 15 minutes, we'll collect them.

This is not a news flash to anyone in this room that brick and mortar retail is struggling as e commerce grows. How does Disney weather that trend? And how are those stores positioned to succeed going forward given the retail footprint?

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

Yes, this is not a news flash is right. I think anyone who follows consumer trends and retail sales has seen that. Physical retail, call it brick and mortar, call it physical retail, is challenged just with changing consumer consumption habits. Our global footprint for our Stores business is 350 stores. That is that has been, over the last decade, the store count has reduced by 30% and it's actually down more than 50% since 2000 when we had our peak store count. We look at optimizing our footprint, rationalizing the way we're addressing this business, looking at how we're designing our stores to make them a compelling consumer experience, to have people want to come in. In general, our stores are smaller than they used to be and not only are they smaller, but they have new IP, incremental IP, that was picked up with acquisitions. So store the way the stores are laid out is different than they were a decade ago. And we also, when you look at our stores, the locations of them, keep our franchises and our name in front of consumers. So you can't people can't go to a Disney park every day, every week, every month, but if you're in a location and your kids or you are big Disney fans, you can go to a store and you're kind of surrounded by the IP and the franchises. So while we still rationalize and address this business on a physical basis, we are also investing more in e commerce and really looking at the direct to consumer channels.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay, let's go to the Media Networks, we'll go to what everyone wants to talk about. You've always said and Bob's always said and people in the first row have always said the company likes its hand with ESPN. So what do you see that gives you that confidence to keep saying we like our hand at ESPN?

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

Well, Michael, I am so glad you asked that question because it's such a long while since anyone else asked us a question on ESPN. So yes, ESPN is a business that we believe is attractive. We have compelling product. We are competitively advantaged. It is a business that we believe live sports has never been stronger and live sports are now being viewed on ESPN through TV, mobile, over the top, digital, audio, and through streaming more than ever before. And some of the recent successes that we've had in live events, and I'm talking really recent, is the NBA Playoffs, they're on right now and I'm glad to say my hometown team is still in the playoff, guess which one that is.

Michael Nathanson – *Analyst, MoffettNathanson*

Knicks.

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

No.

Michael Nathanson – *Analyst, MoffettNathanson*

Joking. I'm joking, joking

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

No, it would be the Boston Celtics.

Michael Nathanson – *Analyst, MoffettNathanson*

Boston Celtics.

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

But the NBA Playoffs, also the recent NFL Draft was very had very strong ratings. And we're in the current MLB season and we're getting good ratings out of Major League Baseball. So when you look at those, we believe that that's compelling content that people want to see. And in fact, in the first calendar quarter, the ESPN[2] audience on a year over year basis was up 15% and when you include out of home viewing and WatchESPN viewership, that added another 10% lift to their audience. So those things I think you would agree that live sports is something that viewers are going to come and view on ESPN. We also, and I know there's been a lot spoken about this, but we believe we have the sports that people want to see. So when you look at

[2] primetime

national the important national sports rights, we have more of those rights than all other sports media combined. And we do have some of those sports that we consider most important NFL, NBA, and MLB and really coveted college sports into the next decade and we believe that that is a competitive advantage.

Michael Nathanson – *Analyst, MoffettNathanson*

One of the things you've said for a few years is there's going to be more virtual MVPDs. So now we've seen the explosion in virtual MVPDs. Can you talk a bit about how Disney's networks fare relative to the traditional distributor world and the virtual world?

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

Sure. Now I think remind me to answer that question, but let me first say that our network, our brand, consumer demand makes our networks compelling to put on these platforms. ESPN was not in some of the early skinny packages, but it is in the digital platforms: Sling, Sony Vue, DIRECTV Now, YouTubeTV, as well as Hulu. We are encouraged by what we see in those in the adoption of those new platforms. I think it's fair to say these are nascent offerings. Many of these have come out in the last year and two have come out, both YouTube and Hulu, have come out in the last six, eight weeks. Hulu just came out earlier this month, the first week in May. So we're very encouraged by what we see there and but once again, we're very bullish on the long term, but you do have to have some time to allow for consumer adoption.

When you look at on a per sub basis, being on these platforms is as good for us as it is on the traditional. So we don't so we view these as being great offerings that are important to us, as profitable for us. And what we like about these new platforms is they are user friendly. The interfaces keep getting better and better. They're also mobile. And Bob Iger has talked a lot about the necessity for these platforms to be all of the three: user friendly, great interface, and mobile friendly. And when you combine those attributes with a lower price point, we believe that provides a very attractive alternative for consumers. So we're very bullish on this in the long run and we're still in the early days.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. So over the many years I've covered your company, it's always been easier to be bearish on ESPN's value to distributors when you're out of an affiliate renewal cycle, right, so that's where we just debate the value of the future of ESPN. So when will the next refresh cycle start on the affiliate fee side?

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

So I think some of you know that we have a small renewal that will be at the end of this fiscal year, our fiscal year ends September 30. So at the end of the fiscal year, we have a small renewal. That will start the renewal cycle. That renewal cycle will take a handful of years to work through the system. And when we look at what's important to us, we're not going to give you all the strategy that we have, but what's important to us when we look at these are not only the rates that our networks get, but how our rates how our networks are put on these platforms, and also it's really important to understand what the full entertainment experience is, what is the distributor going to provide to the consumer.

So we think all of those are very important, but those are just very high level details, and there's a myriad of options and alternatives and things that are part of the negotiating strategy. And while I like you very much, Michael, and everyone in this room, we don't think now is the right time to talk about our negotiating strategy for these, but they are coming up.

Michael Nathanson – *Analyst, MoffettNathanson*

We're providing guidance into the future.

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

Good try, but no.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. In the last rounds, you launched the SEC Network and you established WatchESPN as a paid service. What other products do you see? I know ACC is a network that is coming to the fore possible coming to the forefront, so how big can ACC be? Or is ACC one of the products you're trying to establish along the way?

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

Well, I think during these ACC has not yet launched, but it's coming up. During this round of negotiations, they'll try to get the negotiating, so we'll try to get full distribution as we did with the SEC Network.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. If there was a legitimate concern about ESPN, it's on the changing consumer consumption patterns of sports news. So what are you doing at ESPN to shift this business model to deal with this trend of how all of us now get Boston Celtics news on our phones the moment it happens?

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

It's a great question and I don't I don't think it's something that anyone hasn't already been thinking about. So news and information for sports, consumers have changed the way they consume it. And I have a prop, so this is used a lot for news and information. So mobile phones, mobile devices are used a lot for news and information. ESPN has been a leader in mobile and they've done they've created very innovative projects products through their digital platform. They have continued to do things like rationalize their apps, combine their apps, look at engagement through their interface, through personalization, customization, use of video that's key for sports fans and that is all what they have been working on, and increasing their integration across all of their platforms. So news and information is something that is changing and ESPN has been addressing that change for several years now.

Another thing I just want to talk about is *SportsCenter*. So there's been an awful lot of talk about *SportsCenter* and one of the things that we've done, and it really started about 18 months ago, is we've looked at personality branded personality driven segments of *SportsCenter*. So 18 months ago, we launched Scott Van Pelt at the 12 midnight hour, and since that time, his show has done very well. And in fact, it's the #1 show in his timeslot for males 18 to 34, and that's competing against some late night TV. So that's a very appealing demographic. We've also recently launched in the 6 p.m. hour a personality driven show with Michael Smith and Jemele Hill. And just yesterday, we announced at the Upfront ESPN's Upfront that Sage Steele will be going to Bristol and doing the morning *SportsCenter*, 7 to 10, and we'll also have what we believe is a really good 11 p.m. *SportsCenter* that will have rotating anchors with some of our four best known anchors, including the very engaging and sometimes irreverent Kenny Mayne, so he'll be part of that. And that's the lead in to Scott Van Pelt. So we are addressing *SportsCenter* and really changing it from news and information to more personality driven segments.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Tracy, you want to collect them? I'll keep asking questions.

Since you've been CFO, you really stepped up the buyback efforts of the company. So how do you balance the need to invest in internal growth versus the return of capital to shareholders?

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

Sure. You know, since I've been CFO, our capital strategy has not changed. Before I was fortunate enough to be the CFO of Disney, I was Treasurer for 15 years. So I was very involved in our capital allocation strategy as well as the execution of it. So we haven't changed that. We've always taken a very disciplined and measured approach to capital, and first and foremost, our priority is to invest in our businesses. It's investing in businesses where it's investing for growth and also new initiatives in some of those businesses that we believe can also not only drive growth, but drive strong returns. So that's first and foremost. We also have, over the years, executed upon a very disciplined M&A strategy, that's also been part of our growth, and I think you see with the acquisitions of Pixar, Marvel, Lucas, that those have been very successful and very well integrated into the company.

So when you look at the strength of our balance sheet, which is strong, we've also been able to consistently return capital to shareholders and we've done that through not only buybacks, but also dividends and this is something that we view as a strength of the company. And just last week, we announced that we were going to increase our fiscal 2017 share repurchase, which we had given sort of an expectation of it, would be in the $7 billion to $8 billion range, that it will now be in the $9 billion to $10 billion range. And that, once again, just reinforces our confidence in our company as well as our long term future.

Michael Nathanson – *Analyst, MoffettNathanson*

Yes, as a former Treasurer, I don't know if you agree, but the company to us looks very under levered. So given the stability of your cash flows, why not raise your debt level to something more in line with the rest of the media sector?

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

Well, that's a good question and other people have brought it up from time to time. We do generate a lot of cash, Michael, and we do have a very strong balance sheet. We consider our balance sheet and our financial strength to be not just a financial not just a strategic asset, but also a financial asset. And we are we have less leverage than the other media and entertainment companies, and that's really reflected when you look at the ratings differential in our company versus the other media companies.

When we go to the capital the fixed income capital markets to raise debt, the fixed income market really looks at our peer group as being the large global branded companies. So we're not competing against the media sector. We're really competing against global branded company names. So that's just another differential.

When we think about our balance sheet overall, we think about it providing flexibility, financial flexibility. We have been able to make long term investments, a commitment on our own balance sheet without structured financing too, but on our own balance sheet and we've been able to do that through cycles. And so some of those projects that we had that began before the financial crisis, we were able to continue those projects. We didn't have to slow down. We just continued and completed them on our scheduled timeframe. So that's very important.

We're also able to when we do go to market, we're able to raise debt at very attractive levels and we also, and I'll just quote one of the rating agencies that recently upgraded us, we have exceptional liquidity. And what's great about our liquidity is that that has also served us very well during periods of market stress. So hopefully, we won't have to deal with things like we did a few years ago with the financial crisis, but we believe that we'll still have the same experience we did back then.

Michael Nathanson – *Analyst, MoffettNathanson*

And you guys don't take film financing, that's one of your differences. You don't have to go to third parties for film financing, so you own all your IP and you don't share outside with anyone.

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

Correct, correct.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. So I have some questions from the room. How important are global digital rights when negotiating TV contracts with the major U.S. sports leagues? So you only get the U.S. rights, I know with the NFL you've got some global rights, the NBA also. So could you give us a sense of how, perhaps, the global rights opportunities is now impacting your interest in negotiating new deals?

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

Yes. When you look at sports rights, ESPN is primarily a domestic U.S. business. The other part of the world where they have a significant presence and significant sports rights is in Latin America and we have various channels down there that are better targeted towards the key sports, one of which we all know is football or soccer, but also baseball there are other things that are down there. But Latin America and then we have some license deals in other parts of the world. We have a deal in China, Tencent with Tencent and they've recently done other deals in Africa and in various locations, but we are primarily a U.S. sports company.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. And this, will Disney ever consider bidding for digital sports rights instead of traditional airing rights, so I think recently was that UEFA Champions League. So with BAMTech in the background, how does the interest in digital rights appear to you with BAMTech developing soon?

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

Sure, BAMTech was an investment we should probably give a mention. So I think it was about a year ago, looking yes, about a year ago, last August. We made an investment of $1 billion for about a 30 1/3 of BAMTech and we do have the ability to increase ownership over time and they will be launching a branded ESPN offering later this year, but they will be we're not going to compete against them for digital sports rights, but that's certainly a possibility that we would be a participant as the current third owner in those. The world's changing and ESPN, when I look at sports rights and when either we're looking at renewals and renegotiations or things that are out in the marketplace, they'll consider all things and they'll look at the current environment and make the right decision.

Michael Nathanson – *Analyst, MoffettNathanson*

You had a question that we get and I'm sure you hear this all the time is why would it make sense to separate ABC, ESPN from Disney assets? Some people think it makes sense, so

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

There must be an investment banker in the room. That's something that's talked about. We have a fiduciary responsibility to look at things for shareholders. And we are very deliberate and we look at a lot of things and I think it's fair to say that we look at our businesses. We like the hand we have now, but we continue to look at our array of businesses and do what we believe is in the long term best interest of shareholders.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay, ABC TV Studio yesterday was their Upfront. How do you balance selling outside to other networks versus only acquiring your ABC Studio content for ABC? And maybe turning around, how much of ABC's content is coming from ABC's own production company?

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

So ABC both ESPN and ABC had their Upfront yesterday. ABC Studios is our in house production studio and I think over 60 maybe most of the over 60% of the shows that we picked up this year were ABC Studio shows, and I believe we have a piece of every show. We made some co produced shows in our new slate, but we have a piece in all of those. We produce shows and depending on our slate, when they put together the slate for the week, when they look at whether it's a comedy, whether it's a drama, whether it fits in the schedule, our entertainment people will make a decision whether or not it makes sense and also for the viewership that we have, if it makes sense for our viewers. With some shows that we produce, we own them, but they actually do quite well on other networks. One example that's been, for several years, on the air is *Criminal Minds*. That's a very successful show for CBS, but we own it. So that's just one example and there are a few shows that we'll produce this year that other networks picked up, but we do get first look and we'll make the decision if we think it's right for our network and right for the schedule that we are putting out to the marketplace.

Michael Nathanson – *Analyst, MoffettNathanson*

Going back to virtual bundles, you expressed confidence that these will be quite positive for revenues in the industry going forward. Now that YouTube and Hulu have been in the market for one to two months, have they been sufficient to reverse the acceleration? Or is it too early and it's not known? And perhaps your visibility is not you guys are not up to the so you want to talk a little bit about how much you see and how quickly it's helping?

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

I think the question is really, do you believe that the adoption of the digital MVPDs will be sufficient to offset the loss of traditional cable, that's the basic question. I would say we certainly hope so, but these are these just came to market. They just came to market. People are going to I'm sure they're going to talk about them, they're going to go online, they're going to talk to friends, do you like it, what do you like about it, what do you not like about it. I think it's really too early to tell, but we have seen good adoption, initial adoption, early, early days, and when you have these digital MVPDs, you've got to look at the adoption and also you have to look at the churn, and we're hoping that these new products are compelling enough for those who choose to use them that they will keep them and the trend will be down and the adoption will continue to rise. They are a lower price point so we believe that they will appeal to people that may not have traditional cable, they may be young, they may be getting out of school, they may have just moved out from their parents and they may look it this as a good alternative. So I think we are optimistic, but we're also realists and time will tell.

Michael Nathanson – *Analyst, MoffettNathanson*

And this is a follow up question. On the last call, all calls really, the company has always been very open about what you're seeing in the business, right? And you invested into BAMTech and you've been behind virtual MVPDs. Is there a Plan B is there a Plan B? Or is this is there another plan? People wanted to know if the trends don't stabilize. Or is this the Plan B to what was used to be Plan A, which was the business is the business?

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

Boy, that's a complicated question. Look, I think where we are now in this cycle, these digital MVPDs have just been launched. And I suggest – I mean, I came out of the banking industry for many years and I remember way back when ATMs came on and people were kind of afraid, and over time, I think everybody uses an ATM now. Adoption will occur and I think it'll occur much faster because people are a lot more tech savvy. They know how to download things. They're going to sample, a lot of millennials love to sample things.

So I think right now, where we are in the evolution of the media business, the digital MVPDs, we'll see how they work. Now something else may come, I don't know what that'll be. If there was a magic holy grail someplace, I think we'd all be jumping on horses and going to the pilgrimage. But we don't know and I think we are very we have great minds and people thinking about this. It's a topic we think about daily and we'll see how these work and I'm sure that there will be iterations and modifications that'll come to the market. But right now, I'd say give them a chance, the digital MVPDs.

Michael Nathanson – *Analyst, MoffettNathanson*

Right. And I would say, last question to wrap it up, is when you allocate your capital, your allocation of capital has produced pretty good returns away from the Media Networks business, right? So there's been a long term strategy to invest behind the whole Disney balance sheet and the whole Disney operating divisions, just around, and not only around Media Networks, right?

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

Oh sure.

Michael Nathanson – *Analyst, MoffettNathanson*

So the ROIC improvement at Disney is coming away from the other businesses are kicking in much more higher incremental ROIC.

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

Oh, yes. I think, in closing, our businesses, when you look at our Studio business, our Consumer Products business, our Theme Parks business, they are all very strong. There is a linkage between all those businesses that's IP related. And once again, when you think about what makes Disney unique versus other companies in the media and entertainment world, it's the fact that we can take our IP and we can use it, monetize it, keep it alive, keep the franchises alive through that whole Disney ecosystem. So when you look at that, that has really resulted in improved and very, I would say, very attractive levels of return on capital.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Christine, thank you. Thank you all. We appreciate the support. And we know there's two coming up after this, so thank you very much.

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

Thank you.

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Forward-Looking Statements:

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

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

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

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

Additional factors are set forth in the Company's Annual Report on Form 10 K for the year ended October 1, 2016 and in subsequent reports on Form 10 Q under Item 1A, "Risk Factors".

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