



*Source: The Walt Disney Company*



COMPANY STATISTICS

Market Cap ($ Bn): $228.7

Enterprise Value ($ Bn): $278.9

52-Week Range: $79.1 - $153.4

Dividend Yield: 1.4%

Free Cash Flow Yield (2019): 4.6%

P/E (Current): 19.1x

P/Book (Current): 2.66x

Return on Equity (2019): 20.6%

I rate The Walt Disney Company (DIS) as a **Buy** with a Target Price of $167. My recommendation is driven by the following key points:

* **Unique business model** – DIS has four interconnected business segments through which the company can effectively utilize its brand and internally developed intellectual properties (IP) to generate great synergy. For example, a character or storyline created in Disney’s studio entertainment can be showcased on one of Disney’s media networks, and the character’s toys and merchandises can be sold in Disney stores.
* **Wide competitive moat** – DIShas developed extremely strong competitive advantages through years of continuous investments in both tangible assets (parks, resorts) and intangible assets (IPs, brand name). It is the most family entertainment associated brand, like Apple iPhone with smartphone, Amazon with online shopping, Coca-Cola with soda drinks.
* **The streaming services offer huge growth potential** – As of 30 June 2020, DIS’s streaming services, Disney plus, accumulated 57.5m subscribers. While the streaming business requires large upfront capital expenditures on IP development, movie production and infrastructure, its growth and profitability potential are promising. With the majority of the expenses fixed in nature in the cost structure, this business enjoys high incremental margins as the subscriber base grows.

# INVESTMENT THESIS

The Walt Disney Co. (DIS) is a diversified international family entertainment and media enterprise. It operates through the following segments: Media Networks, Parks, Experiences and Products, Studio Entertainment and Direct-to-Consumer and International (DTCI). The Media Networks segment includes cable and broadcast television networks, domestic television stations, radio networks and stations. The Parks, Experiences and Products segment owns and operates the Walt Disney parks and resorts around the globe. The Studio Entertainment segment produces and acquires live-action and animated motion pictures, direct-to-video content, musical recordings and live stage plays. The DTCI segment licenses the company's trade names, characters and visual and literary properties to various manufacturers, game developers, publishers and retailers throughout the world. The company employs over 223,000 workers and earned global revenue of $69.6 billion in 2019.

**Sales by Geography:** Europe 33%, Asia Pacific 32%, North America 21%, Latin America 13%.

**Market Position**: DIS is a most well-known brand in each of the segments it operates. For example, it is the largest amusement park operator in the world that owns 43.8% market share, with NBCUniversal (21.5%) and other smaller players like Cedar Fair (5.7%) and Six Flags (5.05%) as its major competitors. In terms of the streaming services, Netflix had 193m subscribers around the world at the end of June 2020; Disney Plus had 57.5m subscribers and is growing user base rapidly.

**Shareholders:** Institutional investors hold the majority of Disney's shares at about 63-65% of total shares outstanding. The top 3 institutional shareholders are Vanguard, BlackRock, and State Street.

# Company Overview

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Young Investors Society

**The Walt Disney Company**

Entertainment & Media

Symbol: DIS

**Recommendation: BUY**

Headquarters: Burbank, CA USA

Current Price: $126.59

**Target Price: $167**

High School Name

**LEGEND**

**0** High threat

**1** Significant threat

**2** Moderate threat

**3** Low threat

**4** Insignificant threat

**5** No threat

#1

#19

#11

#13

#10000

#7

#6

**Moat Analysis: *Wide-Moat***

**Source of Competitive Protections:**

* **Brand.** Disney is one of the most iconic brands ever built. The brand is multi-generational, aspirational yet affordable, a symbol of fantastic and unparalleled experience throughout the world.
* **Unique business model**. DIS has been spending billions of dollars of capital in the amusement park segment and the streaming service segment over years. The two segments generate significant synergy. It is quite difficult for competitors to copy.
* **Economies of Scale**. Being a dominant market leader allows DIS to benefit from economies of scale including lower supply costs and customer acquisition costs, and the ability to “fill the channel” with new IP inventions.

**Porter’s Five Forces:**

**Bargaining Power of Customers** – **Low (3 out of 5):** There are major competitors in both amusement park and streaming service segment. While Disney offers high quality services and great experience, some customers may be price sensitivity and opt for low-cost alternatives.

**Intensity of Competitive Rivalry** – **Low (3 out of 5):** While large competitors like NBCUniversal and Netflix continue to impose competitive pressure, Disney’s interconnected businesses help the company deal with the competition and bring in strong revenue streams.

**Bargaining Power of Suppliers** – **Insignificant (4 out of 5):** Technology suppliers, distributors and suppliers of raw materials are considered to have little power given DIS’s leading market position.

**Threat of Substitutes** – **Low (3 out of 5):** There are a variety of substitutes, but DIS offers high quality services and great experience. Customers are loyal and switching costs are high.

**Threat of New Entrants** – **No (5 out of 5):** Setting up a strong position in media and entertainment industry requires a substantial amount of capital input, along with the needed technology, infrastructure and human capital, making it challenging for new players to enter and overcome the competitive pressure from existing large players.

# Competitive Positioning

* **Amusement Park Market** – The global amusement park grew at a compound annual growth rate (CAGR) of around 7% from 2014 to 2019. It is forecasted to decline by 2.7% from $73.5 billion in 2019 to $71.6 billion in 2020 due to the COVID-19 outbreak. The market is then expected to recover and grow at a CAGR of 9% from 2021 and reach $89.5 billion in 2023.

North America was the largest region in the global amusement parks market, accounting for 33% of the market in 2019. Asia-Pacific was the second largest region accounting for 29% of the global amusement parks market. Africa was the smallest region in the global amusement parks market.

Disney is the largest amusement park in the US with a 43.8% market share, followed by NBCUniversal (21.5%), Cedar Fair (5.7%), SeaWorld (5.6%) and Six Flags (5.0%). The amusement park market in the US is rather concentrated with the top 5 players accounting for more than 80% market share.

* **Streaming Market** – The global video streaming market size was valued at USD 42.60 billion in 2019 and is projected to grow at a CAGR of 20.4% from 2020 to 2027. Innovations, such as blockchain technology and Artificial Intelligence (AI), to improve video quality are expected to boost market growth. Recently the popularity of such platforms over broadcast media, such as YouTube and Netflix, have increased considerably.
* While subscriptions to streaming services are not exclusive, meaning one can subscribe to more than one platform, the competition in this market is fierce. As of Jun 2020, Netflix has the greatest number of subscribers of 193mm, followed by Prime Video (150mm). Disney Plus ranked the third with 57.5mm subscribers and has been one of the fastest growing streaming platforms in recent years.

# Industry Analysis



Above are financial statements extracts and key forecasts for Disney.

**Profitability:** Overall, the company has decent and stable margins – operating margins and ROE are over 20%. However, profitability is believed to be significantly impacted due to the Covid-19 pandemic in the coming 2 years. Recovery may occur in 2022, with EPS forecasted to growth 133% in 2022.

**Growth:** The company has delivered a revenue CAGR of ~7% for the last decade. Despite the negative impact from Covid-19, the company is projected to continue high-single digit growth fueled by new IP developments, mergers and acquisitions, ticket price increase and increasing number of subscribers to Disney Plus.

Below are the main drivers behind Disney’s revenue growth:

* **New IP developments** – Disney has the ability to continuously launch new IPs, which will help the company bring in new revenue streams from all of its four business segments.
* **Mergers and Acquisitions** – The Disney-Fox deal occurred in March 2019 is a good example of how the company can grow through strategic mergers and acquisitions. Disney, which already owned the Pixar, Marvel, and the Star Wars brands, also got Deadpool and the Fox-owned Marvel characters such as the X-Men and Fantastic Four.
* **Pricing Power** – Because of Disney’s strong brand and customer loyalty, the company has consistently been able to raise ticket price (~6% CAGR since 2001) above inflation. This pricing power will continue driving revenues and boosting earnings for the park business. The park business accounted for more than 36% of the company’s total revenue in 2019.
* **Disney Plus** – The streaming has recently gained huge popularity. Disney plus is certainly one of the most exciting developments of the company in recent years. Launched in late 2019, Disney Plus acquired 26.5mm subscribers in the first quarter of operation, accumulated 57.5mm subscribers as of Jun 2020, and is projected to have 133.7mm by 2023, representing a CAGR of nearly 30%.

# Financial Analysis

*Source: Seeking Alpha*

# Revenue Drivers

# Valuation



The following are the main investment risks for Disney:

* **Mass lockdown measures pressure theme parks and studio results.** Parks & Experiences/Studio Entertainment represent 26%/14% of segment operating income. Both segments are currently facing massive pressure given temporary closures related to the ongoing coronavirus pandemic. At this stage, there is very limited visibility into when theme parks/movie theater activities will resume to pre-Covid-19 levels.
* **Cyclical advertising revenue exposure.** Roughly 15% of Disney’s revenues are derived from advertising, and the near- to medium-term uncertainty in the ad market related to the COVID-19 pandemic creates significant uncertainty into the magnitude and timing of potential headwinds.
* **Programming expenses tend to grow.** Media companies must invest in their programming, including new shows, syndicated content and live events like sports rights. Under-investment can lead to weakening of cable net brands and/or lower ratings. But investment is no guarantee of monetization as not all content is a hit. Program write-downs are not uncommon in Media. Further, increased competition for high-quality, scripted programming from traditional and tech companies may create upward pricing pressure for talent and content.

# Investment Risks

My 2022 target price is **$167** per share for Disney, which represents ***32% upside*** from the current share price. I arrive at my target price through the following assumptions:

* I use a target multiple of 15x ’22E EBITDA for Media Networks and Studio Entertainment businesses, which represent a slight premium to peers average to reflect Disney’s strong brand name and customer loyalty. A target multiple of 10x ‘22E EBITDA is given to Parks, Experiences, and Consumer Products business.
* DTCI segment is still in premature stage with negative EBITDA, but I have a very positive outlook on its future growth potential and profitability as the no. of subscribers has kept increasing rapidly. DCF method is used to value DTCI business with a long-term perspective, deriving a valuation of $132 bn. Detailed DCF calculation is presented at the end of the report.

**Valuation analysis**: Disney’s stock is currently trading at 39x EV/EBITDA, compared to the 10-year high and low at 41.5x and 6.7x. The current EV/EBITDA is close to the historical all-time high because of the abnormally low EBITDA figure in recent two quarters due to the Covid-19 crisis. In terms of P/B ratio, the company’s current P/B ratio of 2.6x is slightly lower than the 10-year average.

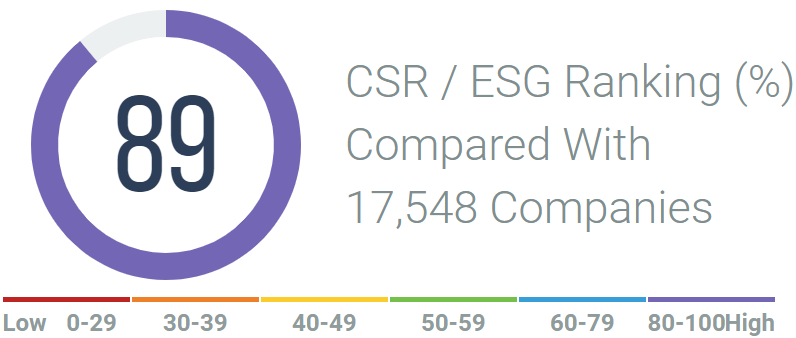


*Source: Capital IQ*

*Source: Disney CSR Report*



*Source: CSRHub*



# ESG Considerations

Bob Chapek has been CEO since February 2020, having served as Chairman of Disney Parks, Experiences and Products since 2018 and Chairman of Walt Disney Parks and Resorts since 2015. As Chairman, he led the largest investment and expansion in the history of Parks, including opening Shanghai Disney Resort, almost doubling the Disney Cruise Line fleet, and adding a suite of new Marvel and Star Wars attractions following Disney’s purchase of Marvel and Lucasfilm.

* **Major Shareholders** – Institutional investors hold the majority of Disney's shares at about 63-65% of total shares outstanding. The top 3 institutional shareholders are Vanguard, BlackRock, and State Street. The top 3 individual shareholders are Robert A. lger, Executive Chairman of Disney, who owns ~0.06% of the company’s total shares outstanding; Christine M. McCarthy, EVP and CFO, who owns ~0.01%; and Alan N. Braverman, EVP and Secretary, who owns ~0.01%.
* **Independence** – The board of directors consists of 10 members, 8 of which are independent (non-company executives). There are no red flags in the company with related party transactions, shady accounting or poor allocation of capital.

# Management & Governance

Generally speaking, Disney as well as its peers are high performers in terms of ESG ratings. Disney ranks in the 89% percentile in a pool of more than 17,000 companies around the world being followed by CSRHub, which is a database website dedicated to tracking and rating companies ESG performance. It is also noted that Disney maintains a higher ESG rating than industry peers most of the time.

**Environment**

* **Sustainable Design:** Disney are aiming for LEED Platinum, a globally recognized sustainable design certification, as well as employee wellness certifications, in the development of its new New York City campus, which will include more than 1 million square feet of office and production space.
* **Energy Efficiencies:** The company continues to drive emissions reductions with a portfolio of projects such as heating and air conditioning upgrades, lighting efficiencies, and operational enhancements across the company. It targets to reduce greenhouse gas emission by 50% from 2012 levels by 2020.

**Society**

* **Charitable Giving:** In fiscal year 2019, Disney made $338.2 million in charitable contributions in the form of cash and in-kind donations
* **Disney VoluntEARS:** In 2019, Disney cast members and employees contributed 612,300 hours of service through the Disney VoluntEARS program to support local communities.

**Corporate Governance**

* **Corporate Governance Guidelines and Standards of Business Conduct** are in place to oversee the behaviors of all the employees including the management team and board directors. Regular trainings are provided to promote the standards.
* **Environmental Governance Council**,comprised of executives from across thebusinesses and key corporate functions, holds accountable for overseeing the integration of environmental considerations into the company’s business operations and strategy.
* **Diversity and Inclusion** – the composition of the board of directors reflects the diversity of the company’s shareholders, employees, customers and guests, and the communities in which it operates. Among the current Board, the independent Lead Director and all four of the Board committee chairs are women.

*Source: Morningstar.com*



# Appendix: DCF Model for DTCI Business