



The Walt Disney Company Q1 FY15
Earnings Conference Call

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Disney Speakers:

Bob Iger

Chairman and Chief Executive Officer

Jay Rasulo

Senior Executive Vice President and Chief Financial Officer

Moderated by,

Lowell Singer

Senior Vice President, Investor Relations

PRESENTATION

Operator

Welcome to The Walt Disney Company's first quarter fiscal year 2015 earnings conference call. My name is Ellen and I will be your operator for today's call. (Operator Instructions) Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.



I would now like to turn the call over to Lowell Singer, Senior Vice President of Investor Relations. Mr. Singer, you may begin.

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

Good afternoon and welcome to The Walt Disney Company's first quarter 2015 earnings conference call. Our press release was issued almost 45 minutes ago and it's available on our website at www.disney.com/investors. Today's call is also being webcast and the webcast and a transcript of the call will be available on our website.

Joining me for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer and Jay Rasulo, Senior Executive Vice President and Chief Financial Officer. Bob will lead off followed by Jay and then, of course, we will be happy to take your questions.

So with that, let me turn it over to Bob and we'll get started.

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

Good afternoon. I'm very pleased to announce The Walt Disney Company had another incredibly strong quarter, with diluted earnings per share up 23% to \$1.27. These results were driven by solid performance across all of our businesses and once again demonstrate the strength of our brands and content, and a proven franchise strategy that will drive long-term value.

Frozen is a great example of this strategy. On March 13th – along with *Cinderella* – we're premiering a new 7-minute short, *Frozen Fever*, bringing back all the beloved characters and voices and introducing a great new song.

This time last year we were excited about the box office success of *Frozen* – which went on to win the Oscar and become the highest grossing animated feature of all time. Now, a full year after its release, we're seeing the true impact of *Frozen* across our entire company.

Overall, retail toy sales in North America were up 4% in 2014, and according to a leading market research firm, much of the credit for that growth belongs to *Frozen*, which was both the biggest and fastest growing toy property of the year. It's also enormously popular in our Parks & Resorts, it's showcased in a successful mobile game, and it gave a significant boost to our home entertainment business for the quarter, along with *Maleficent* and Marvel's *Guardians of the Galaxy*.

Frozen is just one of the 11 franchises at Disney currently driving more than a billion dollars each in annual retail sales. The strong holiday demand for *Frozen*, as well as Mickey & Minnie,



Spider-Man, and *Avengers*, led to the most successful quarter ever for Disney Consumer Products.

Among media companies, Disney stands out -- no one else comes close to our unparalleled collection of strong brands or our pipeline of great content. And our unprecedented ability to leverage creative success and create value across the entire company allows us to adapt to emerging challenges, take advantage of new opportunities and, most importantly, innovate for the future.

For example, who else but ESPN could launch the first-ever College Football Playoff with such enormous and immediate success? The two Semifinals and the National Championship broke previous records to become the three most watched telecasts in the history of cable television – an achievement that speaks to the tremendous potential of this annual event and further strengthens ESPN’s undisputed position as the number one sports brand.

Our Studio is obviously a key franchise driver and we have a strong slate of upcoming movies. We started the fiscal year with Disney Animation’s *Big Hero 6*—which has already generated just under \$500 million in global box office. It’s also been #1 in Japan for five weeks, and has yet to open in some key markets. And *Into the Woods* has been both acclaimed by critics and embraced by audiences.

As I said, next month, one of our most beloved and iconic characters comes to life in Disney’s first-ever live action *Cinderella*. It’s a fresh look at this classic story, and it’s also a stunningly beautiful film. Later in the spring, we’re looking forward to an original Disney adventure called *Tomorrowland*, starring George Clooney and directed by Brad Bird.

As every Marvel fan knows, the highly-anticipated *Avengers* sequel, *Avengers: Age of Ultron*, opens in May. When the first trailer was released in November, fans viewed it more than 34 million times in just 24 hours – the speed and magnitude of that reaction certainly speaks to the incredible excitement around *Avengers*.

Ant-Man debuts in July – bringing another great character to the screen with Marvel’s trademark blend of action, humor, and heart.

We’re also thrilled to have two original Pixar movies on the way this year. In June, *Inside Out* will give audiences an all access pass into the mind of an 11-year-old girl, and at Thanksgiving, *The Good Dinosaur* takes a humorous look at what the world would be like if the asteroid that wiped out the dinosaurs had actually missed.

Of course, for millions of *Star Wars* fans, the first 11 months of this year will be an exciting countdown to the December 18th release of *Star Wars: The Force Awakens*. There is a strong emotional connection to this franchise that transcends geography and generations. The brief teaser trailer released last November has been viewed more than 123 million times.



Having been on the set, and seen most of the footage, I can definitely say their excitement is justified. It marks the beginning of a new era of exceptional *Star Wars* storytelling, as well as an opportunity for continued growth across all of our businesses.

As a truly global company we've talked a lot about the importance of developing local content, and the success of the film *PK* in India is a perfect example. It's now India's highest grossing movie of all time; and with almost \$107 million in global box office, it's also Bollywood's most successful movie ever. Co-produced and released by our Indian subsidiary, UTV, *PK* will soon be on 3,500 screens across China.

This is also a dynamic and exciting time for our Parks & Resorts – with another very strong performance in Q1 and plenty to look forward to including the spectacular Shanghai Disney Resort.

I was in China the week before last and saw amazing progress. We just topped off our signature Shanghai Disneyland Hotel, we're nearing completion on iconic features throughout the park, including the largest castle we've ever built, and we're getting ready to start casting the hundreds of performers we'll need to entertain our guests. It's thrilling to see Shanghai Disney Resort rapidly coming to life. The artistry, complexity, the magnitude, and the detail - it's all quite astonishing.

As you'll recall, after we broke ground on this incredible resort, we announced an \$800 million expansion, significantly increasing both the size of the park and the number of attractions available to our guests on opening day. Even with that expansion, we will complete major construction by the end of this calendar year, and we're planning a spectacular grand opening in Spring of 2016, which we believe is the optimal time to showcase the full grandeur of this world class destination.

Obviously we're proud of our performance, and our record of creating significant value for our company and our shareholders, and we're very optimistic about our future.

And now, I'm going to turn the call over to Jay to take you through the details of our Q1 performance, and then we'll take questions. Jay?

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Thanks, Bob and good afternoon everyone. Fiscal 2015 is off to a great start, as we delivered another strong quarter of financial results. Earnings per share were up 23%, driven by record revenue—up 9% over last year—and 17% growth in segment operating income. The results this quarter, which I'll go over in more detail in a moment, are further evidence that our strategy of investing in high-quality content drives significant, long-term value across our businesses.



At Consumer Products, our broad content portfolio fueled incredibly strong financial results. Segment operating income was up 46% on revenue growth of 22%. Margins expanded by 720 basis points, reflecting strength in both our merchandise licensing and retail businesses. Growth in licensing was driven by *Frozen* and, to a lesser extent, Disney Channel properties, Mickey and Minnie, Spider-Man and Avengers, partially offset by higher revenue share with the Studio. On a comparable basis, earned licensing revenue in the first quarter was up an impressive 23% over last year, which is particularly notable given the size of our licensing business.

Higher results in our retail business were primarily due to the continued demand for *Frozen* merchandise, which drove double-digit growth in same store sales in North America, Europe and Japan, as well as higher online sales in those regions.

At the Studio, the success of our fiscal 2014 theatrical slate continued to drive financial benefits in the first quarter. Operating income was up 33% over last year due to increases in home entertainment, higher revenue share from Consumer Products, and an increase in television distribution.

While we were very pleased with the worldwide box office performance of *Big Hero 6*, theatrical results were lower in the first quarter, reflecting the record-breaking performance of *Frozen* last year.

The increase in home entertainment was primarily driven by higher unit sales of *Guardians of the Galaxy*, *Frozen* and *Maleficent* compared to *Monsters University* and *The Lone Ranger* in Q1 last year. The increase in television distribution in the first quarter was due to better performance of Q1 titles, including *The Avengers*, *Captain America 2*, and *Frozen*, compared to last year's titles.

The Studio recognized a higher revenue share from Consumer Products in the first quarter due to the strong sales of *Frozen* merchandise.

The Parks and Resorts segment had another great quarter. Operating income was up 20% on revenue growth of 9% due to continued strength at our domestic operations. Despite lower results at our international operations, total segment margins were up 190 basis points, with major new initiatives accounting for 80 basis points of the year-over-year increase.

We continue to be pleased with the performance of our recent major investments, as they have contributed nicely to the robust growth of the domestic base business. In the first quarter, growth in operating income at our domestic operations was driven by higher guest spending and attendance at our domestic parks, and higher passenger cruise days at the Disney Cruise Line, partially offset by higher costs. For the quarter, attendance at our domestic parks was up 7%, with Walt Disney World and the Disneyland Resort each setting an all-time attendance record for any quarter. Per capita spending in our domestic parks was up 4% on higher ticket



prices, merchandise and food and beverage spending. Occupancy at our domestic hotels was up 8 percentage points to 89% and per room spending was up 4%.

So far this quarter, domestic resort reservations are pacing up 3% compared to prior year levels, while booked rates are up 4%.

Turning to Media Networks, segment revenue was up 11% and operating income was up 3%, as higher results at Broadcasting were partially offset by lower results at Cable due primarily to higher programming and production costs at ESPN.

Broadcasting operating income increased 35% driven by higher affiliate revenue and higher program sales, partially offset by lower ad revenue. The growth in affiliate revenue was due to contractual rate increases as well as higher rates in new affiliate agreements. Program sales were up in the first quarter due to sales of ABC Studios shows, including *Criminal Minds*, *Scandal* and *Once Upon a Time*. Ad revenue at the Network was down in the quarter as a result of fewer Primetime units sold, partially offset by higher rates. Quarter-to-date scatter pricing at the ABC Network is running 10% above upfront levels.

Cable segment results were down modestly, as lower operating income at ESPN was partially offset by increases at worldwide Disney Channels and ABC Family.

Lower results at ESPN were primarily due to higher programming and production costs and, to a lesser extent, higher marketing costs related to the College Football Playoff and the launch of the SEC Network. This quarter's results reflect ESPN's continued investment in what is already the deepest and broadest portfolio of sports rights. As a result, programming and production expenses were up mid-teens percent during the first quarter due to higher expenses for NFL rights, as this is the first year of ESPN's new, 8-year contract and additional sports rights for the SEC Network.

As we've discussed in the past, we expect growth in cable programming costs to be in the low-teens, and that increase will be heavily weighted towards the first half of the year. We expect cable programming costs to be up about 25% in the first half of the fiscal year and relatively flat in the second half. The cost increase this quarter and what we expect in Q2 are consistent with the first-half and full-year outlook.

ESPN has long-term agreements in place for the most valuable sports rights. While the first year of new contracts may result in above-trend cost increases and adversely affect results in the short-term, we remain confident in our ability to continue to grow ESPN over the long-term. During the first quarter, we renewed a major affiliate distribution deal, marking the completion of new agreements with our ten largest affiliate partners. Due to contractual provisions in ESPN's new affiliate agreements, ESPN will no longer defer a portion of its affiliate revenue for most of its contracts as was previously the case.



Domestic cable affiliate revenue was up 20% in the quarter, reflecting the benefits of new affiliate agreements, lower deferred revenue at ESPN, and the launch of the SEC network. The 20% increase in affiliate revenue includes a year-over-year benefit of \$136 million dollars, as ESPN deferred \$136 million dollars in affiliate revenue in Q1 last year compared to no deferred affiliate revenue in Q1 this year. Adjusted for the timing of deferred revenue at ESPN, domestic cable affiliate revenue was up low double digits.

Ad revenue at ESPN was down 2% in the first quarter. While total day ratings were up, ad revenue was lower as ratings for certain key programs were down compared to last year, partially offset by higher rates. So far this quarter, ESPN ad sales are pacing up 18% on the strength of the first College Football Playoff, which aired last month.

The increase at worldwide Disney Channels was due to higher affiliate revenue at the domestic channel and higher advertising revenue at international channels, partially offset by higher programming costs. The increase at ABC Family was driven by higher affiliate and advertising revenues reflecting an increase in units sold.

At Interactive, operating income increased 36% in the quarter driven by higher results from our mobile games business due to the continued success of *Tsum Tsum* as well as lower product development costs, partially offset by lower results at our console games business. Lower console game performance reflected higher per unit costs driven by Disney Infinity, lower unit sales, and higher marketing costs. The decrease in unit sales was driven by lower sales of catalog titles and Disney Infinity figures, partially offset by higher sales of Disney Infinity starter packs.

We continue to take a balanced approach to capital allocation by investing for long-term, sustainable growth while returning meaningful capital to our shareholders. During the first quarter, we repurchased 15 million shares for about \$1.3 billion dollars and increased our dividend by 34%, from \$0.86 cents per share to \$1.15 per share. Fiscal year to date, we have repurchased 15.5 million shares for about \$1.4 billion dollars.

Overall, we feel great about the first quarter. As we look across our businesses, there is a lot to be excited about in 2015 and beyond. But we are not taking anything for granted, as we recognize we have a lot of work ahead of us. We believe the strength of our brands, coupled with the integrated nature of our company can create long-term, sustainable value for our shareholders.

And with that, I'll turn the call back to Lowell and we'd be happy to take your questions.



Q&A

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

Ok, thank you, Jay. Operator, we are ready for the first question.

Operator

(Operator Instructions) Michael Nathanson, MoffettNathanson.

Michael Nathanson – *Analyst, MoffettNathanson*

One for Bob and one for Jay. So, Bob, now that we've seen the DISH Sling offer, we had a question. We wonder if you had any insight into whether or not the ESPN viewer is also a heavy RSN viewer, and if so, how does that affect the take-up rates for a bundle that doesn't have an RSN but has ESPN?

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

Michael, we don't really have that much data on, one, how much DISH has succeeded in selling the Sling package to its customers. And we don't have data on the customers themselves right now. So we just don't know.

I will say, though, since you give me the opportunity, that it's all designed to attract consumers or households that are either cord-nevers or cord-laters. And we believe that there is an attractiveness to or a real justification for trying to convince particularly millennials to sign up for some form of subscription TV when they might not have signed up for any.

Michael Nathanson – *Analyst, MoffettNathanson*

I guess the question is, are millennials who are sports fans also RSN fans? Or do you think it's a starter package for them using ESPN?

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

We just don't have data. I think your premise is interesting -- that if they want ESPN, chances are they are RSN viewers; and if they are RSN viewers, then they probably have to have the expanded basic bundle. So we're probably -- I'm guessing that -- I'm not sure what you are



inferring here. Maybe what you are suggesting is that there aren't many left? In other words, if they are sports fans, then they probably have to have expanded basic cable, because they'd have to get it to get RSNs. Is that what you are saying?

Michael Nathanson – *Analyst, MoffettNathanson*

Yes, that's what I'm saying.

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

So there's not many left? We'll see. We don't have enough data yet.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. And let me move to Jay -- thanks, Bob. Jay, you said occupancy in the hotels in Disney parks and resorts were up to 89%. Going back to your history of running Parks and Resorts, once you get to 89%, can you talk about what types of pricing leverage do you see historically? Because I think that's probably the best number we've seen pre-recession or post-recession.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You know, Michael, I think hoteliers in general will tell you that to try to fill a hotel beyond 89%, 90%, 91% is extremely difficult because to go beyond that, it takes too many matchups of people who are staying three nights, checking out; replaced by five nights; replaced -- in rapid succession. It becomes quite difficult.

So I think that you are right -- that when you see occupancy in that kind of range, you are getting close to pretty much a full house. And those were historically the numbers at which we started to think about expanding capacity. Of course, relative to the Orlando market, there are still many, many more hotel rooms off-property than there are on-property. And I'm sure they are not experiencing rates of occupancy anything like that.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Thanks, Jay.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.



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

Thank you, Michael. Operator, next question please.

Operator

Jessica Reif Cohen, Bank of America.

Jessica Reif Cohen – *Analyst, Bank of America Merrill Lynch*

Thanks. I guess on the theme parks, two things: on *MyMagic+*, is there any way you can give us some color or quantify the impact on guest spending and guest flow? That was something you mentioned -- that it would improve efficiency. How should we think about the benefits of *MyMagic+*?

And the second question is: in this ramp-up to Shanghai, can you give us some more color or detail on the financial impact in fiscal 2015 as you spend into the opening of 2016?

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

Well, on *MyMagic+*, Jessica -- I'll take this one -- first of all, about 10 million guests have already worn the bands. And so far what we are hearing from them is overwhelmingly positive -- basically, the percentage that rate it as "excellent" is significant.

So what that basically tells us, and what we actually have seen, is that it is serving the purpose that we set out to serve, which is to essentially make the experience more seamless; basically make it easier, to give people an opportunity to enjoy what they do when they visit Orlando or Walt Disney World even more than they used to -- or to make them enjoy more of it, meaning experience more.

Just to give you a for instance, there were days during the holiday season where we were entertaining 250,000 guests at a time on-property. And when you just consider how many guests you have to flow through the gates when the park opens in the morning -- the fact that you have a band that enables you to basically walk right in, touch the band to a kiosk and keep going instead of handing a ticket to a cast member; making sure the ticket is right; and then going in, that's obviously creating a huge improvement, meaning much quicker entrance into the park.

And what this all adds up to is our ability to manage more people at a time without in any way diminishing guest experience. We did see in the quarter a positive impact to the bottom line



from *MyMagic+*, just the beginnings of it. We will continue to see more of that. But we do not have data that we can share with you right now about specific guest spending.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Jessica, this is Jay. Tying in your second question about Shanghai preopening costs -- I'm not going to go into the details of what that will be in fiscal 2015, but following on what Bob just said about *MyMagic+* becoming accretive this quarter, I will tell you that the increase in contribution from *MyMagic+* this year will outweigh the preopening spending on Shanghai Disneyland in our total numbers for fiscal 2015. So that might give you some sense at least that Shanghai will not be a drag on our earnings in fiscal 2015.

Jessica Reif Cohen – *Analyst, Bank of America Merrill Lynch*

Great. Thank you.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

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

Thanks, Jessica. Operator, next question please.

Operator

Doug Mitchelson with UBS.

Doug Mitchelson – *Analyst, UBS*

Thank you so much. So one for Bob, and one for Jay as well. Bob, your comments on Sling TV and not having data on the customers hit squarely on the question I wanted to ask you, which is: with a broadband-only, non-Pay-TV market growing in size, I would think it becomes ever more interesting for Disney to address that. I think the default is to generally support the existing Pay TV bundle and highlight Hulu and Sling as dipping your toe in the water.

But I was hoping you would address whether there is a potentially superior business model for Disney to capture the distribution margin yourself, benefit from dynamic advertising -- targeted, of course; and having that direct relationship with the consumer that you've been



seeking. And I'll just throw Jay's question in there now as well. You have been asked a lot of questions on recent calls about ESPN's top line; I wanted to refocus on margins.

So with the March 2015 quarter, the company is finishing a long and expensive build-out of sports rights. It seems like the rest of the decade you've only got a couple of tough quarters when the NBA hits. Are we thinking about that correctly -- that even if ESPN revenue growth might moderate a bit, cost growth is also moderating. Any reason to think that margins shouldn't generally be flat to up going forward ex those NBA quarters? Thanks so much.

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

Doug, I'll take the first part of the question -- or your first question, since it was directed at me. And you are right; there are 12 million, right now, subscribers to broadband-only service. And that's a subscriber that we are trying to reach with this Sling -- or that DISH is trying to reach with this Sling package.

And we believe that it's a worthwhile experiment or a worthy attempt to try to convince young people or younger people to sign up to cable when they either wouldn't have signed up for it at all or they might have waited, Michael's comment aside. There is definitely an opportunity not just for ESPN, but for other Disney brands to ultimately put product in the marketplace that reach consumers directly.

We think we have that opportunity with a Disney-branded service. We may have an opportunity to bring out a Marvel-type product and possibly even Star Wars. But we also are mindful of the value of the expanded basic bundle to this company. And we do not believe that there is any reason for us to attempt to take out some of this product, particularly ESPN, quickly or right now.

In other words, there is time. If we see that market dynamics are changing in such a way that it's better for us as a company to take the product out directly and to not only improve our margins by taking out the middleman, but to create a closer relationship with the consumer that can be mined for other revenue-generating purposes, then we will do that. But we think if we were to do that now, it would be somewhat precipitous of us. And there doesn't seem to be any reason to be that way.

Doug Mitchelson – *Analyst, UBS*

Understood. And then, Jay?



Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

In terms of your question on costs, let me tell you this, Doug. First of all, there are only a couple of bumps left of big upticks in the ESPN programming cost base over the next, let's call it four or five years.

The first one we are in the middle of, which is our new NFL deal, the launch of the SEC Network, and next quarter in a pretty significant way the College Football Playoff. And the second big one down the road in 2017 is the beginning of our new NBA deal.

Other than those bumps which, as I said, one we are in the middle of -- in fact, we gave you some guidance on costs this year, that we would be experiencing very heavy ESPN programming costs in the first half of the year and much lighter in the second. I can tell you that those numbers are about 25% in the first half of the year and only flat to 1% increase in the second half of the year. And then there's 2017, when the NBA deal kicks in.

So we've told you many, many times -- of course I'm talking about overall cable margins, because that's all we speak of. Other than that, we've told you many, many times: we don't run ESPN on a margin basis. We won't give you guidance on what the margins will look like. But we expect the business to continue to grow. We have those two periods of year-over-year or quarter-over-quarter cost increases. And other than that we still have high expectations for growth in this business.

Doug Mitchelson – *Analyst, UBS*

Thank you very much.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

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

Doug, thank you for those questions. Operator, next question please.

Operator

Alexia Quadrani with JPMorgan.



Alexia Quadrani – Analyst, JP Morgan

Thank you. A few questions, if I can. First, are you seeing the fantastic momentum in the Consumer Products business continue past the holiday season? And how early can we begin to see a ramp in front of *Star Wars*?

And the second question -- sort of bigger-picture question on advertising: it looks like you have a strong start to the year around advertising at ESPN, I guess in part from those very good ratings there. I guess any broader color you can provide on the advertising market, what you are seeing? I think you had mentioned earlier, Bob, that you see a little bit of flattening out of the share shift to digital. I guess any color on that?

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

We can't give you much guidance on Consumer Products right now, except to say that the business that we saw in January was quite strong. And we clearly were seeing some -- I'll call it even post-holiday momentum, which is unique in terms of our experience, and I think it speaks to continued demand for our franchises.

We've got a great lineup of product in the marketplace this year when you consider *Cinderella*, which is in March -- and it's a great film -- and clearly, that's a very important franchise for the company. Then we've got *Avengers* in May.

And then, of course, two Pixar films in calendar 2015, although we don't know that any one of them will drive significant consumer products. And then *Star Wars*, as you mentioned, Alexia, the end of the year.

We are not going to predict whether there will be a ramp-up of buying ahead of *Star Wars*, except that we believe because of the strength of the franchise and the buzz around the movie -- which we saw, certainly, was the case when we put the teaser trailer out just around Christmas-time -- that we are likely to see some buying in advance of the movie of consumer products.

The other thing that I wanted to mention, because we have talked a lot about *Frozen* -- well, you didn't mention it -- is that we are coming out on March 13, attached to *Cinderella* with a seven-minute *Frozen* short that's just great; that has all the key players, both the voice talent, and the character talent -- or the characters, and a great song. And we actually believe it's going to generate some more buzz for *Frozen*, and that should generate more buying in terms of consumer products.

Maybe Jay and I can both address advertising?



Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Yes

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

Well, Jay, why don't you go ahead and take it?

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

So, kind of looking separately at the advertising market for ABC and the advertising market for sports, let me start with the latter. You know, the Q2 marketplace seems to be improved on the sports front. And you know, with the powerhouse lineup of rights that we have in these sporting events that we have in Q2, particularly around the College Football Playoff -- you know, we are going to be able to take advantage of that uptick in the sports marketplace in Q2.

On the ABC front, I think that we are not seeing any radical change in the market from what we have talked about in past quarters. Again, we are very, very happy with the lineup of shows that we've introduced, both on the drama and comedy side. We have more of those coming into the market. And so we are hopeful that we can also take advantage of the dollars that are out there on the primetime side.

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

And one other thing to add: I spoke to the head of ESPN ad sales this morning. There haven't been that many new car launches in the last number of months. I know that one of the big automotives just released results which were quite positive.

We think there's some real potential particularly for ESPN in the automotive category, which has not been a hot category. If you watched the *Super Bowl*, there weren't that many automotive spots in the *Super Bowl*, for instance. But that's an opportunity in the rest of the year for ESPN as car companies roll out more new models, which they haven't been doing.

Alexia Quadrani – *Analyst, JP Morgan*

Thank you very much.



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

Alexia, thanks for the questions. Operator, next question please.

Operator

David Bank, RBC Capital Markets.

David Bank – *Analyst, RBC Capital*

Thanks. I have two questions for whoever is willing to answer them. The first one is a follow-up on the last question, actually. I was a little surprised at the advertising revenue declines at ABC, in that this is one of the most successful seasons to date that I can remember for ABC. 18 to 49, I think you are flat to marginally up. You are really sort of outperforming the rest of the industry.

And I would think with a modicum of pricing, you would have had stronger growth. So maybe looking for a little bit more color there.

The second question is: Jay, can you give us the actual change year over year in total sub count at either ESPN or what you would call the expanded basic bundle? Thanks very much.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Ok, thank you, David. Let me start with the advertising question. So to recap, scatter pricing was up in the market and overall ad sales, as you said, were down, as ABC sold fewer units this year compared to last year. And the lower unit sales can be attributed to a number of factors, and I think a combination of those factors had an impact on this quarter, making the advertising sales numbers lower. And those are related to the length of the show, how the shows are written, the number of promotional spots we put in the shows as opposed to sold spots, the number of ads we insert into the programs, and how we use inventory in the quarter to manage our make-good liability.

Those all combined to deliver, notwithstanding the ratings we had -- the relative ratings we had this season -- to slightly depress our advertising revenue. I think ABC is extremely well positioned this year relative to its peers.

We expect a tightening of inventory as the year progresses. And I think we are well positioned to take advantage of the market conditions, hopefully, as they improve in the course of the year.



On the subscriber side: I'm not going to give you any help there. We don't talk about subscribers. We can't give you any guidance there. So I'm sorry about that.

David Bank – *Analyst, RBC Capital*

Can't blame me for trying. Thanks very much, guys.

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

David, it was a good effort. Thanks for the questions. Operator, next question, please.

Operator

We have Todd Juenger with Sanford Bernstein.

Todd Juenger – *Analyst, Bernstein*

Let me take an effort at looking a little longer-range at the parks, if I may. So as the fruits of the slate of parks investment projects are now, I think, successfully rolling in and Shanghai's grand opening is in sight, I wonder if you are at a stage where you are ready to share with us anything you are thinking about the future horizon beyond that? I know you won't announce any specifics; but just generally, are there types of opportunities that you could generalize that you find particularly interesting at the top of your list? Are there certain things that you considered and rejected? How should investors think about your appetite to continue expanding your parks program?

And then the second follow-up, Jay, if you could, just remind us how you are thinking about leverage. With all the growth in EBITDA and cash flow, I don't think you have issued much debt lately. So just remind us how you think about leverage as you move through the year? Thanks.

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

Todd, in terms of the parks I think what you have to consider is that it's we are in construction to build a sizable AVATAR presence and AVATAR-land at Animal Kingdom in Florida. That's slated to open sometime in 2017.

We have a fair amount of design and development work going on right now to greatly increase -- this is no surprise -- *Star Wars* presence in multiple locations around the world. We'll have more details probably about that later on in 2015. The plans are ambitious, and so it's going to take some time for them to actually be built and open. But let's just say that we've got big plans



for it and a huge belief in that franchise as a parks experience. I think it's also likely that you will see an expansion at Hong Kong and at Shanghai.

Obviously, Shanghai has yet to open. So maybe it would sound somewhat premature. But the size of the land that we have there -- the expansion opportunities in a market that we think is just perfect for a Disneyland experience -- suggests that once we open it's just the beginning in terms of the variety of offerings we will be able to provide.

And then, of course, the franchise that we talked about earlier, which is *Frozen* -- but I think that actually says a lot about other franchises, too. There are clearly more opportunities to mine some of these great franchises across the parks. And when you go to Imagineering, there is an embarrassment of riches, so to speak, in terms of stories and characters that the Imagineers have to draw from to create great park experiences.

And I think one of the things that we are seeing now in our parks, and one of the reasons why the results were so strong across the board Christmas-time is that there is definitely a halo effect that consumers have for Disney based on all of these franchises. And it's not just what exists in the parks; I think you have to include Marvel and you have to include *Star Wars* as well.

The brand strength has never been stronger. The array of franchises has never been greater. We said we've got 11 franchises that are going to generate \$1 billion this year in retail sales. And that just, I think, results in enthusiasm for the brand and enthusiasm for the park experience that we provide. It gives us not only ample opportunities to create from all of that, but for consumers to basically engage with us in more ways and more places than ever before.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Todd, in terms of the balance sheet and our overall perspective on leverage, I guess I'll say that we are very happy with our balance sheet. We are very happy with our strong rating in the debt markets at all three agencies. And it really is a strategic asset for the company -- whether you look at our average cost of debt; the amount of subscription we get to any debt issuance we put out; the rates at which we are able to manage our working capital through commercial paper; and, of course, the ease with which we have thought about and executed on acquisitions without a concern about the impact of those transactions and potential transactions on our rating and on our having the debt capacity to do that.

So I think in general I don't expect you -- you shouldn't expect a radical change in that strategy. It doesn't mean we won't be in the debt markets this year, but I would expect that you will continue to see a balance sheet that reflects kind of the strategic use of -- the strategic positioning of not being overleveraged on the operation of our company and our ability to go to the capital markets.



Todd Juenger – *Analyst, Bernstein*

That's very helpful. Thank you both.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

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

Todd, thanks for the questions. Operator, next question please.

Operator

Ben Swinburne with Morgan Stanley.

Ben Swinburne – *Analyst, Morgan Stanley*

Thank you. Two questions for either of you, the first one on consumer products. Can you help put *Frozen* into context for us, now that you have a calendar year behind you, including the holidays, where you had the inventory where you wanted to? I think years ago we thought *Cars* was the high-water mark in terms of annual revenue contribution. But can you tell us whether *Frozen* has now exceeded that and if you believe that this a recurring and growing licensing contributor year in, year out, irrespective of whether there's film product?

Any comment on the margins, too. I think your incremental margins at CP were in the almost 80% range. So any color on profitability would be really helpful.

And then I just wanted to make sure that the cable guidance was reconfirmed -- the high single-digit OI guidance? Jay, if you just could confirm that, that would be great. Thanks.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay. Let's start with your consumer products question. So, look, I don't think that we can underestimate the impact that *Frozen* has had across our company in all of our businesses; but I don't think it would be right to take from that the implication that even our consumer products business was overly dominated by the *Frozen* franchise this quarter.

You asked whether we think *Frozen* has -- to put words in your mouth, do we think *Frozen* has legs? We absolutely believe that this is the beginning of a long-term franchise for the company.



And that will reflect itself in all of our divisions -- Consumer Products certainly not least of which.

But even if you look at the last quarter, many other franchises were contributors to the success of the Consumer Products division -- by the way, not the least of which was Mickey and Minnie, the Disney Channel franchises. And we like what *Frozen* delivered, but it's certainly not the one and only for us.

We have 11 franchises that now retail at over \$1 billion as of the last year. So our Consumer Products business really has a lot of breadth in addition to depth, and we are only beginning this year to see what the *Avengers* and overall Marvel franchises are going to deliver, which has also been a huge contributor. And I think if you look down the road, you could imagine that we will be adding *Star Wars* to that pantheon in a very, very significant way with the release of that film.

So it's a broad-based business. And I think that *Frozen* will continue to play a big part in it, but I wouldn't make the mistake of thinking that it is a dominant force that you have to worry about repeating year on year in the Consumer Products business.

In terms of margin, obviously the licensing business is incredibly highly leveraged; but I think the real margin story for this past quarter has been the Disney Stores business, where we saw increases both in the physical brick-and-mortar stores in all of the three regions we operate -- which is Japan, Europe, and North America -- as well as the online business in those three regions. So I would venture to say, and I think I'm right about this: we had historic margins in that business this past quarter and it was a big contributor to the margin story for Consumer Products.

Your second question was about OI growth guidance --

Ben Swinburne – Analyst, Morgan Stanley

High single-digit -- yes.

Jay Rasulo – Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company

-- OI growth guidance for our domestic cable. I am only going to repeat -- we don't give quarter-to-quarter or annual guidance on that, but I'm going to reassert what we said back in April last year at our investor day: that fiscal 2013 to 2016 we are expecting high single-digit growth in cable OI, and we still are on target to achieve that.



Ben Swinburne — *Analyst, Morgan Stanley*

Thank you.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

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

Thanks for the questions, Ben. Operator, next question please.

Operator

Jason Bazinet, Citi.

Jason Bazinet — *Analyst, Citigroup*

Two very quick ones. You mentioned \$1.3 billion of buybacks in the quarter and \$1.4 billion fiscal year-to-date. Was there anything that would cause you to be out of the market? Or in other words, if you are in our shoes, do you think we should be moderating our buyback for the quarter?

Second, we've been surprised at the strength in international inbound flights into the Orlando airport, particularly in light of the stronger US dollar. Do you guys have any hypothesis for why international visitors would be up so much? Thanks.

Jay Rasulo — *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay. On buyback, I guess I'll say this -- I'm not going to really give you much guidance on this, but we remain committed to returning capital to shareholders, as we have been, through dividends and buybacks. You know this year we announced a very significant increase in our dividend of 34%, bringing it up to \$1.15. And that happened in this quarter.

And I wouldn't focus too much on the first couple of weeks of this fiscal quarter as an indicator or any kind of guidance as to where we will wind up on the entire fiscal year relative to buyback. So I don't have any big news for you. You know, our dividend is almost \$2 billion that we paid out in Q2. And I think you have to look at capital return to shareholders in aggregate, which is the way we think about it.



Your second question on arrivals -- so I don't think that we know or have seen an impact on international arrivals due to exchange rates. You know I have said for many, many quarters, the overall range of our international business is between 18% and 22% of total attendance at our domestic parks.

Q1 is usually on the low end of that range. It was again on the low end of that range this year. And I think that if there is going to be an effect of the varying exchange rates around the world, it will take a while. And if those exchange rates affect the economies from which our international business is sourced, we might see an impact. But as of yet we have not seen that.

And actually, quarter to quarter, year on year, there wasn't a huge change in our international business between fiscal 2014 and fiscal 2015.

Jason Bazinet – *Analyst, Citigroup*

Thank you very much.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

You're welcome.

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

Thanks a lot, Jason. Operator, next question please.

Operator

Anthony DiClemente with Nomura.

Anthony DiClemente – *Analyst, Nomura Securities*

Thanks. I have one question for Jay first and then one for Bob. Jay, on the broadcasting segment, this has been four straight quarters of operating income growth in addition to the ratings resurgence at ABC. Presumably retrans and affiliate comp are a big part of that growth, so I wonder if you would help us with the shape of the trajectory of retrans and reverse comp over the next two or three years, and maybe even as part of that give us an update as to what you are annualizing on that, either in 2015 or on an annual basis?

And then for Bob, just on acquisitions, when Disney first made the acquisition of Maker Studios, you said that you saw it first and foremost as a distribution platform. And at a high level I was



just wondering if you could give us your thoughts on vertical integration -- or your updated thoughts -- particularly vertical integration in digital. How does a more vertically integrated acquisition like Maker compare strategically for you to more horizontal acquisitions in content, like Lucas or Marvel? Thanks.

Jay Rasulo – *Senior Executive Vice President and Chief Financial Officer, The Walt Disney Company*

Okay. Let me start with your broadcast question. We have said in the past that we expected by fiscal 2015 to be in the \$400 million to \$500 million range in terms of retrans; well, it's 2015 and we are there. We will be there comfortably, but I'm not going to update any further than that.

On the overall broadcast business, you know, I think that we've been saying for many, many years that our play in this business is to be the creator and owner of great shows, and those shows pay back in the aftermarket when we sell them, either to other networks into syndication or, increasingly, sell them to other distributors. And that's what you are seeing in our broadcast results this quarter.

It is exactly strategically where we want to be in this business. And the fact that we have shows on the network today that are being incredibly well received, have legs, and are rating well, is a very good indication for where we can be in this business.

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

To respond to the question about vertical versus horizontal acquisitions and Maker -- first of all, Maker's results in terms of consumption, number of videos streamed since the time that we bought them, has been up substantially. Just huge growth.

And what that tells us is really what our instinct was when we bought them, and that is that we were really interested in, compelled by the substantial increase in consumption of short-form video on digital platforms. We had consumption of short-form video on our own digital platforms, like ESPN.com; Disney.com; ABC. But we didn't have the kind of traction or the kind of traffic that Maker had.

We thought this would be a great opportunity for us to distribute much more effectively in short-form. It also was an entree into a world of creativity that we thought we could tap into, particularly when we allow those that are creating in that space access to our franchises and our brands. So it was kind of a combination of things. It was just distribution expertise that we did not have as much as we thought we should and certainly production and creative expertise that we thought we could use.

And it was, I think, a unique acquisition opportunity for us -- again, given all the growth in short-form consumption. I don't think it necessarily suggests a direction in terms of where we are



heading as a company overall. The power of this company largely is in its brands, and storytelling, and the creativity that runs across platforms and is often distributed by third parties -- whether they are movie theater owners, big-box retailers, or MVPDs, to name a few; or new platforms, like Netflix, and Amazon, and Hulu.

So I think the primary thrust of the company is going to continue to be investing in its brands and its creativity, and selling as broadly as we possibly can. But we like being in the new space as well.

And one last thing, because I think this is going to loom larger and larger in terms of Disney's future -- and we touched upon it a little bit earlier today -- is that I think this company needs to focus more on creating a tighter or a closer relationship to its customers for a variety of reasons. Not only to mine customer data and usage and, obviously, create revenue opportunities from that; but to provide customers with experiences that they want and demand -- basically, to be even more user-friendly, more customizable, more personalized. That's really important in terms of the long-term future of this company. And you will see in various initiatives that are aimed at achieving just that.

Anthony DiClemente – *Analyst, Nomura Securities*

Thank you very much.

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

Operator, thank you for the questions. Operator, I think we have time for one more question today.

Operator

David Miller, Topeka Capital Markets.

David Miller – *Analyst, Topeka Capital*

Hey, guys. Congratulations on the stellar results. Just a couple offbeat questions. I guess I am going last here, so a few of the obvious questions were taken.

Bob, just first of all, I'm surprised you didn't call out the delay in Shanghai. I guess you can't really call it a delay. Is the sort of postponement of the opening just due to -- you know, you want to open this thing kind of coinciding with the Chinese Lunar New Year in the spring? Or were there other nuances?



And then I have a follow-up. Thanks a lot.

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

When we signed the contract for Shanghai, and when we broke ground, we said publicly that we were targeting the end of 2015 as an opening date -- targeting, which I think is important. We obviously were embarking on a very large, fairly complicated project, one of the largest we have ever engaged in. Probably one of the largest ever in China.

After we opened, we decided that the opportunity existed in China and specifically in Shanghai to build something even bigger, with more attractions and, basically, more capacity, so that we could handle more guests. So not only did we design but we agreed with our partners to build approximately \$800 million more in capacity, which obviously added to the scale of what we are building.

So now that we are well into construction, and we released a great photo today of the Disneyland Hotel, which gives you an idea of how far along we are. We believe that targeting the spring -- actually, it was more than targeting; we plan to open in the spring of 2016 -- is much more opportune for us, given the size of what we are doing, what we are building, and the complexity of it.

And given the fact that the weather is better in the spring -- and as you said, David, it is after the Chinese New Year, where we expect there to be huge demand. And it's a bit easier to open after that than right before. I might have misspoken -- I meant after we broke ground, we decided that we would build larger, not after we opened.

David Miller – *Analyst, Topeka Capital*

Right.

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

And so we've got a great project unfolding. I was there the week before last, and every time I go I am just amazed at the scale of it and the variety and the uniqueness of this. And I continue to believe heavily in the opportunity that we've got to bring a great Disneyland experience to the most populous country in the world. My enthusiasm has only grown for it, but because we are building something bigger, and we like spring versus winter, then the spring of 2016 it is. And we probably will be more specific about an opening date, I'm guessing, sometime in the middle of this year.



David Miller – Analyst, Topeka Capital

Okay. And just a brief question on *Inside Out*. And there is just some mild confusion here -- albeit, not that much confusion -- but was *Inside Out*, and I'm just asking out of personal curiosity: was *Inside Out* original Disney IP that sort of got transferred over to Pixar, and Pixar kind of took it over? Or was that from the very beginning original Pixar IP that we are going to see next year? Thanks a lot.

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

No, that's Pixar homegrown. Actually grown from the mind of the great Pete Docter, who directed and created *Up*, and *Monsters* prior to that. It comes out in June of this year. But no, totally -- Pixar through and through.

David Miller – Analyst, Topeka Capital

Thank you very much.

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

All right. David, thank you for those questions. And thanks again, everyone, for joining us today.

Note that a reconciliation of non-GAAP measures that were referred to on this call to equivalent GAAP measures can be found on our Investor Relations website. Let me also remind you that certain statements on this call may constitute forward-looking statements under the securities laws.

We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them, and we do not undertake any obligation to update these statements. Forward-looking statements are subject to a number of risks and uncertainties, and actual results may differ materially from the results expressed or implied in light of a variety of factors, including factors contained in our annual report on Form 10-K and in our other filings with the Securities and Exchange Commission.

Thanks again, everyone, for the time today. And this concludes today's call. Bye.

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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 September 27, 2014 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.