August 1, 2014

Time Warner Inc. (TWX)

2Q14 Preview: Maintaining Estimates

COMPANY UPDATE

Stock Rating **HOLD** Unchanged

Price Target **NA**

Entertainment & Internet

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INVESTMENT HIGHLIGHTS: We make no changes to our 2Q14 estimate for revenue of $6.846B (down 8% y/y), Adjusted Operating Income of $1.47B (down 3% y/y), and EPS from Operations of $0.84 (up 3% y/y). We are adjusting the profit mix by segment a little bit. On TWX's Aug 6 conference call, we are most interested in learning about TWX's plan to create more value over the next 18 months than shareholders could receive from selling their shares to another owner.

2Q14. Key points regarding 2Q14 include:

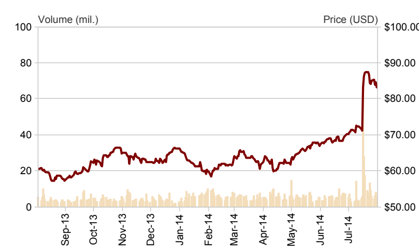
- TWX will release 2Q14 earnings on Wednesday, August 6, 2014 before the market opens and will host a management conference call at 10:30amET to discuss results. The call in number is (800) 446-2782, Passcode: 37544535.
- We make no changes to our 2Q14 estimates and estimate revenue of $6.846B (down 8% y/y), Adjusted Operating Income of $1.47B (down 3% y/y), and EPS from Operations of $0.84 (up 3% y/y). We adjust our profitability mix for Home Box Office and Warner Brothers to reflect: (i) higher than previously estimated programming expenses at HBO resulting in lower profitability; and, (ii) better than expected profitability at Warner Brothers due to the DVD success of *The Hobbit* and the *Lego* movies.
- Nielsen data for 2Q14 indicates that TWX's combined US ratings fell 11% y/y in 2Q14, its weakest performance of the past 6 quarters. In the past, TWX's US ad revenue is typically 9-14% above its US ratings. Therefore, we estimate that TWX will report US TV ad revenue up 1%, in line with guidance of "low single digits".

FY14. We maintain our estimates for FY14 and expect Revenue of $28.9B (up 9% y/y), and we expect EPS from Operations of $4.00 (up 5% y/y).

Rating. We retain our Hold rating.

Stock Price Performance

Time Warner Inc. 08/01/14



	FY 12/31/2013	FY 12/31/2014		FY 12/31/2015	
	Actual	Old	New	Old	New
Rev. (MM)	29,795.0A	28,158.6E	28,158.6E		28,913.1E
Growth	3.7%		(5.5)%		2.7%
EPS: 1Q	0.82A	0.97A	0.97A		
EPS: 2Q	0.83A	0.84E	0.84E		
EPS: 3Q	1.01A	1.06E	1.06E		
EPS: 4Q	1.06A	1.13E	1.13E		
EPS: Year	3.77A	4.00E	4.00E		4.59E
Growth	16.4%		6.1%		14.8%
P/E Ratio	22.0x		20.8x		18.1x

Market Data

Price (07/31/2014)	$83.02
52-Week Range	$88.13 - $57.59
Shares Outstanding	882.10
Market Cap (MM)	$73,231.8
Avg. Daily Volume	7,400,345.0
Cash & ST INV/Share	$2.08
Total Debt/Cap.	40.27%

Relevant disclosures begin on page 12 of this report.

FINANCIAL OUTLOOK & EARNINGS ESTIMATES

Figure A includes our quarterly and FY14 estimates, and compares those to consensus estimates. In this report, we introduce our FY15 annual estimates.

Figure A Quarterly Estimates Data Box

FYE Dec 31:	2Q14E	3Q14E	4Q14E	2014E	2015E
Rev Cur ($mm)	**$6,846**	**$6,420**	**$8,090**	**$28,159**	**$28,913**
Previous ($mm)	$6,846	$6,420	$8,090	$28,159	-
Consensus ($mm)	$6,930	$6,310	NA	$27,730	$28,890
EPS-Cont. Ops	**$0.84**	**$1.06**	**$1.13**	**$4.00**	**$4.59**
Previous	$0.84	$1.06	$1.13	$4.00	-
Consensus	$0.84	$1.03	NA	$4.00	$4.58
P/E				21.5	0.0

Sources: Needham & Company estimates & Yahoo Finance.

2Q14 ESTIMATE CHANGE

We maintain our estimates for 2Q14 and FY14, but in 2Q14 we adjust our profitability mix for Home Box Office and Warner Brothers to reflect: (i) higher than previously estimated programming expenses at HBO resulting in lower profitability; and, (ii) better than expected profitability at Warner Brothers due to the DVD success of The Hobbit and the Lego movies. As a result, we now expect 2Q14 Adjusted Operating Income in Home Box Office of $531mm (up 18% y/y and 3% below our previous estimates), and at Warner Brothers, we now expect Adjusted Operating Income of $180mm (down 2% y/y and 9% above our previous estimates.

2Q14 DISCUSSION & ANALYSIS

We estimate revenue of $6.846B (down 8% y/y), Adjusted Operating Income of $1.47B (down 3% y/y), and EPS from Operations of $0.84 (up 3% y/y). Detailed segment revenue data is expected to be as presented in Figure 1:

Figure 1 June Quarter Analysis: 13A vs Current 14E vs Prior 14E

Time Warner, Inc.

$ and shares in millions, except per share data

Revenue	2Q13A	New 2Q14E	Yr/Yr Chg	Old 2Q14E	New/Old
Turner	$2,627	$2,745	4%	$2,745	0%
Home Box Office	$1,216	$1,398	15%	$1,398	0%
Warner Brothers	$2,941	$2,882	-2%	$2,882	0%
Intersegment Eliminations	($182)	($180)	1%	($180)	0%
Total, ex Time Inc	$6,602	$6,846	4%	$6,846	0%
Time Inc	$833	$0	-100%	$0	
Total Revenue	**$7,435**	**$6,846**	**-8%**	**$6,846**	0%
Adjusted Operating Income					
Turner	$815	$878	8%	$878	0%
Home Box Office	$450	$531	18%	$545	-3%
Warner Brothers	$184	$180	-2%	$166	9%
Corporate	($78)	($100)	-28%	($100)	0%
Intersegment Eliminations	$17	($20)	NM	($20)	0%
Total, ex Time Inc	$1,388	$1,470	6%	$1,470	0%
Time Inc	$124	$0		$0	
Adjusted Operating Income	**$1,512**	**$1,470**	**-3%**	**$1,470**	0%
Restructuring Charge, Other	$0	$0		**$0**	
Operating Income	**$1,512**	**$1,470**	**-3%**	**$1,470**	0%
Interest Expense	($299)	($304)	-2%	($304)	0%
Minority Interest (Expense)	($1)	$0		$0	
Other Income (expense)	($59)	($30)	NM	($30)	
Income Before Tax	$1,154	$1,136	-2%	$1,136	0%
Income Tax Provision	($382)	($381)	0%	($380)	0%
Income from Continuing Operations	$772	$756	-2%	$756	0%
Discontinued Operations	$0	$0	NM	$0	
Net Income	$772	$756	-2%	$756	0%
Add-Back Extraordinary-Net	$0	$0		$0	
Net Income Attributable to TWX S/H's	**$772**	**$756**	**-2%**	**$756**	0%
EPS Continuing Operation	**$0.81**	**$0.84**	**3%**	**$0.84**	**0%**
EPS-Discontinued Operations	$0.00	$0.00		$0.00	
EPS Reported	**$0.81**	**$0.84**	**3%**	**$0.84**	0%
Avg Diluted Shares Out	951	900	-5%	900	0%

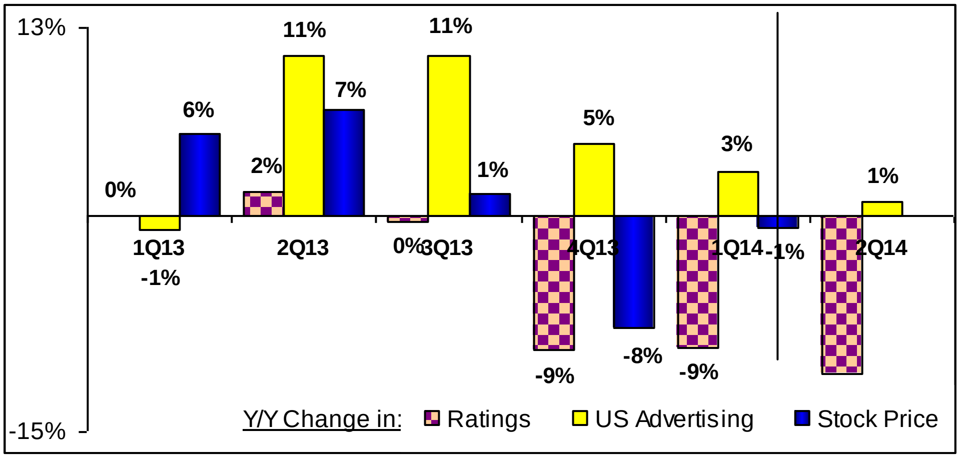
Sources: Company Reports, Needham & Company estimates.

2Q14 Ratings Analysis

Based on Nielsen data, we would highlight the following points from figure B:

- TWX's US ratings were down 11% y/y in 2Q14, its worst performance in the past 6 quarters.
- Over the past 4 quarters, TWX's US ad revenue has been running 9-14% above its US ratings. Therefore, we estimate that TWX will report US TV ad revenue up 1%, in line with guidance of "low single digits".

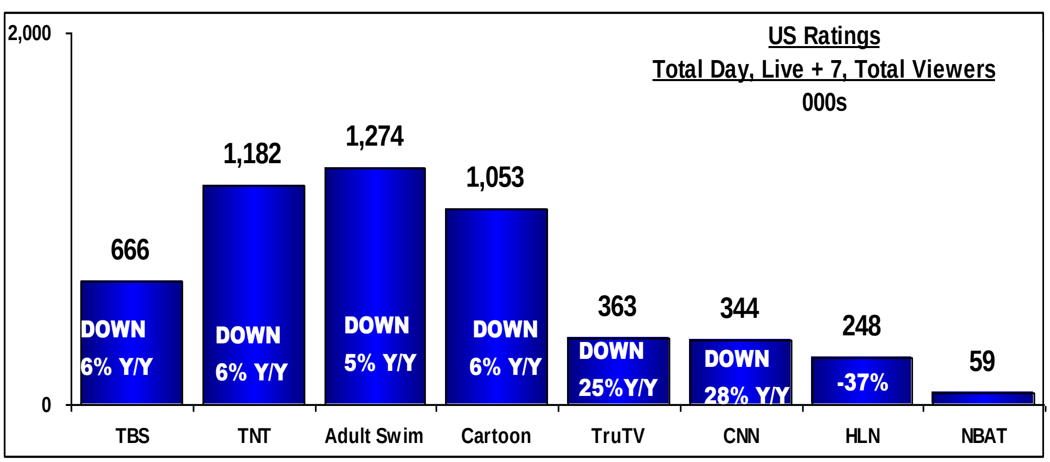
Figure B TWX: Trends in US Ratings, US Ad Revenues, and Share Price



Sources: Nielsen, Company reports and transcripts, Needham & Company, LLC research. Calendar year data. Changes in share price are measured from the last day of the quarter to one week after the earnings call, according to Yahoo finance.

Figure C illustrates that 6 of the 7 TWX key channels we measure reported lower ratings in 2Q14. Only NBAT rose, up 13% to 59K average viewers. In terms of bundle quality, TWX has three US channels that have over 1.0mm viewers, and 2 important general entertainment channels (TBS and TNT) plus Cartoon Network and CNN which represent important niches for the TV bundle. This suggests high bundle quality, although if TWX owned a broadcast network, its negotiating position would be stronger.

Figure C TWX: Major Channel Ratings, Details and Trends



Source: Nielsen, Needham & Company, LLC research. Ratings are for the June quarter, total day, all viewers over 2 years old, and live + 7 days.

VALUATION

Our HOLD rating is based on several forms of valuation, summarized in Figure 2:

Figure 2 TWX: Valuation Summary & Conclusions

		TWX	Industry Average*		
1	EV/Sales	6.5	0.0		
2	EV/OIBDA	13.0	3.7		
3	P/E	20.8	11.7	**Breakeven DCF***	**9.3%**
4	FCF/Share	$2.87	$0.00	Calculated as the	
5	EV/FCF	36.4	3.1	10-Yr EBITDA CAGR required	
6	FCF Yield	3%	-169%	to justify current share price.	

* Represents the averages of CBS, DISCA, DIS, MSG, FOXA, SNI, TWX, VIAB and WWE.

Source: Needham & Company estimates.

- The **"Breakeven DCF"** valuation methodology uses the current share price to calculate the market's growth expectations for the enterprise, including capital efficiency trends. This valuation methodology concludes that TWX must achieve a 10-year OIBDA compound annual growth rate of approximately 9.3% to justify its current share price. (Please see Figure 6.)
- In Figures 7 and 8, we summarize several **valuation multiples** for Sales (6.5x), OIBDA (13x), P/E (20.8x) and Free Cash Flow. TWX's has a 3% free cash flow yield, making it fairly valued in our opinion.

INVESTMENT POSITIVES

- **New Revenue Streams.** We believe the migration of high-quality content to digital platforms will create additional revenue streams over time. We are most optimistic about the pricing power of premium content over mobile devices. A-title quality content will likely remain the most valuable and TWX is one of the largest A-title content creation company's in the US.
- **Free Cash Flow.** We project that TWX will generate approximately $2.6 billion (ie, $2.87 per share) of free cash flow in 2014, which should be available for dividends, share repurchases, and/or acquisitions. (Please see Figure 8)
- **Return of Capital.** TWX is under-levered (2.5x debt/EBITDA) with $3.55B of cash on 3/31/14. Time Warner currently pays a dividend of $1.27 cents a share/year, and in January, 2012 boosted its share buyback authorization an additional $4B. In FY13, TWX repurchased approximately 60.5mm shares of its common stock for approximately $3B.
- **Strong Competitive Positions**
  - TWX's several of the most pre-eminent cable network groups in the US, with fully-distributed, mission critical (to MSOs, telcos, satellite companies) cable channels including, among others, TBS, TNT, Cartoon Network, Boomerang, truTV, TCM (Turner Classic Movies), CNN, and Headline News (HLN). There are only 75 fully-distributed cable networks in the U.S. and TWX owns nearly 10% of them. Offshore, Turner International operates 23 cable brands, including eight US channel brands, plus 15 non-U.S. cable brands in various countries. CNN's channels reach nearly 200 countries.
  - Warner Bros. film studio is the pre-eminent film studio in the US, with one of the finest film and TV libraries in the world.

- Time Inc. is one of the largest, most prestigious, and oldest magazine companies in America, and we expect it to be spun off in the first half of FY14, which should unmask the growth of the TV and film businesses.

INVESTMENT RISKS

- **New Media Monetization.** The transition to the Internet platform has been fraught with economic value destruction for newspapers, music, and yellow pages. We believe that the Internet fractures audiences and gives consumers infinite choice, which makes it more difficult to capture economics for content. In addition, there is a culture of FREE on the Internet that puts downward pressure on all prices. We are more optimistic about monetizing content over mobile platforms, both smartphones and tablets.
- **Ratings.** TWX's cable networks reported audience declines in 2Q14 for all of its major networks. Ratings declines puts downward pressure on advertising revenue because: 1) advertising is sold on a CPM (cost per thousand) viewers' basis, and 2) lower ratings limit TWX's ability to take advantage of the strong scatter market since valuable advertising inventory must be used for audience make-goods rather than sold for cash. CNN's ratings are down in key demos owing to difficult comps that included political advertising last year.
- **Acquisition Risk.** With its underlevered balance sheet and the low asset prices stemming from 2009's credit squeeze, we wonder whether TWX will acquire something big. At the same time, we wonder about TWX's long-term strategy and growth prospects if it does *not* buy something big. Without acquisitions, we estimate that the growth outlook through 2014 for TWX's EPS is about 3%, which appears fairly valued at its current 16.7x PE ratio.

Figure 3 TWX: Quarterly Financial Projections, FY14E

$ and shares in thousands, except per share data	3/31/14A	6/30/14E	9/30/14E	12/31/14E	2014E	3/31/14A	6/30/14E	9/30/14E	12/31/14E	2014E
Revenue										
Turner	$2,593	$2,745	$2,478	$2,701	$10,517	5%	4%	6%	6%	5%
Home Box Office	$1,339	$1,398	$1,293	$1,373	$5,404	9%	15%	9%	9%	11%
Warner Brothers	$3,066	$2,882	$2,829	$4,196	$12,973	14%	-2%	5%	5%	5%
Intersegment Eliminations	($195)	($180)	($180)	($180)	($735)	13%	-1%	0%	-12%	-1%
Total, ex Time Inc	$6,803	$6,846	$6,420	$8,090	$28,159	10%	4%	6%	6%	6%
Time Inc	$742	$0	$0	$0	$742					
Total Revenue	**$7,545**	**$6,846**	**$6,420**	**$8,090**	**$28,901**	**9%**	**-8%**	**-6%**	**-6%**	**9%**
Operating Income										
Turner	$895	$878	$1,115	$986	$3,875	3%	8%	15%	12%	10%
Home Box Office	$464	$531	$410	$433	$1,838	11%	18%	3%	4%	10%
Warner Brothers	$380	$180	$311	$524	$1,396	43%	-2%	3%	-9%	5%
Corporate	($119)	($100)	($70)	($120)	($409)	3%	28%	-29%	5%	0%
Intersegment Eliminations	$6	($20)	($20)	($5)	($39)	-50%	-218%	-211%	-136%	-164%
Total, ex Time Inc	$1,626	$1,470	$1,746	$1,818	$6,660	12%	6%	10%	3%	8%
Time Inc	($90)	$0	$0	$0	($90)					
Adjusted Operating Income	**$1,536**	**$1,470**	**$1,746**	**$1,818**	**$6,570**	**7%**	**-3%**	**2%**	**-3%**	1%
Restructuring Charge, Other	$396	$0	$0	$0	$396					
Operating Income	**$1,932**	**$1,470**	**$1,746**	**$1,818**	**$6,966**	42%	-3%	2%	-3%	8%
Interest Expense	($266)	($304)	($304)	($304)	($1,178)	-8%	2%	1%	1%	-1%
Minority Interest (Expense)	$0	$0	$0	$0	$0					
Other Inc (CW loss+HBO int'l profit)	($6)	($30)	($25)	($25)	($86)					
Income Before Tax	$1,660	$1,136	$1,417	$1,489	$5,702	57%	-2%	-7%	0%	9%
Income Tax Provision	($295)	($381)	($475)	($499)	($1,649)	-23%	0%	0%	-2%	-6%
Income from Continuing Operations	**$1,365**	**$756**	**$942**	**$990**	**$4,054**	103%	-2%	-10%	0%	16%
Disc Ops, 1 Time Items Imp. Comp.	($480)	$0	$0	$0	($480)					
Net Income	$885	$756	$942	$990	$3,574	16%	-2%	-20%	0%	-4%
Add Back Extraordinary-Net	$0	$0	$0	$0	$0					
Net Income	$885	$756	$942	$990	$3,574	16%	-2%	-20%	0%	-4%
Less Net Loss Attributable to Noncontrolling Interests	$0	$0	$0	$0	$0					
Net Income Attributable to TWX Shareholders	**$885**	**$756**	**$942**	**$990**	**$3,574**	19%	-2%	-20%	0%	-3%
EPS-Continuing Operations, ex Time	**$0.97**	**$0.84**	**$1.06**	**$1.13**	**$4.00**	22%	3%	-5%	5%	5%
EPS Discontinued Operations/Other	$0.53	$0.00	$0.00	$0.00	$0.53					
EPS- Reported	$1.50	$0.84	$1.06	$1.13	$4.52	**93%**	**3%**	**-16%**	**5%**	**16%**
Avg Diluted Shares Out	911	900	890	880	895	-5%	-5%	-5%	-5%	-5%

Sources: Company Reports, Needham & Company estimates.

Figure 4 TWX: Annual Inc. Statement Projections, 2013A-2015E

$ and shares in millions, except per share data	2013A	2014E	14/13	2015E	15/14
Revenue					
Turner	$9,983	$10,517	5.4%	$10,833	3%
Home Box Office	$4,890	$5,404	10.5%	$5,728	6%
Warner Brothers	$12,312	$12,973	5.4%	$13,102	1%
Intersegment Eliminations	($739)	($735)	-0.5%	($750)	2%
Total, Ex Time Inc	$26,446	$28,159	6.5%	$28,913	3%
Time Inc	$0	$742	NM	$0	
Total Revenue	**$26,446**	**$28,901**	**9.3%**	**$28,913**	**0%**
Adjusted Operating Income					
Turner	$3,536	$3,875	9.6%	$4,225	9%
Home Box Office	$1,678	$1,838	9.5%	$2,005	9%
Warner Brothers	$1,327	$1,396	5.2%	$1,441	3%
Corporate	($407)	($409)	0.5%	($400)	
Intersegment Eliminations	$61	($39)	-163.9%	($50)	
Time Inc	$6,195	($90)	-101.5%	$0	
Adjusted Operating Income	**$6,532**	**$6,570**	**0.6%**	**$7,221**	10%
Restructuring Charge/Other, net	($80)	$396	NM	($50)	
Operating Income	**$6,452**	**$6,966**	8.0%	**$7,171**	3%
Net Interest Expense	($1,190)	($1,178)	-1.0%	($1,200)	
Minority Interest (Expense)	$78	$0		$0	
Other Income (expense), net	($112)	($86)		($75)	
Income Before Tax	$5,229	$5,702	9.1%	$5,896	3%
Income Taxes Provision	($1,749)	($1,649)	-5.7%	($1,975)	
Income From Continuing Operations	$3,480	$4,054	16.5%	$3,921	-3%
Discontinued Operations/Other 1-Time	$227	($480)		$0	
Net Income	$3,707	$3,574	-3.6%	$3,921	10%
Add-Back 1 Time Items	**$0**	**$0**		$0	
Net Income Attributable to TWX Shareholders	**$3,678**	**$3,574**	**-2.8%**	**$3,921**	10%
EPS Continuing Operations	**$3.79**	**$4.00**	5.4%	$4.59	15%
EPS Discontinued Operations	$0.24	$0.53	119.6%	$0.00	
EPS-Reported	**$3.91**	**$4.52**	**15.8%**	**$4.59**	1%
Avg Diluted Shares Out	943	895	-5.1%	855	-4%

Sources: Company Reports, Needham & Company estimates.

Figure 5 TWX: Target Price Calculation - Traditional DCF, 2015E-2024E

$ and shares in millions, except per share data

Valuation Conclusions			% of Total
Sum of PV of Free Cash Flow [1]		$43,916	44%
PV of Terminal Value Discounted at WACC [1]		$52,798	52%
Value of Operations (WACC Method)		**$96,714**	**96%**
Plus: Excess Cash at 3/31/14		$3,546	
Plus: Non-Consolidated Assets (From PMV)		$800	
Less: Minority Interest		($343)	
Less: Unfunded Retirement Liabilities		$0	
Enterprise Value		**$100,717**	**100%**
Less: LTD at 3/31/14		($20,291)	
Less: Lease Obligations		($3,400)	
Less: Preferred Stock Outstanding		$0	
Less: Value of Options & Restricted Sk, After-tax		($1,200)	
Common Equity Value		**$75,826**	**75%**
Fully Diluted Shares Out, 2014E		910	
DCF Value/Share		**$83.32**	
Current Share Price @	7/31/14	$83.30	
Upside Potential (DCF-Current Price/Current Price)		**0%**	

Standard Discounted Cash Flow (DCF) Valuation

Why We Calculate: DCF is a rigorous bottoms-up valuation of the enterprise focusing on cash flows (not accounting)

Strengths

1 Focuses on operations. Removes financing
2 Focuses on FCF. Removes non-cash accounting
3 Explicitly forecasts capital needs (WC & CapX)
3 Uses a levered beta (widely available)
4 Ent value focus captures entire business model

Weaknesses

1 Many assumptions. Valuation can be manipulated
2 Terminal value big & based on low visiblity projections
3 Model assumes constant debt/equity ratio
4 Complex to calculate
5 Calculates the enterprise value first, then equity value

[1] **Calculation of the Value of Operations (WACC Method)**

FYE 12/31:	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	CAGR '15-24E
EBITDA (after sk comp exp & corp):	**$7,330**	**$7,990**	**$8,709**	**$9,493**	**$10,347**	**$11,278**	**$12,293**	**$13,400**	**$14,606**	**$15,920**	**$17,353**	**9.0%**
- Depreciation	($760)	($775)	($942)	($956)	($965)	($1,055)	($1,057)	($1,050)	($1,148)	($1,129)	($1,097)	
+ Option Exercise Proceeс	$600	$400	$400	$400	$400	$400	$400	$400	$400	$400	$400	
+ Int & Inv Income only	$60	$60	$60	$60	$60	$60	$60	$60	$60	$60	$60	
EBIT	$7,230	$7,675	$8,227	$8,996	$9,842	$10,684	$11,697	$12,810	$13,918	$15,251	$16,716	
Cash Taxes (at 42%)	($2,531)	($3,254)	($3,488)	($3,814)	($4,173)	($4,530)	($4,959)	($5,431)	($5,901)	($6,467)	($7,088)	
Plus: Depreciation	$760	$775	$942	$956	$965	$1,055	$1,057	$1,050	$1,148	$1,129	$1,097	
Plus: Sk Based Comp Exp	$220	$220	$220	$220	$220	$220	$220	$220	$220	$220	$220	
Working Capital Change	($500)	($417)	($456)	($463)	($467)	($510)	($511)	($508)	($555)	($546)	($531)	
Less: Capital Spending	($550)	($556)	($608)	($617)	($623)	($680)	($682)	($677)	($740)	($728)	($708)	
FCF from Operations	**$4,630**	**$4,442**	**$4,837**	**$5,278**	**$5,765**	**$6,238**	**$6,821**	**$7,463**	**$8,089**	**$8,859**	**$9,707**	**9.1%**
PV Discounted at WACC [2]		$4,442	$4,426	$4,420	$4,418	$4,375	$4,378	$4,383	$4,347	$4,357	$4,369	
Sum of PV of Free Cash Flow											$43,916	
Terminal Value of 2024E FCF [3]											$117,303	
PV of Terminal Value at WACC [2]											$52,798	
Discount Period		0	1	2	3	4	5	6	7	8	9	

[2] **Calculation of WACC: (Updated 8/20/11)**

10-Year Risk Free Rate ("RFR")	2.0%
Equity Risk Premium (Ibbotson-Arithmetic)	6.0%
Beta (Yahoo Finance)	1.40
Target Equity/(Debt + Equity)	85%
Debt Rating	BBB
Debt Spread	2.0%
Marginal Tax Rate ("T")	35.4%
WACC	**9.3%**

(RFR+(Equity Risk Premium x Beta)) x % Equity/Total Capital + ((RFR + Debt Spread) x (1-T) x % Debt/Total Capital).

[3] **Calculation of Terminal Multiple (WACC Method)**

WACC	9.3%
Long-term Nominal GDP Growth	1.0%
WACC-GDP Growth	8.3%
FCF Terminal Multiple [1/(WACC-Growth Rate)]	**12.1**
EBITDA Terminal Mutiple	**6.8**

Sources: Company Reports, Needham & Company estimates.

Figure 6 TWX: Breakeven Discounted Cash Flow (DCF) Valuation Calculation, 2015E - 2024E

$ and shares in millions, except per share data

Valuation Conclusions		**2014E**
Sum of PV of Free Cash Flow [1]		$43,869
PV of Terminal Value Discounted at WACC [1]		$53,118
Value of Operations (WACC Method)		**$96,987**
Plus: Excess Cash at 3/31/14		$3,546
Plus: Non-Consolidated Assets (From PMV)		$800
Less: Minority Interest		($343)
Enterprise Value		**$100,990**
Less: LTD at 3/31/14		($20,291)
Less: Lease Obligations		($3,400)
Less: Preferred Stock Outstanding		$0
Less: Value of Options & Restricted Sk, After-tax		($1,200)
Common Equity Value		**$76,099**
Fully Diluted Shares Out, 2014E		910
Breakeven DCF Value/Share		**$83.63**
Current Share Price @	7/31/14	$83.30
Discount to DCF Value (DCF-Current Price/DCF)		0%

Breakeven Discounted Cash Flow Valuation

Why We Calculate: BE DCF uses the current share price to calculate the market's growth expectations for the enterprise.

Strengths

1 Makes no assumption about growth for first 10 years
2 Prevents over-optimism by working backwards
3 Data widely available and model well understood
4 Explicitly forecasts capital needs (WC & CapX)
5 Uses a levered beta (widely available)

Weaknesses

1 Terminal value big & based on low visiblity projections
2 Model assumes constant debt/equity ratio
3 Complex to calculate
4 Calculates the enterprise value first, then equity value

[1] **Calculation of the Value of Operations (WACC Method)**

FYE 12/31:	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	**Required LT Growth Rate**
EBITDA (after sk comp exp & corp):	**$7,330**	**$7,946**	**$8,685**	**$9,492**	**$10,375**	**$11,340**	**$12,395**	**$13,547**	**$14,807**	**$16,185**	**$17,690**	**9.30%**
- Depreciation	($760)	($775)	($912)	($926)	($903)	($953)	($886)	($847)	($888)	($801)	($778)	
+ Option Exercise Proceed	$600	$400	$400	$400	$400	$400	$400	$400	$400	$400	$400	
+ Int & Inv Income only	$60	$60	$60	$60	$60	$60	$60	$60	$60	$60	$60	
EBIT	$7,230	$7,631	$8,233	$9,027	$9,933	$10,848	$11,969	$13,161	$14,379	$15,843	$17,371	
Cash Taxes (at 42%)	($3,066)	($3,235)	($3,491)	($3,827)	($4,211)	($4,599)	($5,075)	($5,580)	($6,097)	($6,718)	($7,365)	
Plus: Depreciation	$760	$775	$912	$926	$903	$953	$886	$847	$888	$801	$778	
Plus: Sk Based Comp Exp	$220	$220	$220	$220	$220	$220	$220	$220	$220	$220	$220	
Working Capital Change	($500)	($417)	($456)	($463)	($467)	($510)	($511)	($508)	($555)	($546)	($531)	
Less: Capital Spending	($550)	($556)	($608)	($617)	($623)	($680)	($682)	($677)	($740)	($728)	($708)	
FCF from Operations	**$4,095**	**$4,417**	**$4,810**	**$5,265**	**$5,754**	**$6,230**	**$6,807**	**$7,462**	**$8,095**	**$8,872**	**$9,766**	
PV Discounted at WACC [2]		$4,417	$4,402	$4,409	$4,410	$4,369	$4,369	$4,382	$4,351	$4,364	$4,396	
Sum of PV of Free Cash Flow											$43,869	
Terminal Value of 2024E FCF [3]											$118,015	
PV of Terminal Value at WACC [2]											$53,118	
Discount Period		0	1	2	3	4	5	6	7	8	9	

[2] **Calculation of WACC: (Updated 8/20/11)**

10-Year Risk Free Rate ("RFR")	2.0%
Equity Risk Premium (Ibbotson-Arithmetic)	6.0%
Beta (Yahoo Finance)	1.4
Target Equity/(Debt + Equity)	85%
Debt Rating	BBB
Debt Spread	2.0%
Marginal Tax Rate ("T")	35%
WACC	**9.3%**

(RFR+(Equity Risk Premium x Beta)) x % Equity/Total Capital + ((RFR + Debt Spread) x (1-T) x % Debt/Total Capital).

[3] **Calculation of Terminal Multiple (WACC Method)**

WACC	9.3%
Long-term Nominal GDP Growth	1.0%
WACC-GDP Growth	8.3%
FCF Terminal Multiple [1/(WACC-Growth Rate)]	**12.1**
EBITDA Terminal Mutiple	**6.7**

Sources: Company Reports, Needham & Company estimates.

Figure 7 TWX: Valuation Multiples

$ and shares in millions, except per share data		
Valuation Conclusions		**2014E**
Market-Based Enterprise Value [1]		$95,148
2014E Sales (From Annual Projections)		$14,734
EV/Sales		**6.5**
Market-Based Enterprise Value [1]		$95,148
2014E EBITDA (From Annual Projections)		$7,330
EV/EBITDA		**13.0**
Target Price		NA
Target Price EV/2015 EBITDA		**NA**
Current Price	7/31/14	$83.30
2014E EPS (From Annual Projections)		$4.00
P/E Ratio		**20.8**
[1] **Calculation of Market-Based Enterprise Value**		
Year End 12/31:		2014E
Current Share Price	07/31/14	$83.30
Fully Diluted Shares Out		910
Market Capitalization		**$75,803**
Less: Excess Cash		($3,546)
Less: Non-Consolidated Assets		($800)
Plus: Unfunded Retirement Liabilities		$0
Plus: Debt at 6/30/13		$20,291
Plus: Lease Obligations		$3,400
Plus: Preferred Stock Outstanding		$0
Plus: Options & Warrants Outstanding		$1,200
Market-Based Enterprise Value		**$95,148**

Sources: Company Reports, Needham & Company estimates.

Figure 8 TWX: Free Cash Flow Valuation

$ and shares in millions, except per share data		
Valuation Conclusions		**2014E**
FCF/Share [2]		$2.87
Current Price	7/31/14	$83.30
FCF Yield		**3%**
FCF [2]		$2,615
2014E EBITDA (From Annual Projections)		$7,330
FCF Conversion Rate (FCF/OIBDA)		**36%**
Market-Based Enterprise Value [1]		$95,148
FCF [2]		$2,615
EV/FCF		**36.4**
Net Debt/EBITDA		2.3
Net Debt		$16,745
Net Debt/Market Cap		**22.1%**
[2] **Calculation of Free Cash Flow**		
Year End 12/31:		2014E
OIBDA		$7,330
Plus: Option Exercise Proceeds		$600
Less: Cash Interest Expense		($1,200)
Minority Interest		$0
Less: Preferred Dividends		$0
Less: Cash Taxes		($3,066)
Less: Change in Working Capital		($500)
Less: Capital Spending		($550)
Free Cash Flow		**$2,615**
Less: Dividends		($1,047)
Free Cash Flow After Dividends		$1,568
Shares Outstanding		910
FCF/Share		**$2.87**
FCF/Share After Dividends		$1.72

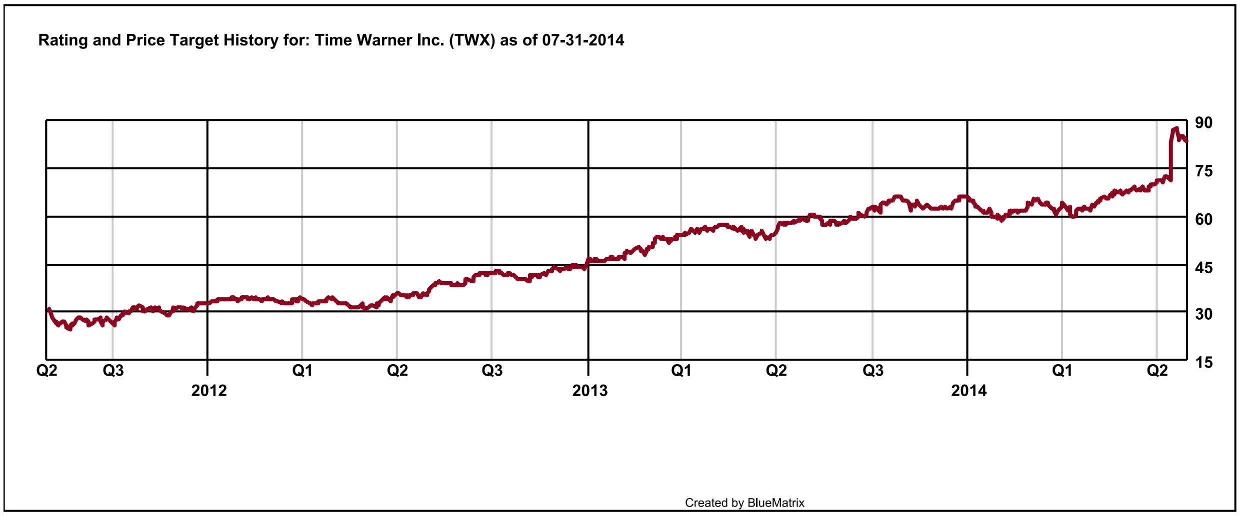
Sources: Company Reports, Needham & Company estimates.

Potential Upside Drivers

- The bulk of TWX's profits come from two of the fastest growing silos with the most pricing power in the media landscape: film and cable networks. TWX owns one of the pre-eminent cable network groups in the US, with fully-distributed, mission-critical (to MSOs, telcos, satellite companies) cable channels including, among others, TBS, TNT, Cartoon Network, Boomerang, truTV, TCM (Turner Classic Movies), CNN, and Headline News (HLN). Warner Bros. film studio is the pre-eminent film studio in the US, with one of the finest content libraries on the planet.

Risks to Target

- Risks to TWX include a weakening economy, a declining advertising market, declining ratings of its produced shows, and rising costs of production as well as sports rights fees, resulting in margin shrinkage.



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Restricted	< 1	0
Under Review	0	0

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