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GLOBAL IDEAS

4 February 2015

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The Walt Disney Co: 1Q15 results beat expectations

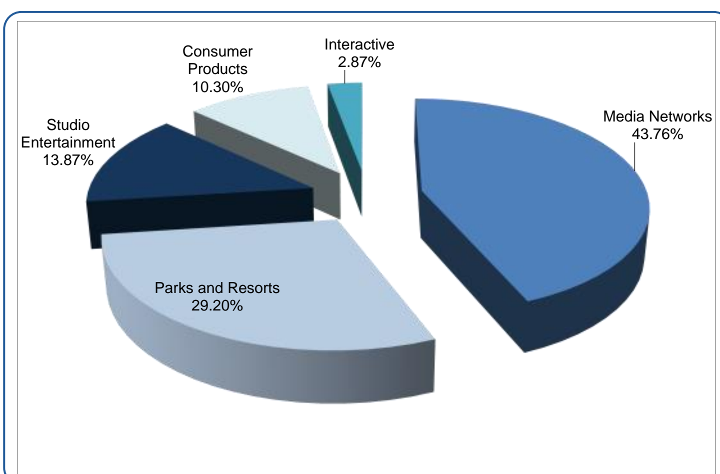
The Walt Disney Company on Tuesday (3 February) reported earnings for 1Q15 which came in ahead of expectations with diluted EPS up 23% YoY to $1.27 vs $1.03 in 1Q14, buoyed by revenue from Frozen, Disney channels & resorts. Consensus estimates had expected $1.08/share. Revenue came in at $13.391bn, above estimates of $12.87bn, a 9% YoY rise. Merchandise tied to its animated hit, Frozen (which was released in November 2013 and has grossed c. $1.3bn globally), continued to boost its results with the Group's consumer-products division reaping the rewards of the blockbuster's merchandise sales. Among the segmental highlights (*see below for a more detailed look at each segment*), revenue at the consumer products division rose 22% YoY to $1.4bn while operating income surged 46%YoY to $626mn, reflecting growth both in its licensed merchandise and sales at its retail stores. The movie studio saw a 33% YoY increase in operating income to $544mn, despite a 2% drop in revenue to $1.9bn, due in part to royalties it receives from consumer products sales. On the flipside the Disney's highly successful ESPN business continued to be impacted by rising sports rights prices as its operating income was down 2% to $1.3bn.

Disney revenue and operating income contribution by segment, 1Q15 vs 1Q14, $mn:

	1Q15	1Q14	% Change
Media Networks	$5 860	$5 290	*11*
Parks and Resorts	$3 910	$3 597	*9*
Studio Entertainment	$1 858	$1 893	*-2*
Consumer Products	$1 379	$1 126	*22*
Interactive	$384	$403	*-5*
TOTAL	$13 391	$12 309	*9*
Operating income	**1Q15**	**1Q14**	**% Change**
Media Networks	$1 495	$1 455	*3*
Parks and Resorts	$805	$671	*20*
Studio Entertainment	$544	$409	*33*
Consumer Products	$626	$430	*46*
Interactive	$75	$55	*36*
TOTAL	$3 545	$3 020	*17*

Source: Company data, Anchor Capital

Revenue contribution by segment, 1Q15:



Source: Company data, Anchor Capital

By segment the contributions were as follows:

- **Media Networks** revenues for 1Q15 increased 11% YoY to $5.9bn and operating income increased 3% YoY to $1.5bn. Within media networks the contributions were as follows:

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We scan the globe looking for good opportunities. We provide our model portfolios, as well as news and views on our watch-list, which is continually reviewed and updated.

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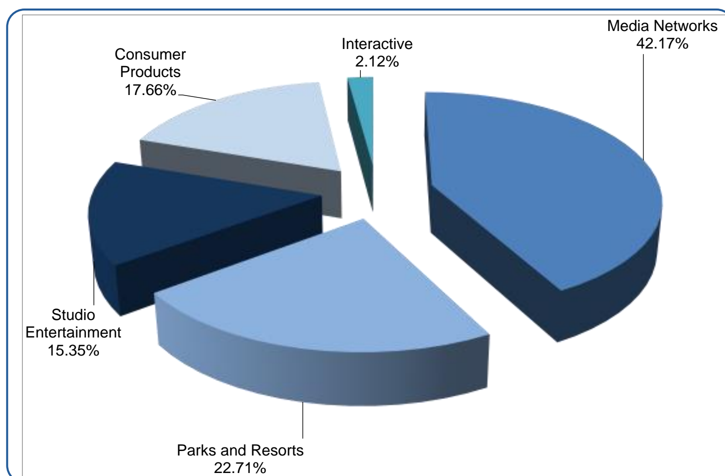
- Operating income at **Cable Networks** decreased 2% to $1.3bn due to a decrease at ESPN (attributed to higher programming and production costs and, to a lesser extent, higher marketing, general and administrative and technical costs and lower advertising revenue). This was partially offset by increases at the worldwide **Disney Channels** (due to higher affiliate rates for the domestic channels and higher international advertising revenues, which were in turn offset in part by higher programming costs) and **ABC Family** (higher affiliate revenue due to higher rates and increased advertising revenue reflecting higher units sold). Operating income at **Broadcasting** increased 35% YoY to $240mn due to an increase in affiliate fees and higher programme sales partially offset by lower advertising revenue. ABC television network saw fewer advertising units sold, but saw an increase at owned television stations due to higher political advertising and an increase from higher primetime rates.

- **Parks and Resorts** revenues were up 9% YoY to $3.9bn and segment operating income increased 20% YoY to $805mn, driven by an increase at its **domestic operations** (Walt Disney World and Disneyland saw higher volumes and guest spending which also reflected increased average ticket prices and higher merchandise, food and beverage spending) partially offset by a decrease at the Group's international operations. Despite a measles outbreak at Disneyland , attendance at domestic parks rose 7% YoY, to an all-time record last quarter and hotel occupancy hit 89%, "about as high as it can go", according to James A. Rasulo, Disney's chief financial officer. **International operations** were driven by higher Shanghai Disney Resort pre-opening expenses, the impact of a weaker Japanese yen on Tokyo Disney royalties and higher costs at Hong Kong Disneyland , partially offset by an increase at Disneyland Paris (higher guest spending, attendance and occupied room nights). On Tuesday's earnings call, CEO Bob Iger confirmed an earlier report in *The Wall Street Journal* that the opening of Disney's ambitious $5.5bn Shanghai theme park "is being pushed back to the spring of 2016 from late 2015".
- **Studio Entertainment** revenues decreased 2% YoY to $1.9bn but operating income increased 33% YoY to $544mn (we note that the 1Q14 results included a much higher base due to the success of Frozen, however, Frozen indirectly also boosted this year's result due to higher merchandise sales contribution). Higher operating income was on the back of an increase in home entertainment results, higher revenue share with the Consumer Products segment due to the performance of Frozen merchandise and higher TV/SVOD distribution results driven by more titles available globally. However, these increases were partially offset by lower theatrical distribution results (Big Hero 6 which performed well but did not equal the success of Frozen). The increase in home entertainment results was driven by higher unit sales (unit sales growth was buoyed by Marvel's Guardians of the Galaxy, Frozen and Maleficent).
- **Consumer Products** revenues were up 22% YoY to $1.4bn and segment operating income rose 46% YoY to $626mn with higher operating income due to increases at the **Merchandise Licensing** and **Retail businesses**. The increase in operating income at Merchandise Licensing was due to the performance of merchandise based on Frozen and, to a lesser extent, Disney Channel properties, Mickey and Minnie, Spider-Man and Avengers. Retail business' higher operating income was on the back of comparable store sales growth and higher online sales in all regions driven by sales of Frozen merchandise.
- **Interactive revenues** decreased by $19mn to $384mn but operating income increased $20mn to $75mn with improved operating results due to an increase at mobile games business driven by the success of Tsum Tsum and Frozen Free Fall as well as lower product development costs due to fewer titles in development. This increase was partially offset by lower results at the console games business due to higher per unit costs driven by the mix of Disney Infinity products sold, lower unit sales and higher marketing costs. The decrease in unit sales was in turn driven by lower sales of Infinity accessories and catalog titles, partially offset by higher sales of Infinity starter packs.

Operating income by division, 1H15:



Source: Company data, Anchor Capital

Disney has had a strong start to FY15 and the company is a quality business which has seemingly done no wrong since Iger took over as CEO. Fortunately his tenure was extended to 2018, two years later than his previously announced retirement date of 2016. Beyond that there has been media speculation that CFO Jay Rasulo and Thomas Staggs, the parks and resorts chairman, could replace him. However, looking ahead, and until then we believe Disney's performance will be further lifted thanks to new Marvel and *Star Wars* movie releases and the grand opening of the Shanghai Disney Resort. While ESPN sports programming costs weighed on the cable networks unit we do note robust and broad-based double-digit segment gains in other divisions and sub-segments (parks and resorts, film studio, consumer products, and interactive).

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In our view the new Marvel movies (Avengers: Age of Ultron etc.) and especially the new Star Wars later this year will not only see its studio division perform better, but toy revenue from Star Wars is likely to result in a spectacular holiday season result (1Q16 - the new Star Wars is due for release in December). Added to that, Star Wars has a significant presence at Disney's theme parks — which could increase attendance in the wake of the movie's release. While Disney is already an extremely successful company, we believe the next few years will be even better for the Group.

Disney's share price surged 3.9% in pre-market traded and was up 2.4% yesterday.

Walt Disney's forecasts are as follows:

The Walt Disney Company				
September y/e	**FY14**	**FY15E**	**FY16E**	**FY17E**
EPS ($)	4.3	4.7	5.5	6.0
% growth		*9%*	*16%*	*10%*
DPS ($)	0.9	0.9	1.0	1.1
P/E	21.8x	20.x	17.2x	15.6x
DY	0.9%	1.0%	1.1%	1.1%
Share price ($)	**94.10**			
12-mnth fwd P/E	18.9x			

Source: Bloomberg, Anchor Capital

Marco de Matos

The business of money: Global asset management and stockbroking

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