Q2 FY21 Earnings Conference Call

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Disney Speakers:

Bob Chapek

Chief Executive Officer

Christine McCarthy

Senior Executive Vice President and Chief Financial Officer

Moderated by,

Lowell Singer

Senior Vice President, Investor Relations

PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Walt Disney Company's Second Quarter 2021 Financial Results Conference Call. (Operator Instructions)

Please be advised that today's conference is being recorded. I would now like to hand the conference over to your speaker today, Lowell Singer, Senior Vice President of Investor Relations. Please go ahead.

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

Good afternoon, and welcome to The Walt Disney Company's second quarter 2021 earnings call. Our press release was issued about 25 minutes ago and is available on our website at www.disney.com/investors. Today's call is also being webcast, and a transcript will be available on our website.

We are once again hosting today's call remotely. So joining me remotely are Bob Chapek, Disney's Chief Executive Officer; and Christine McCarthy, Senior Executive Vice President and Chief Financial Officer. Following comments from Bob and Christine, we'll be happy to take your questions. So with that, let me turn the call over to Bob, and we'll get started.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Thanks, Lowell, and good afternoon, everyone.

It’s been a busy few months and we’ve been pleased to see more encouraging signs of recovery across our company. We ended the second fiscal quarter with adjusted EPS up 32% to $0.79, compared to $0.60 last year. And since then, we’ve continued to make progress across our businesses, as we remain laser-focused on our ongoing recovery, while also fueling long-term growth.

Our strategic focus continues in three key areas. First is direct-to-consumer. We've successfully launched our streaming offerings, Disney+ and Star, in a number of markets internationally. And we've been pleased with the growth and engagement in those markets to date. Our steady cadence of new high-quality, branded content, along with our robust collection of library titles allows us to continually attract new subscribers and retain existing ones.

At the same time, we are also closely monitoring the recovery of theatrical exhibition as consumers begin to return to theaters, and I'll talk more about the specifics later.

Finally, we are focused on the ongoing recovery of our Parks business and the resumption of Disney Cruise Line. There have been some encouraging developments in recent months, particularly with the ongoing rollout of the vaccine and the gradual lifting of government-mandated restrictions. And through this time, we've taken advantage of the opportunity to make improvements to our operating procedures to enhance the guest experience through the use of technology innovations, new ticketing strategies, and other offerings.

We are especially excited that, after being closed for 412 days, we welcomed our first guests back to Disneyland two weeks ago, and the response has been overwhelmingly positive. Bob and I stood on Main Street, U.S.A. on opening day, and it was so wonderful to see the joy on our Cast's and guests' faces and feel the excitement in the air!

It's been fantastic to see Cast Members back at work. Most recently, at Disneyland, we were able to quickly recall more than 10,000 furloughed Cast, and retrain them to be able to operate to the State of California's new health and safety requirements.

We continue to see strong, growing demand from consumers as we are at or near our reduced capacity levels at both Walt Disney World and Disneyland for the current quarter. It's clear our guests are excited to get back to experiencing the magic of Disney - and they also have extraordinary confidence in our safety protocols.

At Shanghai Disney Resort, where they just kicked off their year-long 5th anniversary celebration, the park is operating at or above FY19 levels. We are also encouraged by what we're seeing at Hong Kong Disneyland. And we are hopeful we will be able to announce a re-opening date for Disneyland Paris soon.

Despite the pandemic, we continue to make progress on a number of highly anticipated projects at our parks around the world, including the all-new Avengers Campus, which is set to open at Disney California Adventure on June 4. I had a chance to visit it recently, and the attractions and multiple state-of-the-art experiences are truly phenomenal!

We recently unveiled our newest cruise ship, the Disney Wish, to the public with a virtual live-stream presentation that has been viewed nearly 1.2 million times! The ship is amazing, and it includes the AquaMouse water ride, the first-ever Disney attraction at sea. The Disney Wish will set sail on its maiden voyage in 2022, and bookings open to the general public on May 27.

On the Studio side, we are pleased to be nearing full production levels - and we are also significantly ramping up content creation at our studios, consistent with the guidance we provided at Investor Day. An example of this is 20th Century and Searchlight Pictures, where they are gradually increasing output, and will reach a steady state of 15 and 20 films, respectively, to fuel our General Entertainment offerings across all of our distribution platforms.

We are incredibly proud that Searchlight's *Nomadland* took home Oscars for Best Actress, Best Director - with Chloe Zhao becoming the first woman of color to win the award, and Best Picture. That's five Best Picture wins since 2009 and 43 Academy Awards in total.

Additionally, Pixar's stellar record of award-winning films continues with the studio's animated masterpiece *Soul*, which took home Oscars for Best Animated Feature and Best Original Score. And I'm happy to say that now millions are able to enjoy *Soul* on Disney+ and *Nomadland* on Hulu.

As we have consistently stated, flexibility is a key component of our distribution strategy. And we have outlined three approaches for distributing our films: releases in theaters with a simultaneous offering via Disney+ Premier Access, releases straight to Disney+, and traditional exclusive theatrical releases.

Here's how this translates to our tremendous upcoming film slate…. *Cruella* will be released in theaters and via Disney+ Premier Access on May 28, followed by Pixar's *Luca*, which will be released exclusively on Disney+ on June 18. The highly anticipated *Black Widow* will be in theaters and on Disney+ via Premier Access on July 9. And Disney's *Jungle Cruise*, a hilarious adventure-filled expedition, will be available in theaters and on Disney+ via Premier Access on July 30.

I'm pleased to announce today, that amidst recent signs of increased consumer confidence in movie-going, two films, 20th Century's exciting comedy *Free Guy* and Marvel's action adventure *Shang-Chi and the Legend of the Ten Rings* will be released with a 45-day exclusive theatrical window on August 13 and September 3, respectively.

And, of course, regardless of where they originate, all of our films and episodic series will end up as part of the robust library of content on our DTC platforms.

Like our films, our Disney+ original series have become "must watch" events, starting with the success of *The Mandalorian*, followed by Marvel's *WandaVision* and *The Falcon and the Winter Soldier*. These not only became immediate hits, but part of the cultural zeitgeist. And the anticipation for Marvel's newest series *Loki*, which debuts on June 9, has been through the roof.

The second season of *High School Musical: The Musical: The Series,* the all-new *The Mysterious Benedict Society*, based on the popular young adult book series, and the animated series *Monsters at Work*, are also coming to Disney+ in the next couple of months, just to name a few.

We are uniquely positioned with the most compelling brands and franchises in entertainment, and we continue to deliver the high-quality, one-of-a-kind content that consumers want. That's clearly reflected in the success of Disney+, which amassed nearly 104 million paid subscribers as of the end of the second fiscal quarter. We are on track to achieve our guidance of 230 to 260 million subscribers by the end of fiscal 2024.

Looking at our entire portfolio of streaming services, we expect that as full production levels resume and we get to a more normalized cycle, the increased output will help fuel additional sub growth across Disney+, ESPN+, Hulu and Hotstar.

Hulu and ESPN+ had 41.6 million and 13.8 million paid subscribers, respectively, at the end of the quarter. On Hulu, buzzworthy content continues to boost performance, including the award-winning Hulu Original film *The United States vs. Billie Holiday* and season four of *The Handmaid's Tale*, which premiered to the biggest audience ever for a Hulu Original. And there's lots more coming to Hulu, including Marvel's new animated series *M.O.D.O.K.,* season two of the hit series *Love, Victor*, and season 10 of the wildly popular anthology *American Horror Story* on FX on Hulu.

In March, we launched ESPN+ on Hulu and we are very pleased with its early progress. Viewers who subscribe to both Hulu and ESPN+ are able to watch and engage with the great content that's available on ESPN+ without leaving the Hulu environment.

ESPN+ programming includes thousands of live sporting events, original shows, series and documentaries with the UFC lightweight championship fight airing live on ESPN+ pay-per-view on May 15, the final match of the FA Cup also on May 15, followed by the PGA Championship, Wimbledon, and the highly-anticipated third UFC match-up between Dustin Poirier and Conor McGregor on pay-per-view July 10…. not to mention the incredible additions to our lineup, including NHL and more college football in the fall.

Live sports are a very important component of our content business, and even amidst the challenges of the past year we have continued to build our unrivaled portfolio of sports rights in a disciplined way. While our overall strategy is still very supportive of our linear business, given the important economic value it drives for the company, we are also building out our ESPN+ direct-to-consumer offering. And with every deal we make, we are considering both the linear and DTC components.

With this strategy in mind, we've reached a number of long-term, accretive deals that each play a very specific role as part of our sports portfolio. Some are weighted more towards linear with a significant digital component, such as the NFL and SEC deals, others reflecting an emphasis on direct-to-consumer. These include agreements with the UFC, the PGA Tour, Bundesliga, and the NHL. For example, as part of the seven-year rights deal with the NHL, 75 of the league's live, national games will be available exclusively on ESPN+ and Hulu. And ESPN+ will be the sole home for more than 1,000 out-of-market NHL games, further cementing the service as a "must have" for hockey fans.

And today, I'm excited to announce two additional sports rights deals. We've reached a renewal deal through 2028 with Major League Baseball, with 30 exclusive regular season games, which include 25 Sunday Night Baseball games and Opening Night annually; coverage of the highly anticipated, potential expanded Wild Card series; and the option to simulcast all live MLB coverage from ESPN networks on ESPN+.

We've also signed a historic rights agreement with the top division in Spanish Club football, La Liga. La Liga is one of the world's best and most popular soccer leagues - including a number of the top clubs in the world, and one of the best players in the world, Lionel Messi. And this eightyear deal, covering both English- and Spanish-language rights, brings 380 La Liga matches and a host of La Liga 2 matches per season to ESPN+, beginning in August. And this deal bolsters ESPN+'s position as a top destination for soccer in the U.S., offering fans more than 2,900 matches per season.

When you combine the unparalleled assets of The Walt Disney Company - ESPN, ESPN+, ABC and Hulu - plus our highly engaging digital and social content, it's clear that Disney is the absolute leader when it comes to serving our sports fans in the most effective way possible. We believe in the power of live sports, and are confident our multi-platform rights deals we've made will provide us tremendous value now and into the future.

Overall, we are pleased with the encouraging signs of recovery across our businesses, and we are confident we continue to move in the right direction for our future growth.

And with that, I'll now turn it over to Christine and she'll talk more in-depth about our results for the quarter.

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

Thank you, Bob, and good afternoon everyone.

Excluding certain items, diluted earnings per share for the second fiscal quarter increased 32% versus the prior year, to 79 cents per share. We are beginning to see progress in many of our businesses, after more than a year of adverse impacts from the pandemic. While we are not out of the woods yet, we are pleased with our results this quarter at both our DMED and DPEP businesses.

I'll walk through our results by segment, starting with Media and Entertainment Distribution. Operating income at the segment increased by 74% in the second quarter versus the prior year, due to higher results across all of the segment's lines of business.

At Linear Networks, the increase was driven by growth at both our Domestic and International Channels.

At Domestic Channels, both Cable and Broadcasting operating income increased versus the prior year.

Higher results at Cable were driven by lower programming and production costs and higher affiliate revenue, partially offset by lower advertising revenue. ESPN's results were in line with the guidance we gave last quarter, and ESPN was the most significant contributor to Cable's growth this quarter.

The decrease in programming and production costs was largely due to the timing of the College Football Playoffs. As we mentioned last quarter, fiscal Q2 included only one CFP bowl game - the National Championship; compared to four in the prior year quarter - three CFP bowl games and the National Championship game.

Cable programming and production costs also benefited in the quarter from lower production costs for other live sporting events and lower programming costs at Freeform.

Lower advertising revenue at Cable was primarily due to lower average viewership. At ESPN, domestic advertising revenue decreased significantly in the quarter driven by lower ratings for key programming, in addition to the timing of the College Football Playoffs. Quarter-to-date, domestic advertising revenue at ESPN is currently pacing up significantly versus last year, benefiting from the prior year's lack of significant live sports programming due to COVID.

At Broadcasting, higher results were driven by growth at ABC, partially offset by a decrease at the owned television stations.

At ABC, lower programming and production costs and higher affiliate revenue were partially offset by lower advertising revenue. Programming and production costs were impacted by the shift in timing of the Academy Awards, which took place in the third quarter this year, compared to the second quarter last year. Lower advertising revenue was primarily driven by lower average viewership and the timing of the Academy Awards, partially offset by higher rates.

On our Q1 earnings call, we said we expected the Academy Awards timing shift and lower political advertising at our owned stations would negatively impact Broadcasting results in the second quarter versus the prior year. While we did see those specific adverse impacts play out, overall Broadcasting results were higher than we expected, driven by lower marketing spend due to timing shifts of some new series, in addition to a number of other smaller factors.

Total domestic affiliate revenue increased 5% in the quarter. This was driven by a benefit of 8 points of growth from higher rates, offset by a 4-point decline due to a decrease in subscribers.

Operating results at International Channels increased due to a decrease in programming and production costs and an increase in advertising revenue, partially offset by lower affiliate revenue.

Lower programming and production costs in the second quarter were driven by a higher percentage of content cost being allocated to our DTC business rather than our Networks business, as we continue the international expansion of Disney+ and Star, in addition to channel closures over the past year. Advertising revenue increased primarily due to the timing of BCCI cricket matches, which generally take place in the first quarter, but were in the second quarter this year due to COVID-related timing shifts.

Lower affiliate revenue at our International Channels was due to channel closures as well as an unfavorable foreign currency impact.

At our direct-to-consumer businesses, operating results in the quarter improved by over $500 million versus the prior year, due to stronger results at Hulu and ESPN+.

The increase at Hulu was due to subscriber revenue growth and higher advertising revenue, partially offset by higher programming and production costs related to the Hulu Live TV service. Hulu ended the second quarter with 41.6 million paid subscribers, up from 39.4 million in Q1, inclusive of the Hulu Live digital MVPD service. Paid subscribers to Hulu Live declined modestly to 3.8 million from 4.0 million at the end of Q1, which we attribute primarily to the $10 price increase we took in December, in addition to a modest impact from seasonality.

At ESPN+, improved year-over-year results were driven by subscriber growth and an increase from UFC pay-per-view events. ESPN+ had 13.8 million paid subscribers as of the end of the quarter.

At Disney+, results were comparable to the prior-year quarter, as an increase in subscribers was largely offset by higher content, marketing, and technology costs.

As Bob mentioned earlier, we had almost 104 million Disney+ paid subscribers at the end of the second quarter.

At our annual meeting, we announced we had reached 100 million global paid subscribers. We reached that milestone in early March, so we added subs at a faster pace in the last month of the second quarter than we did in the first two months… and that was despite no major market launches, a price increase in EMEA, and a domestic price increase toward the end of the quarter.

We attribute this success to the strength of our overall content slate, the launch of the Star general entertainment offering in many markets, and the continued growth of Disney+ Hotstar.

Between Q1 and Q2, Disney+ Hotstar was the strongest contributor to net subscriber additions, making up approximately a third of the total Disney+ subscriber base as of the end of the second quarter. However, ARPU at Disney+ Hotstar was down significantly versus the first quarter, due to lower advertising revenue as a result of the timing of IPL cricket matches and the impact of COVID in India. As a reminder, the majority of the prior IPL tournament took place in fiscal Q1, and there were no games in Q2. The current IPL tournament began on April 9th, in fiscal Q3, and was suspended last week given the COVID situation in India.

Disney+'s overall ARPU this quarter was $3.99. Excluding Disney+ Hotstar, it was $5.61. As we move through the remainder of the year, we should start to see the benefit on Disney+ ARPU from price increases we've taken around the world.

Last quarter, we guided to second quarter direct-to-consumer operating income improving modestly versus the prior year. Actual results came in significantly better versus the prior year, due to Hulu advertising sales upside, lower content and marketing expense at Hulu and Disney+, and better-than-expected ESPN+ pay-per-view results.

Content Sales, Licensing, and Other operating income at DMED increased in the second quarter versus the prior year, due to higher TV/SVOD results and lower content impairments, partially offset by lower home entertainment results.

Higher TV/SVOD results were primarily due to an increase in income from sales of episodic content, driven by sales of more profitable programs in the current period and lower write-offs. This was partially offset by a decrease in sales of film content.

The decrease in home entertainment results was driven by the absence of significant title releases in Q2.

Moving on to our Parks, Experiences and Products segment… DPEP's operating income in the second quarter decreased by $1.2 billion year-over-year, as growth at Consumer Products was more than offset by lower results at Parks and Experiences due to the impacts of COVID-19.

At Consumer Products, growth in operating income was due to increases at our merchandise and games licensing businesses.

At Parks and Experiences, results were again adversely affected by COVID-19 related closures and reduced operating capacities versus the prior year.

Disneyland Resort, Disneyland Paris, and our cruise business were closed for all of the second quarter, whereas these businesses closed in mid-March of the prior-year quarter.

Hong Kong Disneyland Resort was open for approximately 30 days during the second quarter, compared to approximately 25 days in the prior-year quarter.

Walt Disney World Resort and Shanghai Disney Resort were both open for all of Q2. In the prior-year quarter, Disney World closed in mid-March and Shanghai closed in late January.

Our parks and resorts that were open during the quarter operated at significantly reduced capacities, yet all achieved the objective of a net positive contribution, meaning that revenue exceeded the variable costs associated with opening.

At Walt Disney World, attendance trends continued to steadily improve throughout the second quarter, and guest spending per capita again grew by double digits versus the prior year.

Disneyland Resort reopened on April 30th, and as Bob mentioned earlier, we are very encouraged by the initial guest response.

Forward-looking bookings for park reservations at both of our domestic parks are strong, demonstrating the strength of our brands as well as growing travel optimism as case counts decline, vaccine distribution ramps, and government restrictions loosen.

Looking ahead, there are a couple of items I would like to mention.

At Linear Networks, we expect a significant decline in operating income year-over-year in the third quarter, largely due to higher sports programming and production costs at ESPN, which we expect to increase by $1.2 billion vs. prior year. This year's Q3 includes marquee events such as the NBA, Major League Baseball, the Masters, Wimbledon, and the European Football Championship, which compares to Q3 of last year, during which we had a limited slate of events due to COVID.

At our Direct-to-Consumer business, we now plan to launch Star+ - our standalone general entertainment and sports streaming service for Latin America - on August 31st. Moving the launch to late summer allows us to leverage a strong sports calendar, which includes the return of European soccer leagues, including La Liga and the Premier League; championship games for the Copa Libertadores, the prominent regional international soccer competition; along with grand slam tennis.

As Bob mentioned earlier, we remain right on track to reach our fiscal 2024 guidance of 230 to 260 million subs, powered by the addition of 30 million paid Disney+ subs in the first half of the year. And notwithstanding our expectation for fewer net sub adds in the second half of the year given the COVID-related suspension of the IPL season and our decision to move the Star+ Latin America launch to the fourth quarter, we remain very optimistic about our future.

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

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

Okay. Thanks, Christine. And as we transition to the Q&A, let me note once again that since we are not all physically together this afternoon, I will do my best to moderate by directing your questions to the appropriate executive.

And with that, operator, we are ready for the first question.

Operator

Our first question comes from Ben Swinburne with Morgan Stanley.

Ben Swinburne – *Morgan Stanley & Co. LLC*

Maybe just starting on the direct-to-consumer side, maybe for Bob. Could you talk a little bit about how the price increases have landed relative to your expectations - both internationally with Star, but also in the U.S. - kind of the impact on churn, and how that might inform your decision-making process going forward on price?

And then I just wanted to ask, I think you guys generated maybe $700 million or so of free cash flow in the quarter. Normally, we don't talk a lot about quarterly free cash flow, but it's been a while. I'm just wondering, Christine, if you think at this point, we're back in free cash flow-positive mode going forward and expect to generate free cash flow for the year?

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

Okay. Ben, thanks for the questions. Bob will take the first one on price response, and then Christine will take the cash flow question.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

All right. Of course, these were our first price increases since we launched. I have to say that we're extremely pleased with how the market reacted to both.

In the U.S., we've not observed any significantly higher churn rate since the price increase.

In EMEA, as we added Star as a sixth brand title, we've actually seen an improvement in our churn rate.

So we seem to be fairly resilient to those price increases. And as such, I think it makes us feel relatively bullish going forward that we still offer a tremendous price value relationship across the world for Disney+.

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

Ben, thanks for the free cash flow question. We don't usually get those. But I would like to comment on it, because it's something that we're tracking not only this year versus last year - we look at it actually weekly, but I'm also looking at it versus fiscal '19, which I consider a more normalized year.

I would say that the upside that we're really seeing - and we're quite pleased with it is since we've reopened Walt Disney World, and we really don't have the impact of Disneyland yet - but we're seeing, as I mentioned, a strong per cap growth in the parks, and that's flowing through the park's cash numbers.

And we're also seeing good, strong cash flow from our Direct-to-Consumer businesses. So those two elements are kind of upside to what we had planned for.

And I would also say that the… there is some choppiness year-over-year because of some of the shifts in sports rights expense timing from last year to this year, but we expect that to be more normalized this year as we get through the year. But we're looking at a more favorable free cash flow than we did when we started off the year.

Operator

Our next question comes from Alexia Quadrani with JP Morgan.

Alexia Quadrani – *JP Morgan Chase & Co.*

One on streaming as well and then one on the Parks. How should we think about really Disney+ subscriber growth going forward? I know you gave a lot of great color in terms of how to think about the cadence for the balance of the year and details on the growth we've seen so far - on the impressive growth we've seen so far. But I'm wondering if you look at what you see internally as major drivers for the step-up - or step-ups until you get to your long-term target - is it really around certain content drops? Is it around eventually moving more into Eastern Europe or other markets in Asia? I guess, what do you guys see as sort of the main drivers for sub growth?

And then just a follow-up, if I can, on the Parks. Any color you can provide on how we should think or how you're thinking about when it's okay to start raising capacity, attendance capacity, particularly at Disney World?

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

Okay, Alexia. Thanks for both questions. Bob, do you want to take both of those?

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Yes, I'll take them both. So on the first one, in terms of the drivers, for sub growth going forward, we really see 4 different elements. First of all is our content slate. As you know, we're spending a lot of money across our variety of franchises in order to create the content that's going to keep consumers coming back and keep not only our sub number growing but also our engagement growing across all of our platforms. So the first one is content slate.

The second one is our general entertainment international growth, driven by our Star brand, and we think that's going to continue to fuel growth for our international territories as well as Disney+.

The third one is continued market expansion in markets where Disney+ has not yet been launched. And as you see, we're announcing Malaysia today, as June 1 and Thailand as June 30. So market expansion will continue to be a piece of it.

But one thing that continues to impress us is the opportunity to have the bundle in the U.S. be even larger. All the metrics that we see, all the performance factors are extraordinarily positive for that. So I would say those are the 4 components that continue to drive us and our bullishness in terms of our ability to continue to project that we're going to hit between 230 million and 260 million subs by the end of '24.

In terms of the parks and when we're going to sort of be able to raise our capacity limits. We've actually already started that; given the guidance that just came today from the CDC and earlier guidance that we got from the Governor of Florida, we've already started to increase our capacities.

Those - obviously, today's guidance that we got from the CDC in terms of those that were vaccinated do not necessarily need to wear masks anymore, both outdoors and indoors, is very big news for us, particularly if anybody's been in Florida in the middle of summer with a mask on. That could be quite daunting. So we think that's going to make for an even more pleasant experience. And we believe that as we're now bringing back a lot of people back to work, that it's going to be an even bigger catalyst for growth in attendance. And we've been quite pleased to date.

So I think you're going to see an immediate increase in the number of folks that we're able to admit into our parks through our reservation systems that we recently implemented. So we're very, very excited about that.

Operator

Our next question comes from Michael Nathanson with MoffettNathanson.

Michael Nathanson – *MoffettNathanson*

Well, I have 2. One is on the gross addition side of Disney+, we heard from Netflix there may have been a pull forward, that maybe perhaps the reopening has impacted gross additions. Can you talk a bit about what you're seeing in some of the more mature or, I guess, developed markets on the gross addition side?

And then you guys have consistently beat us on OI profits or lack of losses, I'd say, on DTC. Which of the platforms is providing the biggest surprise? And does it make you rethink maybe some of the guidance you gave around breakeven, given how strong the year has been so far on the limitation of losses?

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

Bob, why don't you start, and then we'll go over to Christine.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Okay. I'll take the first one. In terms of the additions, we've really seen it across our geographies. When you look at it from a mature versus new. Every single market[1] that we've launched in has exceeded our expectations so far in terms of the new.

But in terms of the mature, keep in mind that we added 30 million households[2] in the first 6 months of the fiscal year, which is in line with our expectations. And domestic continues to contribute to that.

The addition of the Marvel content, and not only the Marvel content, but how strong it's been, and the cadence of additions. And as you know, we'll soon be announcing - or soon be launching *Loki*, that is a tremendous catalyst for growth for us. And in the future, as we get to more new content and serial content coming from Star Wars, we're really, really encouraged by what that's going to mean in terms of engagement. Because as you know, engagement is sort of the precursor for net sub adds.

And so we're very pleased with both our domestic as well as our, let's call it, more mature markets, those that we've been in the marketplace for at least a year, but also our new markets as well.

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

Okay. And I'll take the second part of your question, Michael, and nice to hear your voice.

Look, the biggest drivers for Direct-to-Consumer were coming out of Hulu and Disney+. They're a little bit different.

[1] Region
[2] Paid Subscribers

Disney+, we saw some lower content costs. And that was due to some lower allocated costs for some of our own titles compared to what we had expected.

And at Hulu, there was also some lower content costs, but for different reasons. It was from their third-party content that is coming - that were delayed because of some COVID issues. So content coming in is not coming in as quickly as they had thought. But the most important driver for Hulu is the addressable advertising strength. That continues to be a real upside, and it's going strong, and we expect that to continue. There's real demand for that addressable advertising.

Michael Nathanson – *MoffettNathanson*

Okay. My other question was - I'm sorry, Lowell.

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

Go ahead. Go ahead, Michael.

Michael Nathanson – *MoffettNathanson*

And does that make you rethink your guidance on breakeven time lines given how strong Hulu has been?

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

No. The only guidance that we have reaffirmed was the 2024 total Disney+ global subs. Bob mentioned it. I mentioned it. That's at 230 million to 260 million.

All the other guidance, we have not reaffirmed or changed at this point. We're still going through our long-term planning cycle, so we're not making any changes now.

Operator

Our next question comes from Jessica Reif Ehrlich with Bank of America.

Jessica Reif Ehrlich – *Bank of America Merrill Lynch*

Some of the pictures from the parks look like it's totally full, even with this reduced capacity. So now with capacity increasing, how does that relate to like kind of normal attendance? Even though you don't have international visitors, it still feels like, from what we can see, that it's fairly full, and you said demand is strong. I just wonder if you can comment on that.

And also, any update you can give us, given the strong demand, how that overlays with some of the things you've talked about in the past that didn't really discuss today - the yield management, some of the cost changes you've put in place?

And then sorry for such a long-winded question, but given the tight labor market, are there any issues that you're seeing there either on the cost side or in hiring?

And then finally, on DTC. I mean the slower net add in the second half sounds like it's coming from India, which, of course, is understandable given IPL as well as COVID. But there's also likely to be an impact on ARPU, a positive impact on ARPU. And I'm just wondering, how does that all translate into the operating results (OI)?

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

So Bob, why don't you take the parks questions, and then if you want to start on the Disney+ question. Christine may want to jump in at the end.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Okay. So in terms of the parks demand domestically, our intent to visit at Walt Disney World is growing and is actually already flat with '19, which is obviously our last pre-COVID year. So that's really good news for us. And since we've opened up Disneyland Resort, intent to visit is actually growing as well. So we're thrilled with the guest response to that.

So as capacity limits increase, we don't think we're going to have any problem at all - sort of increasing our attendance to match that capacity. That is not something that keeps any of us up at night.

In terms of our yield management, as you know, we've been practicing yield management for a while, and it's really become an art form with this extraordinarily limited capacities that we've been operating at. But you've seen the margin's very healthy. Our yield is growing up from a very healthy standpoint. Consumers are spending more. And we're doing it under some tremendous cost management parameters because everything has become automated.

And so we've sort of got the perfect positive storm, if you will, where we've got plenty of demand. We've got really great yield management gains and the cost management at the same time.

And in terms of labor, we've had about 80% of our cast members return that we've asked to return. And obviously, one of the gating factors for us to continue to increase capacity is to continue to get more and more cast members back. It thrills us to be able to do that, but we've had no problems whatsoever in terms of trying to get our cast to come back and make some magic for our guests.

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

Christine? I think you're muted?

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

Unmute me. I'm going to talk about - Jessica, I'm going to talk about Direct-to-Consumer and the slower net adds expected for the second half of the year.

That is, in fact, the case. And it is largely due to the COVID-related suspension of the IPL and also that decision that we made to move the Star+ Latin America launch into the fourth quarter. And once again, we did that because of the strength of the sports calendar that we would have upon launch.

The other thing that's going to happen here is with the absence of the IPL games in India - that will also have an impact on advertising revenue. So you could see a decrease in the ARPU and the subs in India if that plays out like we just said.

But the other thing is we did take price increases for domestic U.S. as well as EMEA for Disney+. So our overall ARPU could benefit. So we just took the price increase in the U.S. at the end of March, and we'll see how that plays out in our ARPU in the upcoming quarters.

Operator

Our next question comes from Doug Mitchelson with Credit Suisse.

Douglas Mitchelson – *Credit Suisse AG*

So Lowell, I would say, sort of 2 areas of focus. The first, you started touching on it a bit with the last series of questions. But I think one of the core theses is that coming out of the pandemic, the potential that the parks at Disney are more profitable than pre-pandemic. And you talked about some of those drivers. One of them perhaps when the parks return to 100% of capacity, is that capacity different than it was pre-pandemic? Is it bigger? Are you smarter on pricing? Are margins structurally higher? So one, I'm just curious if you agree with that thesis that the parks could end up being more profitable coming out of the pandemic that it was going in.

And then the second area, the NFL deal was obviously super interesting. And I'm curious, under what circumstances will you consider doing what some peers are doing, simulcasting your football games, Monday Night Football games from either ESPN or ABC onto ESPN+?

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

Doug, thank you. Thanks for the questions. I will turn both of them over to Bob.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Okay. In terms of park and in terms of the relative profitability, as you know, we have - there's a lot of negative impacts, of course, with COVID. But one of the things that it gave us a chance to do as we were forced to stop operation was to completely reexamine how we priced and programmed our tickets. And as you all know, we ended our current annual pass program at Disneyland. And that gives us a chance to sort of create a modern version of a park loyalty program, an affinity program, that isn't necessarily governed by legacy.

And as you know, the net contribution back to the company varies tremendously and was one of the levers that we use to grow yield over the past several years, depending on what type of ticketing structure or a particular guest came in.

With the ability now for us to sort of completely reconsider how we go about our loyalty programs and our frequent visitor programs, we have the chance to make even more advancements, not only in terms of the guest experience and make sure that guests have a tremendous experience no matter what day of the year they come, whether it's a high-demand day or a relatively low demand day, but also the ability to increase our per caps and our yields.

And we've already seen tremendous growth in those as you're seeing over the last couple of quarters. But I don't think we've even scratched the surface in terms of what we can do when we finally restart with some of our programs in terms of making sure, again, that not only do we improve the guest experience, but at the same time, get an adequate return to our shareholders for the type of experience that we do give to our guests. So very positive on those factors.

In terms of the ability to simulcast with ESPN+ and ESPN and ABC, that's actually been envisioned in the deals, and we've gotten a lot of flexibility, not only in terms of our ability to take our programming to our DTC platforms and things like Hulu and ABC. So that's actually been envisioned, and we plan on being fairly aggressive in that way. I think that one of the advantages of the Walt Disney Company in sports is that we've got so many ways to reach our consumer base. And I think the leagues understand that, and we certainly do as well, and I think our guests do as well.

Operator

Our next question comes from Kannan Venkateshwar with Barclays.

Kannan Venkateshwar – *Barclays Bank PLC*

So a couple if I could. I mean, firstly, I guess, Bob, when you look at the vision for sports streaming, you now have digital rights across all the major sports that you carry on ESPN. And you've made some hard choices on the other businesses when it comes to licensing and studios and so on in order to pivot - make a hard pivot to streaming. But that choice with respect to sports streaming, feels like it's still a couple of years off in terms of pivoting ESPN as a business completely towards streaming.

So could you just talk about the longer-term vision now that your sports portfolio is in place? How should we think about ESPN relative to ESPN+? And how are you thinking about the transition being accretive overall?

And secondly, I guess, Christine, the guidance around the second half cadence for DTC subs. The IPL suspension, I guess, could change. I think they're looking at other geographies to run the tournament. If that was to happen, would the outlook change for subscriber growth in the second half?

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

Okay. Kannan, thanks. Bob, I'll hand the sports question to you. And then Christine, you can talk a little bit about IPL impact on subs.

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

We've talked a lot about flexibility when it comes to pivoting between linear and more traditional legacy platforms and our digital rights, direct-to-consumer platforms. And the reason we want that flexibility is because we know things are going to change. And as we've always said, when the right time comes for us to make a step function increase, as we've done with our entertainment platforms, to our sports platforms, and it's accretive to our shareholder proposition, we'll go ahead and do that.

Our longer-term vision is to parallel path both ESPN and ESPN+. But if there's any indication of where we're going with this, I think our recent deals and the flexibility that we negotiated in to go to these direct-to-consumer platforms and specifically ESPN+ or whatever follows ESPN+ in terms of the direct-to-consumer platform, I think that's 100% indicative of our bullishness of not only our capability of doing that, but the viability of doing that.

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

Kannan, and your question around if they move the IPL... about half of the 60 IPL matches that were expected to be played this season have already taken place. So you're looking at the back half, 30 games to be played.

So sure, if they were able to successfully relocate the tournament, we would hopefully see an impact, especially on advertising. And so there would be a positive what we're expecting. It would be better than if there were no rescheduled.

The big issue is going to be when in the quarter- if it overlaps into Q4; or if it goes into the first fiscal quarter, which starts for us in the beginning of October. So if we would have - it would have an impact on it, it just depends on when it would come in. So let's hope they are able to relocate it.

Operator

Our next question will come from John Hodulik with UBS.

John Hodulik – *UBS Securities LLC*

Great. Maybe keeping with the sports rights question. It does look like you guys are sort of bulking up on sports rights. Would you say you still have demand for additional rights if the economics make sense? And I'm thinking sort of Sunday Ticket or the EPL? Or is there sort of a level that you get to in terms of spending where you feel you need to cut it off?

And then given all the rights and the digital platform, does sports gambling become a bigger opportunity for the company and something that you expect to go deeper into?

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

John, thank you. Bob, do you want to take those?

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Yes. Thank you. In terms of the sports rights, we've just recently closed MLB, La Liga, NFL, NHL… so we certainly, as you have suggested, have a full complement of sports to please almost anybody. And then you take that in addition to the NBA rights that we have, and yes, we've got a full house there.

In terms of our appetite for going further, in terms of what's really left, there's not much - well, you mentioned Sunday Ticket. And that's something that we're in conversations with and we're considering and we're thinking about it. Obviously, it's an attractive property, but we'll only do it just like our other rights, if it is something that adds shareholder value.

And that's the filter that we'll continue to look for, and we're really happy with, frankly, the deals that we've got in terms of representing things that are accretive to our shareholders so far, and we'll take that same approach going forward.

In terms of the gambling opportunity, as you know, we stuck our toe in this water in the last couple of years in terms of sports books, links with a few of the players out there. And I think going forward, we see this as an opportunity. We see this as an opportunity. We know that it represents very little risk to the company and very little risk to ESPN. As a matter of fact, it's actually - it builds the brand equity from the research that we've had in terms of some of the younger audience that follows sports because it's such an integral part of the experience. And so we think it's actually a growth vehicle for us, but we'll walk into it carefully and monitor it carefully. But we have a greater appetite to do more and more in that area.

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

Okay. Thanks, John. Operator, we have time for one more question today.

Operator

We have a question from Brett Feldman with Goldman Sachs.

Brett Feldman – *Goldman Sachs Group, Inc.*

You mentioned during your prepared remarks the three primary ways you look to release theatrical content, whether it's in the theaters or on your Direct-to-Consumer platforms. And one of those methods is a simultaneous release in the theaters and Premier Access.

And I can understand during COVID when it was very unlikely that people would be in theaters, but that was a reasonably easy call. It seems like it's going to be a little trickier to make a decision around when a film has the right characteristics for that type of release model going forward. So I was hoping you can maybe give us some insight in terms of what you're weighing when you make that decision.

And in particular, with your big franchises - for example, you'll be doing this with *Black Widow*. What gives you conviction that you can build and nurture and create a lot of enthusiasm around those mega franchises without at least some limited theatrical window?

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

Thanks, Brett. Bob, do you want to take that?

Bob Chapek – *Chief Executive Officer, The Walt Disney Company*

Yes. I'm going to take the second one first. If there's any marker in terms of our ability to continue to build franchises, we know theatrical is a proven way to do that. But our merchandise sales on *Mandalorian* - that never had a theatrical release - is certainly one extraordinary marker in terms of the fact that while theatrical continues to be a great way for us to build franchises, our first big data point using our Disney+ platform to sell merchandise has been extraordinarily successful for us as well.

In terms of the Premier Access, you're absolutely right. As we get into a situation where we're trying to monitor - are consumers ready to go back in the theaters. Of course, 90%, let's say, of the domestic marketplace is open right now. And we're encouraged in terms of polling in terms of that growing going forward.

But if you look at last weekend's box office, for an example, and you compare versus an average of the last 3 years of pre-COVID box office, it was 85% below domestically, and 63% below - or 67% below internationally. So we know the market's not quite there yet.

So the Disney Premier Access strategy, one of the things that gives us right now, and we're grateful for it, is the ability to go ahead and try to release things into the market and try to re-prime the pump, if you will. But at the same time, know that for those consumers that are a little leery still about going into a packed theater, that they can go ahead and watch it in the safety and convenience of their home.

In terms of going beyond this fiscal year, we've not announced exactly what our strategy is going to be in terms of which titles will be theatrical plus Disney Premier Access, which ones will be direct to Disney+, or which ones will go into theaters. But know that we'll continue to watch the evolution of the recovery of the theatrical marketplace, and we'll use that flexibility to make the right call at the right time. But right now, we've only called those films that are in this fiscal year because of the relatively fluid nature of the recovery of exhibition.

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

Brad, thanks 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, including financial estimates or statements about our plans, expectations, beliefs or business prospects and other statements that are not historical in nature, 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 with a variety of factors, including factors contained in our annual report on Form 10-K, quarterly reports on Form 10-Q and in our other filings with the Securities and Exchange Commission.

This concludes today's call. We wish everyone a very pleasant good evening. Thanks.

Forward-Looking Statements

Certain statements in this call may constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding our business or financial prospects, position, strategy, plans, investments, resiliency, growth or future; financial or performance estimates or expectations; estimates of the financial impact of certain items, accounting treatment, events or circumstances; the anticipated availability, timing or nature of, our offerings (including content included within our products and services, theatrical releases and business openings); future operations (ours or others') and related impacts, timing, conditions, precautions or market responses; future consumer sentiment or demand; workforce matters; the continuation of external circumstances (including COVID-19); the future impacts of COVID-19 on our business; and other statements that are not historical in nature. 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 our reorganization announced October 2020, capital investments, asset acquisitions or dispositions, integration initiatives, new or expanded business lines, or cessation of certain operations) or other business decisions, as well as from developments beyond the Company's control, including:

- further changes in domestic and global economic conditions;
- changes in competitive conditions and consumer preferences;
- health concerns;
- international, regulatory, political, or military developments;
- technological developments;
- labor markets and activities;
- adverse weather conditions or natural disasters;
- and each such risk includes the current and future impacts of, and is amplified by, COVID-19 and related mitigation efforts.

Such developments may further affect entertainment, travel and leisure businesses generally and may, among other things, affect (or further affect, as applicable):

- demand for our products and services;
- the performance of the Company's theatrical and home entertainment releases and other content;
- the advertising market for programming;
- construction;
- expenses of providing medical and pension benefits;
- income tax expense; 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, 2020 under Item 1A, "Risk Factors," Item 7, "Management's Discussion and Analysis," Item 1, "Business," and subsequent reports including, among others, quarterly reports on Forms 10-Q, which risk factors should be read together with the above factors.

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