Analyst: Gurcharan Singh

INVESTMENT MANAGEMENT CERTIFICATE PROGRAM January 4, 2017

Consumer Discretionary - Media Conglomerate

The Walt Disney Company

Recommendation	**BUY**
Target (today's value)	$118
Current Price	$104.22
52 week range	$82.65 - $106.75

Share Data	
Ticker:	DIS
Market Cap. (Billion):	$165.86
Inside Ownership	8.2%
Inst. Ownership	59.0%
Beta	0.98
Dividend Yield	1.50%
Payout Ratio	24.8%
Cons. Long-Term Growth Rate	9.4%

	'14	'15	'16	'17E	'18E
Sales (billions)					
Year	$48.81	$52.47	$55.63	$57.10	$62.18
Gr %	8.4%	7.5%	6.0%	2.6%	8.9%
Cons	-	-	-	$57.67	$61.04
EPS					
Year	$4.31	$4.95	$5.76	$5.46	$6.74
Gr %	25.9%	14.8%	16.5%	-5.4%	23.4%
Cons	-	-	-	$5.95	$6.67

Ratio	'14	'15	'16	'17E	'18E
ROE (%)	18.7%	21.4%	21.4%	21.5%	22.0%
Industry	28.1%	36.8%	36.8%	31.1%	45.5%
NPM (%)	16.1%	17.0%	17.0%	16.9%	16.3%
Industry	15.2%	12.7%	12.7%	13.4%	13.7%
A. T/O	0.60	0.61	0.61	0.61	0.64
ROA (%)	9.70%	10.4%	10.4%	10.2%	10.4%
Industry	7.9%	6.6%	6.6%	6.9%	7.3%
D/A	19.7%	21.9%	21.9%		

Valuation	'15	'16	'17E	'18E
P/E	21.4	16.7	18.2	17.5
Industry	22.6	17.2	19.8	16.8
P/S	3.45	2.72	2.98	2.8
P/B	3.5	3.6	3.9	3.8
P/CF	16.5	11.9	14.2	13.7
EV/EBIT	15.1	12.1	12.6	12.6

Performance	Stock	Industry
1 Month	5.1%	-1.7%
3 Month	12.2%	9.4%
YTD	-0.8%	25.4%
52-week	-2.0%	15.1%
3-year	36.7%	19.3%

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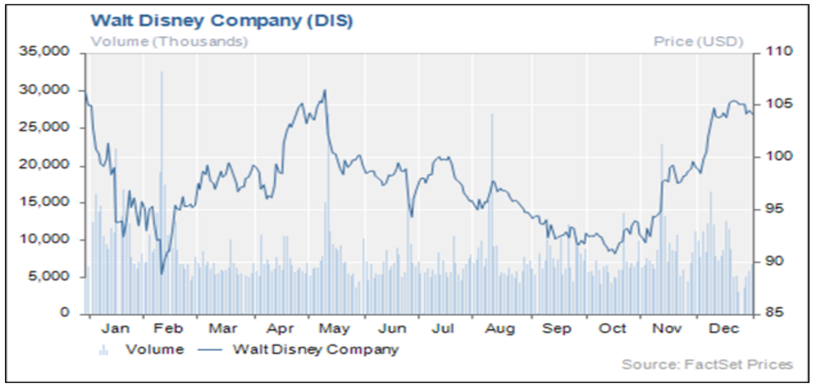


Summary: I recommend a buy rating with a target of $118. DIS has an opportunity to improve on popularity of studio entertainment and grow in the Shanghai market. Furthermore, I believe Disney is a long term buy because of its unique brands; however, a decrease in margins and declining revenues from the media network are significant headwinds. The stock is undervalued based on DCF analysis.

Key Drivers:

- Studio entertainment & content creation: Studio entertainment and content creation is the engine for Disney's revenue. DIS's ability to create unique characters/brands, and integrate it over numerous business segments by connecting to consumers, helps them stay popular. Studio entertainment is most vital because it essentially is another form of advertisement, and it also creates a visual for consumers to digest.

- Media network fees & revenue: Over 40% of DIS's revenue comes from the media network segment, and about 17% of revenue comes from the ESPN network. Affiliated fees are increasing to help offset declining margins, but premium prices could impact long-term future earnings potential if Disney's channels are dropped from TV packages or it raises costs to the user so they find substitutes.

- Expansion of parks & resorts: DIS's greatest growth potential is in Asia. Disney has an opportunity to tap into this new market and offer unique products to a demographic that is interested in the entertainment offered by Disney.

- Macroeconomic trends: DIS's success depends heavily on a strong economy because entertainment is cyclical.

Valuation: Using a relative valuation approach, Disney appears to be overvalued in comparison to the industry; although, DCF analysis yields a $118 target. A combination of the approaches suggests that Disney is undervalued, as the stock's value is about $118 and the shares trade at $104.22.

Risks: Threats to the business include foreign currency fluctuation, competition, maintenance of intellectual property, and consumer preferences.

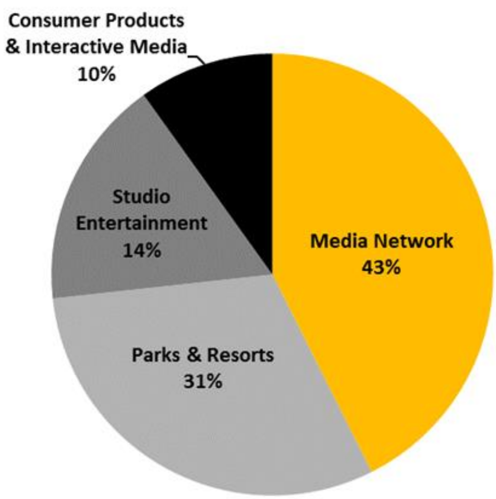
Company Overview

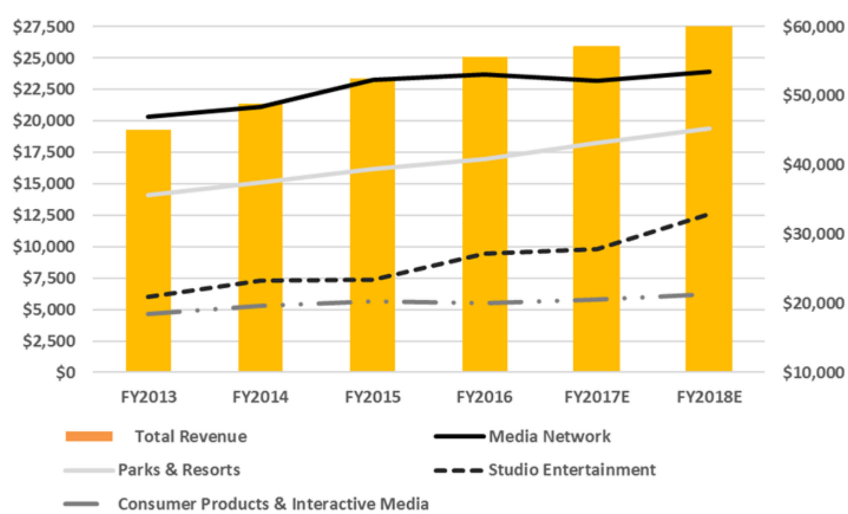
The Walt Disney Company (DIS) along with its subsidiaries is a diversified worldwide media and entertainment conglomerate. The company's mission is to be the world's foremost provider and producer of information and entertainment. Disney also seeks "to develop the most creative, innovative and profitable entertainment experiences and related products in the world." Some of the company's most iconic assets include Lucasfilm, Marvel, ESPN, Pixar, and Disneyland. Disney was founded by brothers Walt and Roy Disney in 1923 and is headquartered in Burbank, California. The company employs approximately 185,000 people, and is one of the most powerful brands in the world.

DIS generates revenue in many geographic regions across the world, which include North & South America, Europe, Asia, Latin America, and others. Although the company is international, 77% of its revenue comes from its operation in the U.S. and Canada. Disney's revenue is derived from the following four business segments:

- Media Networks: revenues are earned from affiliated fees, ad sales, and program sales. Revenue growth was 2% in 2016.
- Parks and Resorts: revenues are earned through sales of food, beverage, merchandise, vacation and cruise packages, rentals and sales of vacation club properties, charges for hotel rooms, and sales from theme park admission. Revenue growth was 5% in 2016.
- Studio Entertainment: revenues earned from the distribution of films in home entertainment, television and theatrical markets, ticket sales from stage plays, licensing from live entertainment events, and the distribution of music. Revenue growth was 28% in 2016.
- Consumer Products & Interactive Media: consumer products portion of revenues are earned from character licensing to third parties for consumer merchandise, tuition from learning centers, publishing of reading material (comic books, magazines, and children's books), selling of Disney merchandise; interactive media portion of revenues are earned through sponsorships and internet advertising, third party licensing to game publishers for devices (smartphones, tablet computers), selling games to distributors and retailers, fees collected through transactions in games, and subscriptions. Revenue declined 3% in 2016. Both segments merged in June 2015 - financial results of merged segments will be reported in fiscal year 2016.

Figures 1 and 2: Revenue sources for DIS, year-end 2016 (left) and revenue history since 2013 in millions (right)





Source: Company reports, 10k

Business/Industry Drivers

Though several factors may contribute to Disney's future success, the following are the most important business drivers:

1) Studio entertainment & content creation
2) Media network fees & revenue
3) Expansion of parks & resorts
4) Macroeconomic trends

Studio Entertainment & Content Creation

In anticipation of the new Lucasfilm movie release, DIS announced plans to construct a new Star Wars-themed park at Disneyland.

Although studio entertainment accounts for only 14% of Disney's revenue (2016), it is a major driver for its current and future growth. The company's popularity, interest, and product demand within its numerous segments are affected by the creation of high quality content with regards to film and television. Essentially, universally acclaimed films will result in more licensing agreements and product variation, further sequels, publishing, television production, and franchise spinoffs. Successful content creation influences the whole brand - it fuels the company. It creates new products and experiences for growth. In addition to being a key driver, the studio entertainment's revenue has been growing over time. The studio segment grew 2.64% from FY12-FY13, a modest 1.21% from FY14-FY15, and an impressive 21.73% from FY13-FY14 due to the positive performance of three Marvel movies and the critically acclaimed Frozen movie. FY15-FY16 grew a high 28% due to the success of proven franchises like Star Wars Episode VII, and unforeseen new franchises like Zootopia. The film business continues to be reliant on sequels and the latest blockbuster releases. Disney will continue to release popular films in FY17 and FY18 (Rogue One: A Star Wars Story, Guardians of the Galaxy Vol. 2, Pirates of the Caribbean: Dead Men Tell No Tales, etc.), so it is poised to outperform its previous year.

Figure 3: Star Wars Episode VII – The Force Awakens (released December of 2015)

Source: Radio Times

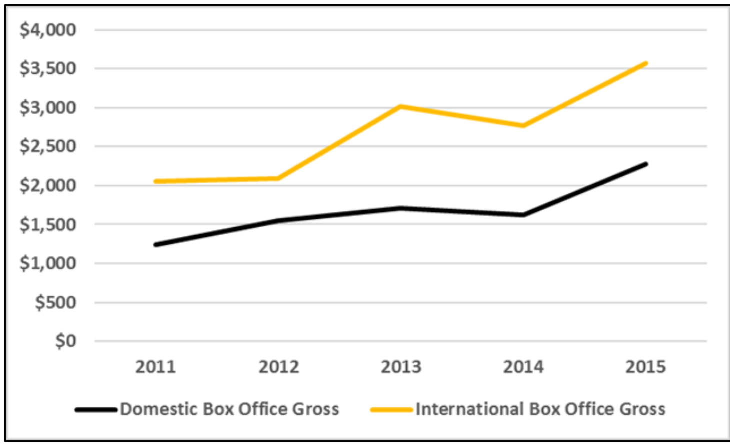
DIS purchased Lucasfilm for $4.06 billion in December of 2012.

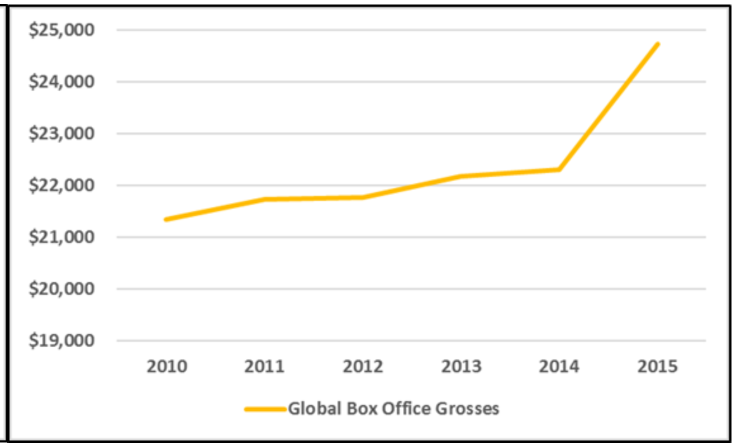
Lucasfilm is a significant asset. Star Wars (rights owned by Lucasfilm) is quite possibly the most popular film franchise in history. Figure 3 displays the recent Star Wars released film that broke numerous box office records. With the first installment already grossing above $2 billion (third film in history to do so), the ROA of the acquisition looks like a bargain. This figure does not take into consideration Star Wars themed merchandise, revenue from other segments, and future releases. History may suggest that acquisitions of this nature drive earnings and growth. Disney's invested in Pixar ($7.4 billion) and Marvel Studios ($4 billion), and Marvel's films alone grossed over $10 billion. To put this into perspective, if Marvel made the $10 billion over 5 years then the purchase price was a P/S multiple of 2. This compares to 2.7 for DIS stock (2016), so the price was a good deal for the firm. Disney's success at creating content with iconic intellectual property suggests that Lucasfilm is a good asset (two more sequels, multiple spinoffs, etc.).

RottenTomatoes is a popular television and film review "aggregator" website. As a gauge, The Godfather, (often regarded as one of the greatest movies ever made), has a score of 99%.

Figure 4 shows Disney's steady increase in box office gross with the exception of a slight dip from 2013 – 2014. Domestic box office growth for Disney rose 41% in 2015 and international box office growth went up almost 29%. In 2016, growth has continued with Walt Disney Studios posting its biggest year ever with $5,851 billion through November 1st 2016. It surpassed Disney's record of $5,844 billion set in 2015. It is important to note that five of Disney's major film brands released in FY16 have an average score of 94% on RottenTomatoes. Figure 5 shows the global box office sales of the top six studios. Sales had been steadily increasing from 2010 – 2014. However, in 2014-2015, growth jumped to 11%. Figure 7 shows the correlation of the major studios. Universal and Disney had a solid 2015. Figure 6 shows that the majority of market share is held by Universal and Disney at 52%; however, figure 7 also shows the very volatile nature of the industry. Past growth does not reflect future earnings for movie studios.

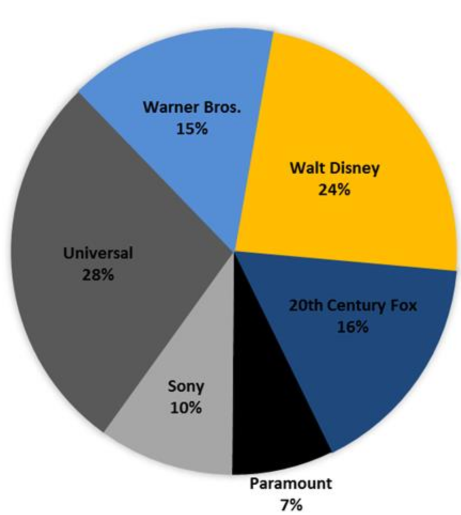
Figures 4 and 5: DIS box office gross in millions (left) and global box office gross of top six studios in millions (right)

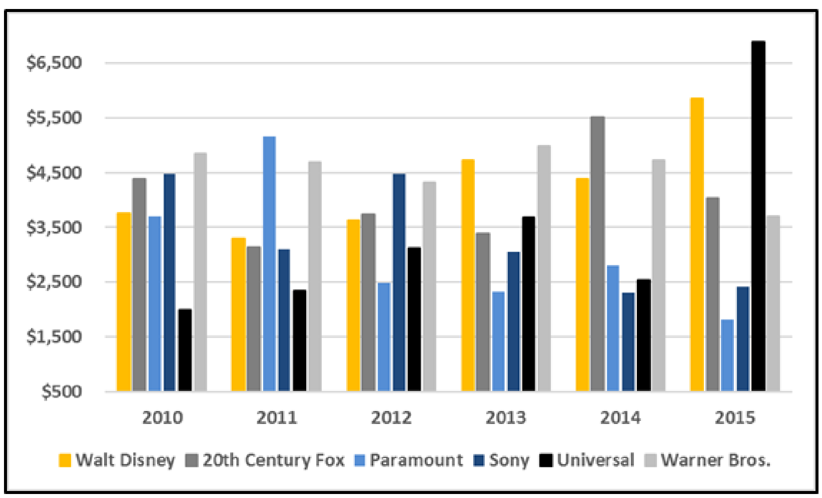




Source: Bloomberg

Figures 6 and 7: Market share of the top six highest grossing studios for 2015 (left) and history of global box office gross of the top six highest grossing studios in millions (right)





Source: Bloomberg

Media Network Fees & Revenue

Disney owns 80% of ESPN, 100% of Disney Channels, 100% of ABC Family, and 50% of the A&E Television Network.

The media network segment of DIS continues to be its greatest revenue-producing segment. Disney's media network segment derives most of its revenue from affiliate fees (carriage fees per month per subscriber from distributors like Dish Network) and advertising. Affiliated fees made up 52% of the media network segment while advertising made up 36% in FY16. There was a 2% increase from affiliated fees and a 2% increase from advertising in FY16. Essentially, the better content it produces and delivers, the more it can earn from advertising and affiliated fees.

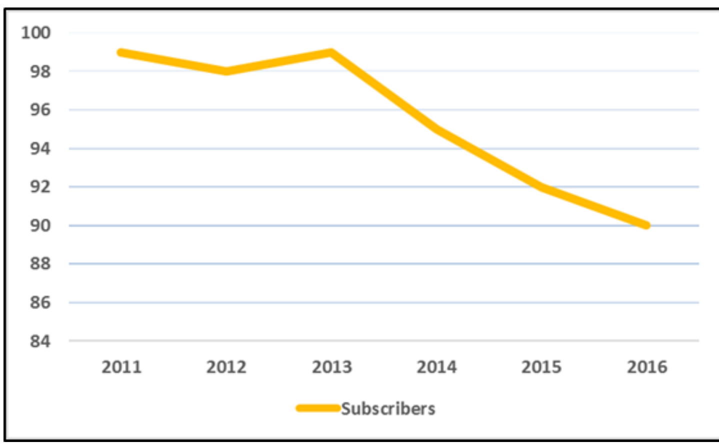
Disney's media network business competes for viewership primarily with other cable and television networks, independent television stations, and other media outlets. Moving forward, a concern is the consistent subscriber loss with ESPN and possible concerns with adverse shifts in television pay landscape.

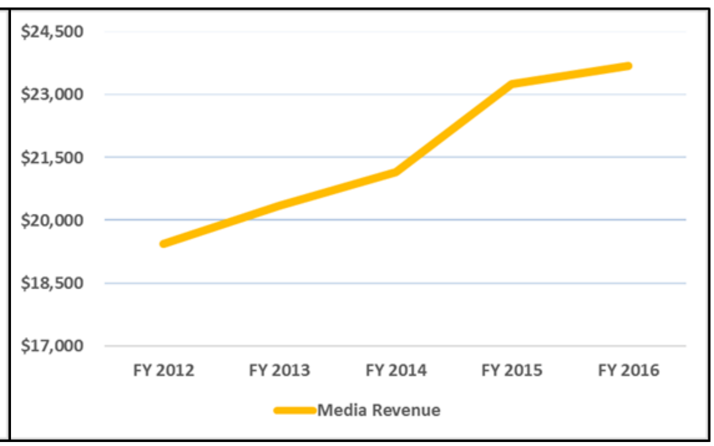
Networks sell time for commercials and the rates received are reliant on the size and characteristics of the audience that the network can provide to the advertiser, in addition to advertiser demand.

Figure 8 shows a consistent drop in ESPN subscribers. There was a 1% decrease in both 2011 and 2012, decrease of 4% in 2014, decrease of 3% in 2015, and a decrease of 2% in 2016. This could be due to increases in cable fees and competition. This is concerning because the ESPN network is a major revenue generator for DIS - $10.8 billon (2014) through advertising and affiliated fees. That is about 20% of Disney's total revenue. In 2015, ESPN generated $9.2 billion in revenue which is about 17% of total revenue, and a decrease of 15% in ESPN revenue from 2014. The ESPN network is one of the most expensive networks in terms of subscriber fees (paid by cable companies) at more than $7.21 a person (2016). To put that into context, the next closest network is TNT at $1.82 a person (2016). One of the reasons why the ESPN network is expensive is because of sports commitments. The network has sports programming commitments that total over $53 billion between 2016-2020. Disney has been trying to offset cable losses by making its content available across various digital platforms (Netflix, Amazon, wireless mobile devices, video games).

Even though there is cause for concern, 2016 was helped by political advertising, the Olympics, and a 7% increase from higher contractual rates. In figure 9, the decrease in ESPN subscribers did not cause media sales to decline. Revenue rose 10% in FY15 and 2% in FY16.

Figures 8 and 9: ESPN subscribers in millions (left) and Disney media revenue history from 2012 to 2016 in millions (right)





Source: Company reports, 10k

Expansion of Parks & Resorts

The parks and resorts segment accounts for 31% of Disney's revenue. The location of the theme parks, resorts, hotels, and cruises are scattered throughout the world, in places like: California, Florida, Shanghai, Tokyo, Paris, etc. The company is highly dependent on this segment as a driver for revenue, ergo it must be continuously updated and remain popular to attract more consumers. A key characteristic that separates DIS from its competitors is the company's brand-building strategy and ability to provide consumers multiple ways of experiencing its unique homegrown/acquired creations. This sustainable competitive advantage boosts notoriety and popularity for the company. The parks and resorts segment does this by offering exceptional experiences through theme park attractions, cruise, hotels, etc.

Disney's most notable future growth for this segment involves expansion of theme parks. Some of the most noteworthy new and expanding attractions involve: Toy Story Land, Disney's Pandora—The World of Avatar and Star Wars Land. It is important to note that Disney's Pandora is based off the highly successful Avatar movie which has the highest box office number of all time ($2.78 billion). This attraction should garner a very large audience since four sequels are planned, which will help create buzz for the park.

Shanghai Disney Resort's grand opening was June of 2016. DIS owns a 43% interest of the theme park, while Shanghai Shendi Group (state-owned enterprise) owns 57%.

Revenue for the parks and resorts segment increased by 6% for FY16. Growth may be attributed to the opening of Shanghai Disney Resort, and increase in theme park attendance. The success of the Shanghai park can create an "ecosystem" of demand for TV programs, books, toys, movies, clothes, etc. Bob Iger, the CEO of Disney, has called Shanghai "the greatest opportunity the company has had since Walt Disney himself bought land in Central Florida" for Walt Disney World in the 1960s. Tapping into this market moving forward could boost revenue for this segment in 2017 and 2018.

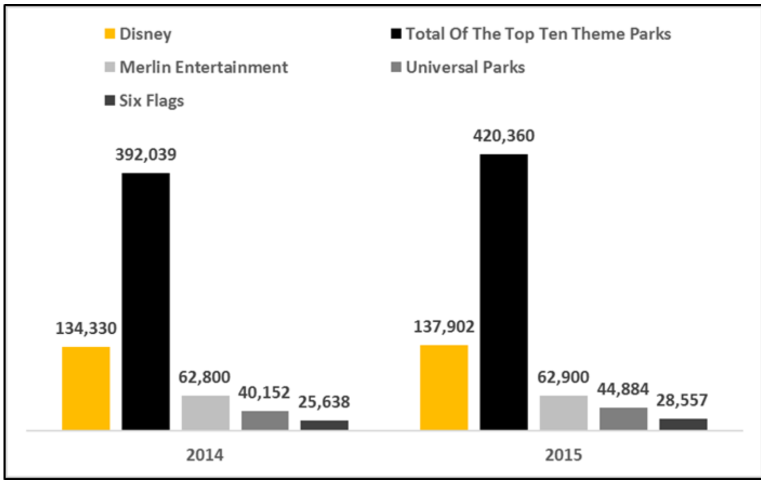
Figure 10 shows the theme park attendance comparison between Disney and its direct competitors. Disney is by far the market leader with attendance at nearly 34% for 2015 compared to the top ten theme parks combined. Taking Disney out the equation results in an even more impressive 49% of the market share compared to the top nine theme parks combined. The next closest rival (Merlin Entertainment) is 15%, followed by Universal Parks and Resorts with 11%. Disney continues to increase its attendance with a 3% gain in 2015, and higher attendance equates to higher revenue potential. I believe this will continue to surge because of the potential in the Asia market.

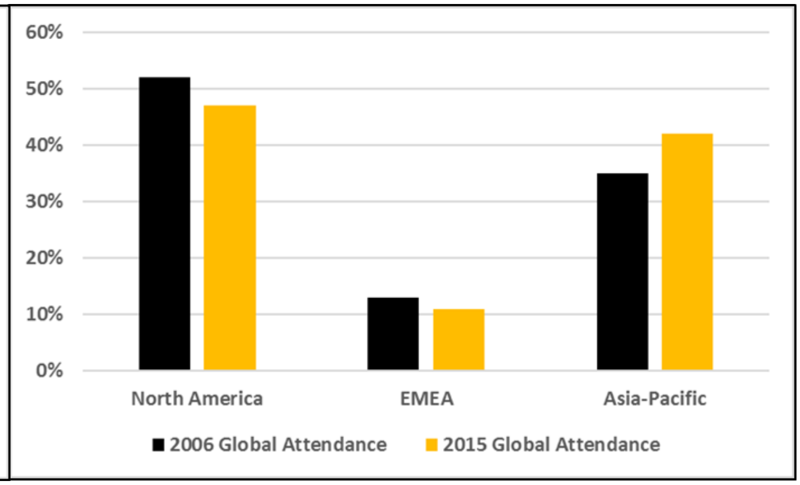
Figure 11 shows the percentage of attendance by geographical region in 2006 and 2015. The distribution of global attendance has shifted towards the east of the globe, with the Asia-Pacific region obtaining 42% (2015) of the major attractions in the world – up 7% from 2006. Meanwhile, attendance is down in North America by 5% and 2% in the EMEA region.

Disneyland Park in Paris opened in April 12, 1992. Cultural miscues and poor execution has turned it into a theme park with struggling profit.

For FY17 and FY18, the growth and dominance has a strong chance to continue because of the company's constant expansion of attractions. Moving forward, one key headwind to consider is the capital expenditure involved in this segment. Disney has relatively high exposure to the "capital-intensive theme park business" because resources are being tied up to a potential project for a long period. A future disaster like Disneyland Paris could occur if proper research and execution is overlooked.

Figures 10 and 11: Theme park attendance for DIS and competitors in thousands (left) and shares of global attendance by region (right)





Source: Bloomberg

<u>Macroeconomic Trends</u>

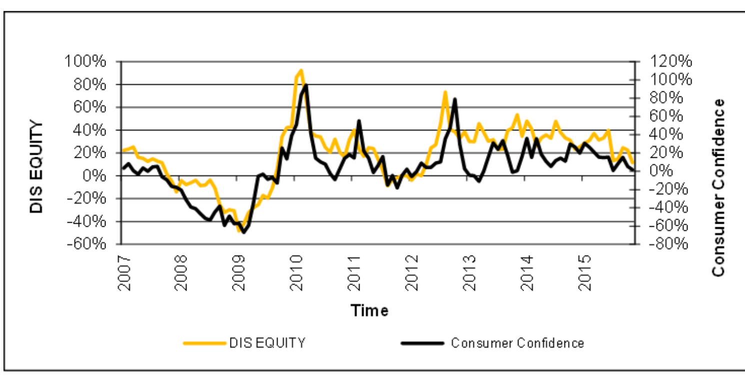
In December 2016, consumer confidence increased to 113.7 – highest level since 2001

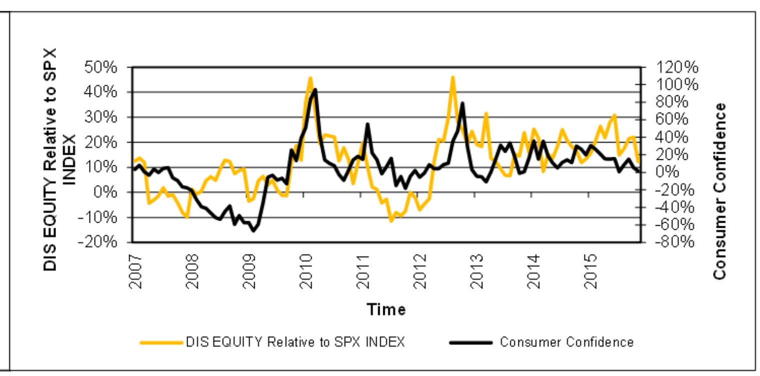
The economy is a significant driver for DIS and the media industry. Disney's products are discretionary in nature, so it is subject to economic cycles. An improving economy boosts consumer confidence and discretionary spending.

Figure 12 shows how DIS performs with consumer confidence on an absolute basis. Disney seems to closely resemble the economic variable from 2009 up until mid – 2012. The yearly correlation is 0.809 (high) and R-square is 0.655. Figure 13 compares consumer confidence and DIS relative to the S&P 500. The yearly correlation is 0.514 which is lower than figure 8, and its R-square is 0.264. This implies that DIS is more cyclical than the average of the S&P 500.

Figures 14 and 15 compare consumer confidence with Disney's closest competitors. The index includes: Time Warner Inc (TWX), CBS Corporation class b (CBS), Viacom class b (VIAB), 21st Century Fox (FOXA), and Comcast Corporation (CMCSA). Figure 10 shows a yearly correlation of 0.724 and a R-square of 0.55. Figure 11 shows a yearly correlation of 0.554 and a R-square of 0.307.

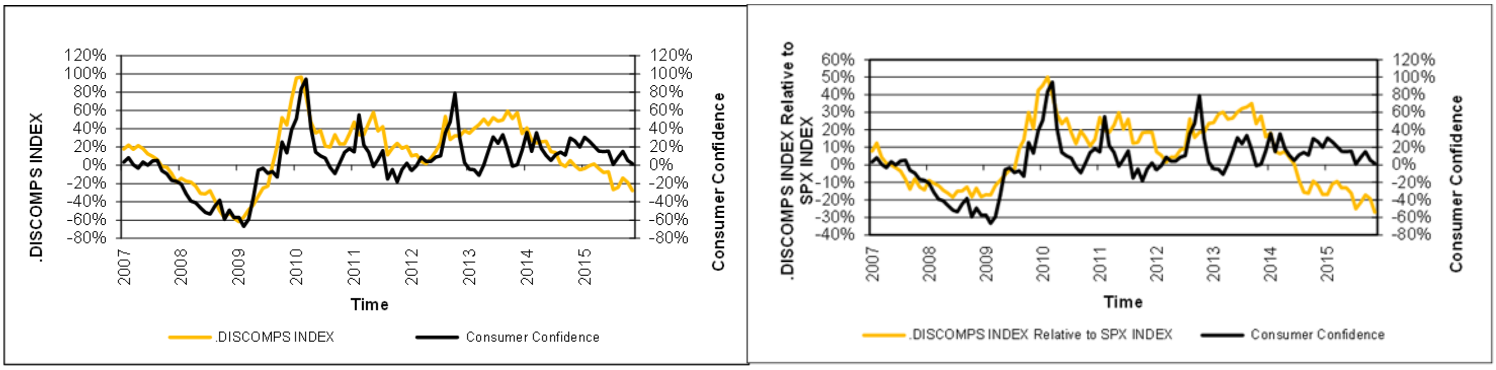
Figures 12 and 13: Consumer confidence compared to DIS (left) and consumer confidence compared to DIS relative to S&P 500 Index (right)





Source: Bloomberg

Figures 14 and 15: Consumer confidence compared to DIS comps (left) and consumer confidence compared to DIS comps relative to the S&P 500 index (right)



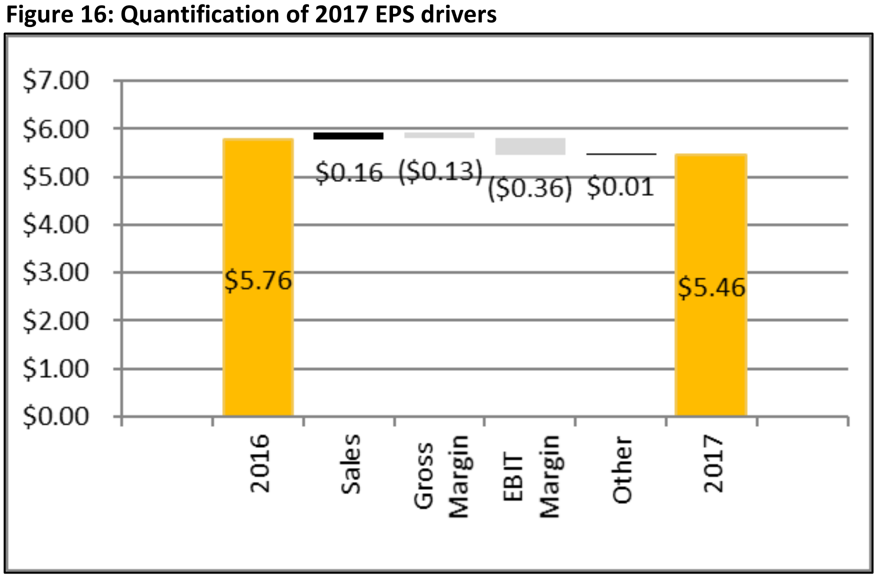
Source: Bloomberg

Financial Analysis

EPS for DIS was $4.31 in 2014 and $4.95 in 2015 – an increase of 15%

I anticipate EPS to decrease to $5.46 in FY 2017. Sales growth is still positive (add $0.16 to EPS) despite lower growth in media revenue, a slowdown of growth in studio entertainment, and a slight increase in international revenue from China. However, the modest increase in sales would be offset by a $0.13 per share decrease in gross margin as direct costs will not slow as much as sales. I further anticipate substantial contraction in EBIT margin by $0.36 due to an increase of about 14% in SG&A. Share buybacks add $0.07 but this is somewhat offset by higher interest and other expenses (-$0.06).

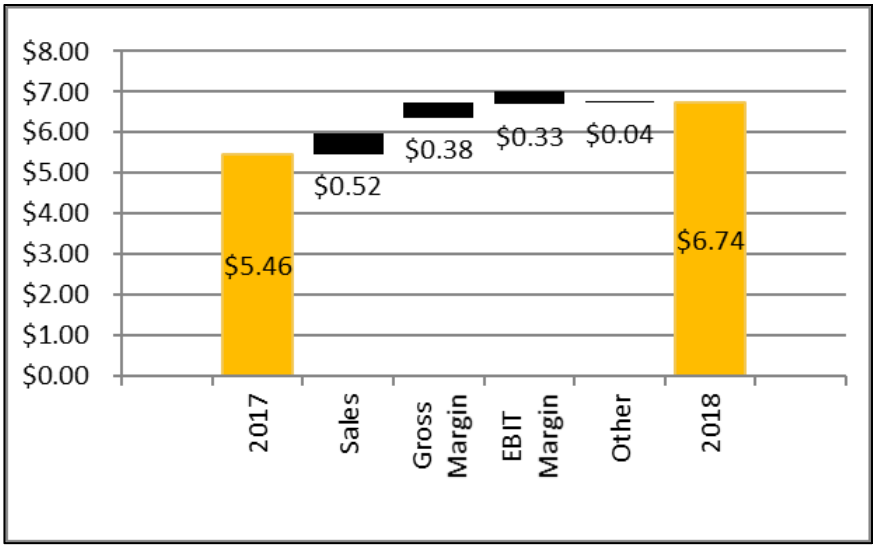
Figure 16: Quantification of 2017 EPS drivers



Source: Company Reports, IMCP

I forecast 2018 EPS to increase $1.28 to $6.74 (22%). Disney will gain $0.52 in EPS from a 9% increase in sales due to growth in the Asia Pacific market, media revenue gaining traction with more direct-to-consumer selections, an increased number of entertainment/products for consumers to stream or experience, and substantial growth of 28.5% for the studio entertainment segment. Gross margin is expected to rise and add $0.38 due to a decrease in sport commitment costs and upcharge for premium pricing for unique content released in 2018. Besides the impact of gross margin on EBIT, I anticipate EBIT margin to rise further ($0.33) because of relatively unchanged SG&A. “Other” is adding $0.04 due to share buybacks.

Figure 17: Quantification of 2018 EPS drivers



Source: Company Reports, IMCP

Estimates versus Consensus

My expectations for 2017 are slightly more conservative compared to consensus. My revenue estimate versus consensus has a difference of 1%. My pessimism is mainly due to the decrease in revenue from media networks. This impacts my EPS estimate as well, resulting in a 9% difference from consensus. However, my projections are much more bullish for 2018. Compared with consensus, I estimate a difference of 2% due to improving margins for the ESPN network, and a stronger slate of movies releases in 2018. The EPS difference is about 1%.

Figure 18: EPS, Revenue and growth estimates vs. Consensus

	Estimates		Consensus	
	2017E	2018E	2017E	2018E
Revenue	$57,097	$62,185	$57,671	$61,043
Growth	2.6%	8.9%	3.7%	5.8%
EPS	$5.46	$6.74	$5.95	$6.67
Growth	5.5%	23.4%	3.3%	12.1%

Source: Factset, IMCP

Revenues

Disney's revenue has increased steadily since dipping by 4.5% in 2009. While I expect that trend to continue, I believe revenue will grow at a slower rate in 2017 due to competition in the media space, and diminished interest with expensive subscription based networks like ESPN. Consumer preference has changed drastically with content being available for access on a multitude of devices, instead of a stationary television that requires an expensive cable subscription. As a result, advertising and affiliate revenue will suffer. For my model, I estimated a decline of 2%. Headwinds will ease, therefore I estimate a 3% increase in 2018. Disney's management team is seeking to expand opportunities for growth, as demonstrated by its strategic acquisition of BAMTech (sports streaming service).

Studio entertainment may suffer slightly in 2017 due to the record breaking previous year, so my estimation of 4% growth seems reasonable since the movie schedule for 2017 compared to 2016 is arguably weaker. The industry is volatile as each fiscal year is highly dependent on blockbuster movie releases that correlate with consumer preference. For 2018, my growth assumption is 28.5% due to a strong pipeline of movies that are established brands.

For 2017 and 2018, I anticipate continued growth in the parks and resorts segment of 7.5% and 6.5% because of an increase in revenue from Disney's theme park in Shanghai. Having the full year's contribution for 2017 and 2018 will benefit the segment, with new popular attractions also being introduced to consumers.

Consumer and interactive products will grow 5% in 2017 and 7% in 2018. Due to the overall growth in Disney's other segments, I expect a trickle-down affect because more attendance with parks and resorts, and more box office revenue from studio performance, should boost sales for this segment.

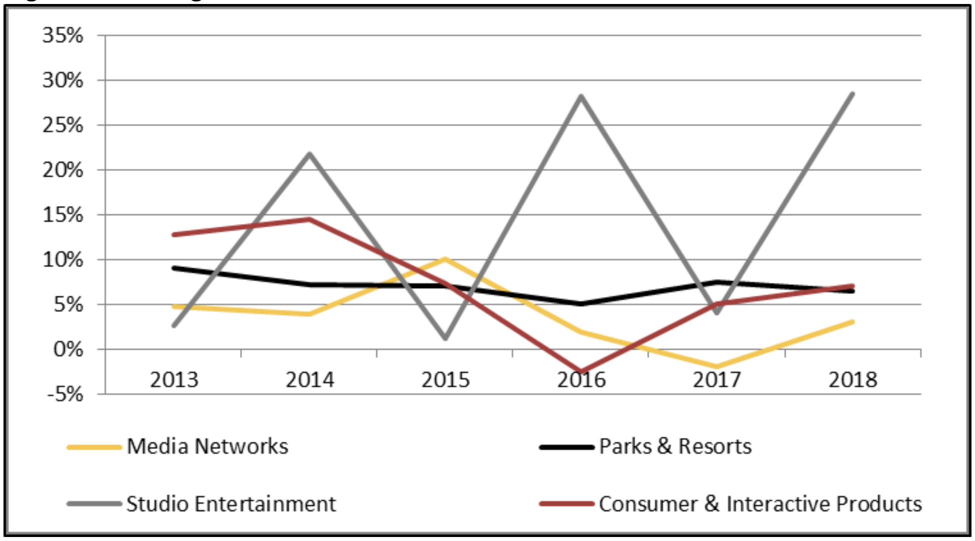
Figure 19: Disney's FY 2017E – FY 2018E revenue segment estimates

	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017E	FY 2018E
Revenue/Sales	$ 42,278	$ 45,041	$ 48,813	$ 52,465	$ 55,632	$ 57,097	$ 62,185
Growth		*6.5%*	*8.4%*	*7.5%*	*6.0%*	*2.6%*	*8.9%*
Media Networks	$ 19,436	$ 20,356	$ 21,152	$ 23,264	$ 23,689	$ 23,227	$ 23,924
Growth		*4.7%*	*3.9%*	*10.0%*	*1.8%*	*-2.0%*	*3.0%*
Parks & Resorts	$ 12,920	$ 14,087	$ 15,099	$ 16,162	$ 16,974	$ 18,247	$ 19,433
Growth		*9.0%*	*7.2%*	*7.0%*	*5.0%*	*7.5%*	*6.5%*
Studio Entertainment	$ 5,825	$ 5,979	$ 7,278	$ 7,366	$ 9,441	$ 9,819	$ 12,617
Growth		*2.6%*	*21.7%*	*1.2%*	*28.2%*	*4.0%*	*28.5%*
Consumer & Interactive Products	$ 4,097	$ 4,619	$ 5,284	$ 5,673	$ 5,528	$ 5,804	$ 6,211
Growth		*12.7%*	*14.4%*	*7.4%*	*-2.6%*	*5.0%*	*7.0%*

Source: Company Reports, IMCP

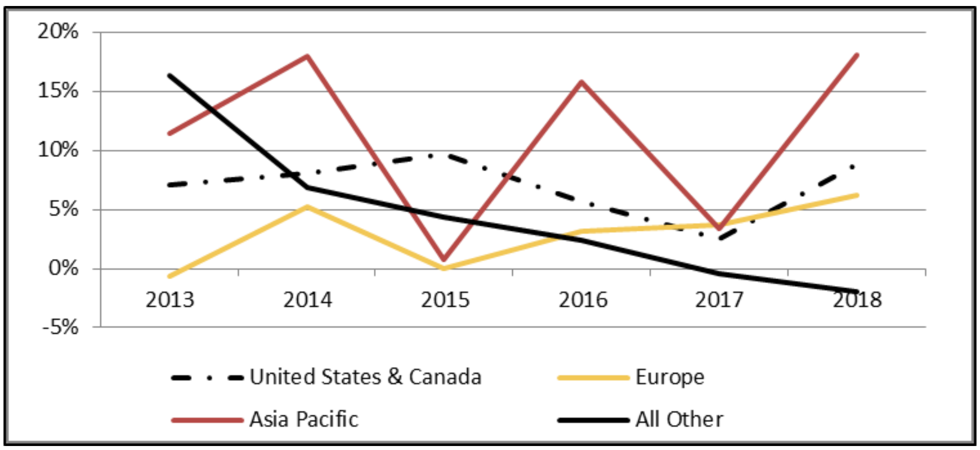
Overall, I anticipate combined international revenue to rise 6.8% in 2017. In 2018, I assume a shift in international revenue to the Asia Pacific region (18% growth) because of consumers in Shanghai being introduced to Disney products and attractions. For domestic revenue (including Canada), I expect an increase of 2.5% for 2017 and 8.8% for 2018. A declining unemployment rate to full employment levels and higher consumer confidence may result in higher discretionary entertainment spending.

Figure 20: DIS Segment Revenue Growth Rates 2013 – 2018



Source: Company Reports, IMCP

Figure 21: DIS Domestic and International Revenue Growth Rates 2013 – 2018



Source: Company Reports, IMCP

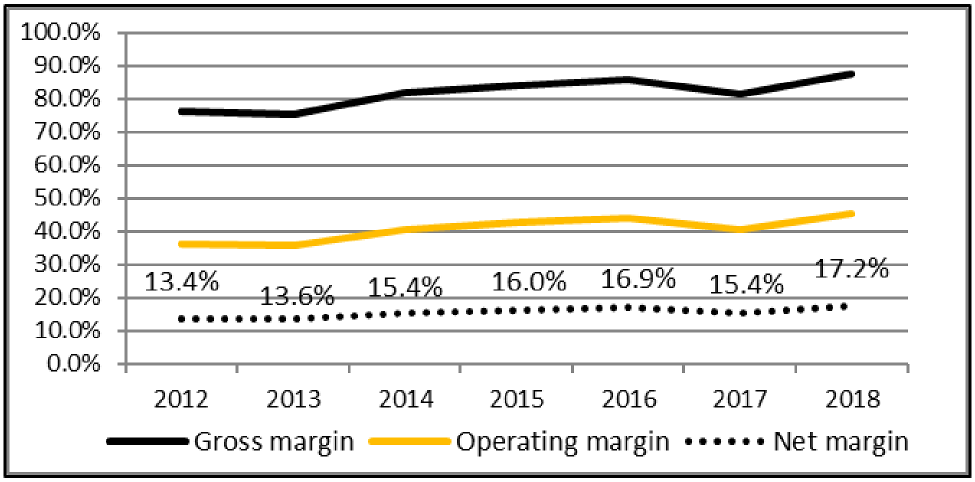
<u>Operating Expenses and Margins</u>

Operating expenses for DIS are primarily of selling, general and administrative, and direct expenses which Include costs such as film amortization, distribution, media programming/production, labor costs etc.

I anticipate margins of 40.5% in FY17, which is a distinct contraction versus FY16's 41.5%. I believe this will be due to sports programming commitment costs. Rights to acquire sports coverage from organizations such as NFL and MLB will jump from $5,030 billion to $5,778 billion – about a 15% increase. Although ESPN is the most expensive network per subscriber, the Disney Channel which features content for children and tweens is the third highest network at $1.49. Moving forward, DIS must control margins for the Disney Channel because increased competition might drive subscriber count down.

For FY18, I project margins recovering to 42.5% because of direct-to-consumer live streaming lowering costs, and reduction of sports commitments. Cost is estimated to be $5,608 which is a decrease of 3%. In figure 22, net margin decreases 9% from 2016 to 2017, and increases 12% from 2017 to 2018.

Figure 22: DIS Percentage of Operating Margin, Gross Margin and Net Margin 2012 to 2018



Source: Company Reports, IMCP

Return on Equity

ROE rose to 19.6% in 2016 which was due to an increase in margins, asset turnover and leverage. This is just continuing the trend since 2013. Better profitability and asset turnover, and higher leverage will cause ROE to rise 1.4% from 2016 to 2018.

Figure 23: ROE breakdown, 2013 – 2018E

5 - Stage DuPont	2013	2014	2015	2016	2017E	2018E
EBIT / sales	21.9%	25.0%	26.7%	27.2%	25.1%	27.9%
Sales / avg assets	0.58	0.59	0.61	0.62	0.61	0.64
EBT / EBIT	97.6%	100.0%	99.2%	98.3%	98.0%	98.3%
Net income /EBT	63.8%	61.3%	60.4%	63.2%	62.5%	62.9%
ROA	7.9%	9.1%	9.7%	10.4%	9.5%	11.0%
Avg assets / avg equity	1.73	1.72	1.78	1.88	1.93	1.91
ROE	13.6%	15.6%	17.3%	19.6%	18.2%	21.0%

Source: Company Reports, IMCP

Free Cash Flow

DIS's free cash flow has been volatile over the last several years. I anticipate both FCFF and FCFE to increase over 22% in 2017. In 2018, they both decline over 40% because of my expectation of DIS investing heavily in capital expenditures in its parks and resorts division - expanding this segment is vital for continued growth and success. NOPAT increases each year, with a slight decrease in 2017 because of the assumption that ESPN operating margins will decrease and affect profit. For 2018, NOPAT increases due to higher growth in studio and parks and resorts segment. As you can see, the firm has nearly $5 billion in FCFE even after the rise in investments in 2018. This FCFE is quite sufficient to fund the firm's share buybacks ($3.5 billion in 2017 and $3 billion in 2018).

Figure 24: Free cash flows 2013 – 2018E

Free Cash Flow	2013	2014	2015	2016	2017E	2018E
NOPAT	$6,798	$7,989	$8,927	$9,961	$9,437	$11,424
Growth	6%	18%	12%	12%	-5%	21%
NWC*	-1526	-1537	-3845	-4486	-4604	-5014
Net fixed assets	67132	69010	71424	75067	76130	82913
Total net operating capital*	$65,606	$67,473	$67,579	$70,581	$71,525	$77,898
Growth	12%	3%	0%	4%	1%	9%
- Change in NWC*	965	-11	-2308	-641	-118	-410
- Change in NFA	5943	1878	2414	3643	1063	6783
FCFF*	-$110	$6,122	$8,821	$6,959	$8,492	$5,051
Growth		-5671%	44%	-21%	22%	-41%
- After-tax interest expense	162	-15	75	171	190	197
FCFE**	-$272	$6,137	$8,746	$6,788	$8,302	$4,853
Growth		-2356%	43%	-22%	22%	-42%

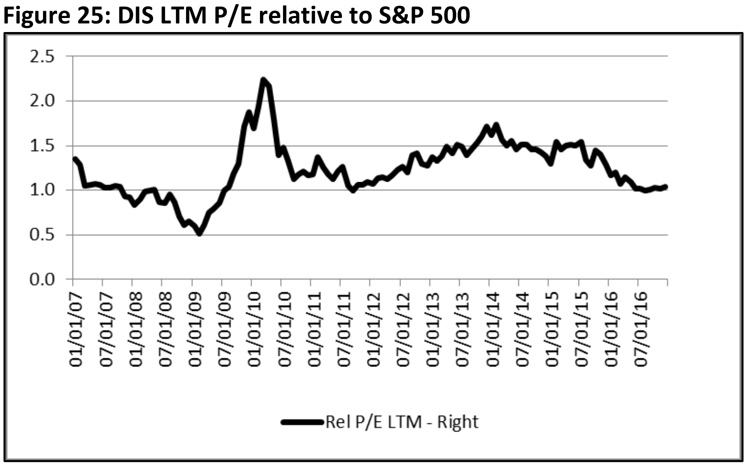
Source: Company Reports, IMCP

Valuation

DIS was valued using multiples and a 3-stage discounting cash flow model. Based on earnings multiples, the stock is fairly priced relative to other firms and is worth $91. Relative valuation shows DIS to be expensive relative to other firms, and is worth $90; This metric may be unreliable because it is not factoring in the growth in Asia and the studio entertainment division. A detailed DCF analysis values DIS at $118. I give this value of more importance because it incorporates assumptions that reflect DIS's long term growth potential. I value the stock at $118.

Trading History

Figure 25: DIS LTM P/E relative to S&P 500



Source: Factset, IMCP

DIS is currently trading about the average relative to the S&P 500. The relative P/E dropped as EPS is expected to decline in 2017 after years of solid growth. The market is more skeptical that growth will rebound in 2018. Although, DIS's current LTM P/E is at 18.20 compared to its five year average of 18.81. This implies that the drop in relative P/E is mostly due to the rise in S&P 500's P/E as it expects the economy and market earnings to rebound.

Assuming the firm maintains a 18.20 LTM P/E at the end of 2017, it should trade at $99.37 at the end of the year. Discounting this back to today at a 9.6% cost of capital results in a target of $90.65.

- Price = P/E x EPS = 18.20 x $5.46 = $99.37

Given DIS's potential for earnings growth, continued profitability, and high brand equity, this seems to be an unusually low valuation even with the concerning headwind of the media segment. However, this makes sense because I am less bullish about near-term earnings than consensus (2017). Utilizing the expected 2017 consensus EPS of $5.95 with TTM P/E of 18.20 results in a price of $108.29 (today's value of $98.78).

Relative Valuation

Figure 26: DIS comparable companies

Ticker	Name	Current Price	Market Value	Price Change 1 day	Price Change 1 Mo	Price Change 3 Mo	Price Change 6 Mo	Price Change 52 Wk	Price Change YTD	Earnings Growth LTG	Earnings Growth NTM	Earnings Growth 2015	Earnings Growth 2016	Earnings Growth 2017	Earnings Growth 2018	Earnings Growth Pst 5yr	Beta	LT Debt/ Equity	S&P Rating	LTM Dividend Yield	LTM Dividend Payout
DIS	DISNEY (WALT) CO	$104.22	$165,862	(0.3)	5.1	12.2	6.5	(2.0)	(0.8)	9.4	3.6%	19.2%	11.1%	4.0%	12.1%		1.43	38.1%	A+	1.43%	24.8%
CBS	CBS CORP	$63.62	$28,286	(1.4)	4.8	16.2	16.9	36.1	35.0	17.0	21.2%	11.8%	24.2%	8.0%	17.6%	22.4%	1.71	166.5%	B	1.04%	17.6%
CMCSA	COMCAST CORP	$69.05	$165,225	(1.5)	(0.7)	4.1	5.9	21.8	22.4	9.5	7.0%	10.9%	7.1%	8.3%	13.3%	20.2%	1.04	106.8%	A	1.59%	31.5%
DISCA	DISCOVERY COMMUNICATIONS INC	$27.41	$10,776	(1.0)	1.2	1.8	8.6	3.2	2.7	14.1	25.2%	-4.3%	17.6%	11.1%	13.0%	0.8%	1.66	151.9%	B-	0.00%	0.0%
FOXA	TWENTY-FIRST CENTURY FOX INC	$28.04	$52,023	(0.8)	(0.2)	15.8	3.7	2.7	3.2	9.8	27.1%	11.0%	0.6%	10.4%	11.0%		1.63	137.9%	B+	1.18%	19.7%
TWX	TIME WARNER INC	$96.53	$74,437	(0.2)	5.1	21.3	31.3	49.8	49.3	14.0	2.0%	14.5%	21.7%	2.4%	10.6%	15.5%	1.01	100.6%	B+	1.67%	27.7%
SIX	SIX FLAGS ENTERTAINMENT CORP	$59.96	$5,520	(0.6)	4.0	11.8	3.5	9.3	9.1	8.0	59.5%	105.2%	-23.4%	56.2%	18.5%	-25.0%	1.08	-8979.3%		3.97%	188.6%
VIAB	VIACOM INC	$35.10	$13,928	(0.5)	(6.4)	(7.9)	(15.4)	(14.1)	(14.7)	3.0	5.4%	0.7%	-32.4%	3.8%	7.1%		1.69	278.1%	B+	3.42%	38.8%
Average			$64,507	(0.8)	1.6	9.4	7.6	13.3	13.3	10.6	18.9%	21.1%	3.3%	13.0%	12.9%	6.8%	1.41	-999.9%		1.79%	43.6%
Median			$40,155	(0.7)	2.6	12.0	6.2	6.2	6.2	9.6	14.1%	11.4%	9.1%	8.2%	12.6%	15.5%	1.53	122.3%		1.51%	26.3%
SPX	S&P 500 INDEX	$2,239		(0.5)	1.8	3.3	6.7	8.5	9.5			7.7%	1.2%	7.6%	12.4%						

Ticker	Website	2016 ROE	P/B	P/E 2014	P/E 2015	P/E 2016	P/E TTM	P/E NTM	P/E 2017	P/E 2017E	2016 NPM	2016 P/S	OM	ROIC	EV/ EBIT	P/CF Current	P/CF 5-yr	Sales Growth NTM	Sales Growth STM	Sales Growth Pst 5yr	Book Equity
DIS	http://www.thewaltdisneycompany.	21.2%	3.85	24.1	20.2	18.2	18.2	17.6	17.5	15.6	16.4%	2.98	25.6%	16.0%	12.1	12.1		4.1%	6.4%	6.2%	$27.04
CBS	http://www.cbscorporation.com	33.6%	5.20	21.5	19.2	15.5	17.8	14.7	14.3	12.2	12.6%	1.94	21.4%	10.3%	11.0			0.9%	4.0%	-0.2%	$12.24
CMCSA	http://www.comcastcorporation.co	15.6%	3.09	23.6	21.2	19.8	20.2	18.9	18.3	16.2	10.4%	2.06	21.2%	8.2%	12.1			4.5%	6.3%	14.5%	$22.35
DISCA	http://corporate.discovery.com	15.7%	2.08	14.9	15.6	13.2	15.3	12.2	11.9	10.5	12.5%	1.66	31.8%	8.4%	12.0			4.2%	6.4%	11.0%	$13.20
FOXA	http://www.21cf.com	23.3%	3.77	18.1	16.3	16.2	18.4	14.5	14.7	13.2	11.7%	1.90	22.5%	8.0%	11.6			5.5%	4.4%	-3.9%	$7.44
TWX	http://www.timewarner.com	18.4%	3.07	23.3	20.3	16.7	17.2	16.8	16.3	14.7	15.3%	2.55	25.5%	8.1%	11.0			6.3%	5.4%	0.9%	$31.45
SIX	http://www.sixflags.com	-605.3%	-299.93	77.9	37.9	49.6	48.7	30.6	31.7	26.8	8.5%	4.20	23.7%	9.9%	20.3	12.9	10.5	7.8%	3.4%	5.3%	-$0.20
VIAB	http://www.viacom.com	34.2%	3.26	6.5	6.5	9.5	9.7	9.2	9.2	8.6	11.7%	1.12	21.9%	9.0%	9.9			2.4%	2.2%	-3.5%	$10.77
Average		-55.4%	-34.45	26.2	19.7	19.8	20.7	16.8	16.7	14.7	12.4%	2.30	24.2%	9.7%	12.5	12.5	10.5	4.5%	4.8%	3.8%	
Median		19.8%	3.17	22.4	19.7	16.5	18.0	15.8	15.5	14.0	12.1%	2.00	23.1%	8.7%	11.8	12.5	10.5	4.4%	4.9%	3.1%	
spx	S&P 500 INDEX			20.6	19.2	19.0			17.6	15.7											

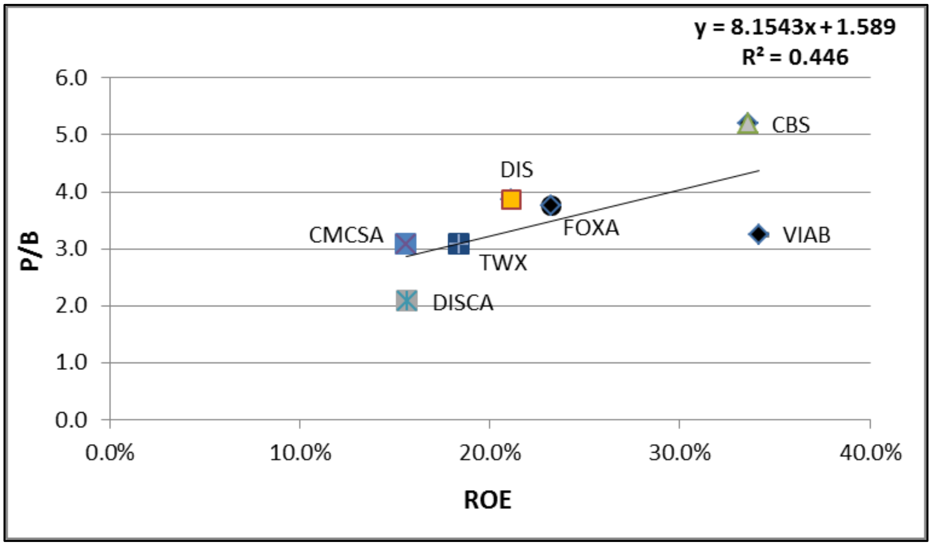
Source: Factset, IMCP

Comparable companies data as of December 31, 2016

Disney is currently trading at a P/E of about the median of its peers (18.0), with a P/E TTM of 18.20 compared to the average of 20.7. The P/E is near the average of the comps, despite difficult 2017 growth, because it is stable compared to its peers since its a conglomerate business with more ways to generate consistent revenue. Long-term, I expect it to trade at a premium as it has a potential for superior growth.

DIS's Long-term debt/equity (38.1%) is considerably lower compared to its peers a (median of 122.3%). Nearly all of Disney's peers have a percentage higher than 100% which suggests that those companies are highly leveraged and more risky. DIS's ROE (21.2%) is higher than the median (19.8%) despite its lower leverage, which means that it is more profitable and/or more efficient with asset turnover. It has a high P/B (3.85 compared to 3.17 median), but this is due to its higher ROE and lower financial risk.

Figure 27: P/B vs NTM ROE



Source: Factset, IMCP

Netflix's does not sell advertisements or pay fees to cable operators.

A more thorough analysis of P/B and ROE is shown in figure 27. The calculated R-squared of the regression indicates that over 45% of a sampled firm's P/B is explained by its 2016 ROE. Note that SIX is excluded from the regression because it is an outlier since it has negative ROE and P/B ratios. According to the graph, DIS has an above average P/B and ROE, and is about the median of the peer group. However, Disney is above the trend line, so this indicates it is overvalued. This may be a fair assessment given the headwinds that DIS is facing with its media segment. Direct to consumer streaming is becoming more prevalent with services like Netflix gaining in popularity. This will result in declining cable subscriptions, which may decrease affiliated fees, ad revenue and ROE. The fair value is $89.71. Keep in mind that this value does not give the company credit for low financial risk.

- Estimated P/B = Estimated 2016 ROE (21.2%) x 8.1543 + 1.589 = 3.32
- Target Price = Estimated P/B (3.32) x BVPS ($27.04) = $89.71

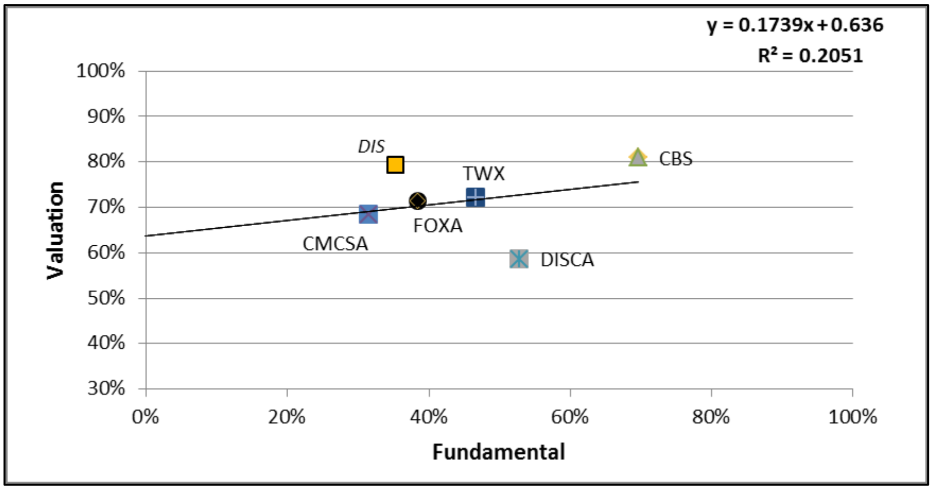
Figure 28: Composite valuation, % of range

		Fundamentals					Valuation				
	Weight	20.0%	20.0%	20.0%	20.0%	20.0%	33.3%	33.3%	33.3%		
		Earnings Growth									
Ticker	Name	LTG	NTM	2016	2017	ROE	P/B	P/S	P/CF	Fund	Value
DIS	DISNEY (WALT) CO	56%	6%	46%	7%	62%	74%	71%	94%	35%	79%
CBS	CBS CORP	100%	36%	100%	14%	98%	100%	46%	97%	70%	81%
CMCSA	COMCAST CORP	56%	12%	29%	15%	46%	59%	49%	97%	31%	68%
DISCA	DISCOVERY COMMUNICATIONS INC	83%	42%	73%	20%	46%	40%	39%	97%	53%	59%
FOXA	TWENTY-FIRST CENTURY FOX INC	57%	46%	2%	19%	68%	72%	45%	97%	38%	71%
TWX	TIME WARNER INC	82%	3%	90%	4%	54%	59%	61%	97%	47%	72%
VIAB	VIACOM INC	18%	9%	-134%	7%	100%	63%	27%	97%	0%	62%

Source: Factset, IMCP

For a final comparison, I created a composite ranking of several valuation and fundamental metrics. Since the variables have different scales, each was converted to a percentile of a maximum before calculating the composite score. An equal weighting of long term growth rate, 2016 and 2017 EPS growth, 2016 ROE and NTM earnings growth was compared to an equal weight composite of P/B, P/S, and P/CF. After eliminating SIX, an extreme outlier, the regression line had an R-squared of 0.21. Further analysis of figure 29 displays DIS above the line, which indicates that it is expensive and overvalued based on its fundamentals.

Figure 29: Composite relative valuation



Source: Factset, IMCP

<u>Discounted Cash Flow Analysis</u>

A three stage discounted cash flow model was also used to value DIS.

For the purpose of this analysis, the company's cost of equity was calculated to be 9.60% using the Capital Asset Pricing Model. The underlying assumptions used in calculating this rate are as follows:

- The risk free rate, as represented by the ten year Treasury bond yield, is 2.45% (12/26/16).
- A beta of 0.95 was utilized since the company is less risky than the market. Although Disney is cyclical, it is a relatively stable business compared to its peers because of its diversified revenue streams.
- A long-term market rate of return of 10% was assumed, since historically, the market has generated an annual return of about 10%.

Given the above assumptions, the cost of equity is 9.60% (2.45. + 0.95 (10.0 – 2.45)).

Stage One - The model's first stage simply discounts fiscal years 2017 and 2018 free cash flow to equity (FCFE). These per share cash flows are forecasted to be $5.16 and $3.05, respectively. Discounting these cash flows, using the cost of equity calculated above, results in a value of $7.25 per share. Thus, stage one of this discounted cash flow analysis contributes $7.25 to value.

Stage Two - Stage two of the model focuses on fiscal years 2019 to 2023. During this period, FCFE is calculated based on revenue growth, NOPAT margin and capital growth assumptions. The resulting cash flows are then discounted using the company's 9.60% cost of equity. I assume 7% sales growth in 2019, rising to 9% in 2023. The ratio of NWC to sales will remain at 2017 levels, and NFA turnover will also remain consistent with 2017 levels as capital is expected to grow with sales. Also, the

NOPAT margin will remain at my 2018 forecast, but I assume a constant 6% growth in after-tax interest as the firm raises debt over time.

Figure 30: FCFE and discounted FCFE, 2017 – 2023

	2017	2018	2019	2020	2021	2022	2023
FCFE	$5.16	$3.05	$4.12	$5.31	$4.16	$5.51	$4.23
Discounted FCFE	$4.71	$2.54	$3.13	$3.68	$2.63	$3.18	$2.22

Source: Factset, IMCP

Added together, these discounted cash flows total $14.84.

Stage Three – Net income for the years 2019 – 2023 is calculated based upon the same margin and growth assumptions used to determine FCFE in stage two. EPS is expected to grow from $5.46 in 2017 to $9.90 in 2023.

Figure 31: EPS estimates for 2017 – 2023

	2017	2018	2019	2020	2021	2022	2023
EPS	$5.46	$6.74	$7.55	$7.93	$8.56	$9.08	$9.90

Source: Factset, IMCP

Stage three of the model requires an assumption regarding the company's terminal price-to-earnings ratio. The P/E of DIS currently trades at 1.0x the S&P 500, but this has come down over time. My model assumes that EPS will grow about the same rate as the market or slightly more. The firm also has established brands and stability. Assuming the P/E of the S&P 500 falls by 2023 to more normal levels and that DIS trades at a premium, an 18.5 P/E in 2023 seems reasonable.

Given the assumed terminal earnings per share of $9.90 and a price to earnings ratio of 18.50, a terminal value of $183.15 per share is calculated. Using the 9.60% cost of equity, this number is discounted back to a present value of $96.27.

Total Present Value – given the above assumptions and utilizing a three stage discounted cash flow model, an intrinsic value of $118.36 is calculated (7.25 + 14.84 + 96.27). Given DIS's current price of $104.22, this model indicates that the stock is undervalued.

<u>Scenario Analysis</u>

Disney is difficult to value because of its diversified revenue streams. As a result, there can be varied growth rates for each one of its numerous business segments. Possible growth in one industry can be offset by declining growth in another business segment. Since Disney is a conglomerate, this can be beneficial or detrimental as my bull and bear case demonstrates.

Figure 32 illustrates my assumptions for the bear and bull case scenario analysis. Disney is a cyclical company and when the economy is prosperous, advertising is more profitable. Disney benefits from a strong economy. In the bull case, I assume a P/E of 20 as investors get excited about growth during a strong economy. A beta of 0.90 was used because it is more stable than its peers due to its diversification. NOPAT/S and S/NFA also increase as higher sales growth push up margins and asset turnover. The value increased to $136.17, which is 15% higher than the base case.

In contrast, in the bear scenario I dropped sales growth 0.5% to 2% from the base case. I assume management will not manage well the changing environment with subscriber losses and more competition in the sports networks. I chose a P/E of 18 as the growth slows. A beta of 1.10 is utilized due to the ongoing revenue headwinds. NOPATS/S and S/NFA will also decrease with sales. The value decreases to $103.27, which is 13% lower than the base case.

Figure 32: DCF target price scenario analysis

Base Case Expectations	2017	2018	2019	2020	2021	2022	2023
Beta	0.95						
Sales Growth	2.6%	8.9%	7.0%	5.0%	8.0%	6.0%	9.0%
NOPAT/S	16.5%	18.4%	18.4%	18.4%	18.4%	18.4%	18.4%
S/NFA	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Terminal Year P/E	18.5						
Bear Case Expectations	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Beta	1.1						
Sales Growth	2.6%	8.9%	6.5%	3.0%	7.0%	5.0%	8.0%
NOPATS/S	16.5%	18.4%	18.3%	18.2%	18.1%	18.1%	18.0%
S/NFA	0.75	0.75	0.74	0.73	0.72	0.71	0.70
Terminal Year P/E	18						
Bull Case Expectations	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Beta	0.9						
Sales Growth	2.6%	8.9%	7.5%	6.5%	8.5%	7.0%	10.5%
NOPAT/S	16.5%	18.4%	18.5%	18.6%	18.7%	18.9%	19.0%
S/NFA	0.75	0.75	0.76	0.77	0.78	0.79	0.80
Terminal Year P/E	20						

Source: IMCP

Base Case	
Value (P/E) Beginning FY17	$ 118.36
Bear Case	
Value (P/E) Beginning FY17	$ 103.27
Bull Case	
Value (P/E) Beginning FY17	$ 136.17

Business Risks

Although I have numerous reasons to be optimistic about DIS, a company as large and multifaceted as Disney could have a wide range of factors affecting future performance. There are several logical reasons for the stock to face possible headwinds:

Consumer preference:

Creating popular content and experiences for media companies is highly dependent on consumer taste. Over time, society may develop new preferences resulting in a potential decrease in profit. If management does not forecast these changes correctly, consumers may go elsewhere.

Exposure to currency fluctuations:

Adverse currency conditions could weigh down profit, and lack of currency hedging could affect operating income. For FY16, Disney forecasted a $500 million loss in operating income which is due to the increased strength of the U.S dollar. Future strengthening of the dollar could continue to negatively impact Disney.

Competition:

Competition in the media industry is immense, with companies fighting for viewership. On demand and live streaming could help competitors break into the market, and provide a service that is cheaper and easily accessible compared to Disney’s programming.

Protection of intellectual property:

Protecting Disney’s decades of established content is vital for the long-term success of the company. The stealing of homemade creations would hurt revenue and increase the cost of defending the rights, so it is imperative for Disney to pursue copyright, trademark, and patent infringements.

Maintenance of gross margin:

Disney relies heavily on the ESPN network because it makes almost 17% of sales. Sports programming costs are increasing in 2017 and 2019 which could hurt earnings.

Appendix 1: Sales Forecast

Sales forecast	Sep-12	Sep-13	Sep-14	Oct-15	Oct-16	Oct-17	Oct-18
Sales	$42,278	$45,041	$48,813	$52,465	$55,632	$57,097	$62,185
Growth		*6.5%*	*8.4%*	*7.5%*	*6.0%*	*2.6%*	*8.9%*
Media Networks	19,436	20,356	21,152	23,264	23,689	23,227	23,924
Growth		*4.7%*	*3.9%*	*10.0%*	*1.8%*	*-2.0%*	*3.0%*
% of sales	*46.0%*	*45.2%*	*43.3%*	*44.3%*	*42.6%*	*40.7%*	*38.5%*
Parks & Resorts	12,920	14,087	15,099	16,162	16,974	18,247	19,433
Growth		*9.0%*	*7.2%*	*7.0%*	*5.0%*	*7.5%*	*6.5%*
% of sales	*30.6%*	*31.3%*	*30.9%*	*30.8%*	*30.5%*	*32.0%*	*31.3%*
Studio Entertainment	5,825	5,979	7,278	7,366	9,441	9,819	12,617
Growth		*2.6%*	*21.7%*	*1.2%*	*28.2%*	*4.0%*	*28.5%*
% of sales	*13.8%*	*13.3%*	*14.9%*	*14.0%*	*17.0%*	*17.2%*	*6.0%*
Consumer & Interactive Products	4,097	4,619	5,284	5,673	5,528	5,804	6,211
Growth		*12.7%*	*14.4%*	*7.4%*	*-2.6%*	*5.0%*	*7.0%*
% of sales	*9.7%*	*10.3%*	*10.8%*	*10.8%*	*9.9%*	*10.2%*	*10.0%*
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
United States & Canada	31,770	34,021	36,769	40,320	42,616	43,679	47,509
Growth		*7.1%*	*8.1%*	*9.7%*	*5.7%*	*2.5%*	*8.8%*
% of sales	*75.1%*	*75.5%*	*75.3%*	*76.9%*	*76.6%*	*76.5%*	*76.4%*
Europe	6,223	6,181	6,505	6,507	6,714	6,966	7,400
Growth		*-0.7%*	*5.2%*	*0.0%*	*3.2%*	*3.8%*	*6.2%*
% of sales	*14.7%*	*13.7%*	*13.3%*	*12.4%*	*12.1%*	*12.2%*	*11.9%*
Asia Pacific	2,990	3,333	3,930	3,958	4,582	4,739	5,597
Growth		*11.5%*	*17.9%*	*0.7%*	*15.8%*	*3.4%*	*18.1%*
% of sales	*7.1%*	*7.4%*	*8.1%*	*7.5%*	*8.2%*	*8.3%*	*9.0%*
All Other	1,295	1,506	1,609	1,680	1,720	1,713	1,679
Growth		*16.3%*	*6.8%*	*4.4%*	*2.4%*	*-0.4%*	*-2.0%*
% of sales	*3.1%*	*3.3%*	*3.3%*	*3.2%*	*3.1%*	*3.0%*	*2.7%*

Appendix 2: Income Statement

Income Statement (in millions)							
	2013	**2014**	**2015**	**2016**		**2017E**	**2018E**
Sales	$ 42,278	$ 45,041	$ 48,813	$ 52,465	$ 55,632	$ 57,097	$ 62,185
Direct costs	25,455	27,226	28,708	30,718	32,520	33,687	35,756
Gross Margin	16,823	17,815	20,105	21,747	23,112	23,410	26,428
SG&A, R&D, and other	7,194	7,960	7,882	7,762	7,984	9,078	9,079
EBIT	9,629	9,855	12,223	13,985	15,128	14,331	17,350
Interest	369	235	(23)	117	260	289	300
EBT	9,260	9,620	12,246	13,868	14,868	14,042	17,050
Taxes	3,087	2,984	4,242	5,016	5,078	4,796	5,823
Income	*6,173*	*6,636*	*8,004*	*8,852*	*9,790*	*9,246*	*11,227*
Other	491	500	503	470	399	470	510
Net income	5,682	6,136	7,501	8,382	9,391	8,776	10,717
Basic Shares	1,794	1,792	1,740	1,694	1,629	1,609	1,591
EPS	$ 3.17	$ 3.42	$ 4.31	$ 4.95	$ 5.76	$ 5.46	$ 6.74
DPS	$ 0.60	$ 0.75	$ 0.86	$ 1.81	$ 1.42	$ 2.18	$ 2.51

Appendix 3: Balance Sheets

Balance Sheet	2012	2013	2014	2015	2016	2017E	2018E
Assets							
Cash	3,387	3,931	3,421	4,269	4,610	4,872	4,265
Operating assets ex cash	110,322	110,178	111,755	112,489	112,356	112,681	113,811
Operating assets	13,709	14,109	15,176	16,758	16,966	17,553	18,077
Operating liabilities	12,813	11,704	13,292	16,334	16,842	17,286	18,826
NOWC	896	2,405	1,884	424	124	268	(749)
NOWC ex cash (NWC)	(2,491)	(1,526)	(1,537)	(3,845)	(4,486)	(4,604)	(5,014)
NFA	61,182	67,132	69,010	71,424	75,067	76,130	82,913
Invested capital	$62,085	$69,537	$70,894	$71,848	$75,191	$76,397	$82,164
Total assets	$74,898	$81,241	$84,186	$88,182	$92,033	$93,683	$100,990
Short-term and long-term debt	17,876	17,337	18,618	19,142	24,189	23,989	25,989
Other liabilities	2,251	4,050	4,098	4,051	3,679	3,309	3,359
Equity	41,958	48,150	48,178	48,655	47,323	49,099	52,816
Total supplied capital	62,085	69,537	70,894	71,848	75,191	76,397	82,164
Total liabilities and equity	$74,898	$81,241	$84,186	$88,182	$92,033	$93,683	$100,990

Appendix 4: Ratios

Ratios	2012	2013	2014	2015	2016	2017E	2018E
Profitability							
Gross margin	39.8%	39.6%	41.2%	41.5%	41.5%	41.0%	42.5%
Operating (EBIT) margin	22.8%	21.9%	25.0%	26.7%	27.2%	25.1%	27.9%
Net profit margin	13.4%	13.6%	15.4%	16.0%	16.9%	15.4%	17.2%
Activity							
NFA (gross) turnover		70.2%	71.7%	74.7%	76.0%	75.5%	78.2%
Total asset turnover		57.7%	59.0%	60.9%	61.7%	61.5%	63.9%
Liquidity							
Op asset / op liab	107.0%	120.5%	114.2%	102.6%	100.7%	101.5%	96.0%
NOWC Percent of sales		3.7%	4.4%	2.2%	0.5%	0.3%	-0.4%
Solvency							
Debt to assets	23.9%	21.3%	22.1%	21.7%	26.3%	25.6%	25.7%
Debt to equity	42.6%	36.0%	38.6%	39.3%	51.1%	48.9%	49.2%
Other liab to assets	3.0%	5.0%	4.9%	4.6%	4.0%	3.5%	3.3%
Total debt to assets	26.9%	26.3%	27.0%	26.3%	30.3%	29.1%	29.1%
Total liabilities to assets	44.0%	40.7%	42.8%	44.8%	48.6%	47.6%	47.7%
Debt to EBIT	185.6%	175.9%	152.3%	136.9%	159.9%	167.4%	149.8%
EBIT/interest	2609.5%	4193.6%	-53143.5%	11953.0%	5818.5%	4957.5%	5785.4%
Debt to total net op capital	28.8%	24.9%	26.3%	26.6%	32.2%	31.4%	31.6%
ROIC							
NOPAT to sales		15.1%	16.4%	17.0%	17.9%	16.5%	18.4%
Sales to IC		68.4%	69.5%	73.5%	75.7%	75.3%	78.4%
Total		10.3%	11.4%	12.5%	13.5%	12.5%	14.4%
Total using EOY IC	10.3%	9.8%	11.3%	12.4%	13.2%	12.4%	13.9%
ROE							
5-stage DuPont							
EBIT / sales		21.9%	25.0%	26.7%	27.2%	25.1%	27.9%
Sales / avg assets		57.7%	59.0%	60.9%	61.7%	61.5%	63.9%
EBT / EBIT		97.6%	100.2%	99.2%	98.3%	98.0%	98.3%
Net income /EBT		63.8%	61.3%	60.4%	63.2%	62.5%	62.9%
ROA		7.9%	9.1%	9.7%	10.4%	9.5%	11.0%
Avg assets / avg equity		173.3%	171.7%	178.0%	187.8%	192.6%	191.0%
ROE		13.6%	15.6%	17.3%	19.6%	18.2%	21.0%
3-stage							
Net income / sales		13.6%	15.4%	16.0%	16.9%	15.4%	17.2%
Sales / avg assets		57.7%	59.0%	60.9%	61.7%	61.5%	63.9%
ROA		7.9%	9.1%	9.7%	10.4%	9.5%	11.0%
Avg assets / avg equity		173.3%	171.7%	178.0%	187.8%	192.6%	191.0%
ROE		13.6%	15.6%	17.3%	19.6%	18.2%	21.0%
Payout Ratio		21.9%	19.9%	36.6%	24.6%	39.9%	37.3%
Retention Ratio		78.1%	80.1%	63.4%	75.4%	60.1%	62.7%
Sustainable Growth Rate		10.6%	12.5%	11.0%	14.7%	10.9%	13.2%

Appendix 5: Cash Flow Statement

Cash Flow Statement	2012	2013	2014	2015	2016	2017E	2018E
NOPAT	$6,419	$6,798	$7,989	$8,927	$9,961	$9,437	$11,424
Growth		6%	18%	12%	12%	-5%	21%
NWC*	-2491	-1526	-1537	-3845	-4486	-4604	-5014
Net fixed assets	61189	67132	69010	71424	75067	76130	82913
Total net operating capital*	$58,698	$65,606	$67,473	$67,579	$70,581	$71,525	$77,898
Growth		12%	3%	0%	4%	1%	9%
- Change in NWC*		965	-11	-2308	-641	-118	-410
- Change in NFA		5943	1878	2414	3643	1063	6783
FCFF*		-$110	$6,122	$8,821	$6,959	$8,492	$5,051
Growth			-5671%	44%	-21%	22%	-41%
- After-tax interest expense	246	162	-15	75	171	190	197
FCFE**		-$272	$6,137	$8,746	$6,788	$8,302	$4,853
Growth			-2356%	43%	-22%	22%	-42%

Appendix 6: 3-stage DCF Model

3 Stage Discounted Cash Flow							
	First Stage		Second Stage				
Cash flows	2017	2018	2019	2020	2021	2022	2023
Sales Growth	2.6%	8.9%	7.0%	5.0%	8.0%	6.0%	9.0%
NOPAT / S	16.5%	18.4%	18.4%	18.4%	18.4%	18.4%	18.4%
S / NWC	-12.40	-12.40	-12.40	-12.40	-12.40	-12.40	-12.40
S / NFA (EOY)	0.75	0.75	0.75	0.75	0.75	0.75	0.75
S / IC (EOY)	0.80	0.80	0.80	0.80	0.80	0.80	0.80
ROIC (EOY)	13.2%	14.7%	14.7%	14.7%	14.7%	14.7%	14.7%
ROIC (BOY)		16.0%	15.7%	15.4%	15.8%	15.5%	16.0%
Sales	$57,097	$62,185	$66,538	$69,864	$75,454	$79,981	$87,179
NOPAT	$9,437	$11,424	$12,224	$12,835	$13,862	$14,693	$16,016
Growth		21.1%	7.0%	5.0%	8.0%	6.0%	9.0%
Change in NWC	-118	-410	-351	-268	-451	-365	-580
NWC	-4604	-5014	-5365	-5634	-6084	-6449	-7030
Growth NWC		8.9%	7.0%	5.0%	8.0%	6.0%	9.0%
- Chg NFA	1063	6783	5804	4436	7452	6036	9598
NFA EOY	76130	82913	88717	93153	100605	106641	116239
Growth NFA		8.9%	7.0%	5.0%	8.0%	6.0%	9.0%
Total inv in op cap	944	6373	5453	4168	7002	5671	9017
Total net op cap	71525	77898	83351	87519	94520	100192	109209
FCFF	$8,492	$5,051	$6,771	$8,667	$6,860	$9,022	$6,998
% of sales	14.9%	8.1%	10.2%	12.4%	9.1%	11.3%	8.0%
Growth		-40.5%	34.1%	28.0%	-20.9%	31.5%	-22.4%
- Interest (1-tax rate)	190	197	209	222	235	249	264
Growth		3.7%	6.0%	6.0%	6.0%	6.0%	6.0%
FCFE w/o debt	$8,302	$4,853	$6,561	$8,445	$6,625	$8,773	$6,734
% of sales	14.5%	7.8%	9.9%	12.1%	8.8%	11.0%	7.7%
Growth		-41.5%	35.2%	28.7%	-21.6%	32.4%	-23.2%
/ No Shares	1609	1591	1591	1591	1591	1591	1591
FCFE	$5.16	$3.05	$4.12	$5.31	$4.16	$5.51	$4.23
Growth		-40.9%	35.2%	28.7%	-21.6%	32.4%	-23.2%
* Discount factor	0.91	0.83	0.76	0.69	0.63	0.58	0.53
Discounted FCFE	$4.71	$2.54	$3.13	$3.68	$2.63	$3.18	$2.22
Third Stage							
Terminal value P/E							
Net income	$8,776	$10,717	$12,014	$12,613	$13,626	$14,444	$15,751
% of sale	15.4%	17.2%	18.1%	18.1%	18.1%	18.1%	18.1%
EPS	$5.46	$6.74	$7.55	$7.93	$8.56	$9.08	$9.90
Growth		23.5%	12.1%	5.0%	8.0%	6.0%	9.1%
Terminal P/E							18.5
* Terminal EPS							$9.90
Terminal value							$183.15
* Discount factor							0.53
Discounted terminal value							$96.27
Summary							
First stage	$7.25	Present value of first 2 year cash flow					
Second stage	$14.84	Present value of year 3-7 cash flow					
Third stage	$96.27	Present value of terminal value P/E					
Value (P/E)	**$118.36**	= value at beg of fiscal yr		2017			

Appendix 7: Porter's 5 Forces

Threat of New Entrants – Low

The barriers to entry for a media and entertainment company are extremely high. The probability for a new company to disrupt Disney's brand is extremely low given the long history of the company. An extreme advantage DIS has over new entrants is that the company is able to produce long-term growth because it has the capital to invest in R&D and marketing. In addition, because of the company's long history, it can rely on past failures and experiences to determine what the consumer's desire. The most significant threat would be entry of an established foreign brand that taps into changes in consumer preference.

Threat of Substitutes - Moderate

Although competitors would be hard pressed to try and duplicate Disney's iconic character creations, there are substitutes for their sports networks. My analysis suggests that Disney's loyal fan base for beloved characters does not translate to a following for their sports networks like ESPN. With big players like Fox sports competing against Disney's sports division, it gives consumers an alternative, resulting in lower viewership. Streaming and VOD also offer a cheaper and faster substitute to subscription based sports networks.

Supplier Power - Low

The company creates large volumes of unique services and products, and volume is critical to suppliers. Disney is a large company so it can purchase quantities in bulk. The products are unique, so suppliers may have less power and may be dependent on Disney's business.

Buyer Power – High

Consumers of entertainment services goods have a great degree of power over content. High prices may cause consumers to spend money elsewhere, especially when it comes to the parks and resorts segment.

Intensity of Competition – High

Although there are relatively few competitors, competition is fierce. Competition is consistently creating and developing content for entertainment, so companies in this space must evolve and keep up to date with demand/preferences.

Appendix 8: SWOT Analysis

Strengths	Weakness
Content Integration Diversified Revenue Streams Brand Equity	Over-Expansion ESPN Margins Capital Expenditures
Opportunities	**Threats**
M&A Activites China Direct to Consumer Streaming	Shift in Consumer Preferences Cable Cord Cutting Competition