The Near Bankruptcy of Disneyland Paris

When Disney CEO Michael Eisner announced his intention to build a theme park near Paris in 1985, there was every reason to believe that the venture was deemed to success. However, just one year after it opened, it was about to go bankrupt. Which left the executives of The Walt Disney Company with a tough decision: abandon their ambitions or inject additional equity into a fragile project.

The destiny of Disneyland Paris illustrates the misfortunes of project financing, demonstrating (i) how complex it can be to forecast cash flow in the absence of reliable comparisons, as well as (ii) the appeal of non-recourse financing as a means of reducing risk for sponsors.

The Genesis of the Project

The Walt Disney Company pioneered the theme park business in the 1950s. By the time Michael Eisner announced his plans for Paris, the company already had three parks, two in the United States and one in Japan. Disneyland Park opened in California in 1955 and Walt Disney World in Florida opened in 1971. The park in Japan opened in 1983.

The aura of the Disney brand had been strong in Western Europe and the profits generated by its cartoons were higher than in North America. So, The Walt Disney Company had high expectations for its new park; hoping to replicate US and Japan successes.

As the site, a new town of Marne-la-Vallée to the east of Paris was chosen, winning over 40 other places across 5 different countries that were considered. The second forerunner was a site near Barcelona, yet, despite good weather, Catalonia was viewed as less attractive strategically. Paris seemed a better option due to its large population, its central location in Europe and the constant flow of the tourists, already attracted by the French capital.

Project Calibration

When they started planning, Disney executives made a paradoxical observation: though their parks had been a success, they never found a formula to maximize the profits.

- In California, due to a lack of space, sufficient hotel accommodations were not constructed. A large part of the revenues that Disney could have captured, went to the hotels opportunistically built by other chains around the place.
- The same problem existed in Florida, not due to land restriction this time, but to the conservative planning of the Disney executives.
- In Japan, the construction and operation of the project was passed to the local partner to avoid the risks, so Disney received only royalties. The success of the park was not up the level with the benefits Disney was extracting from it.

To avoid the frustrations of the previous projects, the Disney executives made two ambitious decisions: they would operate a park without a local partner and they would include a huge hotel complex. The total price tag for all was estimated at $4.4 billion, which is more than three times what was paid for the Tokyo Park. It was the largest investment in Disney history.

The Japanese project was the key reference because it was the only Disney-park built outside of US. It was also very successful. The number of visitors exceeded the most optimistic forecasts and by the late 1980s it was drawing 15 million visits a year, more than either US park. The $1.1 billion loan taken to build a Japanese park was repaid in three years.

Master Agreement with the French Government

The battle between Paris and Barcelona to host a theme park ended up as a political fight between respective governments, since both realized the value of the park in terms of jobs and committed to provide all sort of support to the project. Spain banked on large subsidies; France offered better logistical support.

The final partnership agreement between Disney and the French government was signed in 1987, after two years of negotiations. The French agreed to the following:

- The sale of land of the park at the price of 30% below the market
- The construction of a metro and bus station, parking lots for the visitors, and a road link from the park to the motorway
- Loans to a total value of FRF 4.8 billion at the rate of 7.85% (lower than that applicable to French government bonds at that time)
- The use of VAT rate of 5.5% on all products sold in the park, including those that are usually subject to a higher rate.

In exchange for those advantages, The Walt Disney Company committed to the following:

- Guarantee of a minimum of traffic on a public transportation in the direction of the park – is this level was not achieved, Disney was to compensate the French government
- Opening of one attraction within the park that showcased French culture
- No construction of another Disney theme park within 800 km from the original within a certain period of time
- Retention of a significant share of control over the project for at least five years.

Financing Structure

The choice of the parc's financial structure was hotly debated among Disney's executives. Original plan was to raise debt and equity at the corporate level to fund the project. The advisors suggested a finance structure with a wiser option. The use of project finance would isolate the park from the Disney's balance sheet and would allow to raise additional equity at the level of the project rather than the group, which would avoid dilution for Disney's shareholders.

The structure selected by Disney relied on an SPC set up for building and operating the park and the hotels. The SPC - Euro Disneyland SCA (or Euro Disney) - had total control over the project. Its role was to select a strategy and select and pay the employees§ receive payments from customers, repay the project debt and distribute royalties to Disney for the use of brand and the know-how deployed in the park. Royalties were indexed to turnover and not profits.

Disney controlled 49% of the SPC. The rest of the equity was raised through an IPO organized simultaneously in London and Paris. Completed in November 1989, three years before the park was open, this IPO was one of the largest ever for a company without a track record. Despite the lack of revenues, future operating risks, and a long construction period, the IPO was more than 10 times oversubscribed.

The SPC also raised two tranches of 20-year non-recourse debt. BNP led a syndicate of 39 banks, providing a loan for construction. Indosuez led another group of 30 banks, funding the hotel component of the project.

Although constructions costs were higher than expected, investors cheered the park's opening in April 1992. Shares soared to 165 French francs, more than twice the IPO price (72 francs). In October 1992, Michael Eisner was even appointed Knight of the "Legion d'Honneur", the highest French order of merit.

The Debt Issue

Despite the initial enthusiasm, it quickly appeared that the project was misjudged. Revenues barely covered the costs. The first financial year brought a loss of $900 million. Disneyland Paris could not pay its debt and its shares fell to 11 francs.

The hotel part of the project was particularly underperforming. Rooms were perceived as too expensive, and the tourists preferred to sleep in Paris than in the park. It was a major break from the previous experience. US visitors organized the trip to visit the park, visitors in Europe visited it while visiting Paris, they would go to the park to please the kids, but they would go back to Paris to see it at night.

Europe was also going through the worst economic crisis since World War II. France was in recession and unemployment was high in Europe. The French monetary policy made it worst, because while trying to keep French franc's inflation under control, the increasing prices for foreigners discouraged people from visiting.

Errors in the Design of the Project

The park itself was not what the European visitors expected. The climate was a problem, the park designed like its US and Japanese counterparts, was situated in a much colder environment. The attractions were not adapted for winter and the turnover fell sharply as the fall approached.

Weekdays was another problem, contrary to the US custom and Disney's expectations, the European parents would not take a day off at work and school to take their kids to the Disneyland. French kids have more vacations than their peers in US and the parents are reluctant to have them miss a day at school. So, the empty part during the week frustrated the Disney executives and the overcrowded park on the weekends frustrated the visitors, who had to stand in lines.

Catering was another disappointment. Disney did not foresee French visitors wanting both breakfast and lunch at the park, but with most of them staying in Paris, they wanted to eat when they arrive. Breakfast being a problem, lunch was not better: Disney's no-alcohol policy was incomprehensible for the Europeans.

Tokyo's par success was the reason why the park was open in Paris, but it was also a reason why it failed. Disney executives were not insensitive to the cultural differences, they even dedicated part of the Japanese park to the Samurais, but they resisted "localizing" the attraction, making Disney park a totally American experience, their only concession was a presence of the sushi restaurant and kimono costumes worn by Mickey and Minnie on New Year's Day. Given the popularity of Disney cartoons in Europe, it was clear why the Disney executives tried to replicate their Japanese and American success there.

Restructuring

Disney was forced to act. Ticket and hotel prices were lowered. Partnerships with tourist agencies were signed to bring in new visitors. Attractions were adapted for winter, food for local taste and some restaurants started selling soft alcohol.

The rumors spread that the park would close, though it was not an option for Disney. The only option was to restructure. Crisis talks between Disney, Disneyland Paris and the park's creditors resulted in the following:

- A major capital increase in which Disney would take a leading role
- A waiver of 18 months' interest payment by the banks
- A postponement of the principal repayment by three years

- The cancellation by Disney of several hundred million of receivables due from Euro Disneyland SCA
- A waiver of all royalty payments due to Disney for five years
- A sharp reduction of royalty payments after that.

This restructuring was accepted by the lenders in 1994. Also, a Saudi prince Al-Waleed took a 10% stake in Euro Disney, becoming the second largest shareholder of the park after Disney itself.

Epilogue

This gave Disneyland Paris some breathing space, but troubles resurfaced later in 2002, when the second park, The Walt Disney Studio was open next to the original park. This massive investment resulted in a new agreement struck with the creditors in 2004.

The same recipe was applied: debt restructuring, cut in royalty payments, and capital increase. In 2017 Disney took a full control of the project and offered to buy out the remaining shareholders. It marked end of the ill-fated adventure in project finance and resulted in one of Europe's main tourist attractions.