The Walt Disney's CEO Discusses F3Q 2013 Results - Earnings Call Transcript

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Doug Mitchelson - Deutsche Bank

Jessica Reif-Cohen - Bank of America Merrill Lynch

Alexia Quadrani - JP Morgan

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The Walt Disney Company (DIS) F3Q 2013 Earnings Conference Call August 6, 2013 5:00 PM ET

Operator

Welcome to the Q3 2013 Walt Disney Company Earnings Conference Call. My name is Leslie, and I will be your operator for today. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.

I will now turn the call over to Lowell Singer, Senior Vice President of Investor Relations. Mr. Singer, you may begin.

Lowell Singer

Okay, thanks Leslie. Good afternoon, everyone, and welcome to the Walt Disney Company's third quarter 2013 earnings call. We issued our press release about 45 minutes ago. It's available on our website at www.disney.com/investors. Today's call is also being webcast. And after the call, we will post a transcript of the call to the website.

Joining me for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer, and Jay Rasulo, Senior Executive Vice President and Chief Financial Officer. Jay is going to lead off today. He will be followed by Bob and then we will be happy to take your questions. So, with that, let me turn it over to Jay, and we'll get going.

Jay Rasulo

Thank you, Lowell, and good afternoon everyone. Earnings per share in the third quarter, excluding items affecting comparability were $1.03. Given the number of headwinds we faced in the quarter, we are very pleased with the financial results we delivered. In the third quarter media networks was once again the largest contributor to our performance. Operating income at cable networks was up a healthy 12% in the quarter, while operating income at broadcasting was down compared to last year. Our strong cable performance was due to continued growth at ESPN and higher equity income from our investment in A&E Television Networks.

ESPN's growth was driven by increased affiliate revenue and to a lesser extent higher advertising revenue. ESPN's programming and production costs were higher in the quarter, which relates contractual rate increases for Major League Baseball rights and our expansion of the X Games. I mentioned affiliate revenue was the driver of growth at ESPN in the third quarter. If you call, last quarter, we told you we are expecting ESPN to recognize $73 million less in previously deferred revenue in Q3 compared to last year. As it turned out, ESPN actually recognized $64 million more in previously deferred affiliate revenue in Q3 compared to last year. The $137 million swing was the result of ESPN meeting certain programming commitments in the third quarter, which were met in the fourth quarter last year. ESPN was able to meet those programming commitments in Q3 due to the airing of incremental hours of Wimbledon programming. As a result of this shift, ESPN has now recognized all previously deferred affiliate revenue for the year. As such, ESPN will recognize no deferred affiliate revenue in the fourth quarter, which is $172 million less than last year.

ESPN cash ad sales were up 9% in the quarter, which is roughly in line with the ad sales pacing we discussed on our Q2 call. ESPN's reported ad revenue was up 3% as a result as the increase in cash ad sales was partially offset by lower ratings. The decline in ratings during the quarter was primarily related to NBA comparability issues. During the quarter, ESPN aired fewer NBA regular season games compared to last year when the lockout created a more back-end loaded schedule. Also, ESPN air fewer play-off games and those match-ups delivered lower ratings in last year's playoff games. So far this quarter, ESPN's cash ad sales are pacing up 11%.

At Broadcasting, lower operating income in the quarter was primarily due to three factors. First, higher prime-time programming cost as a result of airing more hours of acquired programming, which was more expensive on a per hour basis. Second, lower program sales compared to last year. If you recall, we sold Grey's Anatomy and Castle in the third quarter last year and had no comparable sales this year. And third, lower advertising revenue as a 7% decrease in station ad revenue offset a modest increase in ad revenue at the ABC Network.

Affiliate revenue at the ABC Network was up nicely in the quarter, but the increase wasn't sufficient to offset these three items. Quarter-to-date scatter pricing at the ABC Network is running mid-teens above upfront levels. ABC and ESPN recently completed their respective upfronts and we feel great about the pricing increases achieved and the amount of inventory each network was able to sell.

We continue to be very pleased with the performance of our parks and resorts business. The segment delivered another quarter of solid growth as our recent investments at Walt Disney World and the Disneyland Resort continue to payoff. Revenue was up 7% and operating income was up 9% in the quarter due to growth at our domestic parks and resorts. As we noted during last year quarter's call, Q3 segment operating income was adversely impacted by an estimated $35 million as a week of the Easter holiday shifted into Q2 this year. Adjusting for this shift, segment operating income growth in Q3 would have been up 15%. Higher operating income at our domestic parks and resorts was primarily due to increased guest spending, occupied room nights, and attendance partially offset by higher costs including ongoing spending for growth initiatives.

During the quarter, attendance at our domestic parks was up 3% with Walt Disney World and the Disneyland Resort each setting new Q3 attendance records. Per capita spending was up 7% on higher ticket prices and food and beverage spending.

Average per room spending at our domestic hotels was comparable to prior year and even though available room nights increased in the quarter occupancy was comparable to prior year. So far this quarter domestic reservations are pacing up 3% compared to prior year levels while book rates are up 4% versus prior year. Total parks and resort segment margins were up 40 basis points in the third quarter compared to prior year. The year-over-year change in Q3 margins was adversely impacted by an estimated 140 basis points due to the timing of the Easter Holiday and spending on growth initiatives.

At the studio we released two films in the third quarter Iron Man 3 and Monsters University both of which performed exceptionally well at the box office. Iron Man 3 generated $1.2 billion in global box office revenue however it faced a difficult comparison with the Avengers which generated $1.5 billion in global box office last year and this is the third highest grossing film of all time.

Monsters University box office performance compared favorably to that of Brave last year, however operating income at the studio declined year-over-year. This decline was due to pre-released marketing expenses for the Lone Ranger and the aforementioned Avengers, Iron Man theatrical comparison. The Avengers also had a strong DVD sales in Q4 last year so the DVD release of Iron Man 3 in Q4 this year faces a difficult comparison which we expect to result in a headwind to the studios Q4 results of about $45 million.

Needless to say we're disappointed with the performance of the Lone Ranger and in light of the film's box office results we expect to incur loss on the film in Q4 of between $160 million and $190 million. Consumer's products growth and operating income resulted from increases in merchandise licensing and retail. The increase in licensing was primarily due to the inclusion of Star Wars in this quarter's results. Also earned licensing revenue was up 3% versus last year and that growth is on a comparable basis which excludes any revenue from the newly acquired Star Wars property. The performance of our retail business was driven by higher comp store sales in North America and Japan and higher online sales in North America.

We continue to return capital to shareholders by repurchasing our stock during the third quarter; we repurchased 12.6 million shares for about $800 million. Fiscal year-to-date we repurchased 57 million shares for $3.2 billion and with that I'll now turn the call over to Bob.

Bob Iger

Thank you Jay and good afternoon. We're pleased with our performance in Q3 and we believe we're well positioned going forward. I would like to address a couple of specifics about our businesses starting with ESPN which was one again a key driver in Q3, Jay commented about ESPN's ratings in the quarter and I would like to add some perspective. In an average week more than 113 million Americans tune in or log on to access ESPN content with the average person spending almost 7 hours a week engaged with ESPN Media on a variety of platforms.

In Q3 nearly 9 out of 10 homes with access to ESPN tuned in to at least one of the ESPN networks. Since 96% of sporting events are watched live, sports are virtually DVR-proof making ESPN incredibly valuable to advertisers as well as cable operators. We have ranked the ESPN the number one network in perceived value for 13 years in a row and the most important network for nine straight years. Even though ESPN is a clear market leader, it continues to refine its sports portfolio, expand original programming, invest in new technology, and innovate to enhance the fan experience.

ESPN's recent acquisition of the exclusive rights for U.S. Open tennis is growing array of digital services including WatchESPN and the new SEC Network next summer are a few recent examples of ESPN's constant innovation that will deliver even greater value to consumers, operators, and advertisers. And with so many of the major sports rights locked up for the next 10 years, given ESPN's brand strength and its continued focus on investment and innovation, we remain confident in ESPN's value and its position as the number one brand in sports over the long-term.

Our acquisition of Marvel also continues to drive real value for us across the company. Following the record setting performance of The Avengers last year, the huge success of Iron Man 3 this summer continue the Marvel momentum, which bodes incredibly well for upcoming Marvel releases including Thor: The Dark World, Captain America: The Winter Soldier, Guardians of the Galaxy, and of course, Avengers 2. We previewed this late at Comic-Con a couple of weeks ago and the phenomenal audience reaction is anything to go by, there is huge appetite for more great Marvel content. There is also a great deal of excitement around ABC's new series and Avengers spin-off called Agents of S.H.I.E.L.D. The first episode got a standing ovation at Comic-Con along with rave reviews. And this month Disney XD premieres its third animated Marvel series.

We continue to be extremely pleased with the creative success of our Animation Studios, Monsters University opened in June to become the latest in Pixar's unbroken string of hits, Planes from Disneytoon Studios opened this Friday, and Frozen, another great movie from Disney Animation will introduce two new Disney princesses when it opens in theatres at Thanksgiving.

We are also looking forward to the launch of Disney Infinity on August 18. We have showcased Infinity to a number of audiences and we are very encouraged by the overwhelmingly positive response we are getting across the board from retailers, reviewers, and consumers alike. And we are also very proud of the several best of awards that Disney Infinity earned at this year's E3. So, given what's ahead for Disney, ABC, ESPN, Pixar, and Marvel as well as the upcoming Star Wars Episode 7, we are incredibly well-positioned for growth and expect solid results in 2014, '15, and beyond.

I am going to turn this call back over to Lowell, so that we can take your questions.

Lowell Singer

Thanks Bob. Leslie, we are ready for the first question.

Question-and-Answer Session

Operator

Thank you. (Operator Instructions) Our first question comes from Doug Mitchelson with Deutsche Bank. Please go ahead.

Doug Mitchelson - Deutsche Bank

Well, thanks so much. Jay, a clarification, I am trying to figure out the math on the fiscal 4Q loss for loan range, what might help is could you give us a sense of the P&A expense that was in June in prior versus what might have been in the fiscal fourth quarter? And then either Jay or Bob, you talked about ESPN at length, Bob, if you got us any competitive impact in the upfront or in the current ad market related to the entry of Fox Sports 1?

Jay Rasulo

Hi, Doug. Let me start, it's Jay. So, the $160 million to $190 million range that I gave you is the impairment that we will take on the asset of the film and then the operating loss that we will experience in Q4. And you will get a very explicit breakout of those numbers in the Q basically it's like 86 on impairment than the rest. We don't know of course what the actual operating loss will be. The reason that we are recognizing that in the fourth quarter just for all of your ratification is that the accounting rules for film cost impairments were amended by the financial accounting standards board and adopted by us of course right thereafter in Q1 of fiscal year '13. Under the old rules if a film was released at the end of the quarter but prior to the company's filing it's statements then the films performance resulted in impairment the company generally was required to record that impairment in the previous quarter in this case would have been Q3 but under the new rules the impairment analysis is limited to information that was available as of quarter end and therefore doesn't incorporate the actual performance of the film after the balance sheet date so that number is a Q4 number, in the past it would have been the Q3 number.

Bob Iger

The second part of the question Doug ESPN has strong upfront both in terms of the increases on the CPM front (ph) and in terms of overall revenue and did not detect any impact whatsoever from any new competitive forces including Fox Sports 1.

Lowell Singer

Operator next question please.

Operator

Next question is from Jessica Reif-Cohen with Bank of America Merrill Lynch. Please go ahead.

Jessica Reif-Cohen - Bank of America Merrill Lynch

I have two questions one now that you've decided to keep Hulu just wondering if you can give us your vision for how it may change or evolve and the second thing is obviously the press for the last two days have been completely focused on retrans. I was just wondering if you can give us your take on how you know how much longer these kind of battles can go on and before you think the government will start to step in.

Bob Iger

On the Hulu front Jessica we as you know with our co-owner Fox explored a sale for considerable amount of time and went free far down the road in terms of that process and during that time we became more and more convinced that there was real strategic value to Hulu and there was value from a financial perspective meaning we could grow it at a rate that would be overall positive for the shareholders of our company. We also decided when we decided to keep it to infuse Hulu with approximately $750 million of new capital that is aimed at strengthening it's team, strengthening it's technology because we believe we need to continue to invest in the technology platform and of course strengthening it's contents or it's programming which is you know we've seen new entrants and there are other entrants in the marketplace do extremely well with. I won't get specific in terms of the direction because we're going to leave that to the management team of Hulu but we think that there is considerable opportunity here and that opportunity will bode well for both Hulu itself but also for content owners who will have a robust platform to sell the content to and for the creative side who will have another entity to sell programming to, or to create for.

On the retrans front we never like to see battles like this obviously because we think that sometimes they bring attention to the business that isn't necessarily helpful, that said maybe you would expect this from a programmer but we feel strongly about the need for broadcasters to be paid adequately for the value that they deliver both to consumers or customers of multi-channel services and to the distributors themselves. Even though these broadcast stations can be as you know obtain for free, over the year we know that distributors repackage these signals and in fact sell them as part of other services to consumers and thus we think we should get paid. We also believe that the combination of programming both national and network and local particularly news is really compelling as evidenced by the ratings of these stations deliver compared with the ratings of numerous other channels and therefore we think that the station should get paid accordingly.

I don't really have details about this negotiation so I don't really want to weigh in specifically about it but I don't sense that the government is closed to jumping into the fray on this one. I think they probably prefer that we work this out or that owners of stations and distributors work this out themselves but I don't get a sense that there is government intervention that is imminent because of this.

Lowell Singer

Thanks Jessica. Operator next question please.

Operator

Next question is from Alexia Quadrani with JP Morgan. Please go ahead.

Alexia Quadrani - JP Morgan

Alright, thank you. Just staying on the broadcast theme there, could you give us an update on how you view, I guess, the ABC Network going into the fall season? Should we expect also on that topic a lift from the Scandal (indiscernible) in the fiscal fourth quarter? And are you still comfortable with the guide of that I think $400 million to $500 million re-trans revenue by 2015?

Bob Iger

Okay. We do feel comfortable with the guide on the re-trans revenue by 2015 of $400 million to $500 million. We love Scandal and it has been sold to I guess a couple of entities and it also is being sold internationally, but the impact in the fourth quarter is relatively small. As it relates to the ABC Network going into the season we have been saying now for a few quarters that ABC is due to put on its schedule a couple of new strong shows to replace what was the foundation of the schedule over the sort of Desperate Housewives, Lost, Grey's Anatomy years. We are hopeful that their new schedule will deliver what ABC needs, not only in terms of what I will call the downstream revenue through owning the programs, but also from a ratings perspective and ultimately an advertising perspective. We think they have got a couple of really hot comedies and a couple of hot dramas I mentioned one earlier in S.H.I.E.L.D. I mean, we are going to go into the fall feeling relatively bullish about ABC's ability to strengthen its schedule and deliver better bottom line, but until the season unfolds you never can quite tell.

Jay Rasulo

Alexia, just as a follow-up since you asked about Broadcast, as Bob said, the Scandal number is pretty small, but there is a little bit of headwind in the fourth quarter, because last year, we sold Castle and Wipeout in the fourth quarter to the tune of about $40 million. So, we will not see that, that revenue repeated in the fourth quarter this year. And not that it relates directly to Broadcast, but to the Media Group in general. We are making some investments. You have all heard about Fusion, our joint venture with Univision, as well as the channel we bought in Germany called Das Vierte and that will create headwinds of about $25 million for Q4.

Alexia Quadrani - JP Morgan

Okay Thank you very much.

Bob Iger

Thanks Alexia. Operator, next question please.

Operator

Next question is from Ben Swinburne with Morgan Stanley. Please go ahead.

Ben Swinburne - Morgan Stanley

Thank you. Bob, could you talk a little bit about the parks top line trends in the domestic market, particularly the per caps, which has remained really strong. I know you guys put in some pricing during the quarter and I would love to hear your thoughts and how you thought about that pricing in this economy, and given the investments you have made and sort of the sustainability of kind of monetizing all of the CapEx over the last several years in that segment? And then Jay, can I ask you on ESPN or on cable in general, I looked in the Q it looks like if you adjust for the deferrals the affiliate revenue growth was sort of in the 6% to 7% range, I just want to see if you had a number around ESPN for the quarter that was clean so we could understand the trends there?

Bob Iger

Overall, the business for our parks domestically is quite good, good enough for us to take another price increase, but this one was somewhat different, and that I think for the first time, we created price differential between the Magic Kingdom and the other parks for the obvious reason that the Magic Kingdom is the most popular park, the most iconic. And so we thought there was an opportunity there. And we didn’t sense any backlash from the marketplace at all. And as you said, we have had strength not just in terms of attendance growth, but we have had strength in terms of spending, not just ticket prices, but room rates and merchandise and food and beverage. I would say that – we have also had increase in international attendance. Year-to-date, it’s up domestically 7% both Orlando and in California. And so we think that bodes well. And we think that we are well positioned in this quarter, particularly coming off the third quarter, Magic Kingdom in Florida had record numbers as Jay mentioned in the third quarter. By the way that was also true for our park in Tokyo and our park in Hong Kong is also doing quite well. If we are seeing softness in our parks unit, it’s in Europe, at Paris, which Jay also mentioned.

So, we think we are well positioned. We have got new product in the marketplace. We are not finished with Fantasyland in Orlando. We still have one big attraction to open, which is going to open in 2014. Cars Land and the impact of that on California Adventure has also continued to show great strength, although in California we are lapping the success of the opening a year ago a bit.

I’m not sure that I’ve anything else I would necessarily want to add, we have a lot of other product coming beyond Fantasy Land ultimately we’re going to add Avatar as we have said although we have not announced an opening date yet in Florida, couple of years out at least and we’re going to continue to invest in Disney Land, we have got some pretty exciting things that we will be announcing over the next couple of months.

Ben Swinburne - Morgan Stanley

You didn’t mention MyMagic Plus, any comment on how that’s impacting the business at this point?

Bob Iger

It's really having not an impact from a revenue perspective really at all because we’re still rolling it out and what I would call test phase the reason for that is that this is a very significant undertaking from a technological perspective and we really want to make sure that we walk before we run because we don’t really want to overload our technological backbone. So we’re in what I will call another beta phase that started in August 2nd and it is basically designed for us to have a full roll out, the probable full roll out in the early part of fiscal ’14 and that’s when you will start to see an impact from a revenue perspective but right now we’re mostly heading cost associated with Magic Plus ahead of what will be we believe some interesting revenue generating opportunities.

I can also say that it's working meaning those that are using it and we have got a number of people that have used it have reacted very well. This test that we’re in right now should be probably be used by over 80,000 people or 80,000 guests based on the reservations that we have written against with this initiative attached to them.

Jay Rasulo

On your question of ESPN affiliate revenue I think you mentioned then 6%, you were a little bit low the cable affiliate revenue for Q3 grew in high single digits ESPN of course is the biggest number and it grew a little bit higher than that but still in the high singles.

Ben Swinburne - Morgan Stanley

Even if I adjust for the deferrals?

Jay Rasulo

Yes. If you unadjust it it's closer to 10%.

Lowell Singer

Operator next question please.

Operator

Next question is from Anthony DiClemente with Barclays. Please go ahead.

Anthony DiClemente – Barclays

Bob: I would love to get your thoughts on just a general theme of consolidation elsewhere in the media eco-system I guess two big areas where there has been some consolidation or talk of it would be media buying on the agency side and then of course cable distribution and so I was wondering if you thought at that scale in other parts of the ecosystem could impact your business in anyway and then I've a follow-up.

Bob Iger

Well on the advertising agency front that announcement was made only recently and so we don't haven't any sort of really experience in terms of how to judge it, I would say we're studying it that doesn't in any way mean that we're worried about it necessarily but it's still pretty new and we want to understand what it's potential impact could be before we comment about it publically. In terms of consolidation on the distribution front, this is probably the most robust era we have ever seen from a distribution perspective meaning the number of outlets that are available to often sent (ph) to other content owners to distribute their product has grown significantly and pretty dramatically in some cases, obviously Netflix is probably the most recent one and we feel that some consolidation among cable owners if that occurs is going to have no impact whatsoever on our business because there are so many buyers in the marketplace. We also have as you know an array of services that everybody wants fortunately and therefore we think that we have basically the kind of leverage necessary not just to gain access but to achieve the kind of pricing that we need to achieve to grow our businesses.

Anthony DiClemente – Barclays

And just one quick follow-up we are heading the football season here I'm just wondering as ESPN has looked at it's matches up for the upcoming NFL Season and college football, I mean is there anything to lookout for in terms of the ratings outlook number one and then just this question maybe a little out there but given digital distribution and authentication wondering if there is anything that we should we mindful of that maybe the ESPN ad sales force has done be it packaging on digital ad sales or innovative forms of mobile distribution of your robust football package at ESPN? Thanks.

Bob Iger

I have long since learned that judging the football schedule before the season unfolds can be, I guess, a bit premature. I either overreact to it meaning thinking that it's positive or overreact the other way season by season. And I discover year-after-year that until you really see how these teams play what dynamics occur – as you know it a star quarterback gets injured and suddenly a team that you have two or three times becomes substantially less attractive than before. So, I don't want to judge this one except to say that at least on paper going in, we feel that we have got a good solid schedule. Last year, we were somewhat disappointed by our results. That's not just a function of how teams ultimately perform, but sometimes, the quality of the game, I am not suggesting – what I mean by that is how competitive a game is. So, it's just too tough to predict. I like the schedule going in this time around, but I have been there many times before only to find out that I might have been wrong and the opposite is true. We have been pleasantly surprised.

On the other question that you asked, ESPN has been selling multi-platform advertising for quite a long time. I don't know the percentage, but it's extremely high in terms of the number of buyers that ESPN that buy across their various platforms from their digital services to radio, to their magazine, to their channels. And they have grown that nicely. The Watchapp is an opportunity for them to generate more advertising revenue and they are in fact selling ads for the Watchapp, but the numbers even though they are in the probably tens of millions of dollars at this point, they are still relatively small when compared to their total both advertising revenue and their total revenue, but we believe that they will continue to grow. And we obviously believe that I'd say that the penetration of mobile media and not only how fast it has occurred, but how quickly it's being adopted by the consumers, one of the most dramatic changes we have seen in the media business in a very long time. And I think provides us with a great opportunity considering the fact that we have been at the forefront in many respects of making sure that we are putting products on the mobile platforms or making the product that we have available on non-mobile platforms available via mobile.

Anthony DiClemente - Barclays

Thanks Bob. Much appreciate it.

Bob Iger

Thank you, Anthony. Operator, next question please.

Operator

Next question comes from Todd Juenger with Sanford Bernstein. Please go ahead.

Todd Juenger - Sanford Bernstein

So, we haven't talked much about the film or consumer products business yet so let me turn there. On the film side, I think it's fair to say that the summer box office was not great, at least domestically probably a pretty crowded schedule and some audience fatigue. How should we think about that going forward for you guys, especially given your reliance on Marvel and Lucasfilm and the risk that you are a little bit highly leveraged against sort of the Sci-Fi superhero genre, I know your risk of longer term fatigue of that? Then the related question is how should we think about the opportunity in the consumer products side, especially from Lucasfilm and I guess still a little bit from Marvel as you really try and capitalize on those properties? How long does that take to get through the system and into the retail shelf? And should we think about that is incremental or is some of that displacing other shelf space and just changing the mix a little bit? Thanks.

Bob Iger

Okay. Let's first characterize summer box office, these last number of summers have been very competitive and quite crowded. I don't know that this summer got any more crowded or more competitive than before although certainly there was a lot of attention paid to it. We actually think we had an excellent summer and that we ended up with Iron Man 3, which did over $1.2 billion in global box office, which is substantially above what Iron Man 2 and Iron Man 1 did and the highest Marvel box office film of all time next to Avengers. We actually think Avengers helped Iron Man 3 and we believe that the impact of Avengers will be felt on future Marvel products, particularly Thor, which is coming up first and then Captain America, and of course, Avengers 2. There has been a lot said I know about the risk of basically high-cost tent-pole films, and we certainly can attest to that given what happened with Lone Ranger, and Jay went into the details.

We still believe that a tent-pole strategy is a good strategy that one way to rise above the din and the competition is with a big film, not just a big budget but big story, big cast, big marketing behind it. We think that the Disney, Pixar, Marvel and ultimately the Star Wars Lucas Brand will actually contribute to our ability to rise above that then and compete quite effectively but we also know and I know I'm probably saying the obvious but you still have to make really strong films. So I don't know that the dynamic has changed that much expect that if there are tempo films being made I guess technically there is more risk in the marketplace. But we have known all about that risk for quite some time. As we look forward as I mentioned we feel very confident in them obviously. I mentioned three of them Guardians of the Galaxy as another one which we're very excited about and that the Marvel character library is only being mined from the tip of the iceberg perspective we will be mindful of not going to the well too often because it's hard to make great films and so our charge to Marvel is bring films to market where you really believe in the stories and the story tellers.

Disney Live Action, we're going to continue to make probably in the neighborhood of five to at the very, very most 10 but most cases it's less than that, Live Disney, Live Action Films. Some will be tempo films like we have Maleficent coming up as for instance Tomorrowland is another one, some will be much lower budget films like Saving Mr. Banks which is coming up at the end of this calendar year and of course we believe in Lucas and Star Wars which is '15 and then our animation strategy is clearly working. We did almost 260 million in box for Monsters 2 and we're hopeful that it's going to exceed $400 million in box office outside the United States which will make it I think the fourth highest grossing Pixar film of all time with Toy Story and Nemo and one other ahead of it that's a pretty good story. We like what's happening with Disney Animation. We have had a couple of real hits in Tangled and in Wreck It Ralph and we believe in Frozen coming up and we've got a really fine movie coming up this weekend in Plains (ph) which is made by Disney 2 studios but it bears the Disney brand was that one point going to be a direct a video and we looked at it and we saw the quality we decided that bring it up theatrically was a wise move.

So I know that's a long way of my saying that we think that Marvels, Disney, Pixar, Lucas Branded film strategy is a good one for us not only because of what we believe it can deliver from a box office perspective but the obvious value it delivers to this company across so many platforms from games, Infinite is a good example to our consumer products and you've to consider publishing as part of that because the digital side of publishing and of course what it means for us and our products we're evidence of all of these branded franchise films is clear both domestically and internationally across all of our products businesses.

On the consumer products front we believe that there is upside or incremental earnings from the mining of the consumer products that will come from not only the marble franchises but also from Lucas even though there have been a lot of Star Wars, a lot of Star Wars product out in the marketplace. We think that when we put these companies together combining the teams and taking all these great product to market that there is a substantial potential not only to increase sales but to increase royalties for these products and so we view the consumer product side of these acquisitions as truly additive.

Lowell Singer

Operator next question please.

Operator

Next question is from David Bank with RBC Capital Markets. Please go ahead.

David Bank - RBC Capital Markets

So I guess a question with respect to CapEx and capital allocation I think while there are always ample opportunities to invest in the business it seems like the perception is that CapEx is sort of peaked and probably headed downward trajectory wise, yet your leverage is still amongst the lowest in the industry and what are your thoughts in terms of increasing capital returns overtime? Is there something in particular you're keeping that powder (ph) dry for, what are your thoughts around that?

Bob Iger

Thanks, David. I am probably not going to reveal anything to you that you haven't heard me say before, but let me reiterate how we think about this. I think that you, first of all, you are correct in that. Our belief is that a lot of the capital investment we have been engaged in, particularly in parks and resorts over the past three or four years plus the deployment of capital in acquisitions will yield returns such that we will have the great problem of dealing with increasing cash flow as the years go by. We look very hard for internal and organic ways to invest our capital above our rate of return. We think that's why our investors give us their money to invest. And I think we have demonstrated a pretty good track record at finding projects in our businesses that allow us on an incremental basis to create returns that are very, very attractive to shareholders. That being said, we are not departing from kind of the formula we have used in returning capital to shareholders, where we have consistently returned 20% or so of the cash generated by the company to shareholders in terms of buybacks.

If you look at this year's buyback plan, you see that it's so far this year pretty consistent with that at $3.2 billion. Remember, we committed buy in the Lucas shares over two years. And if you look at last year's CapEx – I am sorry buyback versus this year's you will see that it is nicely up. And to sort of comment on keeping your powder dry, we are not cash hoarders. We have an excellent balance sheet that we worked very hard at keeping as a strategic asset for the company to allow us access to the capital markets. You see our interest expense is way down this year. That's due to the fact that we have been able to both refinance high-cost debt like we had at Disneyland Paris as well as borrow money at record levels in terms of the issues we have made. So, we feel very good about our balance sheet, access to cash, we don't feel the need to afford cash. So, if we do not find ample internal opportunities in terms of investment or interesting acquisitions, then we will in fact increase our returns to shareholders.

David Bank - RBC Capital Markets

Thank you.

Bob Iger

You are welcome. Operator next question please.

Operator

Next question is from Marci Ryvicker with Wells Fargo. Please go ahead.

Marci Ryvicker - Wells Fargo

Thanks. I have two questions. I think the first, there seems to be a little bit of variability in affiliate fee growth from quarter-to-quarter. And Jay, I think you made it a point to call this out during an Investor Conference some point in late May. So, is there any way to think about affiliate fee growth in fiscal Q4 or even beyond and just other than new contracts coming on what are the various puts and takes for affiliate fee growth? So, that's the first question. And then second just in the broadcast sector, is there any color on how you are pacing right now at the broadcast networks and stations?

Jay Rasulo

Okay. On the first half, I appreciate your, I will call it frustration. I didn't hear frustration in your voice, but the difficulty in quarter-to-quarter forecasting of affiliate fees and it has to do with the way we build for instance, let me give you an example. In Q2, our affiliate revenue benefited from an extra day in the billing cycle in 2012 so-called leap year and that effects the growth in that quarter more than you might imagine. Relative to giving you some insight into Q4, we are looking at high single-digit growth in terms of affiliate revenue. And I am sorry I can't help you with all the adjustments that come in and out every quarter in terms of how that affiliate number grows. The range is pretty tight, I will tell you that, but within a couple of percentage points, it's very hard for you guys to predict that accurately.

In terms of pacing's, I'll say this the stations are pacing down in Q4 in part due to comp issues that we have last year, we have the benefit of the Emmy's which is 3 to 4 percentage points of growth in ad revenues this year. The Emmy's will be on CBS. We won't have that. So, that will obviously affect and there is some more challenging political comp this year versus last year and that again is a couple of percentage points which is effecting the ad pay in that stations.

Lowell Singer

Thank you Marcy. Operator next question please.

Operator

Next question is from David Miller with B. Riley & Company. Please go ahead.

David Miller - B. Riley & Company

Couple of questions, Jay on the prognostication of losses for Lone Ranger the 160 to 190 I'm just curious why give a range now, why do you not, I mean why give a range at all is it just because the film is just sort of swimming around various theatrical markets overseas and you're just kind of waiting to see what the final number is or are you just kind of weigh into additional analysis, why give a range why not just kind of pinpoint a little bit more exactly what the loss is going to be and then Bob correct me if I'm wrong but I believe your NBA contract comes up for renewal with ESPN in 2016 with the emergence of Fox Sports 1 and just given Rupert sort of ready, fire, aim kind of mentality with regard to sports rights in general. If Fox Sports 1 wants to overbid or bid against you for the NBA and you come to the termination that you cannot make the NBA work in terms of your ROIC targets. Are you prepared to walk away from the NBA in the same way that you guys walked away from the NHL? Thanks very much.

Jay Rasulo

I will be brief on the reason for the range. We're only opening 40% of international markets with Lone Ranger and it goes all the way out to I think Japan opened in September if I'm not mistaken. So, I think that's the last market, so that's the reason for the ranger.

David Miller - B. Riley & Company

Got it.

Bob Iger

The NBA David is very important to ESPN both from a quality of programming perspective but also from a volume perspective and it's certainly a priority of ESPN to extend their relationship with the league. I think the league would believe that it would beneficial for them as well to stay on ESPN which is a very, very important platform for them. I don't want to sound in anyway as though we're complacent but I think it would be safe to assume that we're reasonably confident that we will be able to extend that relationship and I do not want to at any way give any prediction or whatever is what we might do if the price gets to a point that it's substantially above what we expected.

Lowell Singer

Thanks David. Operator we've time for one more question.

Operator

Okay. The last question comes from Barton Crockett with Lazard Capital Markets. Please go ahead.

Barton Crockett - Lazard Capital Markets

Now on the topic on the expansion of distribution and then opportunity right now for Disney that you brought up early on the call. There has been a lot of press reporting about you know new over the top services that could emerge you know companies like Intel, others that have reported. I was wondering without kind of commenting specifically about a company if you could talk generally about this type of service in terms of your belief in the probability that we can see something materially over the next few quarters and the possibility of getting some type of material minimum guarantee that could be noticeable in your P&L.

Jay Rasulo

I don't know that you will see much impact in the next few quarters although I think it may be some new distributors out there that are looking to make content deals in the near term, you mentioned Intel being potentially one of them. I still believe that overall these new platforms whether they are over the top or not offer us more and new opportunities to monetize their content and our approach to them will probably be somewhat consistent with how we have approached other distributors both incumbents and new distributors. We look with an open mind towards a distributors that we believe the ability to create a viable platform in terms of their ability to us for our content but also a viable platform for the consumer one with a good interface and one that's likely to ultimately stick in terms of distribution. So I don't think that you're going to see substantial change in the environment meaning distribution environment in the near term because of these but I think it's safe to say that over certainly the next five years there is going to be more than one new entrants in the marketplace.

Bob Iger

Thank you Barton 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 website. Let me also remind everyone that certain statements on this call may constitute forward-looking statements under the securities laws. We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them and we do not undertake any obligation to update these statements. Forward-looking statements are subject to a number of risks and uncertainties and actual results may differ materially from the results expressed or implied in light of a variety of factors, including those contained in our Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. This concludes today's call. Have a good afternoon, everyone.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.

Executives

Lowell Singer - Senior Vice President, Investor Relations

Bob Iger - Chairman and Chief Executive Officer

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Analysts

Doug Mitchelson - Deutsche Bank

Jessica Reif-Cohen - Bank of America Merrill Lynch

Alexia Quadrani - JP Morgan

Ben Swinburne - Morgan Stanley

Anthony DiClemente – Barclays

Todd Juenger - Sanford Bernstein

David Bank - RBC Capital Markets

Marci Ryvicker - Wells Fargo

David Miller - B. Riley & Company

Barton Crockett - Lazard Capital Markets

The Walt Disney Company (DIS) F3Q 2013 Earnings Conference Call August 6, 2013 5:00 PM ET

Operator

Welcome to the Q3 2013 Walt Disney Company Earnings Conference Call. My name is Leslie, and I will be your operator for today. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Please note that this conference is being recorded.

I will now turn the call over to Lowell Singer, Senior Vice President of Investor Relations. Mr. Singer, you may begin.

Lowell Singer - Senior Vice President, Investor Relations

Okay, thanks Leslie. Good afternoon, everyone, and welcome to the Walt Disney Company's third quarter 2013 earnings call. We issued our press release about 45 minutes ago. It's available on our website at www.disney.com/investors. Today's call is also being webcast. And after the call, we will post a transcript of the call to the website.

Joining me for today's call are Bob Iger, Disney's Chairman and Chief Executive Officer, and Jay Rasulo, Senior Executive Vice President and Chief Financial Officer. Jay is going to lead off today. He will be followed by Bob and then we will be happy to take your questions. So, with that, let me turn it over to Jay, and we'll get going.

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Thank you, Lowell, and good afternoon everyone. Earnings per share in the third quarter, excluding items affecting comparability were $1.03. Given the number of headwinds we faced in the quarter, we are very pleased with the financial results we delivered. In the third quarter media networks was once again the largest contributor to our performance. Operating income at cable networks was up a healthy 12% in the quarter, while operating income at broadcasting was down compared to last year. Our strong cable performance was due to continued growth at ESPN and higher equity income from our investment in A&E Television Networks.

ESPN's growth was driven by increased affiliate revenue and to a lesser extent higher advertising revenue. ESPN's programming and production costs were higher in the quarter, which relates contractual rate increases for Major League Baseball rights and our expansion of the X Games. I mentioned affiliate revenue was the driver of growth at ESPN in the third quarter. If you call, last quarter, we told you we are expecting ESPN to recognize $73 million less in previously deferred revenue in Q3 compared to last year. As it turned out, ESPN actually recognized $64 million more in previously deferred affiliate revenue in Q3 compared to last year. The $137 million swing was the result of ESPN meeting certain programming commitments in the third quarter, which were met in the fourth quarter last year. ESPN was able to meet those programming commitments in Q3 due to the airing of incremental hours of Wimbledon programming. As a result of this shift, ESPN has now recognized all previously deferred affiliate revenue for the year. As such, ESPN will recognize no deferred affiliate revenue in the fourth quarter, which is $172 million less than last year.

ESPN cash ad sales were up 9% in the quarter, which is roughly in line with the ad sales pacing we discussed on our Q2 call. ESPN's reported ad revenue was up 3% as a result as the increase in cash ad sales was partially offset by lower ratings. The decline in ratings during the quarter was primarily related to NBA comparability issues. During the quarter, ESPN aired fewer NBA regular season games compared to last year when the lockout created a more back-end loaded schedule. Also, ESPN air fewer play-off games and those match-ups delivered lower ratings in last year's playoff games. So far this quarter, ESPN's cash ad sales are pacing up 11%.

At Broadcasting, lower operating income in the quarter was primarily due to three factors. First, higher prime-time programming cost as a result of airing more hours of acquired programming, which was more expensive on a per hour basis. Second, lower program sales compared to last year. If you recall, we sold Grey's Anatomy and Castle in the third quarter last year and had no comparable sales this year. And third, lower advertising revenue as a 7% decrease in station ad revenue offset a modest increase in ad revenue at the ABC Network.

Affiliate revenue at the ABC Network was up nicely in the quarter, but the increase wasn't sufficient to offset these three items. Quarter-to-date scatter pricing at the ABC Network is running mid-teens above upfront levels. ABC and ESPN recently completed their respective upfronts and we feel great about the pricing increases achieved and the amount of inventory each network was able to sell.

We continue to be very pleased with the performance of our parks and resorts business. The segment delivered another quarter of solid growth as our recent investments at Walt Disney World and the Disneyland Resort continue to payoff. Revenue was up 7% and operating income was up 9% in the quarter due to growth at our domestic parks and resorts. As we noted during last year quarter's call, Q3 segment operating income was adversely impacted by an estimated $35 million as a week of the Easter holiday shifted into Q2 this year. Adjusting for this shift, segment operating income growth in Q3 would have been up 15%. Higher operating income at our domestic parks and resorts was primarily due to increased guest spending, occupied room nights, and attendance partially offset by higher costs including ongoing spending for growth initiatives.

During the quarter, attendance at our domestic parks was up 3% with Walt Disney World and the Disneyland Resort each setting new Q3 attendance records. Per capita spending was up 7% on higher ticket prices and food and beverage spending.

Average per room spending at our domestic hotels was comparable to prior year and even though available room nights increased in the quarter occupancy was comparable to prior year. So far this quarter domestic reservations are pacing up 3% compared to prior year levels while book rates are up 4% versus prior year. Total parks and resort segment margins were up 40 basis points in the third quarter compared to prior year. The year-over-year change in Q3 margins was adversely impacted by an estimated 140 basis points due to the timing of the Easter Holiday and spending on growth initiatives.

At the studio we released two films in the third quarter Iron Man 3 and Monsters University both of which performed exceptionally well at the box office. Iron Man 3 generated $1.2 billion in global box office revenue however it faced a difficult comparison with the Avengers which generated $1.5 billion in global box office last year and this is the third highest grossing film of all time.

Monsters University box office performance compared favorably to that of Brave last year, however operating income at the studio declined year-over-year. This decline was due to pre-released marketing expenses for the Lone Ranger and the aforementioned Avengers, Iron Man theatrical comparison. The Avengers also had a strong DVD sales in Q4 last year so the DVD release of Iron Man 3 in Q4 this year faces a difficult comparison which we expect to result in a headwind to the studios Q4 results of about $45 million.

Needless to say we're disappointed with the performance of the Lone Ranger and in light of the film's box office results we expect to incur loss on the film in Q4 of between $160 million and $190 million. Consumer's products growth and operating income resulted from increases in merchandise licensing and retail. The increase in licensing was primarily due to the inclusion of Star Wars in this quarter's results. Also earned licensing revenue was up 3% versus last year and that growth is on a comparable basis which excludes any revenue from the newly acquired Star Wars property. The performance of our retail business was driven by higher comp store sales in North America and Japan and higher online sales in North America.

We continue to return capital to shareholders by repurchasing our stock during the third quarter; we repurchased 12.6 million shares for about $800 million. Fiscal year-to-date we repurchased 57 million shares for $3.2 billion and with that I'll now turn the call over to Bob.

Bob Iger - Chairman and Chief Executive Officer

Thank you Jay and good afternoon. We're pleased with our performance in Q3 and we believe we're well positioned going forward. I would like to address a couple of specifics about our businesses starting with ESPN which was one again a key driver in Q3, Jay commented about ESPN's ratings in the quarter and I would like to add some perspective. In an average week more than 113 million Americans tune in or log on to access ESPN content with the average person spending almost 7 hours a week engaged with ESPN Media on a variety of platforms.

In Q3 nearly 9 out of 10 homes with access to ESPN tuned in to at least one of the ESPN networks. Since 96% of sporting events are watched live, sports are virtually DVR-proof making ESPN incredibly valuable to advertisers as well as cable operators. We have ranked the ESPN the number one network in perceived value for 13 years in a row and the most important network for nine straight years. Even though ESPN is a clear market leader, it continues to refine its sports portfolio, expand original programming, invest in new technology, and innovate to enhance the fan experience.

ESPN's recent acquisition of the exclusive rights for U.S. Open tennis is growing array of digital services including WatchESPN and the new SEC Network next summer are a few recent examples of ESPN's constant innovation that will deliver even greater value to consumers, operators, and advertisers. And with so many of the major sports rights locked up for the next 10 years, given ESPN's brand strength and its continued focus on investment and innovation, we remain confident in ESPN's value and its position as the number one brand in sports over the long-term.

Our acquisition of Marvel also continues to drive real value for us across the company. Following the record setting performance of The Avengers last year, the huge success of Iron Man 3 this summer continue the Marvel momentum, which bodes incredibly well for upcoming Marvel releases including Thor: The Dark World, Captain America: The Winter Soldier, Guardians of the Galaxy, and of course, Avengers 2. We previewed this late at Comic-Con a couple of weeks ago and the phenomenal audience reaction is anything to go by, there is huge appetite for more great Marvel content. There is also a great deal of excitement around ABC's new series and Avengers spin-off called Agents of S.H.I.E.L.D. The first episode got a standing ovation at Comic-Con along with rave reviews. And this month Disney XD premieres its third animated Marvel series.

We continue to be extremely pleased with the creative success of our Animation Studios, Monsters University opened in June to become the latest in Pixar's unbroken string of hits, Planes from Disneytoon Studios opened this Friday, and Frozen, another great movie from Disney Animation will introduce two new Disney princesses when it opens in theatres at Thanksgiving.

We are also looking forward to the launch of Disney Infinity on August 18. We have showcased Infinity to a number of audiences and we are very encouraged by the overwhelmingly positive response we are getting across the board from retailers, reviewers, and consumers alike. And we are also very proud of the several best of awards that Disney Infinity earned at this year's E3. So, given what's ahead for Disney, ABC, ESPN, Pixar, and Marvel as well as the upcoming Star Wars Episode 7, we are incredibly well-positioned for growth and expect solid results in 2014, '15, and beyond.

I am going to turn this call back over to Lowell, so that we can take your questions.

Lowell Singer - Senior Vice President, Investor Relations

Thanks Bob. Leslie, we are ready for the first question.

Question-and-Answer Session

Operator

Thank you. (Operator Instructions) Our first question comes from Doug Mitchelson with Deutsche Bank. Please go ahead.

Doug Mitchelson - Deutsche Bank

Well, thanks so much. Jay, a clarification, I am trying to figure out the math on the fiscal 4Q loss for loan range, what might help is could you give us a sense of the P&A expense that was in June in prior versus what might have been in the fiscal fourth quarter? And then either Jay or Bob, you talked about ESPN at length, Bob, if you got us any competitive impact in the upfront or in the current ad market related to the entry of Fox Sports 1?

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Hi, Doug. Let me start, it's Jay. So, the $160 million to $190 million range that I gave you is the impairment that we will take on the asset of the film and then the operating loss that we will experience in Q4. And you will get a very explicit breakout of those numbers in the Q basically it's like 86 on impairment than the rest. We don't know of course what the actual operating loss will be. The reason that we are recognizing that in the fourth quarter just for all of your ratification is that the accounting rules for film cost impairments were amended by the financial accounting standards board and adopted by us of course right thereafter in Q1 of fiscal year '13. Under the old rules if a film was released at the end of the quarter but prior to the company's filing it's statements then the films performance resulted in impairment the company generally was required to record that impairment in the previous quarter in this case would have been Q3 but under the new rules the impairment analysis is limited to information that was available as of quarter end and therefore doesn't incorporate the actual performance of the film after the balance sheet date so that number is a Q4 number, in the past it would have been the Q3 number.

Bob Iger - Chairman and Chief Executive Officer

The second part of the question Doug ESPN has strong upfront both in terms of the increases on the CPM front (ph) and in terms of overall revenue and did not detect any impact whatsoever from any new competitive forces including Fox Sports 1.

Lowell Singer - Senior Vice President, Investor Relations

Operator next question please.

Operator

Next question is from Jessica Reif-Cohen with Bank of America Merrill Lynch. Please go ahead.

Jessica Reif-Cohen - Bank of America Merrill Lynch

I have two questions one now that you've decided to keep Hulu just wondering if you can give us your vision for how it may change or evolve and the second thing is obviously the press for the last two days have been completely focused on retrans. I was just wondering if you can give us your take on how you know how much longer these kind of battles can go on and before you think the government will start to step in.

Bob Iger - Chairman and Chief Executive Officer

On the Hulu front Jessica we as you know with our co-owner Fox explored a sale for considerable amount of time and went free far down the road in terms of that process and during that time we became more and more convinced that there was real strategic value to Hulu and there was value from a financial perspective meaning we could grow it at a rate that would be overall positive for the shareholders of our company. We also decided when we decided to keep it to infuse Hulu with approximately $750 million of new capital that is aimed at strengthening it's team, strengthening it's technology because we believe we need to continue to invest in the technology platform and of course strengthening it's contents or it's programming which is you know we've seen new entrants and there are other entrants in the marketplace do extremely well with. I won't get specific in terms of the direction because we're going to leave that to the management team of Hulu but we think that there is considerable opportunity here and that opportunity will bode well for both Hulu itself but also for content owners who will have a robust platform to sell the content to and for the creative side who will have another entity to sell programming to, or to create for.

On the retrans front we never like to see battles like this obviously because we think that sometimes they bring attention to the business that isn't necessarily helpful, that said maybe you would expect this from a programmer but we feel strongly about the need for broadcasters to be paid adequately for the value that they deliver both to consumers or customers of multi-channel services and to the distributors themselves. Even though these broadcast stations can be as you know obtain for free, over the year we know that distributors repackage these signals and in fact sell them as part of other services to consumers and thus we think we should get paid. We also believe that the combination of programming both national and network and local particularly news is really compelling as evidenced by the ratings of these stations deliver compared with the ratings of numerous other channels and therefore we think that the station should get paid accordingly.

I don't really have details about this negotiation so I don't really want to weigh in specifically about it but I don't sense that the government is closed to jumping into the fray on this one. I think they probably prefer that we work this out or that owners of stations and distributors work this out themselves but I don't get a sense that there is government intervention that is imminent because of this.

Lowell Singer - Senior Vice President, Investor Relations

Thanks Jessica. Operator next question please.

Operator

Next question is from Alexia Quadrani with JP Morgan. Please go ahead.

Alexia Quadrani - JP Morgan

Alright, thank you. Just staying on the broadcast theme there, could you give us an update on how you view, I guess, the ABC Network going into the fall season? Should we expect also on that topic a lift from the Scandal (indiscernible) in the fiscal fourth quarter? And are you still comfortable with the guide of that I think $400 million to $500 million re-trans revenue by 2015?

Bob Iger - Chairman and Chief Executive Officer

Okay. We do feel comfortable with the guide on the re-trans revenue by 2015 of $400 million to $500 million. We love Scandal and it has been sold to I guess a couple of entities and it also is being sold internationally, but the impact in the fourth quarter is relatively small. As it relates to the ABC Network going into the season we have been saying now for a few quarters that ABC is due to put on its schedule a couple of new strong shows to replace what was the foundation of the schedule over the sort of Desperate Housewives, Lost, Grey's Anatomy years. We are hopeful that their new schedule will deliver what ABC needs, not only in terms of what I will call the downstream revenue through owning the programs, but also from a ratings perspective and ultimately an advertising perspective. We think they have got a couple of really hot comedies and a couple of hot dramas I mentioned one earlier in S.H.I.E.L.D. I mean, we are going to go into the fall feeling relatively bullish about ABC's ability to strengthen its schedule and deliver better bottom line, but until the season unfolds you never can quite tell.

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Alexia, just as a follow-up since you asked about Broadcast, as Bob said, the Scandal number is pretty small, but there is a little bit of headwind in the fourth quarter, because last year, we sold Castle and Wipeout in the fourth quarter to the tune of about $40 million. So, we will not see that, that revenue repeated in the fourth quarter this year. And not that it relates directly to Broadcast, but to the Media Group in general. We are making some investments. You have all heard about Fusion, our joint venture with Univision, as well as the channel we bought in Germany called Das Vierte and that will create headwinds of about $25 million for Q4.

Alexia Quadrani - JP Morgan

Okay Thank you very much.

Bob Iger - Chairman and Chief Executive Officer

Thanks Alexia. Operator, next question please.

Operator

Next question is from Ben Swinburne with Morgan Stanley. Please go ahead.

Ben Swinburne - Morgan Stanley

Thank you. Bob, could you talk a little bit about the parks top line trends in the domestic market, particularly the per caps, which has remained really strong. I know you guys put in some pricing during the quarter and I would love to hear your thoughts and how you thought about that pricing in this economy, and given the investments you have made and sort of the sustainability of kind of monetizing all of the CapEx over the last several years in that segment? And then Jay, can I ask you on ESPN or on cable in general, I looked in the Q it looks like if you adjust for the deferrals the affiliate revenue growth was sort of in the 6% to 7% range, I just want to see if you had a number around ESPN for the quarter that was clean so we could understand the trends there?

Bob Iger - Chairman and Chief Executive Officer

Overall, the business for our parks domestically is quite good, good enough for us to take another price increase, but this one was somewhat different, and that I think for the first time, we created price differential between the Magic Kingdom and the other parks for the obvious reason that the Magic Kingdom is the most popular park, the most iconic. And so we thought there was an opportunity there. And we didn't sense any backlash from the marketplace at all. And as you said, we have had strength not just in terms of attendance growth, but we have had strength in terms of spending, not just ticket prices, but room rates and merchandise and food and beverage. I would say that – we have also had increase in international attendance. Year-to-date, it's up domestically 7% both Orlando and in California. And so we think that bodes well. And we think that we are well positioned in this quarter, particularly coming off the third quarter, Magic Kingdom in Florida had record numbers as Jay mentioned in the third quarter. By the way that was also true for our park in Tokyo and our park in Hong Kong is also doing quite well. If we are seeing softness in our parks unit, it's in Europe, at Paris, which Jay also mentioned.

So, we think we are well positioned. We have got new product in the marketplace. We are not finished with Fantasyland in Orlando. We still have one big attraction to open, which is going to open in 2014. Cars Land and the impact of that on California Adventure has also continued to show great strength, although in California we are lapping the success of the opening a year ago a bit.

I'm not sure that I've anything else I would necessarily want to add, we have a lot of other product coming beyond Fantasy Land ultimately we're going to add Avatar as we have said although we have not announced an opening date yet in Florida, couple of years out at least and we're going to continue to invest in Disney Land, we have got some pretty exciting things that we will be announcing over the next couple of months.

Ben Swinburne - Morgan Stanley

You didn't mention MyMagic Plus, any comment on how that's impacting the business at this point?

Bob Iger - Chairman and Chief Executive Officer

It's really having not an impact from a revenue perspective really at all because we're still rolling it out and what I would call test phase the reason for that is that this is a very significant undertaking from a technological perspective and we really want to make sure that we walk before we run because we don't really want to overload our technological backbone. So we're in what I will call another beta phase that started in August 2nd and it is basically designed for us to have a full roll out, the probable full roll out in the early part of fiscal '14 and that's when you will start to see an impact from a revenue perspective but right now we're mostly heading cost associated with Magic Plus ahead of what will be we believe some interesting revenue generating opportunities.

I can also say that it's working meaning those that are using it and we have got a number of people that have used it have reacted very well. This test that we're in right now should be probably be used by over 80,000 people or 80,000 guests based on the reservations that we have written against with this initiative attached to them.

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

On your question of ESPN affiliate revenue I think you mentioned then 6%, you were a little bit low the cable affiliate revenue for Q3 grew in high single digits ESPN of course is the biggest number and it grew a little bit higher than that but still in the high singles.

Ben Swinburne - Morgan Stanley

Even if I adjust for the deferrals?

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Yes. If you unadjust it it's closer to 10%.

Lowell Singer - Senior Vice President, Investor Relations

Operator next question please.

Operator

Next question is from Anthony DiClemente with Barclays. Please go ahead.

Anthony DiClemente - Barclays

Bob: I would love to get your thoughts on just a general theme of consolidation elsewhere in the media eco-system I guess two big areas where there has been some consolidation or talk of it would be media buying on the agency side and then of course cable distribution and so I was wondering if you thought at that scale in other parts of the ecosystem could impact your business in anyway and then I've a follow-up.

Bob Iger - Chairman and Chief Executive Officer

Well on the advertising agency front that announcement was made only recently and so we don't haven't any sort of really experience in terms of how to judge it, I would say we're studying it that doesn't in any way mean that we're worried about it necessarily but it's still pretty new and we want to understand what it's potential impact could be before we comment about it publically. In terms of consolidation on the distribution front, this is probably the most robust era we have ever seen from a distribution perspective meaning the number of outlets that are available to often sent (ph) to other content owners to distribute their product has grown significantly and pretty dramatically in some cases, obviously Netflix is probably the most recent one and we feel that some consolidation among cable owners if that occurs is going to have no impact whatsoever on our business because there are so many buyers in the marketplace. We also have as you know an array of services that everybody wants fortunately and therefore we think that we have basically the kind of leverage necessary not just to gain access but to achieve the kind of pricing that we need to achieve to grow our businesses.

Anthony DiClemente - Barclays

And just one quick follow-up we are heading the football season here I'm just wondering as ESPN has looked at it's matches up for the upcoming NFL Season and college football, I mean is there anything to lookout for in terms of the ratings outlook number one and then just this question maybe a little out there but given digital distribution and authentication wondering if there is anything that we should we mindful of that maybe the ESPN ad sales force has done be it packaging on digital ad sales or innovative forms of mobile distribution of your robust football package at ESPN? Thanks.

Bob Iger - Chairman and Chief Executive Officer

I have long since learned that judging the football schedule before the season unfolds can be, I guess, a bit premature. I either overreact to it meaning thinking that it's positive or overreact the other way season by season. And I discover year-after-year that until you really see how these teams play what dynamics occur – as you know it a star quarterback gets injured and suddenly a team that you have two or three times becomes substantially less attractive than before. So, I don't want to judge this one except to say that at least on paper going in, we feel that we have got a good solid schedule. Last year, we were somewhat disappointed by our results. That's not just a function of how teams ultimately perform, but sometimes, the quality of the game, I am not suggesting – what I mean by that is how competitive a game is. So, it's just too tough to predict. I like the schedule going in this time around, but I have been there many times before only to find out that I might have been wrong and the opposite is true. We have been pleasantly surprised.

On the other question that you asked, ESPN has been selling multi-platform advertising for quite a long time. I don't know the percentage, but it's extremely high in terms of the number of buyers that ESPN that buy across their various platforms from their digital services to radio, to their magazine, to their channels. And they have grown that nicely. The Watchapp is an opportunity for them to generate more advertising revenue and they are in fact selling ads for the Watchapp, but the numbers even though they are in the probably tens of millions of dollars at this point, they are still relatively small when compared to their total both advertising revenue and their total revenue, but we believe that they will continue to grow. And we obviously believe that I'd say that the penetration of mobile media and not only how fast it has occurred, but how quickly it's being adopted by the consumers, one of the most dramatic changes we have seen in the media business in a very long time. And I think provides us with a great opportunity considering the fact that we have been at the forefront in many respects of making sure that we are putting products on the mobile platforms or making the product that we have available on non-mobile platforms available via mobile.

Anthony DiClemente - Barclays

Thanks Bob. Much appreciate it.

Bob Iger - Chairman and Chief Executive Officer

Thank you, Anthony. Operator, next question please.

Operator

Next question comes from Todd Juenger with Sanford Bernstein. Please go ahead.

Todd Juenger - Sanford Bernstein

So, we haven't talked much about the film or consumer products business yet so let me turn there. On the film side, I think it's fair to say that the summer box office was not great, at least domestically probably a pretty crowded schedule and some audience fatigue. How should we think about that going forward for you guys, especially given your reliance on Marvel and Lucasfilm and the risk that you are a little bit highly leveraged against sort of the Sci-Fi superhero genre, I know your risk of longer term fatigue of that? Then the related question is how should we think about the opportunity in the consumer products side, especially from Lucasfilm and I guess still a little bit from Marvel as you really try and capitalize on those properties? How long does that take to get through the system and into the retail shelf? And should we think about that is incremental or is some of that displacing other shelf space and just changing the mix a little bit? Thanks.

Bob Iger - Chairman and Chief Executive Officer

Okay. Let's first characterize summer box office, these last number of summers have been very competitive and quite crowded. I don't know that this summer got any more crowded or more competitive than before although certainly there was a lot of attention paid to it. We actually think we had an excellent summer and that we ended up with Iron Man 3, which did over $1.2 billion in global box office, which is substantially above what Iron Man 2 and Iron Man 1 did and the highest Marvel box office film of all time next to Avengers. We actually think Avengers helped Iron Man 3 and we believe that the impact of Avengers will be felt on future Marvel products, particularly Thor, which is coming up first and then Captain America, and of course, Avengers 2. There has been a lot said I know about the risk of basically high-cost tent-pole films, and we certainly can attest to that given what happened with Lone Ranger, and Jay went into the details.

We still believe that a tent-pole strategy is a good strategy that one way to rise above the din and the competition is with a big film, not just a big budget but big story, big cast, big marketing behind it. We think that the Disney, Pixar, Marvel and ultimately the Star Wars Lucas Brand will actually contribute to our ability to rise above that then and compete quite effectively but we also know and I know I'm probably saying the obvious but you still have to make really strong films. So I don't know that the dynamic has changed that much expect that if there are tempo films being made I guess technically there is more risk in the marketplace. But we have known all about that risk for quite some time. As we look forward as I mentioned we feel very confident in them obviously. I mentioned three of them Guardians of the Galaxy as another one which we're very excited about and that the Marvel character library is only being mined from the tip of the iceberg perspective we will be mindful of not going to the well too often because it's hard to make great films and so our charge to Marvel is bring films to market where you really believe in the stories and the story tellers.

Disney Live Action, we're going to continue to make probably in the neighborhood of five to at the very, very most 10 but most cases it's less than that, Live Disney, Live Action Films. Some will be tempo films like we have Maleficent coming up as for instance Tomorrowland is another one, some will be much lower budget films like Saving Mr. Banks which is coming up at the end of this calendar year and of course we believe in Lucas and Star Wars which is '15 and then our animation strategy is clearly working. We did almost 260 million in box for Monsters 2 and we're hopeful that it's going to exceed $400 million in box office outside the United States which will make it I think the fourth highest grossing Pixar film of all time with Toy Story and Nemo and one other ahead of it that's a pretty good story. We like what's happening with Disney Animation. We have had a couple of real hits in Tangled and in Wreck It Ralph and we believe in Frozen coming up and we've got a really fine movie coming up this weekend in Plains (ph) which is made by Disney 2 studios but it bears the Disney brand was that one point going to be a direct a video and we looked at it and we saw the quality we decided that bring it up theatrically was a wise move.

So I know that's a long way of my saying that we think that Marvels, Disney, Pixar, Lucas Branded film strategy is a good one for us not only because of what we believe it can deliver from a box office perspective but the obvious value it delivers to this company across so many platforms from games, Infinite is a good example to our consumer products and you've to consider publishing as part of that because the digital side of publishing and of course what it means for us and our products we're evidence of all of these branded franchise films is clear both domestically and internationally across all of our products businesses.

On the consumer products front we believe that there is upside or incremental earnings from the mining of the consumer products that will come from not only the marble franchises but also from Lucas even though there have been a lot of Star Wars, a lot of Star Wars product out in the marketplace. We think that when we put these companies together combining the teams and taking all these great product to market that there is a substantial potential not only to increase sales but to increase royalties for these products and so we view the consumer product side of these acquisitions as truly additive.

Lowell Singer - Senior Vice President, Investor Relations

Operator next question please.

Operator

Next question is from David Bank with RBC Capital Markets. Please go ahead.

David Bank - RBC Capital Markets

So I guess a question with respect to CapEx and capital allocation I think while there are always ample opportunities to invest in the business it seems like the perception is that CapEx is sort of peaked and probably headed downward trajectory wise, yet your leverage is still amongst the lowest in the industry and what are your thoughts in terms of increasing capital returns overtime? Is there something in particular you're keeping that powder (ph) dry for, what are your thoughts around that?

Bob Iger - Chairman and Chief Executive Officer

Thanks, David. I am probably not going to reveal anything to you that you haven't heard me say before, but let me reiterate how we think about this. I think that you, first of all, you are correct in that. Our belief is that a lot of the capital investment we have been engaged in, particularly in parks and resorts over the past three or four years plus the deployment of capital in acquisitions will yield returns such that we will have the great problem of dealing with increasing cash flow as the years go by. We look very hard for internal and organic ways to invest our capital above our rate of return. We think that's why our investors give us their money to invest. And I think we have demonstrated a pretty good track record at finding projects in our businesses that allow us on an incremental basis to create returns that are very, very attractive to shareholders. That being said, we are not departing from kind of the formula we have used in returning capital to shareholders, where we have consistently returned 20% or so of the cash generated by the company to shareholders in terms of buybacks.

If you look at this year's buyback plan, you see that it's so far this year pretty consistent with that at $3.2 billion. Remember, we committed buy in the Lucas shares over two years. And if you look at last year's CapEx – I am sorry buyback versus this year's you will see that it is nicely up. And to sort of comment on keeping your powder dry, we are not cash hoarders. We have an excellent balance sheet that we worked very hard at keeping as a strategic asset for the company to allow us access to the capital markets. You see our interest expense is way down this year. That's due to the fact that we have been able to both refinance high-cost debt like we had at Disneyland Paris as well as borrow money at record levels in terms of the issues we have made. So, we feel very good about our balance sheet, access to cash, we don't feel the need to afford cash. So, if we do not find ample internal opportunities in terms of investment or interesting acquisitions, then we will in fact increase our returns to shareholders.

David Bank - RBC Capital Markets

Thank you.

Bob Iger - Chairman and Chief Executive Officer

You are welcome. Operator next question please.

Operator

Next question is from Marci Ryvicker with Wells Fargo. Please go ahead.

Marci Ryvicker - Wells Fargo

Thanks. I have two questions. I think the first, there seems to be a little bit of variability in affiliate fee growth from quarter-to-quarter. And Jay, I think you made it a point to call this out during an Investor Conference some point in late May. So, is there any way to think about affiliate fee growth in fiscal Q4 or even beyond and just other than new contracts coming on what are the various puts and takes for affiliate fee growth? So, that's the first question. And then second just in the broadcast sector, is there any color on how you are pacing right now at the broadcast networks and stations?

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

Okay. On the first half, I appreciate your, I will call it frustration. I didn't hear frustration in your voice, but the difficulty in quarter-to-quarter forecasting of affiliate fees and it has to do with the way we build for instance, let me give you an example. In Q2, our affiliate revenue benefited from an extra day in the billing cycle in 2012 so-called leap year and that effects the growth in that quarter more than you might imagine. Relative to giving you some insight into Q4, we are looking at high single-digit growth in terms of affiliate revenue. And I am sorry I can't help you with all the adjustments that come in and out every quarter in terms of how that affiliate number grows. The range is pretty tight, I will tell you that, but within a couple of percentage points, it's very hard for you guys to predict that accurately.

In terms of pacing's, I'll say this the stations are pacing down in Q4 in part due to comp issues that we have last year, we have the benefit of the Emmy's which is 3 to 4 percentage points of growth in ad revenues this year. The Emmy's will be on CBS. We won't have that. So, that will obviously affect and there is some more challenging political comp this year versus last year and that again is a couple of percentage points which is effecting the ad pay in that stations.

Lowell Singer - Senior Vice President, Investor Relations

Thank you Marcy. Operator next question please.

Operator

Next question is from David Miller with B. Riley & Company. Please go ahead.

David Miller - B. Riley & Company

Couple of questions, Jay on the prognostication of losses for Lone Ranger the 160 to 190 I'm just curious why give a range now, why do you not, I mean why give a range at all is it just because the film is just sort of swimming around various theatrical markets overseas and you're just kind of waiting to see what the final number is or are you just kind of weigh into additional analysis, why give a range why not just kind of pinpoint a little bit more exactly what the loss is going to be and then Bob correct me if I'm wrong but I believe your NBA contract comes up for renewal with ESPN in 2016 with the emergence of Fox Sports 1 and just given Rupert sort of ready, fire, aim kind of mentality with regard to sports rights in general. If Fox Sports 1 wants to overbid or bid against you for the NBA and you come to the termination that you cannot make the NBA work in terms of your ROIC targets. Are you prepared to walk away from the NBA in the same way that you guys walked away from the NHL? Thanks very much.

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

I will be brief on the reason for the range. We're only opening 40% of international markets with Lone Ranger and it goes all the way out to I think Japan opened in September if I'm not mistaken. So, I think that's the last market, so that's the reason for the ranger.

David Miller - B. Riley & Company

Got it.

Bob Iger - Chairman and Chief Executive Officer

The NBA David is very important to ESPN both from a quality of programming perspective but also from a volume perspective and it's certainly a priority of ESPN to extend their relationship with the league. I think the league would believe that it would beneficial for them as well to stay on ESPN which is a very, very important platform for them. I don't want to sound in anyway as though we're complacent but I think it would be safe to assume that we're reasonably confident that we will be able to extend that relationship and I do not want to at any way give any prediction or whatever is what we might do if the price gets to a point that it's substantially above what we expected.

Lowell Singer - Senior Vice President, Investor Relations

Thanks David. Operator we've time for one more question.

Operator

Okay. The last question comes from Barton Crockett with Lazard Capital Markets. Please go ahead.

Barton Crockett - Lazard Capital Markets

Now on the topic on the expansion of distribution and then opportunity right now for Disney that you brought up early on the call. There has been a lot of press reporting about you know new over the top services that could emerge you know companies like Intel, others that have reported. I was wondering without kind of commenting specifically about a company if you could talk generally about this type of service in terms of your belief in the probability that we can see something materially over the next few quarters and the possibility of getting some type of material minimum guarantee that could be noticeable in your P&L.

Jay Rasulo - Senior Executive Vice President and Chief Financial Officer

I don't know that you will see much impact in the next few quarters although I think it may be some new distributors out there that are looking to make content deals in the near term, you mentioned Intel being potentially one of them. I still believe that overall these new platforms whether they are over the top or not offer us more and new opportunities to monetize their content and our approach to them will probably be somewhat consistent with how we have approached other distributors both incumbents and new distributors. We look with an open mind towards a distributors that we believe the ability to create a viable platform in terms of their ability to us for our content but also a viable platform for the consumer one with a good interface and one that's likely to ultimately stick in terms of distribution. So I don't think that you're going to see substantial change in the environment meaning distribution environment in the near term because of these but I think it's safe to say that over certainly the next five years there is going to be more than one new entrants in the marketplace.

Bob Iger - Chairman and Chief Executive Officer

Thank you Barton 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 website. Let me also remind everyone that certain statements on this call may constitute forward-looking statements under the securities laws. We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them and we do not undertake any obligation to update these statements. Forward-looking statements are subject to a number of risks and uncertainties and actual results may differ materially from the results expressed or implied in light of a variety of factors, including those contained in our Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. This concludes today's call. Have a good afternoon, everyone.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.