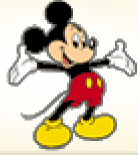

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Q4 and Full Year FY06 Earnings Call

NOVEMBER 9, 2006

Disney Speakers:

Bob Iger
President and Chief Executive Officer

Tom Staggs
Senior Executive Vice-President and CFO

moderated by,

Teri Klein
Vice President, Investor Relations

PRESENTATION

OPERATOR

Good day, ladies and gentlemen, and welcome to the fiscal full year and fourth quarter 2006 Walt Disney earnings conference call. My name is Angela, and I'll be your coordinator for today. [OPERATOR INSTRUCTIONS]. And now, I would like to turn the presentation over to your host for today's conference, Ms. Teri Klein, Vice President, Investor Relations. Please proceed, ma'am.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Thank you. Hi, everyone and thank you for joining us. A quick note that for your convenience, our Investor Relations website will provide not only a replay of this call but also an MP3 file and an archived written transcript of today's remarks. Here with us in Burbank are Bob Iger, Disney's President and Chief Executive Officer, and Tom Staggs, Senior Executive Vice President and Chief Financial Officer. Bob will lead off followed by Tom and then we'll open up the call to you for Q & A, so let me turn the call over to Bob and we'll get started.

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

Thank you, Teri, and good afternoon. I'm pleased to report that we have had a great year by just about every measure. We posted record revenues, record net income, record cash flow and record operating income for our 2006 fiscal year, bolstered by a strong fourth quarter performance. In doing so we delivered our fourth straight year of double digit earnings growth and continued to improve capital returns.

Our performance is a tribute to a flourishing culture of creative excellence and a clear strategy executed by our strong Management team. The creation of high quality content, the use of technology to expand consumer access, and a focus on growing in international markets forms the core of our strategy. We are also building a portfolio of digital assets to enhance and expand Disney's creative offerings. Our goal is to connect more directly with consumers and to have them connect more directly to us, and we are investing in new platforms, making new alliances and pursuing new opportunities.

We believe our overall strategy can create a self- reinforcing cycle that produces great returns. Key franchises, both new and traditional, appear and reappear across different businesses, platforms, and markets, all along growing in new audiences of multiple generations.

This was patently clear this year with the performance of *Pirates of the Caribbean: Dead Man's Chest* and all its ancillary businesses, from video games to books and Halloween costumes. In terms of global box office, *Pirates* is the number one movie of the year and the third biggest in history, crossing the $1 billion mark. We expect the DVD and downloadable version available in time for Christmas, as well as *Pirates 3*, which opens

May 25th, and a soon to be launched *Pirates* online multi player game to be successful additions towards becoming one of our biggest cross platform franchises.

While we are proud of our ability to build on an existing franchise like *Pirates*, we're equally enthusiastic about the long term prospects for some of our new creative properties, particularly at Disney Channel. *High School Musical* has set global performance records across multiple categories, including Billboard's best selling record of the year, the top selling TV home video release of 2006, and believe it or not, a New York Times Best Seller. We expect *High School Musical* to assert itself as an even more powerful presence in the coming year. There is a sequel movie, a national concert tour, thousands of licensed play performances in schools and drama clubs across the country, and a new merchandise line.

We're also impressed with the momentum of *Hannah Montana*, a hit Disney Channel show which yielded the first ever TV show soundtrack to debut at Number one on the Billboard Hot 200, where it remains for a second week. Alongside these newcomers, some of our most beloved characters have also been retaining their vigor. Mickey is starring in *Mickey Mouse Clubhouse*, the top cable show among 2-5 year olds, and in *Kingdom Hearts Two*, one of the year's biggest selling video games. *The Little Mermaid* is also capturing the imagination of a new generation and since its October 3rd debut, some 6 million units of the limited release DVD has been sold and we believe sales could exceed 10 million units worldwide.

Since we made our movies available on the Apple platform in mid September, almost half a million have been downloaded. This underlines the strength and uniqueness of our film library and indicates there is a consumer appetite for movie downloads that complements demand for DVDs. We're also pleased with the Pixar integration. It has spurred tremendous creative energy at the Disney Animation Studios and brought into our Company a wealth of talent and exciting new Pixar projects. I am sure that those of you who have already seen the trailer for next summer's *Ratatouille* can see why we think it will enthrall kids and adults alike.

Speaking of Pixar, over 5 million *Cars* DVDs were sold in their first two days in stores, putting the DVD on track to be the industry's 2006 biggest seller in the U.S. *Cars* is already the number one animated movie of the year and the number two film in the domestic box office and we expect to see a holiday boost for *Cars* merchandise, which has been one of our biggest lines of the year with retail sales around $1 billion.

At Parks and Resorts, we're coming off a highly successful 50th Anniversary Celebration and we expect continued strong attendance supported by several exciting new attractions. These include *Expedition Everest* at Animal Kingdom and the *Finding Nemo Submarine Voyage* at Disneyland, which opens next summer. We're also encouraged by the enthusiastic early reaction to the *Year of a Million Dreams* campaign. At the same time, we're leveraging the creative skills and operational expertise of our Parks and Resorts team to expand new lines of related businesses and into new territories.

Interactive game publishing is another area in which we are bringing to life existing characters and developing new content that crosses multiple business lines, and we see tremendous opportunity in the fact that kids and tween games account for about half of the $17 billion annual video game market. Our *Kingdom Hearts* game franchise alone has sold over 10 million copies globally, and we are increasing investment over the next several years to publish our own titles, the majority of which will be Disney branded. The emphasis on great content and innovative application of technology at our Media Networks is both enhancing the consumer experience and allowing us to reach more people more often. Over the last year, approximately 85 million of our TV shows, movies, and shorts have been played or downloaded on iTunes, DisneyChannel.com and ABC.com. At the same time, both networks, ABC and Disney Channel, have seen ratings increases.

By airing three of the top five shows on network television, ABC won the first six weeks of primetime in adults 18 to 49, the key sales demographic, marking its most competitive start to any TV season in nearly 30 years, and achieving the best season start of any broadcast network in seven years. ABC has retained its number one status on Sunday nights with the pairing of *Desperate Housewives* and our new success, *Brothers & Sisters*. By moving *Grey's Anatomy* and adding new hit *Ugly Betty* to Thursdays, ABC ratings have jumped more than 150% among adults 18-49 on the night over the comparable point last season. In addition, approximately 12 million ABC TV programs have been purchased since October 2005 via iTunes downloads. Viewers are also able to watch six of our primetime shows for free on advertiser supported ABC.com, starting the day after they air on the network. There have been almost 19 million requests for these episodes since we made them available just six weeks ago.

The multiplatform strategy is reaching viewers in new ways at our cable networks as well, and in the fourth quarter, Disney Channel posted its highest ever ratings for total day and for primetime with kids 6-11 and tweens 9-14, highlighting our strong slate of original programs, many of which have crossed over to other platforms like music and

merchandising. Since June, 53 million shows have been played at DisneyChannel.com, again illustrating that TV viewing and web use can reinforce rather than cannibalize each other when you have a terrific product.

ESPN has evolved into a massive multimedia machine with *Monday Night Football* achieving all-time household audience records on cable. On October 23rd alone, 11.8 million households watched the New York Giants beat the Dallas Cowboys. ESPN led ratings for ad supported cable last month with an average 3.5 million primetime viewers and a grip on all key male demos. Its success has also sent a surge of viewers to ESPN.com, and for the first eight weeks of *Monday Night Football*, we have averaged over 27 million page views each game day.

Our efforts to harness digital technology on behalf of consumers has prompted substantial ongoing upgrades of the ESPN.com and ABC.com sites and we will take another big step forward early next year by launching an all new Disney.com, already a premier family destination on the web. Families will be able to enjoy a wide range of Disney content from shows to movies and games in a safe and friendly environment, and parents will be able to do everything from arrange a family getaway at one of our parks or on one of our cruise ships, to purchasing Disney products. For kids it will be the ultimate in customizable web networks where they can watch their favorite Disney shows, play new interactive online games like *Pirates*, chat with their friends and swap music play lists.

The third element of our growth strategy is global expansion. In emerging markets where disposable income is rising and mass communications infrastructure is growing, we made forceful strides last year to strengthen our market presence, particularly in India and China. Hong Kong Disneyland is our anchor in China and earlier this year, the highly successful theatrical run of *The Lion King* introduced Disney to a whole new audience in Shanghai. In addition, we're focusing on retail merchandising through the licensing of thousands of Disney corners at big box stores and through the fast growing mobile entertainment sector.

To expand in India, we acquired a local kid's channel, Hungama. Disney channels reach 30 million households and hold the largest share of the children's TV market. We also recently signed a distribution deal for our Consumer Products line.

Finally I'd like to emphasize our continued commitment to financial discipline. Our improved return on invested capital is a direct result of combining creative excellence with a sharp focus on bottom line results. Our emphasis on creative excellence serving

the consumer and improving the environment at Disney had other benefits this past year as well. In October, *Business Week* named Disney as the number one company for new college graduates to launch a career. We also recently announced that we are putting our brand and characters to work in favor of healthier food options for kids at our Parks and in our licensed Consumer Products here in the United States. In the coming months, we look forward to rolling out that initiative globally as well. So we've made great progress in fulfilling the pledge made last year that Disney would be admired for its performance, for the quality and integrity of our products and people, and for being modern, innovative, and willing to take intelligent risks.

We look forward to building on that pledge in 2007, and with that, I'd like to turn the call over to Tom Staggs to provide more detail on the quarter and the year.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Thank you, Bob.

We began our 2006 fiscal year with a set of high goals and performance expectations, and it's a pleasure to report that we've exceeded them across-the-board. We've discussed in the past that we use three key financial metrics in assessing our overall performance, and as a means of gauging how well our strategic initiatives are translating into delivering value to our shareholders. They are earnings per share, ROIC and after-tax cash flow. In 2006, we delivered earnings per share growth of 34%. We boosted return on invested capital for the fourth year in a row and we delivered record after-tax cash flow from operations of over $6 billion and record after-tax free cash flow of over $4.7 billion.

Creative success and innovation, especially around branded products with franchise potential, are the critical factors that drive our Company's performance. The huge success of *Pirates of the Caribbean*, *Narnia* and *Cars* were obviously the highlights of our year at the Studio and we expect each of these properties to have a positive effect on our Company for years to come. At our live action business, we've reduced our overall investment levels and sharpened our focus on a smaller number of releases. In Feature Animation, the incorporation of Pixar adds to our already unparalleled library of animated content. At home video, greater efficiency in our marketing and distribution drove improved results for both the quarter and the year.

At our Media Networks, ESPN delivered double-digit growth in both revenue and operating profit for the fourth quarter and for the year. ESPN's ratings were up by 22% in households for total day and 20% for primetime in Q4, led by the success of *Monday Night Football*, which is generating significant ratings gains and double-digit CPM increases versus last year's Sunday night games. In the fourth quarter, we also recognized $87 million more in deferred affiliate revenues at ESPN than we did in Q4 last year.

Our Media Networks results were dampened somewhat in the fourth quarter, largely because of launch costs for Disney Mobile and a $32 million impairment charge for FCC licenses primarily associated with our ESPN radio stations. However, for the year, ABC's rating success led to substantial growth and operating income at the network, making it the biggest contributor to Broadcasting's 31% growth in 2006.

We're seeing solid scatter sales for the network again in Q1 with primetime CPMs pacing ahead of 2006 upfront levels by low to mid-single digits, which is generally consistent with what we saw last quarter as well. At our Television Stations, Q4 ad sales were up by low single digits, but so far in the December quarter, TV station ad sales are up by double-digit percentages, spurred by political advertising.

At our Theme Parks, outstanding results again provided evidence of a significant, sustainable competitive advantage we have nurtured and reinforced in this business. Parks ended 2006 with operating profit up 30% and margins up 240 basis points to 15.5% on a consolidated basis. Excluding the effect of consolidating Disneyland Resort Paris and Hong Kong Disneyland Resort, margins increased to just over 19%. Given the success of the 50th Anniversary Celebration in Q4 of last year, our combined domestic Parks attendance came in flat for the quarter, as the 7% decline at Disneyland was offset by an increase of 5% at Walt Disney World. However, guest spending at both our East and West Coast Parks grew by 4%.

Disneyland Resort occupancies were off somewhat to a still strong 92%, while occupancies at Walt Disney World increased to 83%. Per room spending increased by 5% at both our Disneyland and Walt Disney World Resorts. Looking ahead, rooms on the books at our combined domestic Parks are trending in line with the prior year for the December quarter, which is encouraging given that we had record holiday attendance during this quarter last year. Results at our International Theme Parks in Q4 reflected increased attendance and guest spending at Disneyland Resort Paris, as well as a full quarter of operations at Hong Kong Disneyland versus two weeks in the prior year.

At Consumer Products, we again delivered meaningful gains in our merchandise licensing business. The strength of our *Cars*, *Princess*, and *Pirates* lines helped drive double-digit increases in earned royalties for the year, which is a key indicator of a thriving licensing business. As expected, our ramp up of development spending in video games dampened our overall Consumer Products performance.

Our performance in 2006 set a high bar, but we go into 2007 with a great foundation and confidence that our strong operating performance will continue. More importantly, we will invest more in programming and other initiatives that we are optimistic can drive longer term performance and capital returns. As we've discussed in the past, our goal is to highlight for you the key swing factors that could impact our performance rather than give specific earnings guidance for any particular quarter or year.

Bob talked about our strategy of creating and leveraging strong content across different businesses and platforms and in 2007, our business will reflect this approach. At our Studio, for example, we have the Q1 release of *Pirates Tw*o and *Car*s on DVD, as we continue to capitalize on the success of these hit films. The two most notable theatrical releases for next year in terms of both investment and expectations are our third installment of *Pirates of the Caribbean* and the new Disney/Pixar film, *Ratatouille*, both of which come out next summer. Other key titles in our 2007 slate include *Déjà Vu* from producer Jerry Bruckheimer and starring Denzel Washington, which comes out in two weeks, *Wild Hogs* coming this spring with Tim Allen and John Travolta, and our next Disney feature animation release *Meet the Robinsons*, opening at the end of March. Our outlook for Consumer Products also anticipates that the popularity of the *Pirates* and *Cars* properties, added to existing franchises like *Princesses*, *Mickey*, and *Pooh*, will drive another year of robust growth in earned royalties. However, we expect that a $70 million decrease in minimum guarantee recognition in fiscal '07 versus what we recognized in 2006 will make comparisons difficult for the segment overall.

In media nets, assuming continued strength in the ad market and our ratings, we believe we could generate solid profitability and growth, led once again by ESPN and the ABC network. We've already taken steps to fortify ESPN's lineup with *Monday Night Football*, and our NASCAR event coverage begins in February. We will also continue to invest in our creative pipeline and with this in mind, in 2007, we're allocating resources to new content development at our Disney Channels around the world and ABC Family, as well as the new digital initiatives like Disney Mobile and Disney.com. In total, we believe our internet and download revenues could total approximately $700 million in fiscal '07.

As Bob indicated, we are increasing our investment in video games with roughly 30% more in development spending expected in fiscal 2007 than in 2006. Video games represents an important long term growth opportunity for us with the potential for very attractive returns on our investment. Looking ahead, we are targeting an increase in our annual video game development investment of roughly $350 million over the next five to seven years.

At our Parks, we believe that the *Year of a Million Dreams* celebration can help drive attendance across our properties. With the strength of our assets and competitive position, and given a positive economic climate, we remain confident in our ability to deliver continued growth at our Parks business. We will also see an approximately $190 million decrease in pension and post-retirement medical expense next year due to the increase in the discount rate used in calculating these expenses. The biggest portion of that reduction will benefit the Parks.

Our Pixar transaction closed more than halfway through fiscal 06, meaning we'll see a substantially greater dilutive effect from that deal in fiscal '07, a portion of which will be offset by our share repurchases.

We had about $0.05 per share in favorable tax impacts in 2006 that we do not expect to recur in 2007 related to the declining FSC/ETI benefit that we've discussed in prior disclosures.

With regard to our pending radio transaction, we've had discussions regarding possible modifications to the agreement to facilitate Citadel's post-closing financing. We would now anticipate closing the transaction in the first half of calendar year 2007. Upon completion of the transaction, the portion of our radio assets involved will be treated as discontinued operations. Accordingly, financial results for the assets included in the deal would be excluded for all periods. These assets represented roughly $0.04 of our 2006 EPS.

Our cash flow generation in fiscal 2006 was extraordinary and it reflects our commitment to maximizing the cash efficiency of our operations and our balance sheet. This year we generated after-tax free cash flow per share well above our after-tax earnings per share. Although we will continue to generate substantial after-tax free cash flow, that disparity is unlikely to continue. Much of the difference comes from our move to decrease our overall investment in live action films, the timing of certain spending and amortization expenses, and timing and improvements in our working

capital. In 2007, we also expect an increase in our overall capital expenditures in the neighborhood of $400 to $500 million. Roughly half of this increase will occur at Theme Parks and the majority of the rest will be related to digital initiatives at Media Networks.

In past earnings calls, we've laid out our priorities for investing our cash flow. Our first choice is to invest in existing or new business opportunities that can generate growth and strong returns. Our second preference is to use cash for share repurchase and dividends, and it is likely that our free cash flow will afford us the opportunity to continue returning capital in this way.

In 2006, our strong cash flow and financial position allowed us to aggressively repurchase our stock. At the time of the Pixar transaction, we indicated that we would be aggressive in buying our stock and we are well ahead of the pace we set at that time. During the year, we repurchased 243 million shares of Disney stock for $6.9 billion, with 96 million of those shares purchased in the fourth quarter. In fact, over roughly the last two years, we have repurchased nearly $10 billion worth of our stock, while at the same time strengthening our financial position. Our repurchase activity reflects not only our discipline in returning cash to shareholders, but also our confidence in our ability to grow shareholder value over time. We also target modest sustainable dividend increases and we will recommend that the Board continue that pattern when it meets at the end of this month.

In 2006, our efforts resulted in unquestionable success. We're obviously pleased with those results but we are by no means complacent. In fact, we are more focused than ever on continuing to extend and capitalize on our Company's strengths to deliver growth and value to our shareholders in fiscal 2007 and beyond. Now, we would be happy to take a few questions.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Thanks, Tom. Operator we are ready to take the first question, please.

Operator

[OPERATOR INSTRUCTIONS]. Your first question will come from the line of Anthony Noto with Goldman Sachs. Please proceed.

Anthony Noto – *Analyst, Goldman Sachs*

Thank you very much. Tom, in the swing factors that you mentioned, you didn't mention syndication revenue and in the past you've talked about $1 billion of syndication revenue over five years. Could you just talk about how this impacts the spread between '07 and the subsequent years? And then Bob, at our conference in September, you had talked about the Disney.com initiative. Could you talk about the progress you've made against that and when it may launch and what the prospects are in 2007? Thank you.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Anthony, with regard to syndication, we have said that the shows that we have on the air and that we own, we did expect to generate over $1 billion in contribution to operating income over the five year period and we still believe that to be the case. We have a large amount of availability in 2006. We've probably got a little bit less availability in 2007, so it's not a ramp up year to year that we would project at this point, but I think you will see strong syndication contributions across the period over the next four or five years anyway.

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

Regarding Disney.com, a rather extensive project is underway that began mid calendar year and should conclude some time after the first of the year that will result in a re-launch of the site that's going to have extremely robust features in shopping, television, movies, travel, music, social networking and community. It will be highly customizable, particularly for different demographic groups, extremely robust in terms of its ability to support new media, and basically, state-of-the-art in terms of general features and utilities.

I'm extremely excited about the progress. It's been a companywide effort. All the business units are behind it. It's going to offer consumers a fairly deep, convenient and seamless experience on all things Disney and we'll be revealing more of its features and all of the details some time after the New Year.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great. Thank you. We'll take the next question, please?

Operator

Your next question will come from the line of Doug Mitchelson with Deutsche Bank Securities. Please proceed.

Doug Mitchelson – *Analyst, Deutsche Bank*

Thank you very much. My questions are on ESPN but I was also wondering if anything has changed since last quarter regarding the impact on Disney from the potential options issues at Pixar from prior to its acquisition. Looking at ESPN, just two clarifications as we look out to '07. You added NASCAR programming this year, and I am wondering how much the impact on cost might be and how the amortization schedule for that contract will look. And as you are headed towards the finish line potentially with negotiations with Comcast, should we expect any change in the base rate charge for ESPN or just a change in how fast its rate grows going forward and should we expect another round of affiliate revenue deferrals as the new contracts are assigned?

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

With regard to your first question, it's been widely reported in the press that many companies received inquiries from the SEC and the Justice Department related to stock option grant practices and we too have received such inquiries related to stock option grants at Pixar prior to the acquisition. Our Board is conducting an independent review of them. However, as we previously said, we aren't aware of any basis under which stock options that were issued by Pixar would have a material impact on our financial statements.

Tom will handle your question about NASCAR. Before he does, on Comcast, we are in the final stage of the negotiations. It's actually possible that a deal could be signed within the next week and the details at this point are not something we're going to disclose except that what we've said in the past in terms of general rate structure remains. I'm actually really pleased with where we are because I think this gives us the

ability with Comcast to expand our businesses together and points to what I think is going to be a very healthy relationship in the future.

It's clear that their investment in technology, not just in their standard business but in their new businesses, particularly broadband and in the phone service area, provide us with significant opportunities as the owner of great brands and great content to really expand our relationship with them and to provide services to their customers that's going to be great for both companies. So, we're really looking forward to concluding the deal and really looking to a future I think is going to be pretty interesting.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

With regard to NASCAR, I'd anticipate at this point that the accounting treatment for NASCAR will be like football, a gradual increase over time. The payment stream for NASCAR has modest increases and the amortization will therefore mirror the payment stream. I think one thing to bear in mind is that we have a big chunk of the NASCAR season in fiscal 2007 but not a whole season.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Thanks. We're ready for the next question, please?

Operator

Your next question will come from the line of Jessica Reif Cohen with Merrill Lynch. Please proceed.

Jessica Reif Cohen – *Analyst, Merrill Lynch*

Thanks. I would like to follow-up on something Bob said and then ask my question. So I hope the first one doesn't count. Bob, what you just said about Comcast, could you do an exclusive -- it sounds really interesting. Can you do anything exclusive meaning no other provider can have what you will offer them?

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

Well, as you know, Jessica, the general approach has been to pursue non-exclusive relationships with distributors, but I think I'm just going to contradict that a little bit. You should think about our relationship with these distributors in a way that might be analogous with our relationship with mass retailers, in that we do business with all of them and that in general the overall relationship is not exclusive, but we create products that are unique to each relationship, in effect exclusive, that give these retailers the ability to sell things that others can't sell.

So, a good example of that would be the classic Pooh line that we have with Target, where they have some exclusivity but we sell Pooh products to all mass retailers. And so, I think what you could think about in terms of Comcast is that access to our main products, ESPN, the Disney Channel, et cetera, will be non-exclusive, but the possibility of creating something that's unique just to that relationship with Comcast that they could use as a differentiator is something that we're going to explore.

Jessica Reif Cohen – *Analyst, Merrill Lynch*

Thank you. Okay here is my question. On Disney Channel, you have had really an incredible amount of hits over the last few years. Are you prohibited by your cable contracts from offering advertising? I mean, given the ratings growth, would you reconsider that if you can. And the amount of number one music titles in the last couple of months has also been astounding. Can you break out that music number?

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

The Disney Channel carriage agreements, which particularly when we close Comcast and when we eventually get Time-Warner done, are all long term deals, do preclude us from selling advertising in a traditional way. They do give us the ability to create some relationships with sponsors that I'll call PBS-type advertising.

We're not really considering changing that structure because the fee structure that we've negotiated for the channel is rather significant, and we like the fact that it's in effect a guarantee that doesn't fall prey to competitive issues or the ups and downs of an advertising market; however, given the success that we've had with Disney Channel programming and given how incredibly successful our efforts on new media platforms are turning out, particularly DisneyChannel.com and ultimately Disney.com, we have

the ability on those services to convert usage to advertising, and we're starting to see some very, very exciting trends in that regard.

That's also true, by the way, at ABC.com where we're growing our advertising very, very nicely in our streaming on ABC.com. So when we look to the Disney Channel again, we see basically status quo with no advertising but a pretty high rate structure compared to the rest of the business, and then basically using content fairly aggressively on new media platforms to grow revenue in that direction.

On music, I'll let Tom talk to the numbers, but one of the things that's very exciting, particularly as we focus on the Disney brand and the kind of programming that we're creating, is creating business opportunities that go well beyond the platform that the product is originally created for. Obviously that was true with *Pirates*, which was a theme park attraction and look what has been done with that, but also with *Hannah Montana* or *That's So Raven* or *The Suite Life of Zack and Cody*, and a number of other programs. *High School Musical* is a great example, a product that we find, with the Disney brand, we can essentially exploit in many different ways, and music is one way and the success this past year has been extraordinary, and we're really focused on growing that in the future. We think we have created a very interesting formula to be successful in music, and it's Disney branded and I think there's some interesting opportunities there.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes, I think that music has become more important to us and Bob Cavallo and his team have done a great job of building up that business. Less than 10% of the growth at the Studio was represented by the growth in music, so it's still a relatively small piece of the Studio but it's an important piece and as Bob said one that we hope to grow over time.

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

There's also a great synergy when it comes to music between the Disney Channel, Disney.com, Radio Disney and the Disney phone and there will be very, very robust music offerings that in effect tie into one another across all of those platforms.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great. Thanks. We're ready for the next question, please?

Operator

Your next question will come from the line of Kathy Styponias. Please proceed.

Kathy Styponias – *Analyst, Prudential*

Thank you. Tom, I'm wondering if you can just break out for us from 06- '07 what you expect to spend incrementally for both video games and for Disney Mobile. I know you said you expect to spend an incremental $350 million but that's over the next 5 to 7 years. What kind of impact should we expect in the coming year? Thanks.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Sure. I mentioned in the prepared remarks we would be up about 30% in spending in 2007 for video games and that's up from 2006 around $100 million so it's about a $30 million increase in the development spend there and as you know, Kathy, we amortize the development spend as it's incurred, and so that will dampen the profits at games and Consumer Products as a whole because a lot of what they're spending on is for future release post-2007, so that has an impact.

With Mobile I think the thing to think about is we are ramping up the spending at Disney Mobile as it just launched late this year. But, when you look at the Media Networks line as a whole, it will be offset by the decreased spending at ESPN Mobile because we've transitioned that into a part of our licensing business, so that won't be a driver of year-over-year increased spend on a combined basis in Mobile.

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

And Kathy, since you brought up games, what we're trying to accomplish is to basically build a Disney branded game business and we have been buying or building developers. We actually just announced yesterday a developer that will be located in Salt Lake City called Fall Line that's going to be focused on making Disney branded product for the new Nintendo Wii platform as well as the Nintendo DS platform.

I mentioned in my remarks that a very large portion of the games business is kid and tween business and we have a huge number of Disney assets, both new and what I'll call library assets that we can exploit in games, *Kingdom Hearts* is certainly a great example of that. With all of the activity for *Pirates* and ultimately all of the things we'll be able to do in animation, our goal is ultimately to end up with a significant games business and we believe we'll be able to do so by deploying the strategy that we've been deploying these last few years which is to essentially build organically and make opportunistic, relatively low cost acquisitions, versus being in the market to buy a large existing game publisher.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great. Thanks. Ready for the next question, please?

Michael Nathanson – *Analyst, Sanford Berstein*

Thanks. I have one for Tom. Tom, you mentioned that you would spend $400 million more in Cap Ex at Theme Parks this year, and I was wondering where is that investment going and should we assume this is a new level of spending that will continue or is it incremental?

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

The $400 to $500 million increase is actually for overall capital expenditures so I'm glad you asked that so we can clarify it in case it wasn't clear before, so that's total Company and roughly half of that increase is at Theme Parks Predominantly that's spending on new attractions as you would suspect and the Theme Park capital expenditures domestically were only a little bit over $600 million this year so I would expect that the run rate of those numbers would be a little bit higher than that.

As we said before, we expect spending at our domestic Parks to be meaningfully under $1 billion, as vague as that might be, and I think that the trend that you're seeing here gets us back up but comfortably under that $1 billion mark. The biggest piece of the remainder of that capital expenditure increase is really on new media initiatives, ESPN taking up a big chunk of that as we continue to invest in its cross platform capabilities as Bob discussed in his comments.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great, thanks. Ready for the next question, please?

Operator

[OPERATOR INSTRUCTIONS]. Your next question comes from the line of Aryeh Bourkoff with UBS. Please proceed.

Aryeh Bourkoff – *Analyst, UBS*

Thanks very much. Good afternoon, guys. Just one, can you confirm that for fiscal '07 you're targeting double-digit operating income growth at ESPN? I know you do have some costs with sports, but can you achieve that and then secondly for Bob, can you talk about which areas of digital media revenue you mentioned in the numbers for '07 are you most excited about in terms of breaking out some of the key components of that digital media revenue number? Thanks.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

We've said in the past we're targeting double-digit growth for ESPN on average from 2004-2009, and we purposely speak in terms of average growth rates because year over year variables are hard to predict over the long run, and we don't like to give guidance in the first place, so we give it somewhat begrudgingly. Having said all of that, we expect another year of strong growth from ESPN in 2007 that is generally consistent with that overall goal.

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

And in terms of the growth in our digital media business in '07, we're expecting growth to come in multiple directions from downloads and streams, from advertising supported experiences, to purchases, and I'm not going to point at any one aspect that might grow faster than the others except that we believe we'll see significant growth. I mentioned a number of numbers in my opening remarks. To put it in perspective, just on the advertising side, ABC.com, which has been streaming shows really since May but they did it for a month in May and they have been at it regularly since September,

has experienced over 19 million episodes requested of six television programs, and we've assembled a group of about 36 different advertisers to sponsor those shows, one advertiser per show, and the CPM rate, now admittedly it's early, is four to five times the CPM rate and delivery of adults 18-49 in primetime, which is a rather significant number and that comes because one, there is a rich demographic associated with it, younger, higher income, but secondly, the recall rates of advertising are tremendous.

We said after the May experiment that over 85% of the people that watch the episodes remember the advertiser that was in those episodes and that obviously provides advertisers with value that is just tremendous and so we believe particularly as we build out our capability, ABC.com, ESPN.com, Disney.com, that the ability to grow advertising online for these media assets is significant. At the same time, we've done extremely well on the iTunes platform and we've launched on two other movie platforms and given some of the announcements made this past week, we believe we'll have opportunities to sell movies and television shows on many other new platforms and since those deals are not exclusive and we're taking basically a platform-agnostic approach, our growth in what I'll call purchases is going to increase substantially too.

And lastly, the aspect of these cable deals that we're excited about is video-on-demand, for both movies and television shows. On the movies side, there will be purchases and on the TV side, it will be a combination of advertiser supported and purchased, and again we think we've got some interesting opportunities to raise revenue both from a pay-per-view experience as well as from an advertiser experience.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great thank you. Next question, please?

Operator

Your next question will come from the line of Lowell Singer with Cowen & Co. Please proceed.

Lowell Singer – *Analyst, Cowen & Co.*

Thanks. Tom I just have two quick modeling questions. Can you talk a little about what you are expecting your tax rate to be in '07 and do you expect a similar pattern of deferrals at ESPN as we've seen the last two years? Thanks.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Sure. As I mentioned, the FSC/ETI benefits which deal with extraterritorial income are beginning to sunset. The biggest driver that you should look for to change in the tax rate over this year is really what amounts to about $0.05 a share that comes from what we saw in 2006 that we will not see in 2007, and so that will be the biggest driver to change. As you can imagine, that drives up the rate by several points. We also had some settlements of prior tax matters and so that has an impact as well so you'll see an increase in the tax rate. It's a bit early in the year to predict an exact rate but something closer to the 37% range we've talked about in the past as being about where we would come out.

I'm sorry, you asked about ESPN deferral. Well, because of growth in the affiliate rates and the fact that we've got new contracts to be signed and this can vary depending on when we might complete the discussions with Comcast and with Time-Warner, sitting here today, I would expect that roughly $180 million more in revenue would be deferred from the first half of the year to the second half of the year than we deferred in fiscal 2006. So that gives you a rough order of magnitude that could be impacted by the timing of the deals.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Thanks, next question please?

Operator

Your next question will come from the line of David Miller of Sanders, Morris, Harris, Please proceed.

David Miller – *Analyst, Sanders Morris Harris*

Yes, hi. Congratulations on the stellar results. Tom, I have two brief questions for you. The Children's Place, I believe will begin to pay royalties to Disney in the second anniversary of the closing of that deal which I think is the current quarter, so if you could refresh my memory as to what the formula of that is, that would be great, and then at this point, given where Disney stock is and given where the current market conditions, are you favoring a spin-off or a split off or a combination of both with regard to Radio? Thanks very much.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

With regard to The Children's Place, you're right. The royalty holiday does sunset this year and as they've disclosed in their documentation the base business has a 5% royalty to it, online revenue royalties are at 10%. We haven't made any predictions about what that comes out to be and of course they are ramping up into an important holiday season, so it would be premature for me to do that anyway. And with radio, I guess the core of your question is spin versus split. We said that when we get down to near the closing of that transaction, we would make a final determination on the spin versus split. And I don't want to make too big a deal out of it.

We'll make a decision at that point in time. Either one we're distributing the value of that business to our shareholders on a very tax efficient basis, tax treatment is basically the same, and so either way, it's a very efficient way to distribute the value of that business and that deal, so we think that we will make the decision down the road.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Thank you. Next question, please?

Operator

Your next question will come from the line of Vijay Jayant with Lehman Brothers. Please proceed.

Vijay Jayant – *Analyst, Lehman Brothers*

Thanks. Tom, in terms of your hotels, given your occupancy is pretty high, when do you start thinking about expanding in rooms and how much before they sort of come on line do you need to plan for that, and if I may on a second question, on *Pirates of the Caribbean*, given they were filmed together, is the cost in '07 for the third movie compared to the one in 06, is it equal, is it proportionally higher in one year over the other? Thanks.

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

In terms of your first question, we haven't announced any additional expansion of rooms. We did announce an expansion of our vacation clubs, but that's a different business. As you mentioned we had an excellent year from an occupancy perspective. In fact, and I found this to be very interesting fact, we have the largest on site population in Orlando as a percent of the total Orlando hotel occupancy in 2006 and so we're obviously utilizing our investment in hotels quite well. We'll take a wait and see approach in terms of further expansion. We've been focused a lot on the family suites business and we added about 200 family suites to a hotel called the All Star in Orlando. They've done extremely well.

We're going to look for opportunities to build out more family suites because of the trends we're seeing in that business but at the moment no definitive plans to build any new hotel capacity. Again we had a great year this past year, helped a lot by the 50th anniversary. We believe heavily in our *Year of a Million Dreams*, but no immediate need now to add more capacity.

And the other thing I want to point out is one of the things we've done in terms of growth is we've taken market share, obviously, and a lot of that has to do with the strategy that we put in place a couple of years ago, which was both a pricing strategy and strategy that had us adding on all kinds of essentially new benefits to guests who were staying in on property hotels versus off property hotels. That occupancy factor that I mentioned earlier is clearly a result of a strategy that is definitely working.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes. I think that's an important thing I would have added is that we were successful in bringing people on property, so new hotels is something we study but as Bob said we'll

continue to study it and make the move when and if the time is right. With regard to *Pirates Two* versus *Pirates Three*, it comes as no surprise *Pirates Two* was an expensive film and *Pirates Three* will also be an expensive film. We studiously avoid giving out the exact numbers. *Pirates Three* will be somewhat more expensive than *Pirates Two* but the good news really is that Jerry Bruckheimer, Gore Verbinski, and Bruce Hendricks, who manage production, do a great job making sure that spending adds up on the screen, and that really showed up in *Pirates Two*, and we think it will show up again in *Pirates Three* so we think it's money well spent and we're kind of looking forward to this summer.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great, thank you. Next question, please?

Operator

Your next question will come from the line of Spencer Wang with Bear Stearns. Please proceed.

Spencer Wang – *Analyst, Bear Stearns*

Thanks, good afternoon. Just one question on advertising, Tom, if I take out the $171 million in deferred affiliate revenues, looks like the organic revenue growth was 6 to 7%, so the affiliate revenues were up low double digits. Does that mean that ad revenues were up flat to low single digits and similarly on Broadcasting, why was revenue growth only 1.4%? Thanks.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Well, I think you're looking at a couple different things there. One is that now in the fourth quarter there was $87 million more recognized in deferred revenues than there was in the prior year and so I think the organic revenue growth might be a little higher than the one that you said and we've talked about the fact that there are moderating growth rates but also the fact we're confident in our ability to translate the growth rates we'll see into continued strong results at ESPN so I feel pretty good about that overall. I think we're in good shape there. Broadcasting, as a whole in terms of revenue growth, I think one of the most important things to remember is that there was *Monday Night*

Football in the year and in the fourth quarter last year and the fourth quarter this year did not have *Monday Night Football* on ABC so *Monday Night Football* comes with a lot of revenues but a lot of costs so that makes the year-over-year revenue comparison difficult.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great, thank you. We'll take the next question, please?

Operator

Your next question will come from the line of Imran Khan with JP Morgan. Please proceed.

Imran Khan – *Analyst, JP Morgan*

Yes, hi, thank you. One question for Bob and one question for Tom. So, Bob, you talked about that 0.5 million film downloads on iPod. It's being reported that Wal-Mart and Target are a little uncomfortable with your iPod initiatives. I was wondering, have you heard anything from them and if so, how have you tried to balance that with the very high margin business that you generate from Wal-Mart and Target and secondly, Tom, you had very strong ratings on ABC. I was wondering, can you give us some color, how should we think about ABC margins? Thank you.

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

In general, our relationship with mass retail is actually very strong which is evidenced by our growing DVD business as well as our growth in our Consumer Products business, and we're in a lot of discussions with a lot of different retailers about their own digital download capabilities and we actually expect to cooperate with them when they launch such services. Clearly, the digital download initiatives, particularly movies, have created some tension over issues like pricing and windowing, but we ultimately believe that tension is going to dissipate over time as we learn more about how the business is impacting the consumer.

I also want to emphasize that Disney's presence at mass retail is sizeable. It comes in many different forms, and in general, we've seen great growth both in our direct to licensing relationships with mass retail and our relationships through third party

licensees at mass retail. The sale of Disney DVDs at mass retail is very, very robust these days. If you look, interestingly enough, at the last year and if you look at the top ten video titles, a number of them were Disney, *Narnia* clearly was one of them, and so was *Little Mermaid* but *Bambi* and *Lady and the Tramp* were in that number as well, and so the Disney DVD business at retail is in good shape.

We haven't seen any impact by the way that is negative or cannibalistic from our download experience and actually believe that we're growing market share rather than moving business from one platform to the other. Have we had discussions? Yes, absolutely. In general though I think our relationship with these retailers is in good shape.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

With regard to ABC margins, I think I'd offer up a couple things to think about. Number one as I mentioned before, *Monday Night Football* came off of the network, and that's important obviously from a revenue standpoint, and from a margin standpoint because we lost money on *Monday Night Football* on the network, and last year we also had the *Super Bowl*. I think the way to think about the *Super Bowl* is that it had a bunch of revenue associated with it that when you combine the network and the television stations, that was offset by the rights costs.

The other thing I'd mention is that we had good results in the upfront. We continue to have strong ratings and so far, we've had a robust spot market, so that all bodes well. The other piece of the equation is I think that if you look at programming costs, the average cost per hour of entertainment programming for ABC and primetime should be about even this year versus last year, and so that's going to give you the opportunity for strong margin improvement at ABC this year.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great, thank you. We have time for just one more question.

Operator

And your final question will come from the line of Jason Bazinet with Citigroup. Please proceed.

Jason Bazinet – *Analyst, Citigroup*

Thanks so much. Given the appreciation on your share price over the last year or so, I was wondering if there's been any change in thinking in terms of your preference for dividends over share repurchases at all? Thanks so much.

Tom Staggs –*Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Well, we still like both, by the way, and I think you should expect us, as I mentioned, to recommend an increase in the dividend to the Board. It's of course for them to consider and determine, but I think you should also expect us to continue to be buyers of our stock despite the run up, given our outlook for long term value growth. We don't tend to be short-term stock watchers. We would like to think about our value in long-term basis, and I think that that makes us very comfortable today with the continued repurchase program and our strong cash flow.

Teri Klein – *VP, Investor Relations, The Walt Disney Company*

Great, thank you. Well, thank you again for joining us today. Note that a reconciliation of non-GAAP measures referred to in this call to equivalent GAAP measures can be found on our Investor Relations website.

Let me also remind you that certain statements on this Conference Call may constitute forward-looking statements under the securities laws. These statements were made on the basis of Management's views and assumptions regarding future events and business performance as of the time the statements were made and Management does not undertake any obligation to update these statements. These statements are subject to a number of risks and uncertainties and actual results may differ materially from those expressed or implied in light of a variety of factors including factors contained in our Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. This concludes Disney's Fiscal Year End 2006 Conference Call. Thank you.

Operator

Ladies and gentlemen, we thank you for your participation in today's conference. This does conclude the presentation and you may now disconnect. Good day.

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, 2005 and in subsequent reports on Form 10-Q under Item 1A, "Risk Factors".

Reconciliations of non-GAAP financial measures to equivalent GAAP financial measures are available on Disney's Investor Relations website.

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