The Walt Disney Company

Q1 FY16 Earnings Conference Call

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Disney Speakers:

Bob Iger

Chairman and Chief Executive Officer

Tom Staggs

Chief Operating Officer

Christine McCarthy

Senior Executive Vice President and Chief Financial Officer

Moderated by,

Lowell Singer

Senior Vice President, Investor Relations

PRESENTATION

Operator

Welcome to the Walt Disney first quarter FY16 earnings conference call. My name is Bianca and I will be your operator for today's call. (Operator Instructions)

Please note that this conference is being recorded. I will now turn the call over to your host, Mr. 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 2016 earnings call. Our press release was issued about 40 minutes ago and is available on our website, at www.disney.com/investors. Today's call is also being webcast and a replay and a transcript will be available on our website.

Joining me for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer, Tom Staggs, Chief Operating Officer, and Christine McCarthy, Senior Executive Vice President and Chief Financial Officer. Bob, Tom and Christine will each make some comments and then, of course, we will be happy to take your questions. So with that, let me turn the call over to Bob and we'll get started.

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

Thanks, Lowell. And good afternoon everyone.

I am thrilled to announce that our Q1 performance was the greatest single quarter in the history of The Walt Disney Company, and a phenomenal start to fiscal 2016. Revenue was up

14%, net income was up 32%, and adjusted earnings per share were up 28% to $1.63, which is our highest quarterly EPS ever, and is also our 10th consecutive quarter of double-digit EPS growth.

We had tremendous performance across our portfolio of businesses. With the incredible success of *Star Wars: The Force Awakens*, our Studio delivered $1 billion in quarterly operating income for the first time in history. Our Parks and Resorts also made history, with nearly a billion dollars in operating income. And our Consumer Products & Interactive business set another record, with $860 million in OI.

Our results clearly show that our long-term strategic focus and investments in brands and franchises are driving remarkable value in these businesses, greatly increasing their impact on the company and further diversifying our future growth.

Over the last 10 years, we've built an enviable collection of vibrant, valued and admired brands. We've also created, acquired or re-envisioned several of the worlds' most valuable franchises. And we're fully leveraging these assets across our portfolio of businesses and around the globe.

Of course, nothing reflects the impact of this strategy better than the phenomenal resurgence of the Star Wars franchise, and there's no better way to propel this franchise into the future than producing quality products. It's been absolutely thrilling to see the reaction to our first Star Wars feature film, *The Force Awakens*. Audiences and critics alike really love this movie. It's the only film in history to ever reach $900 million in domestic box office and, as you may have heard, it crossed $2 billion in global box office over the weekend, more than doubling the worldwide box office for the last Star Wars release a decade ago.

Breaking records at the box office is only the beginning. Global retail sales for Star Wars merchandise in the first quarter exceeded $3 billion, more than triple the global retail for this franchise in Q1 of last year. Star Wars is also driving unprecedented growth for our mobile games, and EA's launch of *Star Wars Battlefront* was the biggest video game release in Star Wars history, with more than 13 million units sold.

Filming of *Star Wars: Episode VIII* -- the next chapter of the legendary saga -- has just commenced and it will be in theaters December 2017. And production of *Episode IX*, a 2019 release, has also begun.

In the meantime, we'll keep fans engaged in the Star Wars universe and further expand the franchise with the release of *Rogue One* this coming December. It's a compelling and original, stand-alone story about a band of rebels attempting to steal the plans for the Death Star… set just prior to the events in the very first *Star Wars* movie -- *Episode IV: A New Hope*.

Filming of *Rogue One* is virtually completed and we absolutely love what we've seen so far. This is the first of a set of planned stand-alone stories, and we're already in preproduction on our next one, for release in May of 2018.

And on the Parks front, later this year, we'll break ground on spectacular new Star Wars-themed lands in Disneyland and Walt Disney World.

Clearly, Q1 saw the impact of our extremely successful "re-launch" of the Star Wars franchise, as well as its enormous potential to drive value across our entire company for the foreseeable future. Given our unparalleled mix of some of the world's best IP and strongest brands, we're well positioned for continued growth over the long term, regardless of changing dynamics in the media landscape.

Turning to a subject that has gotten a lot of attention lately, ESPN and the status of the bundle. In the last couple of months we've actually seen an uptick in ESPN subs, which is encouraging. We are also pleased with what we're hearing from DISH about the response to SlingTV, a light package that includes ESPN. The service appears to be growing nicely and is proving very attractive to young consumers in particular -- significantly over-indexing among Millennials -- and has been quite successful in bringing previous cord-cutters back to Pay TV along with new subscribers. SlingTV is clearly additive to the robust MVPD universe, and our networks benefit accordingly.

The popularity of sports and the strength of ESPN add great value for consumers who want lighter packages and we're currently in discussions with new and existing distribution partners to create an array of innovative new services and light packages featuring ESPN.

We will continue to focus on subscriber trends, moving quickly to embrace and create opportunities to drive value in the evolving market. It's interesting to note that Nielsen has significantly lowered its estimate of losses of multi-channel households in 2015. Regardless, in any market, we believe ESPN is well-positioned to continue to thrive for many reasons, including the demand for sports programming -- especially live sports -- is undiminished and consumption is at an all-time high. Last year, 95% of Americans with a multi-channel bundle watched sports, and 81% of those viewers watched ESPN content. Across all platforms, more than 200 million adults engage with ESPN in an average month. In other words, four out of five adults in this country connect with ESPN on some platform every month, usually more than one.

ESPN has the sports that most people want. It holds more national sports rights than all other sports media combined. And it has the most important rights secured into the next decade, including the NFL, the NBA, Major League Baseball, and the most coveted college sports.

Consumers, advertisers and operators see great value in ESPN. The vast majority of consumers still see tremendous value in the multi-channel universe, and they consistently rank ESPN as the #1 or #2 most valuable channel within it.

ESPN's ad revenue continues to grow, thanks to its proven ability to reach audiences that advertisers value most. In fact, ESPN's ad sales significantly outpace the market, growing three times faster than television advertising overall over the last six years. MVPDs just ranked ESPN #1 in perceived value for the 16th year in a row due in part to the fact that ESPN drives more local ad sales and broadband subscriptions than any other service in the market.

The expanded basic bundle will remain the dominant product for consumers for the foreseeable future, but competition from new video services and products will only grow. Better user interfaces and greater mobility make these newer services enormously appealing, especially among young people. And many of our brands, including Disney, Marvel, Star Wars, and ESPN are tailor made for over-the-top, direct-to-consumer, app-based video products. So, expect innovation and continued pursuit of new distribution opportunities.

Our results this quarter clearly demonstrate that our focus on high-quality, branded content and franchises to diversify our asset mix, our ability to use technology to aggressively create new opportunities, and our ambitious global growth, are paying off with record performance. We're proud of our achievements, we're excited about the future, and we're confident in our ability to continue to drive growth across the entire company.

I'm going to turn the call over to Tom to walk you through some highlights across the company, and then Christine will take you through the details of our performance in Q1.

Tom?

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

Thanks, Bob. Hello everyone.

As Bob just highlighted, the strength of our branded programming networks gives us confidence in our ability to continue to grow our Media Networks business. In addition, the marketplace offers a range of other new opportunities for us. They include our continued investment in the future of Hulu as both a compelling consumer platform and another active buyer of high-quality content; our investment in and collaboration with Vice; our distribution agreement with Alibaba for *DisneyLife* in China; and ESPN's undertaking with Tencent in China as well. Our opportunistic approach also led to our successful Marvel series on Netflix, which helps extend the Marvel franchise and broaden its reach.

As importantly, after a decade of strategic, value-creating acquisitions and capital allocation, our other businesses have grown significantly, increasing their impact on our results. This purposeful diversification across branded franchises with attractive long-term potential, along with an aggressive approach towards leveraging new technologies and driving global growth are the key strategies we laid out a decade ago.

With branded content from Disney, ESPN, ABC, Pixar, Marvel, and Star Wars -- we have the most valuable collection of branded franchises and other high-impact IP in the world. And few companies have embraced the promise of new technology as enthusiastically and effectively as ours. These strategies are bearing significant fruit today and continue to guide our path for the future.

We've invested heavily over the last several years to significantly expand our Parks and Resorts business. Those efforts include the creation of *Cars Land* and transformation of Disney California Adventure, introducing *MyMagic+* and doubling the size of *Fantasyland* at Walt Disney World, doubling the size of our cruise fleet, and adding three new lands in Hong Kong.

The record results for the quarter -- which include all-time high global attendance, record results for our domestic parks and our best Q1 results ever for Disney Cruise Line -- reflect the impacts and value creation of these investments.

We're already benefiting from the success of Star Wars at our parks as well. Since December, more than six million guests have experienced new and refreshed Star Wars attractions and features in our parks, and this year we're rolling out even more themed attractions in parks and resorts around the world, including *Star Wars Day at Sea*, which debuted on the *Disney Fantasy* last month.

Our most important single new initiative at Parks is Shanghai Disneyland, which will have its grand opening on June 16th. Tickets will officially go on sale on March 28th, an announcement that has been incredibly well received in China.

Bob and I were just over there and we couldn't be more pleased or excited with how well our preparations are going, thousands of new cast members have already been hired, ride testing has started on the attractions, and the anticipation is palpable, and growing. Shanghai Disney Resort is going to be a tremendous source of pride for everyone involved. It's one of the most extraordinarily creative and innovative projects in the history of our company, which makes it the perfect way to firmly establish Disney in the hearts and minds of the people of China as well as an attractive and profitable place to deploy our capital for the long term.

Our franchise-focused strategy is driving growth across the company, including in our Consumer Products & Interactive business. Star Wars was obviously a huge driver of Consumer Products & Interactive results for the quarter, but it wasn't the only one. We are also very pleased with licensing growth this quarter for Marvel, led by *Avengers*. As we've discussed previously, we have 11 franchises that generated more than $1 billion each in annual retail sales for the last two fiscal years, making our Consumer Products business uniquely broad and deep.

Our acquisitions of Pixar, Marvel and Lucasfilm gave us some of the most valuable IP in the world. They also brought some of the world's most gifted storytellers and innovators to Disney, unlocking even more creative potential across the company.

Bob touched on the ambitious slate of upcoming Star Wars films, but that is just one aspect of our incredible Studios' pipeline. We have two films from Disney Feature Animation this calendar year, starting with Disney Animation's *Zootopia*, an incredibly original, charming and very funny movie opening March 4th. This Thanksgiving, we'll release *Moana*, a comedy-adventure with incredible music, very much in keeping with the tremendous legacy of Disney Animation.

As you know, a sequel to *Frozen* is in the works. In the meantime, Disney Animation is creating the first-ever *Frozen* television special, which will air on ABC during the 2017 holiday season. And, following the tradition of *Lion King*, *Beauty and the Beast* and *Aladdin*, we have a new *Frozen* stage musical slated for Broadway in 2018.

Turning back to animation, we just celebrated the tenth anniversary of our Pixar acquisition. Pixar and our incredibly talented colleagues there have positively impacted every aspect of our company and contributed mightily to our success. Looking ahead, Pixar has as strong a line-up of films as we've ever seen. *Finding Dory*, the long-awaited sequel to Pixar's beloved movie *Finding Nemo*, opens this June. 2017 will bring us *Cars 3* plus another Pixar original film set in Latin America, called *Coco*. In 2018 comes *Toy Story 4*, followed by *The Incredibles 2* in 2019.

From Disney live-action, in April we'll bring Mowgli, Baloo and a host of other classic characters to life in a new way with the release of *The Jungle Book*. Johnny Depp returns this May as the Mad Hatter in *Alice Through the Looking Glass* and again in 2017 as Jack Sparrow for our fifth installment in the hugely successful *Pirates of the Caribbean* franchise. 2017 will also feature Disney's live-action version of *Beauty and the Beast*.

In addition, we have a fantastic slate of Marvel movies that extends through the end of the decade. *Captain America* and *Iron Man* face off in an epic battle when *Captain America: Civil War* opens in May. The movie features some of the most popular Marvel heroes, and we believe it will prove to be one of our best Marvel movies yet.

In November, we're launching another compelling character into the Marvel cinematic universe with the release of *Doctor Strange*, starring Benedict Cumberbatch. Marvel's *Guardians of the Galaxy* return next year, along with *Thor: Ragnarok*. In 2018, we'll release three more Marvel movies: *Black Panther*, *Avengers: Infinity War*, and *Ant-Man and the Wasp*. And with more than 7,000 characters in the Marvel universe you can expect the Marvel storytelling to continue.

We're excited about the future of all of our great brands, and the opportunity they provide to drive continued growth and value for our company across our businesses, around the world, and through platforms both old and new.

And now, I'll turn the call over to Christine to walk you through our results in more detail.

Christine?

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

Thanks, Tom and good afternoon everyone. It's worth noting again, fiscal 2016 is off to a phenomenal start. We delivered strong revenue growth of 14% during the first quarter to a record $15.2 billion dollars. Earnings per share, excluding items affecting comparability, were up 28% to a record $1.63.

Studio Entertainment had its most profitable quarter ever, and that's following record full-year results in fiscal 2015. Operating income was up 86% to over $1 billion dollars. The growth in operating income was primarily due to the fantastic worldwide theatrical performance of *Star Wars: The Force Awakens*. Home entertainment and television distribution results were also up in the quarter, demonstrating our Studio strategy continues to create value beyond the theatrical window.

The success of *Star Wars* at the box office also drove increased demand for *Star Wars* merchandise. Operating income at the recently combined Disney Consumer Products & Interactive Media segment was up 23%, and segment margins were up over 500 basis points to 45% driven by the growth in merchandise licensing and games, primarily on the strength of *Star Wars*. On a comparable basis, earned licensing revenue was up an impressive 23% in the first quarter, and that doesn't include the deferred revenue from *Star Wars: Episode VII* merchandise sold in the fourth quarter last year. The growth in Games was due to higher licensing revenue from *Star Wars Battlefront*, partially offset by lower Infinity results. The Disney Stores also benefitted from sales of *Star Wars* merchandise, however, the increase in the quarter was offset by very strong sales of *Frozen* merchandise in Q1 last year.

At Parks and Resorts, operating income was up 22% in the first quarter and reflects the favorable timing of the New Year's holiday period relative to our fiscal calendar, which we discussed on last quarter's call. We estimate this shifted about $90 million dollars in operating income into Q1 this year that was recognized in Q2 last year.

Our domestic operations had another great quarter. We continued to see strong demand from guests, specifically at our domestic parks and at Disney Cruise Line. Attendance at our domestic parks was up 10% in the quarter, and per capita spending was up 7% on higher admissions, food and beverage, and merchandise spending. Per room spending at our domestic hotels was up 9% and occupancy was up 3 percentage points to 92%. Our Cruise business had its best Q1 ever driven by higher ticket pricing and onboard spending, and that's despite a three-week dry dock of the *Disney Dream*.

Growth in domestic operations was partially offset by a decline at our international parks as a result of lower operating income at Disneyland Paris, which was closed for four days in November, as well as pre-opening spending at Shanghai.

So far this quarter, domestic resort reservations are pacing up 2% compared to prior year levels, while booked rates are up 4%.

At Media Networks, operating income was lower in the first quarter compared to prior year. However, operating income would have grown in line with the 8% revenue growth we delivered when adjusted for the timing of the College Football Playoff and an adverse impact from foreign exchange.

Results in our Cable business were lower in the first quarter as higher programming and production costs offset increases in advertising and affiliate revenue.

The higher costs in Q1, which we discussed during our Q4 earnings call, were due to the timing of the six New Year's Eve and New Year's Day College Football Playoff bowl games, including the two semi-final games, which aired on ESPN. These games aired during the first fiscal quarter this year, whereas they aired during the second fiscal quarter last year. Higher programming and production costs also reflected contractual rate increases for key sports rights, including the NFL and college football, partially offset by the absence of rights costs for NASCAR.

Advertising revenue at ESPN was up almost 25% in the quarter, reflecting the timing of the six bowl games, as well as the strong advertising marketplace for sports in general. We estimate that ESPN's ad revenue would have been up about 14% adjusted for the timing of the bowl games and the absence of NASCAR. Underlying ad trends remain very strong, however, due to the timing of the College Football Playoff, ad sales are pacing down in the second quarter versus prior year.

Broadcasting operating income was down in the first quarter as growth in affiliate and advertising revenue was more than offset by higher programming costs and increased equity losses from our investment in Hulu.

Ad revenue at the ABC Network was up 8% in the first quarter due to an increase in units sold, higher rates and a shift in the timing of New Year's Eve programming to Q1, offset somewhat by lower ratings. So far this quarter, scatter pricing at the Network is pacing high-teens above upfront levels.

Media Networks affiliate revenue was up 4% in the first quarter, driven by a 7 percentage point increase in rates, partially offset by roughly a 2 percentage point decrease due to lower subs and a 2 point decrease from unfavorable foreign exchange rates. Broadcasting affiliate revenue was up more than the segment average, while Cable affiliate revenue, adjusted for FX, was up approximately 3.5%. Recall that we have fully lapped the launch of the SEC Network and don't have any major affiliate agreement renewals in fiscal 2016.

During the first quarter, we repurchased 21.1 million shares for $2.4 billion dollars. Fiscal year to date, we've repurchased about 35.5 million shares for approximately $3.8 billion dollars.

Overall, we feel great about the start of the fiscal year. Our strategy of investing in high-quality content, supported by the best brands in media, continues to pay off. We are mindful of the evolutionary changes taking place in our industry, and we feel we are well positioned to thrive in this evolving landscape due to the strength, depth and diversity of our businesses.

And with that, I will now turn the call over to Lowell for Q&A.

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

Thanks, Christine. Operator, we are ready for the first question.

Operator

Thank you sir. We will now begin the question and answer session. (Operator Instructions)

And we have our first question from UBS. We have Doug Mitchelson. Doug please go ahead your line is open.

Doug Mitchelson – *Analyst, UBS*

Thanks so much. Two questions. One, Bob, you outlined the record results at Film, Consumer Products, and Theme Parks. And I think investors are wondering, can it get any better than this? If you could help us just understand what the drivers of growth going forward in that business might be. Tom ran us through all the content that's coming. But are there particular initiatives that increase efficiency, or is this just, you think content in the future will continue to be better and better?

And then any clarification on the Cable Networks affiliate fee growth, 3.5% ex-FX, are you guys confident as you look forward that revenue growth in the Cable Networks business will be in line to ahead of operating expenses on a go forward basis, if that makes sense?

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

Well, we are not going to give guidance, Doug. But I will start by saying, as a response to the second part of your question, that we fully expect our Media Networks, including ESPN, to continue to deliver bottom line growth, which means that revenue growth is going to outpace spending.

Obviously, we are not going to give guidance on Film and Parks and Consumer Products, but I think you should look at a few things. First of all, the intellectual property cycle is not only robust, but in some cases, really still growing. If you look at Star Wars and you look at Marvel as examples of that. But we've got an incredible pipeline, as Tom outlined earlier, of Pixar and Disney animated films, and Disney live action. We also know that those films drive a lot of business across Parks and Resorts and Consumer Products. So I would say that the Studio will continue to provide more growth opportunities for the company, and that includes growth internationally, because China continues to grow as a market.

Consumer Products is really a great story for this quarter, because that is one business that while it did benefit significantly from Star Wars, we also saw continued success from other franchises -- and growth -- notably Marvel, which is a great sign. We expected that Star Wars was going to cannibalize some of our other franchises more and it didn't materialize.

And lastly on the Parks front, we have -- obviously, plans to build out -- domestically, we're building *AVATAR Land* and we're breaking ground, in fact soon, on Star Wars lands in the two domestic parks. And with Shanghai coming on board in June, while there are start-up costs this year, you can expect that that's going to drive growth for Parks and Resorts for many years to come.

So we feel really good about how all four of our businesses are positioned. And then I think you have to also consider what the media landscape looks like, and that is that there is a voracious appetite for high-quality intellectual property, particularly branded. And there isn't a new platform that launches that is not interested in licensing or gaining access to our channels or to our intellectual property. And we believe that we're going to see continued expansion across the world in new platforms, and that will create opportunities for us to grow.

Doug Mitchelson – *Analyst, UBS*

Thank you very much, Bob.

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

Doug, thank you. Operator, next question please.

Operator

From MoffettNathanson we have Michael Nathanson. Please go ahead sir.

Michael Nathanson – *Analyst, MoffettNathanson*

Thanks. I have two for Bob. First one is on ESPN. Bob, could you go back and clear up the differences in an answer you gave in August about what you thought the source of ESPN subscriber declines were versus what Skipper said in the Journal about skinny bundles? We want to understand, how much do you think the decline is from cord cutting versus skinny bundles? I wanted to put those two comments together.

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

It was a timing issue. At the time that I made the comments last August, we were seeing some sub erosion from both sides, from skinny bundles and from essentially a decrease in the total number of subs. At the time, because of what Nielsen was telling us, we concluded that most of it was coming from simple loss of subs. Once Nielsen corrected those numbers, reducing the loss of subs by some 2 million subscribers -- or 2 million households, I should say -- we concluded that, at that point, our sub loss was largely due to the fact that ESPN was not part of skinny bundles that had launched.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. And then you mentioned this $3 billion Star Wars Consumer Products. One of the questions we wanted to understand is, what do you think the tail is on *Star Wars*? Will it look like *Frozen*, where it gets stronger as consumers become more familiar with the product, or do you think it's more akin to -- tied to the release dates of these movies?

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

Well look, Star Wars has always been one of the most popular franchises in the world. And when we acquired it in 2012 all the way up to September, we continued to see -- saw some pretty robust sales of Star Wars merchandise, even though a film had not been in the marketplace since 2005. So we knew that when we brought a film out, it was going to greatly enhance sales of Star Wars merchandise. And not only did it do that, but it did it well beyond what our expectations were.

Don't forget, we did not bring new merchandise out for Star Wars until September 4th, and the movie came out in December. So we're still seeing quite a significant tail, even in this quarter, from the sale of Star Wars merchandise across the world. And by the way, one thing that's very interesting is, that is not just a U.S. phenomenon. And in fact, we saw some pretty interesting Consumer Products sales, even in markets where the movie didn't perform as well as either we had hoped or as well as other markets.

So with *Rogue One* coming out at the end of this year and then *Star Wars: VIII* and *IX* planned for 2017 -- meaning calendar year -- and for 2019, add another stand-alone film, we think that, while I don't want to predict that it's going to be steady state, that we're not seeing just something aberrational right now, but what we're seeing is the establishment of an old franchise but at a much higher level in terms of global interest and sales.

Michael Nathanson – *Analyst, MoffettNathanson*

Okay. Thank you.

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

Thank s, Michael. Operator, next question please.

Operator

From J.P. Morgan we have Alexia Quadrani. Please go ahead.

Alexia Quadrani – *Analyst, J.P. Morgan*

Hi. Thank you. I just have one on Parks and then a follow-up on Cable. First on Parks, we've seen another great quarter of very strong profit growth at Disney's domestic parks. I'm trying to get a sense of how much longer that impressive growth can continue and any color you can provide on how we should think about profitability for the rest of this year, given all the moving pieces with Shanghai.

And then a follow-up on Cable, just wanted to check and make sure that you are still comfortable with the high-single digit affiliate revenue CAGR over the next three-year guidance.

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

Alexia, it's Tom. Let me talk about the Parks. Bob mentioned that we have broken ground on the two Star Wars Lands. And of course, we think that's going to be a nice catalyst down the road. Before that, we will open *AVATAR* at Walt Disney World. So we have a cadence of new attractions here domestically that we think guests will really embrace. I think we also see opportunities, given the strong occupancy of room nights that we see, to consider expanding our hotel capacity down the road. So I think there are many avenues for us to continue to grow that business.

Of course, Bob talked about Shanghai and the growth that that will drive for us internationally. And remember, that while we open this June, we also have significant room for expansion there over time. So we believe that the good news is that guests continue to really embrace our product. We think there's room to grow that product and continue to expand.

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

Yes, I will take the second one. Hi Alexia, it's Christine. In reference to your question about the guidance update that was given in the 3Q call back in August, there is no change to that guidance and we're still very comfortable with it.

Alexia Quadrani – *Analyst, J.P. Morgan*

Thank you.

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

Thanks, Alexia. Operator, next question please.

Operator

From Bank of America Merrill Lynch we have Jessica Reif Cohen. Please go ahead.

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

Thank you, two different questions. On Theme Parks, U.S. demand seems insatiable year after year, driven by, obviously, your intellectual property and new attractions. With China four months away -- and you guys seem very, very excited about it -- how different -- I know you do tons of studies of the market -- how different do you think Chinese consumers will be over the long term, not just into the opening?

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

Well, Jessica, all of our research tells us that our intellectual property and our guest service and our parks experience will resonate extremely well with our Chinese guests. At the same time, we've taken great care to make sure that we designed Shanghai specifically for that marketplace in terms of the layout of the park, the food that we're serving, the type and scripting of the shows that we're putting on. So we are definitely adapting to that market, but we have real confidence that it's going to be a product that's going to resonate, and resonate for generations to come.

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

Okay, great. And then the second question, you know ESPN -- obviously a hyper focus by the market -- can you talk a little bit about the drivers of recent sub growth coming from Pay TV? Is it more cooperation between programmers and distributors? And secondly, are you close to your minimum thresholds with Pay TV operators? Meaning, should we be concerned that in your next cycle of contract negotiations -- we heard that you said none this year -- but is there any concern that the next go round will be more difficult?

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

You know, we don't know exactly what the drivers are, or were, for the uptick that we've seen recently in terms of sub growth. We believe that we've benefited from the growth of certain light packages that ESPN has been part of, particularly DISH. But I think you have to conclude that sports is very, very popular in this country. And when you look at the percentage of people that access sports on television and across markets and that access it -- across platforms, rather -- and that access it on ESPN, it's among the most, if not the most, popular programming out there. In fact, if you look at the studies that we've done among distributors, it's #1 or #2 in terms of value creation for them for 16 straight years. If you ask consumers, they say the same thing, it's #1 or #2 in terms of the most valuable channels that they get.

So I actually believe -- and I know you want to know about the floors in terms of our agreements -- but I actually believe that this notion that either the expanded basic bundle is experiencing its demise or that ESPN is cratering in any way from a sub perspective is just ridiculous. Sports is too popular. And it's not just at ESPN. Just look at how the *Super Bowl* did, as a for instance, which I realize is a penultimate event, but day after day, week after week, month after month, year after year, live sports ends up being among the highest rated programs across television. And ESPN has this incredible -- as you know -- incredible set of license agreements with all the major sports. It's got the best menu of live sports that is out there.

So we actually feel good about it. What we're trying to do now is we're engaging with virtually all of the traditional platform owners in pushing ESPN into light packages. And the success that DISH has experienced we think is a great selling point in that regard. At the same token, we're also looking at other opportunities with new platform providers that are emerging in the marketplace.

We don't comment on our relationship -- or the contractual relationship with the distributors, but it's safe to assume, we have not really touched the so-called floor element of those agreements in about 15 years. And we do not foresee, by the way, that the next round of negotiations, whenever they are, are going to be particularly difficult for us, because we come to the table, just with ESPN alone, with a product that people love.

And the other thing to note is the value of it from an advertising perspective. ESPN's ad pacing, as Christine mentioned, has been tremendous. And if you look over the last six years, it's advertising growth is three times the growth of television advertising. So you have a product that's great for distributors, it's great for consumers, and it's great for advertisers. And I believe really -- I guess, with great confidence, that it's going to thrive in whatever new media world order we're experiencing.

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

Great. Thank you.

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

Thank you, Jessica. Operator, next question please.

Operator

From Credit Suisse we have Omar Sheikh. Please go ahead sir.

Omar Sheikh – *Analyst, Credit Suisse*

Hi, everyone. So I'm going to surprise you by not asking a question about ESPN. I've got a couple questions. First, to Bob, if I can, and that's on Hulu. I wondered, Bob, if you could just update us on your current thinking on Hulu. How are subs going right now? Where do you think that business can get to in terms of subscribers in the domestic U.S. market? How do you think about potential international expansion? How does it fit into the Disney strategy? I'm just interested to hear your thoughts on that.

And then the second question, for Christine, maybe. Christine, you mentioned that there were some start-up or pre-opening costs in Shanghai. I wonder if you could just update us on what that number was in the quarter and how we should think about perhaps phasing of those costs in the current quarter as well? Thank you.

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

We're bullish on Hulu, and that's reflected in the level of investment that we and our other partners are putting into Hulu. First of all, we like new platforms, we like their appeal to young people, particularly millennials. Clearly, the user interface and the mobility of these new platforms is really attractive. It's also a great platform to license our product to, and we've actually derived a fair amount of revenue from doing that.

We believe that we're going to continue to invest in Hulu, and that while I don't want to speak for Hulu completely, their investment strategy is going to be to continue to license off-network movies, et cetera, but also to grow their original programming, which they're doing nicely.

I don't want to speculate where Hulu goes, but it fits very well into Disney's strategy in terms of our investment in new technology platforms and our support of new distribution opportunities.

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

Hi Omar. It's Christine. On the Shanghai question, back on our last conference call, we said the pre-opening costs, you should expect them to be in the $300 million range. Now that's an annual number. We have not broken them down by quarter, but you can expect those pre-opening costs to ramp into the open, which is going to be in mid-June. And also, given that we'll be only fully operational for a little more than three months during the year, the pre-opening expenses will impact the full-year results.

Omar Sheikh – *Analyst, Credit Suisse*

Okay, great. That's very good. Thanks.

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

Omar, thank you very much. Operator, next question please.

Operator

From Morgan Stanley we have Ben Swinburne. Please go ahead Ben.

Ben Swinburne – *Analyst, Morgan Stanley*

Thank you. Christine, can you just help us think about expense growth at Cable through the rest of the fiscal year? You mentioned that you've now passed College Football, so I think peak growth is now behind us. But how should we be thinking about that the rest of the year?

And then related, Bob, I'm just trying to square the subscriber growth comment with the subscriber headwind in the 10-Q. And I think part of this may be we're talking Nielsen and then paid subs. But are you saying you expect the subscriber headwinds to abate as we move through the next few quarters, given what you're seeing, or am I reading too much into that?

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

I'll take the second part of the question, then Christine can take the first. What I was talking about in terms of an uptick was recent. So the uptick that we talk about really didn't have much of an impact on this quarter. So what we believe we've seen, or what we have seen, recently is that subscriber trends going in the negative direction have abated somewhat. We're not making any predictions about them going forward, because we really don't know. We just feel great about the product, and we believe that, again, the predictions that many have made are more dire than they should be.

Ben Swinburne – *Analyst, Morgan Stanley*

Thanks for clarifying.

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

Okay. Ben, on the Cable programming costs, as we said on the last conference call, we expect fiscal 2016 Cable programming and production costs to be up low- to mid-single digits, and we are managing -- outside of the programming costs -- we are managing aggressively other costs at ESPN.

Ben Swinburne – *Analyst, Morgan Stanley*

Thank you.

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

Thank you, Ben. Operator, next question please.

Operator

From Nomura we have Anthony DiClemente. Please go ahead sir.

Anthony DiClemente – *Analyst, Nomura*

Thanks for taking my questions. First, for Christine -- Christine or Bob. Just thinking about the Disney balance sheet, it's the strongest in the media industry, it's stronger than most companies in the United States. When you look at what's going on in the economy, and the media economy broadly, do you think about your balance sheet as a competitive advantage in any way?

And more specifically, what are the things that you can do to utilize the Disney balance sheet, not only financially, but also strategically, whether it be more acquisition of IP, whether it be incremental capital spending on positive ROI projects, or whether it be being opportunistic with stock buybacks, given some of the dislocation in the market? Thanks.

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

Thanks, Anthony. Yes, you know when you look at the Disney balance sheet, it is the strongest in the media space. There's no question about that. We do view it as an asset. And when we look at the things that we could do with it, your list of acquisitions, investing in our own businesses, having the flexibility to increase buyback, my answer to that would be all of the above. So we do look at the leverage that we have, which is a little over 1x, the credit rating that we have, which is a single A rating, as all being very beneficial for us to be flexible for all sorts of opportunities, as you indicated.

Anthony DiClemente – *Analyst, Nomura*

Thanks, Christine. And then one for Bob. Given the divergence in maybe the narrative, at least, between the non-media side of Disney and the Media Networks side, I wonder would Disney ever consider separating its businesses into two, with Cable and Broadcast on one side and the Studio, Parks, Consumer Products & Interactive on the other? I guess what the question is getting at is, maybe you can just remind us of the synergies between the Media Networks and the non-Media businesses at Disney. Thank you.

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

I'm not going to talk about separating those assets. We fully expected that our Media assets are going to continue to contribute to our growth. We also are designed, as a company, to leverage intellectual property across a lot of our businesses, or to leverage the collection of brands nicely in the marketplace. And that also is reflected in the way we operate the businesses from an expense perspective, with consolidation in many different areas.

So if you look at the profile of the company, interestingly enough, since 2009 -- you look at the growth profile -- the company has grown on a compounded basis by 14%, the Media Networks have driven about 8% compounded a year, and the rest of the Company grew 23%. So 8% a year is pretty strong. 23% is extraordinary. 14%, pretty damn strong, too.

I think that what that says is really, is that over that period of time, we've actually diversified our ability to generate growth and profitability, and that was very purposeful. These investments that we made in Pixar and Marvel and in Lucasfilm, and the investments that we've made in our Parks, were designed for us to diversify our bottom line or our growth. And that was not just across businesses, but really across the world, because a lot of these businesses are global in nature, unlike some of our Media assets.

Anthony DiClemente – *Analyst, Nomura*

Okay. Thanks Bob.

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

Anthony, thanks for the question. Operator, next question please.

Operator

From Citigroup we have Jason Bazinet. Please go ahead sir.

Jason Bazinet – *Analyst, Citi*

A quick question for Ms. McCarthy. When I look at the buybacks, I think it was a record dollar amount last quarter and second highest, the quarter you just printed. Should investors view that decision to buy back as much stock as you are a function of what you think the intrinsic value of your equity is relative to what it's trading at? Or is it more a function of the very lean balance sheet and the lack of M&A opportunities, i.e., other, better uses for your cash?

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

Thanks Jason. The way we buy back our stock, we do keep an eye on our intrinsic value. So obviously, the amount of stock we bought is an indication that we believe that our stock is a great investment, and it is well below that intrinsic value. The strength of the balance sheet does afford us a lot of flexibility, so we're able to react to these opportunities, especially when the market dislocates in our name or the market overall. So we have taken opportunities to be aggressive so far this year, and we intend to do it going forward for the balance of the year.

Jason Bazinet – *Analyst, Citi*

Thank you.

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

Thank you, Jason. Operator, next question please.

Operator

From Sanford Bernstein we have Todd Juenger. Please go ahead sir.

Todd Juenger – *Analyst, Sanford C. Bernstein*

Hi. Thank you. Bob, I want to pick up on the comment you just made, if you don't mind. I was actually playing with the math myself. You talked about the 14% growth since 2009 and the different components of that. Is it wrong to think then that when you talked about an organic growth rate, I'll call it high-singles, and then obviously great contributions from both organic investments in the Parks and M&A delivered something like 14% total growth for the company.

So thinking forward from here, should we think about the company as a high-single grower, or do you think the assets you've put in place get you to that double-digit rate that you've had for the past five-plus years, or will more M&A investment be required? How should we think through the natural growth rate from here? Thank you.

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

You should think nothing but happy thoughts about this company. I don't know what else to say. We're not going to give any guidance whatsoever. We believe that we've distinguished ourselves in the media sector, not only with our growth these last number of years, but with the assets that we've collected and with the growth potential that we've created for this company going forward. And we will leave it at that.

Todd Juenger – *Analyst, Sanford C. Bernstein*

All right. I didn't mean to ask an unfair question. I understand. Given that.

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

I didn't take it was unfair, but as you know, we're not going to go there. But I do think it's important -- and I don't mean to be too wordy -- but if you look at the profile of the company, we have four businesses that are going to deliver growth for this company: Parks and Resorts, Media Networks, the Studio, and Consumer Products. And there was a time not that long ago where we were getting growth really from just a couple of them, and some, like the Studio, somewhat lumpy in nature, meaning there were good years and there were bad, based on the slate. I'm not suggesting that every year we grow, because there will be ups and downs in some cases, but they will be much flatter in nature, meaning you can expect that the bottom line contribution from the businesses will continue on essentially a more consistent basis than they were -- than you saw in the past.

Todd Juenger – *Analyst, Sanford C. Bernstein*

That's helpful. If you don't mind, a very quick follow-up that follows right in line with that. If you think about the Parks and the exposure to the cyclicality of a recession, the footprint at the Parks has changed a lot since the last recession. Any comment you can make upon the risk to revenue or margins or growth rates, whenever the next recession comes to Parks? Thank you.

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

No, I don't think there's anything I can add to that. Sorry.

Todd Juenger – *Analyst, Sanford C. Bernstein*

Okay. Thank you.

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

Thanks, Todd. Operator, next question please.

Operator

From Guggenheim we have Michael Morris. Please proceed Michael.

Michael Morris – *Analyst, Guggenheim*

Thanks. Good afternoon, guys. Two questions. First on Hulu, can you talk about -- you mentioned you're confident and you feel good about it. Help us understand why you're not concerned that at the $12.00 price point for the ad-free version that it doesn't represent a cannibalization risk to your core business.

And then second, if we could talk about the affiliate growth number, the 4% that you just reported. Most of your peers that have television stations have growth significantly above that in their retransmission fees, and I'm curious, are you seeing a higher rate in retransmission and therefore, a lower rate on the Cable side? What's the balance between those components when we look at that 4%? Thank you.

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

Do you want to address that?

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

Christine took you through the relative growth on the affiliate fees. And we are very pleased with where we've been going on the retransmission side of the equation, in fact, we are well ahead of the guidance we gave some time ago and expect that growth to continue. So we feel very good about that and the relative contribution between the two. So I don't really want to address the nature of the growth at other companies, the mix is often different and they're coming off of different bases, as well.

With regard to Hulu -- look, the Hulu business model has evolved over time and continues to. We've noticed that they have added subscribers rather nicely. That has not been overly driven by the ad-free portion of the equation. That's actually a small part of the subscriber base. And at this point, we're not overly concerned with the impact of that to the ecosystem as a whole. We will obviously keep our eye on it. And as Bob has indicated previously, we take a balanced approach to both those businesses and then also how we think about positioning our programming within them, and we will continue to do that.

Michael Morris – *Analyst, Guggenheim*

Great. Thank you. And just back on the first question -- or I guess, maybe my second -- on the growth rate. Was there anything unusual in the first quarter that impacted that 4% growth rate, or is that, as you're looking at what we're seeing right now, a fair run rate maybe with a little bit of variance for either FX or for the subscriber numbers that Bob referenced?

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

I think Christine's comments pretty much summarized it. I wouldn't say that there's anything unusual. Obviously, the foreign exchange impact is something that we wouldn't expect to see continue year after year, depending on clearly where foreign exchange goes. But other than that -- and also, as Bob has indicated, some of the trends that we see on the subscriber side have shown at least initial signs of abating somewhat, and we'll watch those very carefully.

Michael Morris – *Analyst, Guggenheim*

Great. Thanks Tom.

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

All right, Mike. Thank you for the question. Operator, we have time for one more question today.

Operator

From FBR Capital Markets we have Barton Crockett. Please go ahead sir.

Barton Crockett – *Analyst, FBR Capital*

Okay thanks for squeezing me in. I wanted to ask about the comment earlier that you can have growth in earnings at Media Networks, even with this lower affiliate fee growth trajectory. I was wondering if you could tell us how we get there, given what we know from the step-up in sports rights. I know you don't want to guide, but qualitatively, are we looking at cost cutting? Or are we looking at other revenues coming in to make up the gap for the sports rights cost pressure that we see coming up?

Tom Staggs – *Chief Operating Officer, The Walt Disney Company*

Well, Barton, I think the context that I'd give you on that is, first of all, you've seen how we've successfully grown our advertising revenues. And especially with the branded services and programming that we have, we continue to get a great response from advertisers, both on our linear channels and on new platforms. So that looks good, and I think that trend will continue. And I think we've discussed the affiliate side of the equation. The only other thing to keep in mind is that as new sports contracts kick in, next year as an example, that will sometimes cause a shift in terms of how the growth is coming, but the overall growth story is intact. So I think that gives you what color is available there.

Barton Crockett – *Analyst, FBR Capital*

Okay. Great. I'll leave it there. Thank you.

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

Barton, thank you for the question. 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.

This concludes today's call. Have a great rest of the day, everyone.

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Forward-Looking Statements:

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

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

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

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

Additional factors are set forth in the Company's Annual Report on Form 10-K for the year ended October 3, 2015 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.