The Australian Finance Podcast Episode Transcript

Episode: Investment Case Study - The Walt Disney Company (NYSE: DIS)
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Episode transcript:

Owen:
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Kate:
Welcome back to this episode of The Australian Finance Podcast. And in this episode, I'm joined by a special guest, who hasn't actually been on the Finance Podcast before, but I work with on a daily basis, Cathryn Goh, who's one of our investment analysts here at Rask Invest.

Cathryn:
Thanks, Kate. It's good to be here.

Kate:

Yeah, so it took a bit of convincing, but I finally got Cathryn on the show. She's been working with Owen and I for a few years now, but yeah, podcast debut.

Cathryn:
I know.

Kate:
Okay. So what we're talking about today, we're actually going to go deeper on last week's episode. So if you listen to last week's episode, which I highly recommend you do before today's one, we covered a brief five-point checklist for some things to look out for when you're researching stocks, whether that's Australian companies or companies overseas. And then in this episode, we're actually going to go one step further and apply that checklist in a practical way to a company that we all know and love, the Walt Disney Company, which is listed on the New York Stock Exchange.

Kate:
So this episode's part two of our five-part shares month series, that we've put together because we've had a lot of requests to go more in-depth on certain topics. And so each episode is going to get a little bit more advanced and technical. So next week, if you stay tuned to the series, we're going to have a episode with Owen and one of our senior investment analysts at Rask Invest, Kevin. And they're going to take what we discuss today to the next level, and talk about some of the more technical aspects of investing and valuation. And then after that, we're going to have a special share month Q&A episode. So if you have any questions after last week's or today's or next week's episode, send them to podcast@rask.com.au, and use the subject line shares month, just so we can pull them out.

Kate:
And then finally, in week five, all four of us are going to gather, and we're going to talk about where we'd invest a hypothetical $10,000 portfolio. So stay tuned for that one, it should be fun. And if you haven't listened to last week's episode, so week one of our shares month, please give that one a listen, because it does set the scene for what we're going to discuss today.

Kate:
So without further ado, I'm going to let Cathryn introduce herself, because it is her podcast debut. So, Cathryn, what do you do at Rask?

Cathryn:
Well, I am an investment analyst is my official title. So basically what I do is just look for really great businesses that our members at Rask Invest and Rask Rockets can invest in.

Kate:
Yeah. So how did you get into investing? Did you study finance at school or university?

Cathryn:

Yeah. So I did a commerce degree at university, but I guess my journey to finance and investing kind of got started right when I was about to turn 18. So I was with Commonwealth at the time, Commonwealth Bank, and I had a Youthsaver account. So I think when you turn 18, CBA no longer considers you a youth. So here are your options, wanted me to go to a standard everyday account. And I remember looking at the different options and interests that was on offer, and I just thought, "This is really low." So I did a little bit of research, and that's when I came across high-interest savings accounts, ETFs, and that's where the whole journey started.

Kate:
So you got hooked on the Dollarmites programme, and stayed with them ever since then. Yeah. So what's the favourite part of your day? So when you're researching companies and all the other things you do here, what do you find the most enjoyable?

Cathryn:
I think the best part is really just learning and finding new, innovative businesses. I mean, with technology, with innovation these days, there's just continuously new ways to do things, new products on the market.

Kate:
Yeah. And I think that's what Owen did talk about in our episode last week, of just how much you learn by researching different companies about the world. And you get to put so many different skills to use. That obscure book you read about forests might actually have some application on what you're doing in your investment research. And is there any really interesting companies you've come across in your investment journey?

Cathryn:
Yeah. So one that comes to mind is a company called EML Payments. It's on the ASX, under the ticker code EML. And it just operates across a broad spectrum of the whole payments industry, from payments technology, to gift card solutions, to virtual account numbers. So, yeah.

Kate:
Yeah. Awesome. So today we're going to be talking about the Walt Disney Company. And as a disclosure, I did check my brokerage account last night, I own about $200 worth of Disney shares. I don't know if that even gets me a share. I'm not sure what the price is today.

Cathryn:
190, so one.

Kate:
Okay. So I own just over one share. Okay. That's good to know. And I think one of our other analysts, Kev, owns a couple of shares. Do you own any Disney shares?

Cathryn:
I don't know.

Kate:
But you probably do through an ETF that you own.

Cathryn:
Yes, I would say so.

Kate:
Yeah. Yeah. So you actually listening might actually own Disney shares already through an exchange traded fund, or your super fund that's invested in the US market, because it is one of the biggest companies over there. So why didn't we choose Disney? We wanted a company that everyone knows and loves, that you've had exposure to since birth, probably. I think most of us have grown up on the Disney animations and movies, maybe the Pixar movies. We've had some sort of touch point. If we're American we'd probably have been to Disney World by now. I mean 12 million plus people go to Disney World every year. I mean, not during COVID, but before that. So you've already got some sort of touch point and understanding Disney in a way, but you probably don't know just how many companies they own.

Kate:
Maybe you've heard about the Marvel Universe. Can anything top the last Avengers movie? I don't know. It's pretty good. The Disney Worlds, the resorts, they've got cruise ships now, they've got their own travel companies, they have the Disney+ streaming service, which is something I became very familiar with during COVID. They have their own publishing line with novels and picture books for all ages. They own ESPN, Hulu, Star Wars franchise, National Geographic, and there's just so much. If you go onto their website, there's at least 1,000 different subsidiaries and companies below it.

Cathryn:
There's a good graphic going around on the internet, we'll put it in the show notes. But it's basically a Mickey Mouse kind of shape, and in it, you've just got all the different parts of the Disney business, and it's just huge.

Kate:
Yeah. And the amount of people they employ as part of their worlds and everything else is just amazing. I'll just read this, but it's straight from their website, that, "The mission of the Walt Disney Company is to entertain, inform and inspire people around the globe through the power of unparalleled storytelling, reflecting the iconic brands, creative minds, and innovative technologies that make ours the world's premier entertainment company." I think that does sum up what they do. And so Cathryn, before we launch into applying the checklist to Disney, what's your favourite Disney product or service?

Cathryn:
I think it's pretty hard to go past Marvel, the Marvel franchise. But going back a bit further in terms of my childhood, I feel like Finding Nemo. I was a big fan of Nemo growing up.

Kate:
Yeah. They had some amazing films. I have been enjoying Marvel recently. I think I went and watched maybe the whole back catalogue during COVID. There's a lot of great films coming out, and they're just coming out with more and more all the time. So there is a lot of creativity behind the scenes there. I mean, you were pointing out last week, just looking at the end credits of a Marvel film, just the sheer number of people. It goes for five, 10 minutes.

Cathryn:
While you wait for the post credit scene.

Kate:
Yeah. The best part. All right. So I think it's a good time to launch into the checklist. So I'm going to put each part of the checklist to Cathryn, and she's going to talk about some of the research she's done on that, and some of the things that she's pulled out while doing a brief overview look at Disney. All right. So to start with, what does Disney actually do?

Cathryn:
Yeah. Well, that's also the first place that I was start as well when looking at a business. So just trying to understand what it does, the different products, how it makes money. So for Disney, you'll be able to find this in the financial reports. So they always break it down into different divisions. So in Disney's case, they broke it down to four divisions. You have the studio entertainment division, which is just the movies. So you've got Marvel, 20th Century Fox, Pixar, Walt Disney Pictures, Lucasfilm, which is the Star Wars franchise. Just a little fun fact here, Marvel Endgame, it grossed US $2.8 billion at the box office. And Disney made around $900 million in profit just from that movie alone.

Kate:
That's pretty sweet.

Cathryn:
Yeah. So that's one division. Then the next one is media networks. So you've got TV broadcasting. So Disney owns ABC in America. And it also includes domestic cable networks. So the Disney Channel, ESPN, National Geographic. Then you've got the direct-to-consumer segment, which is just basically Disney's streaming services. So Disney+, Hulu and ESPN+, which is like the US version of Kayo. And then last but not least, we have parks, experiences and products. So this is Disneyland theme parks and resorts, and then also merchandise, licencing and retail. So when you see Disney products, characters on t-shirts, toys, games, a lot of them is made by Disney itself, but then a lot of them are also licenced to third-parties, who then pay to put a Disney character on a t-shirt for example.

Kate:
There's a lot of money in licencing that people don't really realise, isn't there?

Cathryn:
Yeah. Every single Marvel character, Star Wars figurines, t-shirts. Disney all gets paid.

Kate:
Yeah. Uniqlo, maybe a year ago, had a whole line of different Disney t-shirts. They must've had to pay quite a bit for that deal.

Cathryn:
Definitely.

Kate:
Yeah. Awesome. So what about, how does Disney make money? So Disney makes money through all those different sections, but what are some of the areas that it makes most of the money and revenue from?

Cathryn:
Good question. So pre-COVID the parks and products division was Disney's largest segment. So it brought in about 40% of Disney's revenue. And this was closely followed by media networks, which brought in around 35%. But in a COVID world, where parks were shut, the streaming services really took off, and now it generates roughly around the same amount of revenue as the parks and products division.

Kate:
Okay. So that's what Disney does. Now how do we look at this... We talked a bit about this last week with Owen, about the circle of competence and how you understand a business. So let's talk about investing within your circle of competence. If we just go back a step, what is your circle of competence?

Cathryn:
So circle of competence is all about being self-aware. So knowing what you know and what you don't know. And it's not so much about knowing the size of the circle or what you know, but more so about where the boundaries are, so you don't stray too far away from what you know. So for example, a mechanic knows more about cars than I do. A doctor would know how to interpret clinical trials better than I would. So they would have what we call an investing edge when it comes to automotive businesses or biotechnology companies. It's inside their circle of competence, but it might not be inside of mine. So tying this back to Disney, someone who's grown up watching Disney movies or subscribes to Disney+ would know more about the product, so it would be closer to the centre of their circle of competence.

Kate:
Yeah. So do you think it's within yours?

Cathryn:
I would say. I think it's in most people's circle of competence.

Kate:
We've all watched enough Marvel movies. And I don't think it's too complicated to understand what they do. There's a lot, it might take you a long time to get a handle on all the different aspects of Disney, but it's not too complex. It's not like a biotechnology company or a cloud computing, that's doing something that's really hard to get your head around.

Cathryn:
Yeah, exactly. It's not technical in that nature.

Kate:
Yeah. So using that to advantage, why is it so important to invest in what you know?

Cathryn:
Yeah. So we've got a simple graphic that explains this visually, and we'll put this in the show notes. But essentially, as an investor, you don't really want to be straying too far outside of your circle of competence. And for one, there's a sleep at night factor. So when you understand a company, you feel more comfortable investing in it. So imagine you've just started investing and you put $5,000 into a hot tip that you found on social media, and then the next day it falls 20%. Without really knowing or understanding the business, you wouldn't be able to tell whether that share price fall was justified, or whether it was just the market overreacting.

Cathryn:
Another point is that it helps you avoid mistakes. So if you're straying outside of your circle of competence, that basically it means that you don't probably understand what the business does, or how the product works, or the industry dynamics. And without knowing this type of information, you're more likely to make mistakes. And then finally, you can also use what you know to your advantage. So every investor has a different set of skills and experience that can give them an edge. And a common place to start is with your own profession, because you're likely to have behind the scenes knowledge that other people wouldn't know. So say if you're an accountant, you'd likely have intimate knowledge of Xero, the cloud software provider. Or for example, I spent a few years at Domino's, so I understood the relationship between franchises and the head office, and the different product margins across different products.

Kate:
Yeah. So it is important to sort of look at what do you understand and what you don't, and really stick within that. You can expand your circle of competence by research and learning and talking to people, but it does take time and effort.

Cathryn:
Yep.

Kate:

Awesome. So now we've covered a little bit about what Disney does as a business, and some of the different revenue sources. I think it's time to talk about step two on our checklist, which is who runs it? And what is the management team behind it? What are their incentives? The board. Even looking at the foundational roots of Disney. In preparation for this episode, I got a bit distracted and started listening to this podcast about the foundation of Disney, and trying to build EPCOT Theme Park and the future of tomorrow world. And it was just fascinating to read a bit more about the roots. But Cathryn, are you able to talk a little bit about why it's important to look at the management team and board and their track record?

Cathryn:
Yeah, of course. So with management, what we're basically looking at is incentives, track, record and pedigree. So in terms of track, you can do a quick Google search, or check their LinkedIn profile for their past experience. And ideally, what we want to see is relevant industry experience, experience at notable companies, experience in a similar role, things like that. So for example, the analyst team and I were looking at a company yesterday and it had a CEO who previously ran a different business that went into administration, so that would be a red flag. We also like companies that are run by founders, because the company is essentially an extension of themselves. It's pride as well as salary on the line. So I know for example, Owen with Rask, he owns a big chunk of the business, his name's on the door and you see each day he just works so hard.

Kate:
Yeah. There's just a different kind of work ethic there, if you are the founder and the person running the company.

Cathryn:
Totally.

Kate:
Yeah. So sadly we can't resurrect Walt Disney from the dead. But what are some of the ways that we can look at the incentives as well?

Cathryn:
Yep. So in terms of incentives, we're looking at how the management team are incentivized. So as potential shareholders, we're investing for the long-term, and we want to make sure that the person running the business is aligned with shareholders and has a similar long-term mindset. So with incentives, one of the things we look for is skin in the game, which essentially just refers to whether or not management own shares in the company that they run. So, as the saying goes, CEOs of public companies will only buy shares in the company for one reason, i.e. they think the share price is going to go up, but they'll sell their shares for many.

Cathryn:
So ideally, you want your CEO and management team to own lots of shares in the company that they run, because having their own wealth tied up in shares of the company, it should compel

them to work harder and to do the right thing for the company and for shareholders over the long run.

Kate:
Yeah. And I know on the selling side, people read a lot into the reasons why directors and CEOs sell shares. They often write in their releases that it's for tax reasons.

Cathryn:
Classic.

Kate:
So it's always interesting there of what sales are important to take note of, and what are more of maybe they're just buying another home or something like that.

Cathryn:
A boat.

Kate:
Yes, a boat. Great tax haven there. So if we want to apply this thinking to Disney's management team, what are some of the things that you looked at in your research there?

Cathryn:
So looking at the management team at Disney, I think the name that most people would be familiar with is Bob Iger. So Bob became the CEO of Disney in 2005, but he'd been working for companies that are now part of Disney since the 1980s. So with Bob, you've got a person with a wealth of industry experience and a tremendous track record. So he oversaw the acquisitions of Pixar, Marvel, Lucasfilm, 20th Century Fox, and he's also got plenty of skin in the game. So he holds around 1.3 million shares, which based on the current share price of around $180, it's worth around $240 million.

Kate:
Oh, so he's got a little nest egg there.

Cathryn:
Just a little bit. Yeah. So last year, some people might remember that Bob stepped down from the CEO position and is now on the board, and another Bob, Bob Chapek replaced him. So this was an internal hire. He'd been part of Disney's succession plan. And he's been with Disney for about 30 years, across different parts of their business.

Kate:
So they seem to really favour hiring people internally, that have been working with them a long time.

Cathryn:

Yes. Which makes sense for a company like Disney, which does so much and has so much going on under the hood.

Kate:
Yeah. It probably takes a decade to just understand all the different aspects of the business.

Cathryn:
Yeah. I think they've only been maybe six or seven CEOs in Disney's history.

Kate:
Yeah. Yeah. And so in terms of incentives, I don't know if you had to look at what his salary is?

Cathryn:
Yeah. So a quick calculation you can do is assessing a CEO's shareholding relative to their annual salary. So for example, Bob Chapek, he held nearly 13,000 shares at the beginning of this year, and he has an annual base salary of about 320K. So his shareholding represents around eight times his annual income, so It will take him about eight years to earn a salary equivalent to his shareholding.

Kate:
Wow.

Cathryn:
Yeah. And another thing you can do, just to be mindful of, is how the CEO is paid. So in Bob's case, just 10% of his salary is fixed, which is that 320K, and the remaining 90% is tied to performance, which creates even more alignment for shareholders, because it means he has to perform well, otherwise he forgoes that 90% of his income.

Kate:
Does he get paid that additional money for performance in shares? Or just-

Cathryn:
It's a mix. Yeah. Shares, bonuses, stock options.

Kate:
Yeah. Okay. So he does have quite a few incentives to keep working. It's definitely very interesting, especially for him following such a legendary CEO, who's really made his mark in the world and on the company.

Cathryn:
Big shoes to fill. Yeah.

Kate:

Yeah. Okay. So now that we've had a look a bit about some of the incentives and why it's important to look at the management team and the board, let's look at Disney's moat. So that's the third part of our checklist. And we'll start with just an overview of what is a moat again.

Cathryn:
Yeah. So a moat is basically a competitive advantage. So it's a way that a company can fend off its competition. And the analogy comes from back in the old days with medieval castles, there's that little ring of water that runs around the outside of the castle, to try to make it harder for enemies to attack. So in terms of business moats, there are many different types. For example, there's brand. So you think Nike, Louis Vuitton, they essentially sell the same product, but their brand is what you're paying for.

Cathryn:
There are also things called switching costs, so the cost of switching over to a competitor. For example, I use Spotify. I've used Spotify for many, many years now. It's got all my playlists, all my saved songs, it knows my own music tastes and can recommend me new songs, new playlists. So even though I am a huge Apple fan, I still haven't switched over to Apple Music. So that's an example of switching costs.

Cathryn:
There's also a thing called network effects, where a platform or a service becomes more valuable as more people use it. So perhaps I think the pioneer of this would have been Facebook. So the more of your friends that joined Facebook, the more valuable it is to you, because you can interact with more of your friends, you can message them, all sorts. Another example would be Afterpay. So the more merchants that offer Afterpay, the more valuable it is for you as a consumer, because you have more choice.

Kate:
It's a bit of a cycle there, because as more people start using Afterpay, more shops start offering Afterpay, and suddenly every business in Australia is offering Afterpay as an option. I saw the other day that Airtasker was offering you the ability to Afterpay finding someone on there to mow your lawn or something like that. It's amazing how many places are using it now.

Cathryn:
Totally. Yeah.

Kate:
All right. So we've had a look at just a bit of revision on what is a moat. I think the next thing we need to look at is what actually makes Disney's stand out from its competitors, and what is Disney's moat? And what stops other brands from coming across the water and attacking Disney's castle?

Cathryn:

Yeah. So the big one for Disney would be its brand and intangible assets. So the stuff that you can't physically see, but the licences, the patents, the goodwill. So obviously Disney is such an iconic brand, it's something that everyone would have likely grown up with in their childhood. There's the emotional tie. And then in terms of licences, Disney owns the rights to every Disney character, every Marvel, Star Wars, Pixar.

Kate:
A lot. A lot there. And I mean, just building their theme parks, the sheer scale and volume and how they've been built over decades. For someone to actually try and replicate that, it would be almost impossible.

Cathryn:
Definitely. Yeah. Another one is also, as you were saying, scale. So just the sheer size of the business. They've got huge production capabilities, thousands of employees. And that also leads to diversification across all of its different product lines. So last year, the theme parks, cruises had suffered during COVID, but streaming services offset a lot of that weakness.

Kate:
And I know you had a look at how many employees they have.

Cathryn:
Yeah. I think it was about 220,000 pre-COVID, so a huge number.

Kate:
Yeah. I think we had a look. They had to lay off a few people, a few tens of thousands of people from the theme parks when they were closed last year, because you just can't keep paying for all your Mickey Mouse actors while there's no theme park open. But I think Disney's a resilient business, that will keep popping back up no matter-

Cathryn:
Yep. Stood the test of time.

Kate:
... what happens. And what about stickiness? I know you talked a bit about brand will, but how does Disney stand out there?

Cathryn:
Yeah, so I think especially for it's Disney+ streaming services, it's just getting harder to give it up. So the more content it adds... I think there's a new thing called Star.

Kate:
Yeah. It had a recent integration, so added heaps of new shows.

Cathryn:

So the more content it adds, it's just harder to give it up. So switching costs become higher, and the product just becomes even more stickier.

Kate:
I think Disney+ is a really valuable part of their business, that they only launched last year, but I think it's doing really well for them.

Cathryn:
Yeah. It's growing at ridiculous numbers.

Kate:
Yeah. And they increased the price, didn't they?

Cathryn:
Just a little bit.

Kate:
Just a little bit. I'm currently on a TV break, but I have spent a lot of time watching different shows on the app, and they're not all Disney shows anymore, you've got a lot of different options. So it's very exciting. And I also thought the interesting thing they're doing is premiering their new movies. So you could pay to see it in the cinema, but you could also use the app and you could pay an upgrade cost to actually watch the movie on your TV. And you could gather a group of friends to come and watch the premiere together in your home, which is quite a cool thing.

Cathryn:
Yeah. I think Mulan was one of the first movies they trialled that on.

Kate:
And it gives them another option to then just doing a cinema release, which adds to diversification of revenue.

Cathryn:
Definitely.

Kate:
Okay. So now we've talked a little about Disney's moat, which I think is pretty big. Let's talk about whether Disney's in a growing industry. And these questions maybe a little bit harder to answer than some smaller companies that we might discuss, because they've just got so many revenue lines and different companies underneath, that all sort of fit into different industries. But what was your initial thoughts when you did research on whether Disney's in a growing industry?

Cathryn:

Yeah. So the first thing that you look at is go through management presentations. So they'll often quote our TAM or total addressable market, and they'll give you a figure. And then you can cross reference that with industry reports. So there's companies like IBISWorld, Gartner, Statista, to try to back up those figures. But with Disney, in order to see growth, again, you can look at their segment report, and you can see the revenue growth of each different division.

Cathryn:
So for example, last year, the media networks division grew by around 14%, but this was mostly due to the acquisition of 21st Century Fox, which boosted the numbers a bit. Then the studio entertainment business, it fell by 13%, because no one was able to go to the movies. Parks and products division fell by 37%, which is probably more resilient than I expected, except it's also important to note that Disney's financial year runs to the end of September, so it would have included around five months of pre-COVID activity. But yeah, the shining light here really is the streaming services. So it jumped by 81% revenue, and it's clear to see that this is the growth driver behind Disney going forward.

Kate:
And they're just getting started there, aren't they?

Cathryn:
Yep.

Kate:
Yeah. So what about some important industry figures to look at? If you want to do a bit of a research comparing Disney to some of the other companies in the industry, how do you go about that?

Cathryn:
Yep. So just a couple of figures that I've found, you can just... Google is your best friend here. But pre-COVID, the film industry had been consistently generating even more revenue each year. And in 2019 hit a record $100 billion. But obviously with COVID, it's hit a bit of a snag. And same with the parks division. Even though Disney is generating quite a lot of money from its merchandise licencing and retail business, with the parks still closed, that's still going to be a drag on sales. But in terms of the streaming services, the company has around 95 million Disney+ subscribers, 35 million Hulu subscribers and about 12 million ESPN+ subscribers.

Kate:
So quite a few people there.

Cathryn:
Yep. And they're growing at really fast, high double digit growth rates.

Kate:

Yeah. So when you're researching the company and you can see how many different industries Disney companies fall into, they've got the cruise line, which that was obviously stopped last year, but that falls into a different industry to their streaming service, to maybe their movies, which are slightly different. Would you break them all apart and compare them to their competitors individually? Or did you find something to compare Disney to as a whole?

Cathryn:
With Disney, it's pretty tricky just because it does so much across movies, TV, streaming services. There are a lot of companies that just does one of those things. So obviously you've got Netflix, in terms of the film production there are many different filming studios. But I think the closest competitor listed would be ViacomCBS. So it's listed on the NASDAQ, and it's the company behind Paramount Pictures, Nickelodeon, plenty of TV networks, like Showtime, CBS, MTV, Comedy Central. And people might remember that last year, Channel 10 was bought out by CBS. So this is the company behind it. So yeah, it's one of the companies you can use as a comparable, but there's no real comparative company to Disney.

Kate:
Yeah. I think that we did pick a challenging one in the fact that it's so big, but I guess it makes it a little bit more fun to research and have a look at, just because it's got so many different segments. But that I guess leads to its diversification of revenue streams, and it helps the business be more resilient, because they're not just doing one thing.

Cathryn:
No.

Kate:
Yeah. So I know that we've looked at some of the different divisions, we've looked at some of the numbers. So to sum all that up, do you think Disney is a growing company?

Cathryn:
Yes, I would say so. It's been around for a very long time. It's proven that it can innovate and that it can get on to the next big thing. And in terms of streaming, streaming is here to stay. It's going be big.

Kate:
Yeah. And they're quickly iterating. I mean they brought Disney+ in to start to compete there. And I think that was a great move launching it at the start of COVID last year. I don't know if they planned that or not.

Cathryn:
I don't think so.

Kate:

Surely they've probably spent a bit of time building the infrastructure out, but that was really good to see. And even if some of their revenue lines, like the cruising and the theme parks, were halted last year, they've got plenty of other revenue sources to help them keep growing over time.

Cathryn:
Yeah. Another thing he is also when a big thing happens, it's important to note whether it's a structural change or whether it's a temporary setback. So in the case of COVID, I think it's more of a temporary setback, in terms of parks will eventually reopen, everyone will flock back to Disneyland, go on Disney Cruises, stay in their resorts, and so on.

Kate:
Yeah. Yeah. It's interesting. It's good to think about whether people still want those businesses once they come back. And I'm sure that people will still want to go to theme parks and things like that. All right. So the final part of our checklist, and I'm sure the part that everyone's most excited about, is what's Disney actually worth, AKA what's their valuation? So let's do a bit of a revision on valuation, Cathryn.

Cathryn:
Yeah. In terms of valuation, there's a saying that goes around where price is what you pay, value is what you get. So the price is what's on offer to you as an investor. And if you've got a value in mind, which is informed by your research and your analysis, you can then determine whether that's a fair price to pay. So for example, a Disney+ subscription is now $12, I think.

Kate:
Yeah. They recently raised prices.

Cathryn:
And if you like Marvel, Star Wars, National Geographic, you might determine that the value of the subscription to you is worth more than the $12, so you happily pay it. But if you don't really care about Marvel, you don't have kids who are interested in Disney Pixar, the value of the subscription might be less than $12. So what you value it at determines whether or not you purchase it.

Kate:
Yep. So how do you move from that mindset of just comparing the value of something as a consumer? So I'm looking at the Disney+ subscription and going, "Hey, is that going to be worth my $12 each month? Am I going to get enough value out of it?" Or if I was looking at Disneyland, "Hey," I don't know, that's probably like $100 or $200 because that's a bit more expensive, "but is the value I'm going to get from the rides and the experience and the magic, is it worth the cost?" So, how do you move from that consumer valuation mindset to actually valuing business as a whole company, where there's so many other investors out there and all these millions of consumers around the world?

Cathryn:
So the only real difference between investing and consuming is that there are formulas for valuing businesses. And you're following the whole company, not just you or I think the thing is worth. So one way to look at valuation is to look at ratios. It's just a very simple way to look at it. And there's something called the P/E ratio or the price to earnings ratio. And it compares a company's share price to its earnings per share. So earnings, profit, income, it all means the same thing. And you can find this in a company's annual report. So just how much profit it makes each year. And you divide that by the number of shares.

Cathryn:
So the P/E ratio is basically looking at how much a company is worth or the share price relative to how much money it makes. So when you look at P/E ratio, it's common for people to use the metric and say, "Okay, the P/E ratio is high, that means that a company is expensive." And I say that in quotation marks, expensive, because often a high P/E ratio implies that it's a growth company, it's focused on growth. Whereas something like say Woolies or Coles, they'll have a P/E ratio that's much lower because it's more of a blue chip dividend play as opposed to a growth company.

Kate:
So when people say, "Buy stocks that have low P/E ratios," what do you say to that?

Cathryn:
I would say that it's not a hard and fast rule, and it's important to compare apples to apples. So if you're looking at a growth company, you want to compare the P/E ratio to other similar growth companies and not comparing Afterpay to Woolworths, for example.

Kate:
So did you find out Disney's P/E ratio in all of this?

Cathryn:
Yes. So interestingly, Disney did not make a profit last year. So that's where this metric falls down. Without a profit, you can't get the P/E ratio. But what you can do, is you can do a forward P/E ratio. So the estimate of what forward earnings this year, what the earnings will be. So if you just go onto Yahoo! Finance, you'll be able to see the forward P/E, which currently says 38 times. And this is quite a bit higher than I think Disney's historical P/E ratio of around 20. So that's pricing in quite a bit of growth for the subscriber streaming channels, I would assume.

Kate:
I know everyone's very excited about that at the moment. So if you can work out the P/E ratio, is it something you should rely on when you're working out valuation?

Cathryn:
It's definitely an easy and quick way to just get a sense of how the market feels about a company. In Google Finance, it's often one of the first things that you can see, but I definitely

wouldn't use it in isolation. So it's important to use some other different tools, which I think Owen and Kevin will go into next week, just to get a better handle on valuation.

Kate:
Okay. Awesome. So I think that about wraps up point five of our checklist. So we have covered a lot in today's episode, and I'd really encourage you to do some research on Disney, read the annual report, read some of their key financials. And try and explore each of these numbers yourself, and see if you can find these numbers. And you can do a bit of Sherlock Holmes-ing and detective work on your own.

Kate:
So just to summarise some of the key points we covered today and what Cathryn spoke about, firstly, we looked at what Disney does and just the sheer number of companies underneath it. And I think it's really interesting to look at all the different industries it has its fingers in there.

Kate:
And then secondly, we looked at how the company's run. We looked at the current CEO and management team, and how they're incentivized, what their salary is, how many shares they have in the company, and that's really important as well. And having a look at their track record, whether that's on LinkedIn or previous interviews, seeing what the CEO and board have done prior to this.

Kate:
Then thirdly, we looked at what Disney's moat is and how it's different from its competitors, and how all the different aspects of Disney help it survive and thrive in the long run.

Kate:
Then fourthly, we had to look at whether Disney's in a growing industry, and it's got so many different parts of the business, so it's a bit hard to work that one out. But actually, just sort of looking at each different section of the business, and whether that's growing into the future, and what are the new aspects of the business they're adding on?

Kate:
And then finally, we had to look at what the company's worth. And we talked about one potential option that you can use to look at, which is the price to earnings ratio. And we actually have a tutorial of that on Rask Education, so I'll include that in the show notes. I think there's a video as well, so you can have a look into that there.

Kate:
All right. So I think we made it to the end there, Cathryn. You came on your very first podcast.

Cathryn:
I did. We made it.

Kate:
You made it. So this is the first time we've done this, so definitely let us know your thoughts. And don't forget, this episode is part of our five-part share month series. So if you have any questions after today's episode, or if you try to do some of this research on your own, you come across a roadblock, send them into us at podcast@rask.com.au, and use the subject line shares month. And we'll include those questions in our upcoming shares Q&A episode, where I'll be with three other share analysts. I'll be the only one that's not an analyst in the room, so we'll see how that goes. But we'll try and answer as many questions as possible. So definitely let us know your feedback after this episode, and we really hope you enjoyed it. And thank you, Cathryn, for joining me.

Cathryn:
Thanks, Kate. Thanks everyone for listening.

Kate:
Thanks for tuning in to this episode of The Australian Finance Podcast, where our mission is to improve the financial futures of all Australians. If you'd like to learn more, create a free account at rask.com.au/account, to download free episode workbooks, bonus resources and take our amazing, free personal finance courses.

Speaker 1:
You can also join our online community by following the link in the description. If you enjoyed the show, what we'd love is for you to leave us a snappy review on iTunes. And you can follow us on Twitter and Instagram @RaskAustralia. Kate and I are also on both of those channels. Finally, if you have any feedback, suggestions for episodes or guests to come on the show, or you just have a question for us, shoot us an email at podcast@rask.com.au.