MOI GLOBAL

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Chief Investment Officer, Silver Ring Value Partners

WIDEMOAT Investing Summit

SILVER RING VALUE PARTNERS

DISCOVERY COMMUNICATIONS (DISCK) WIDE MOAT 2019, HOSTED BY MOI GLOBAL

Gary Mishuris, CFA | Managing Partner, Chief Investment Officer

BIOGRAPHY

GARY MISHURIS, CFA

Managing Partner,
Chief Investment Officer

Professional Experience:

- Silver Ring Value Partners (2016-present): Managing Partner, Chief Investment Officer
- F.W. Olin Graduate School of Business (2018-present): Instructor, *Value Investing Seminar*
- Manulife Asset Management (2011-2016): Managing Director, Lead Portfolio Manager of the U.S. Focused Value strategy
- Evergreen Investments/Wells Capital Management (2004-2010): Vice President, Senior Equity Analyst/Portfolio Manager
- Fidelity Management & Research (2001-2004): Equity Research Associate

Education:

Massachusetts Institute of Technology
Bachelors of Science in Economics, Computer Science (2001)

OBJECTIVE AND STRATEGY

The Fund seeks to compound capital over the long-term through a concentrated portfolio of well-researched securities.

Why Silver Ring Value Partners:

Competence:

Time-tested intrinsic value investment philosophy and process that have generated good results in the past.

Alignment:

Structured so that the investment manager can only build meaningful net worth if the clients do well over a number of years.

Passion:

Motivated by the intellectual challenge of investing and the desire to make a positive impact on others.

COMPETITIVE ADVANTAGE

Long-term Time Horizon – ability to take advantage of market inefficiencies

Limited Asset Base to preserve the ability to invest in the most inefficiently priced securities

Micro-Economic Focus – concentrate on opportunities where the key drivers of investment success are company- and industry-specific factors

Temperament to consistently implement a rigorous value investing process developed over fifteen years of professional experience

INVESTMENT PHILOSOPHY

- **Intrinsic Value:** A stock is a partial ownership interest in a business with its worth determined by the underlying business's long-term economics.
- **Margin of Safety:** An investment's margin of safety is determined by the combination of the *quality* of the underlying company and the discount from a conservative appraisal of intrinsic value offered by the *price*.
- **Long-term Time Horizon:** The focus is on achieving the best possible *compounding of capital* over a period of many years rather than managing short-term volatility of returns.
- **Rational and Disciplined Execution:** The market occasionally misprices securities for behavioral reasons. These arise due to market participants reacting to developments emotionally rather than rationally and to some market participants' misaligned incentives. By remaining rational and disciplined in the implementation of my process, I can both take advantage of the market's mistakes and guard against making mistakes of my own.
- **Concentrated Portfolio:** Investment opportunities that combine a company of high quality with a price that is at a material discount to intrinsic value are infrequent. After constructing a portfolio where being wrong on any single judgment should not result in a material loss of principal for the portfolio as a whole, additional diversification is more likely to increase rather than reduce risk by forcing the inclusion of increasingly inferior investments.

MENTAL MODEL

- **Common investor thinking when a stock goes up significantly that they didn't buy (or sold):**
  - "I missed it, it's too late to buy now"
  - **"The easy money has been made"**
- If there has been material positive change in the business or new evidence that the thesis is tracking, then that thinking can frequently be a *behavioral mistake*.
- The correct way to think in such a situation is **"The *hard* money has been made**, let me re-examine the current relationship between price and value."

DISCOVERY COMMUNICATION (DISCK) INVESTMENT

Original Investment

- Increased to a 10% position on November 22nd, 2017 and hedged with long-term put options (for reasons explained in the original presentation included in the appendix)
- Results so far, through June 25th, 2019:

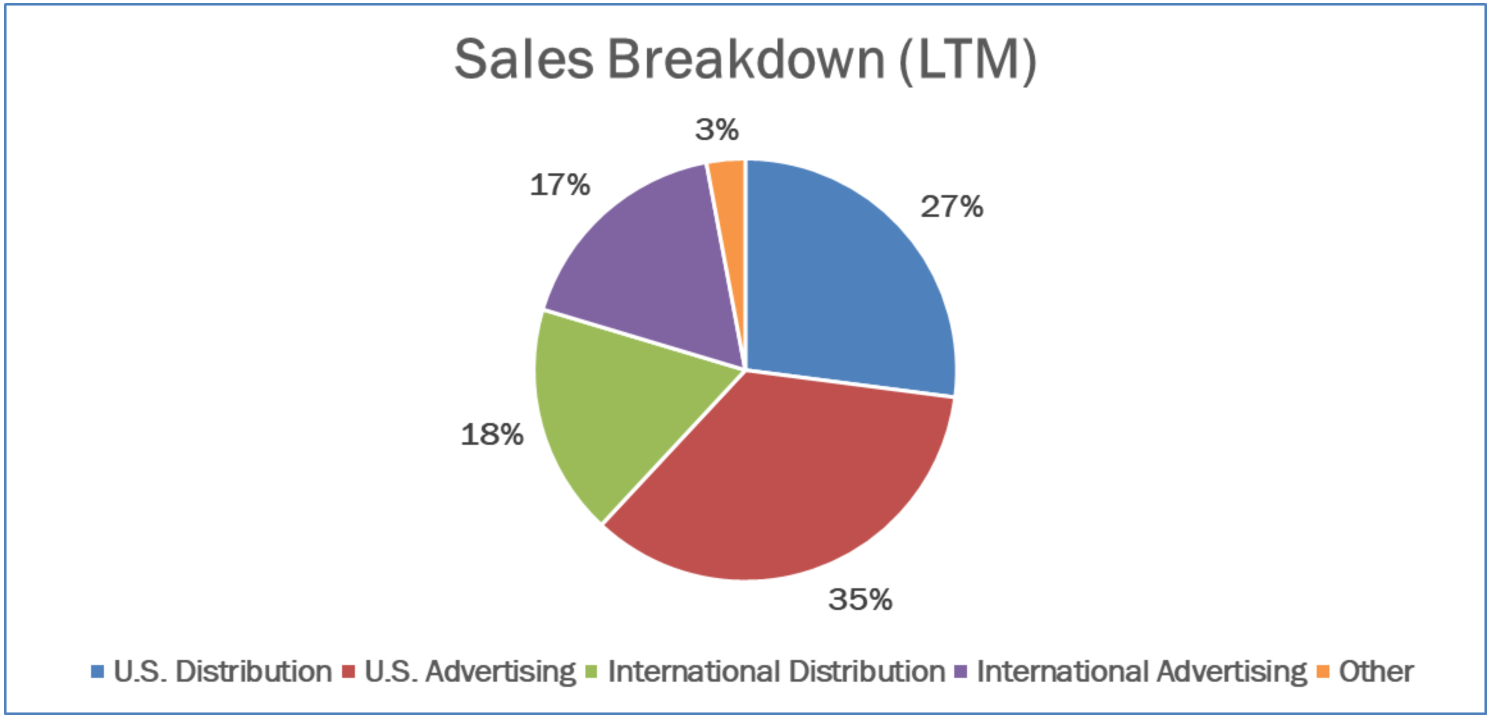
Discovery Communications (DISCK) Results So Far			
Position Size	Original Price	Price on 6/25/2019	Total Return
Discovery Communications (DISCK)	$16.77	$27.57	64%
Put Option (Jan 2020, Strike = $15)	$3.24	$0.10	-97%
Hedged DISCK Investment	**$20.01**	**$27.67**	**38%**
S&P 500 Index			16%
Hedged DISCK Investment minus S&P 500			**22%**

- The point is *not* the results. The point is that I believe Discovery to be a *better* investment today than it was in November 2017!

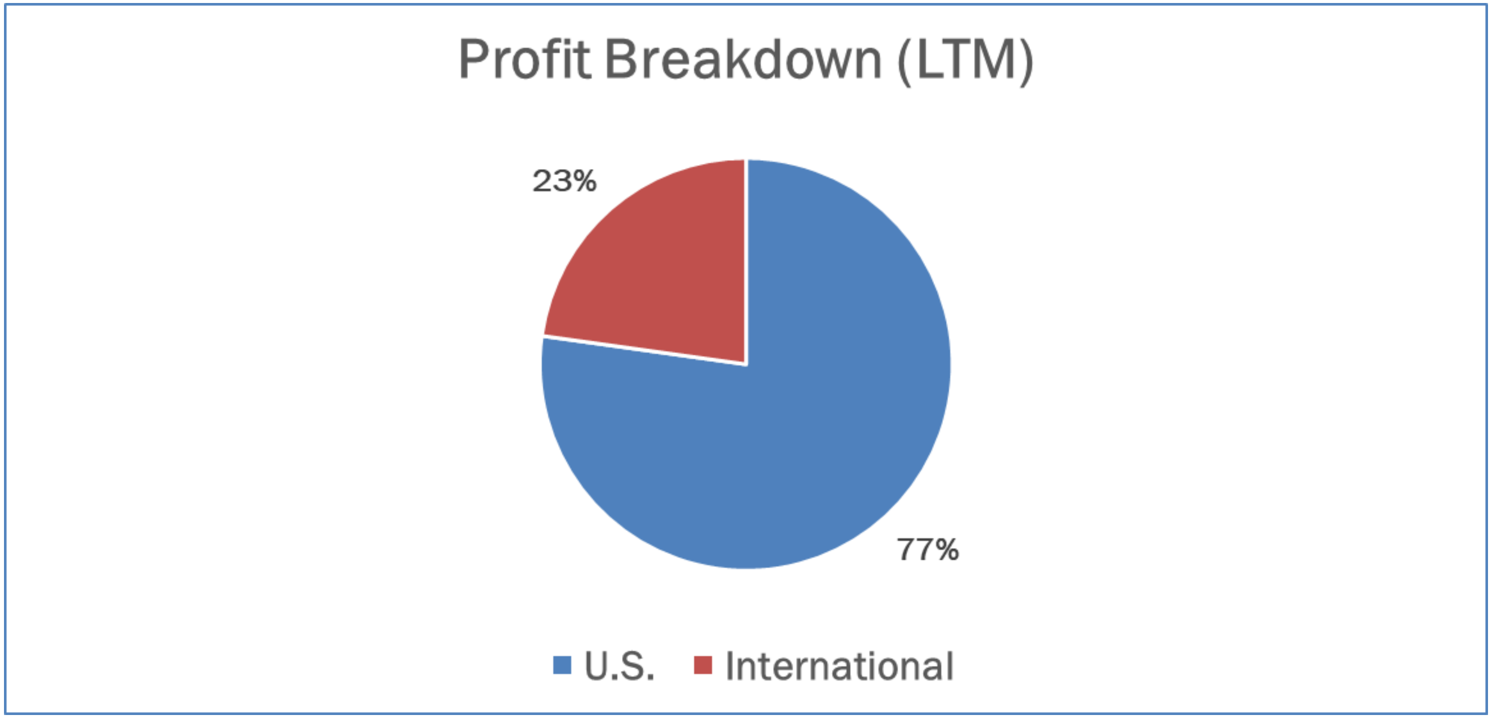
BUSINESS OVERVIEW

- Global cable network operator focusing on non-fiction content; owner of Discovery, HGTV, Food, Travel, Animal Planet, TLC and Eurosport networks; ~ 20% share of U.S. Cable TV viewership
- Three sources of competitive advantage: Brands, Library of Content and Distribution
- Revenues come from both advertising (cyclical) and affiliate fees (not cyclical, long-term contracts)
- Inelastic demand results in pricing power on both sides of the business

BUSINESS OVERVIEW



BUSINESS OVERVIEW



RISKS

- Risks in November 2017:
  – Secular erosion of core business due to consumers opting out of cable bundles and reducing their consumption of traditional TV programming
  – High financial leverage + tightening covenants following acquisition of Scripps Networks International
  – Deal integration risk, such as culture clash and departure of key personnel, following acquisition of Scripps Networks International

RISKS

- Risks in June 2019:
  - Secular erosion of core business due to consumers opting out of cable bundles and reducing their consumption of traditional TV programming
  - ~~High financial leverage + tightening covenants following acquisition of Scripps Networks International~~
  - ~~Deal integration risk, such as culture clash and departure of key personnel, following acquisition of Scripps Networks International~~

RISKS

High financial leverage + tightening covenants following acquisition of Scripps Networks International

– Debt/EBITDA was close to 5x post deal-close in 2017, with covenants not too far away (5.5x and tightening)

– Debt/EBITDA = 3.8x as of Q1 2019, on track to be under the target of 3.5x, which maps to an investment-grade rating

– Option-adjusted spread on Discovery's *30-year* bond is ~ 240bps

RISKS

Deal integration risk, such as culture clash and departure of key personnel, following acquisition of Scripps Networks International

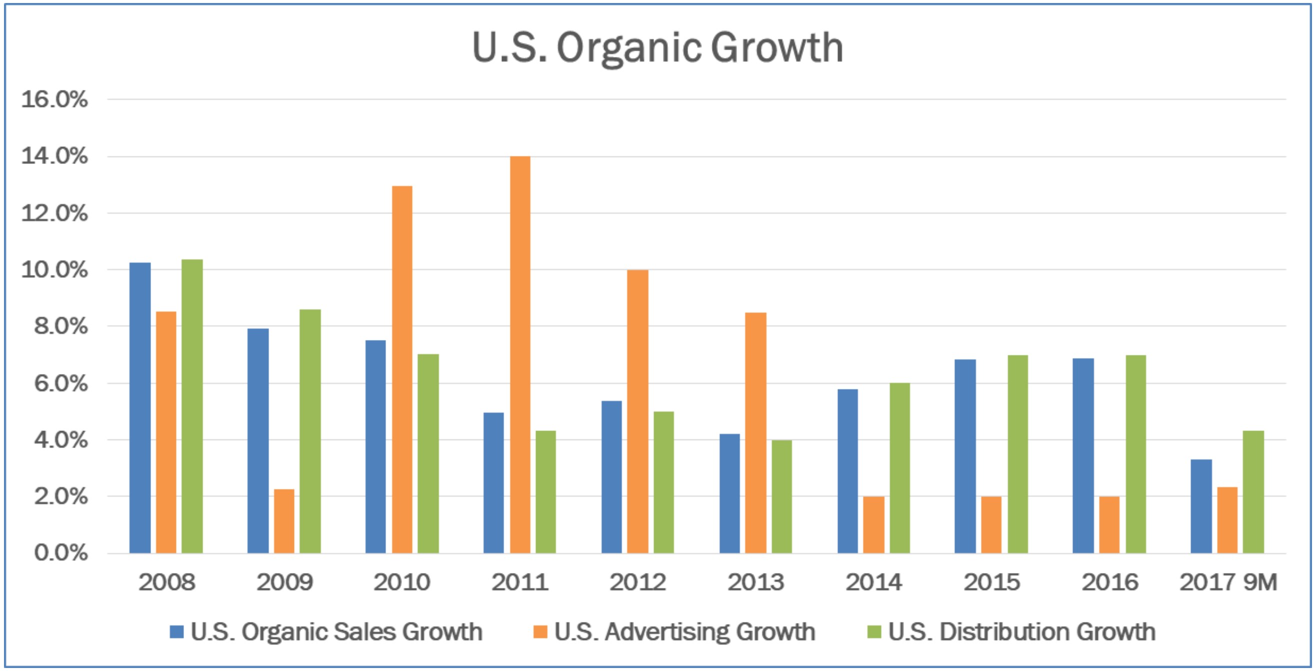
- Management installed a number of ex-Scripps executives in senior roles
- No evidence of meaningful unwanted departures or other cultural issues
- No evidence of other integration issues
- Cost synergy targets exceeded
- If there were material integration issues, the odds are good we would have seen their impact ~ 2 years out from deal close

RISKS

Secular erosion of core business due to consumers opting out of cable bundles and reducing their consumption of traditional TV programming

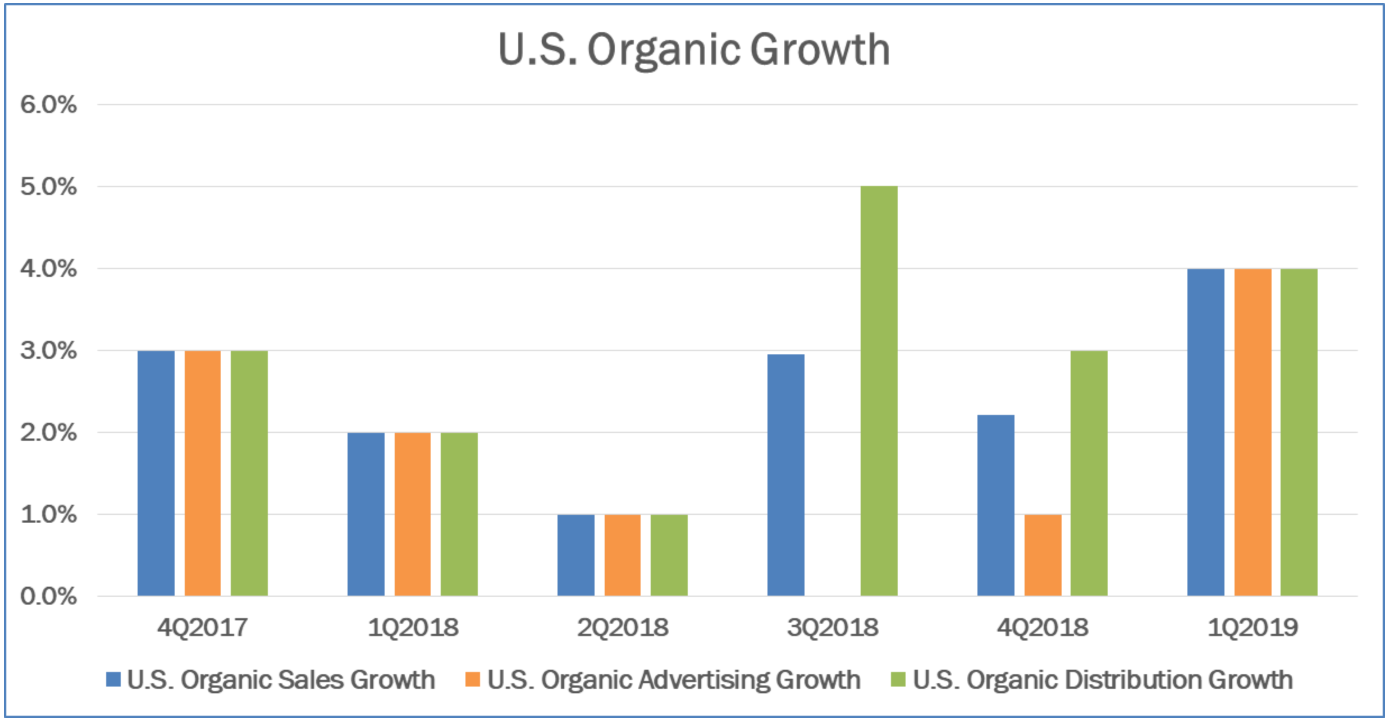
- Thesis has been (and is) that inelastic demand leads to pricing power which allows the company to grow revenues despite moderate declines in ratings and subscribers
- Company has gotten on all material distribution platforms at attractive economics since the deal closed
- Organic revenue growth has been positive in the U.S. despite declines in ratings and subscribers

GROWTH



- Growth at the time of the original presentation

GROWTH



- Single digit positive organic growth in the U.S. despite low single digit subscriber declines and mid/high single digit ratings declines

GROWTH

- Growth at the time of the original presentation

GROWTH

- Low single digit organic growth internationally
- 1Q 2019 declines due to comparisons vs. prior-year Olympics, would have been + low single digits otherwise.

VALUATION

“We don't use complicated valuation models because we want investments that are so obvious as to not need one.”

- Warren Buffett

VALUATION

- Discovery earned ~ \$3.40 in Free Cash Flow per share in 2018
- 2019 should be somewhat higher
- At < \$28/share the stock is at ~ 8x FCF/EPS
- Leverage is at sustainable levels
- FCF/EPS is likely to grow moderately over time

VALUATION

- Updated DCF value range: \$13 (worst) - \$47 (base) - \$78 (best) vs. price at \$28
- Base Case implies 12.5x normalized forward EPS/FCF
- If you were to buy the whole business, hold it forever and I were correct on my Base Case scenario, your IRR would be ~ 16%

VALUATION

- Still large downside as secular threats have not been completely disproven (although probability is lower now than in 2017)
- Bundle can still break in the U.S. at some point
- Earnings/FCF need to be adjusted for the advertising revenues being above mid-cycle due to where we are in the economic cycle

CURRENT RISKS

– Secular risk still exists
– Risk that company goes on a large shopping spree vs. buying back shares
– CEO who is very promotional in his communication – risk that there are hidden problems that I don't know about

POSITION SIZE

- Large position for the partnership
- Hedged with 2020 put options with $27.50 and $25 strikes which I switched to from lower strike put options as the stock went up to manage risk
- Will need to reconsider position size in 2020 if price to value gap does not close as reasons for hedging now less compelling than they were originally

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APPENDIX

Original Presentation on Discovery Communication (DISCK) as presented at the MOI Global Best Ideas 2018 conference in January 2018

INVESTMENT PROCESS

Thesis Summary

Discovery Communications is undervalued because:

1. The company has a meaningful competitive advantage based on its **brands, distribution** and **content library**
2. The market is correct about the presence of secular challenges in the US media market, but is wrong about their magnitude, in part because it **underestimates the company's *pricing power***
3. The market is underestimating the long-term resilience and growth potential of Discovery's international business
4. The announced Scripps Networks (SNI) acquisition does pose meaningful risks, but at the same time if it is successful it is likely to meaningful increase the company's competitive position, earnings power and value per share

On a standalone basis, when I made Discovery Communications (DISCK) a 10% position in November, it was trading at under 40% of my Base Case value estimate, but with over 50% downside to my Worst Case estimate (which includes an unfavorable outcome of the SNI acquisition). Because of this, I structured the investment in combination with a $15 January 2020 Put option. This gave up some expected return, increasing the **Base Case price to value relationship from 39% to 46%, while at the same time substantially reducing the downside to the Worst Case to a more manageable 25%.** Given that the next two years are very likely to resolve the success or failure of the SNI acquisition and the company's ability to de-lever, and somewhat likely to give us material information on whether we are right on the magnitude of the structural issues facing the industry and the company, the Put option makes sense in this situation as it is a **one-time insurance against a specific adverse outcome** rather than an ongoing cost of the position. As a sanity check, **the stock + the Put option combination were trading at under 7x my estimate of 2020 post-integration EPS,** a point in time during which the company should be at a sustainable level of financial leverage and from which is should be growing its profits.

At current prices, with the stock having risen ~ 30% to $22, the investment is still very attractive, although choosing the $20 strike price instead of $15 for the Put would bring the magnitude of downside to similar levels as the original investment.

INVESTMENT PROCESS

Security Research and Valuation

Five-Step Research Process

Step 1	Step 2	Step 3	Step 4	Step 5
Company Quality Assessment	Analysis of Key Economic Variables	Financial Modeling	Valuation	Behavioral Checklist

The goal is to answer the following two questions:

- How predictable is the long-term economic outcome of the business?
- What is a reasonable range of intrinsic values?

INVESTMENT PROCESS

Security Research and Valuation

Step 1 **Company Quality Assessment**

- **Business Quality** – industry's structural attractiveness and company's sustainable competitive advantage
- **Management Quality** – track record of operations and capital allocation as well as alignment of incentives
- **Balance Sheet Quality** – ability to withstand temporary adversity without reducing security value

INVESTMENT PROCESS

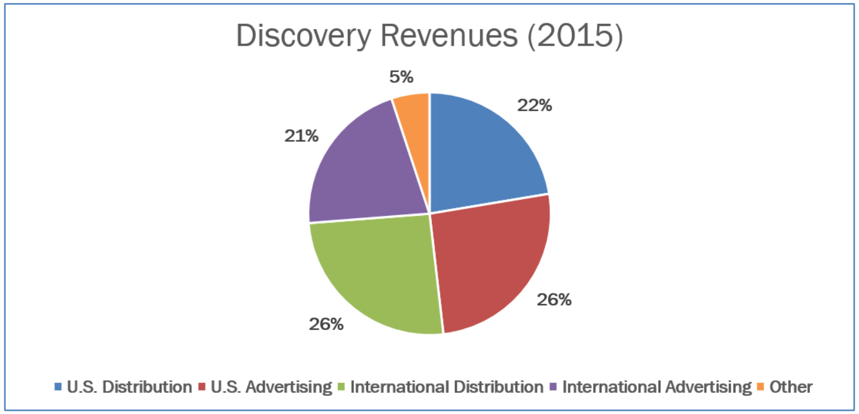
Business Quality: Company Description

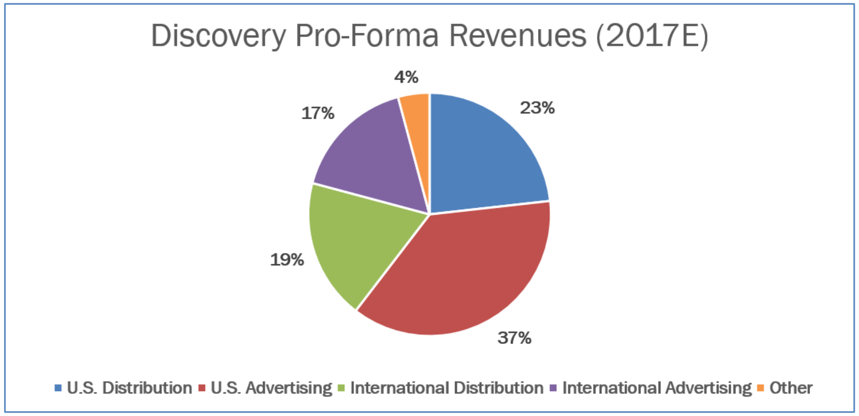
Source: Discovery 2017 Scripps Merger presentation

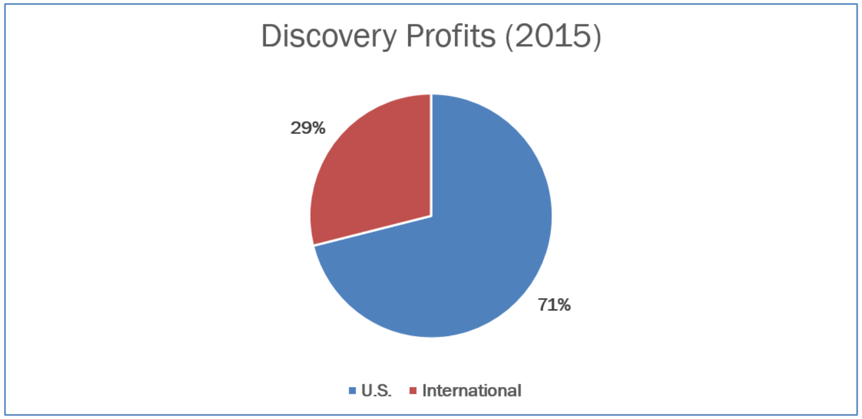
Discovery is a global cable network company focused on non-fiction content

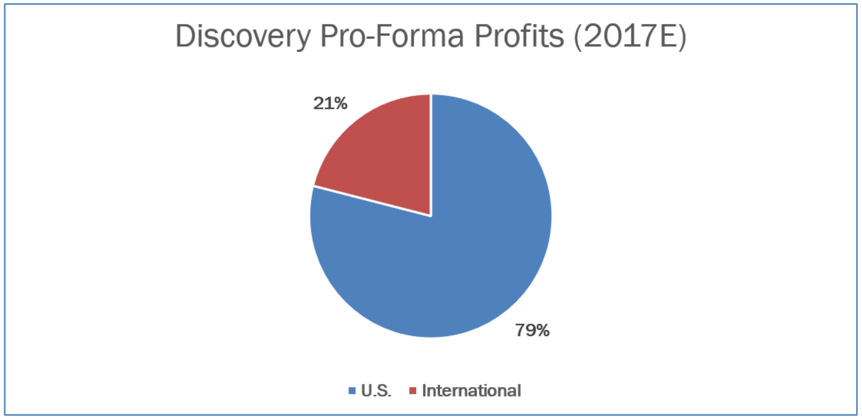
INVESTMENT PROCESS

Business Quality: Company Description









Source: Company Reports

INVESTMENT PROCESS

Business Quality: Structural Industry Attractiveness

Porter Forces Analysis: TV Video Content Industry

Barriers to Entry: Medium

- Distribution with Pay TV providers
- Capital and time to create compelling content
- Brands to consistently attract audiences

Power of Suppliers: Low/Medium

- Most talent and service providers have low differentiation and are easily substitutable
- Key sports leagues have strong bargaining power
- High profile talent has bargaining power by commanding inelastic viewer demand

Competition: Medium

- Competition is predominantly based on differentiation of content, not on price
- Distributors typically sign 5-7 year carriage deals with automatic price escalators
- Desirable unique content creates inelastic demand and strong pricing power

Power of Buyers: Medium

- Pay TV distributors have some bargaining power, but less than that of Content Providers
- Distributors have been consolidating, increasing their bargaining power
- There is less differentiation among distributors than content providers, and each market has 3-4 comparable distributors

Threat of Substitutes: Medium

- Improved Internet availability and speeds are lowering the barriers to alternatives such as Netflix and Amazon Prime Video
- Increased availability of other media such as Internet, mobile technologies

Conclusion: Video Content industry is of **Above Average structural attractiveness**

INVESTMENT PROCESS

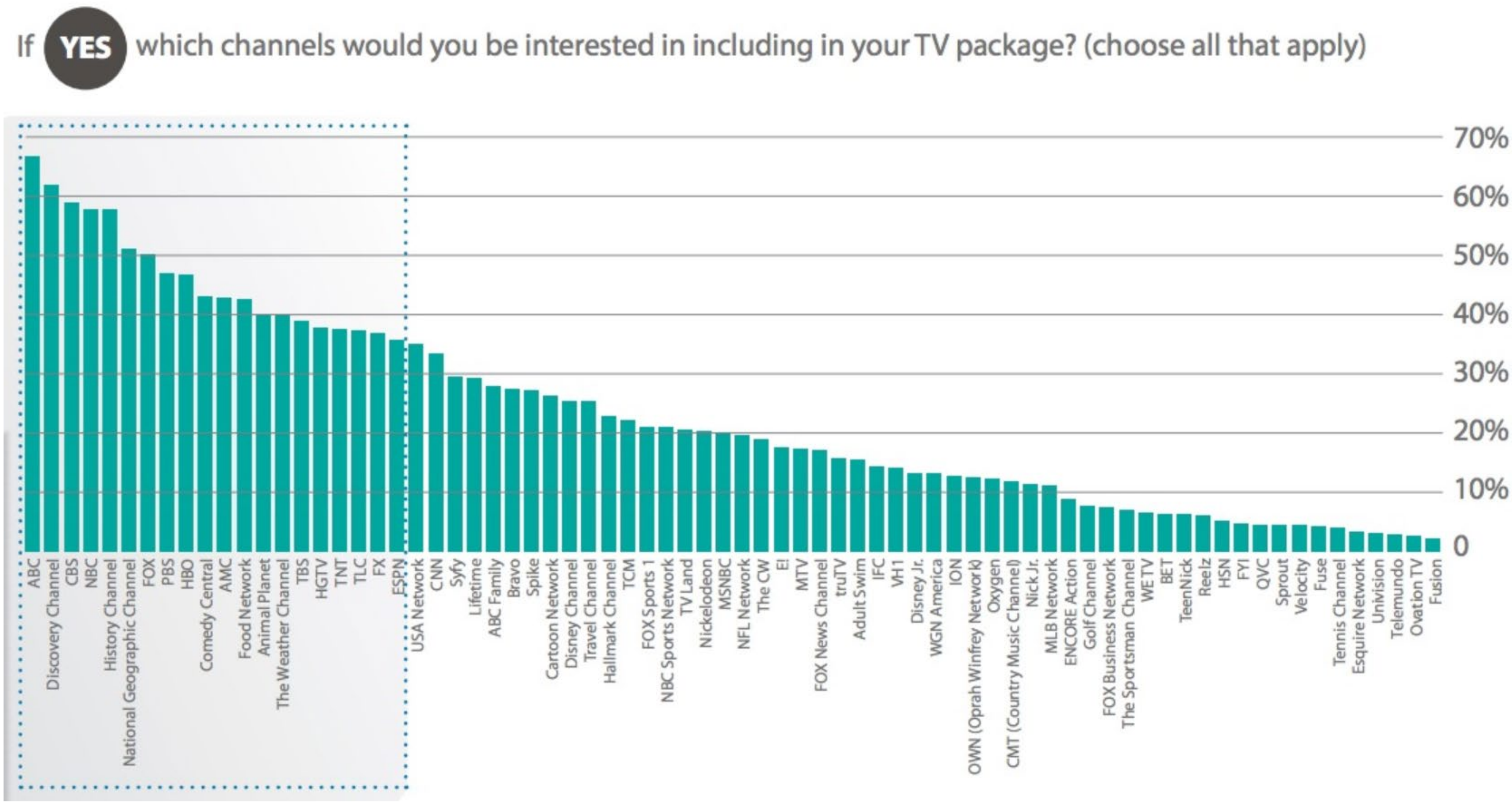
Business Quality: Competitive Advantage

Sources of Sustainable Competitive Advantage

1. **Brands** – Cable networks such as Discovery, Animal Planet, Food Network and Travel are brands loved by viewers and serve as the go-to destinations for their respective genres
2. **Distribution** – domestically the company's main networks have broad distribution on the basic tiers. Internationally a number have strong carriage in many markets in Europe and Latin America that would take many years for a competitor to replicate.
3. **Content Library** – the company is vertically integrated and owns the rights to almost all of its content. Much of its content travels well internationally and its deep library makes it easy to enter new markets once distribution is secured.

INVESTMENT PROCESS

Business Quality: Competitive Advantage



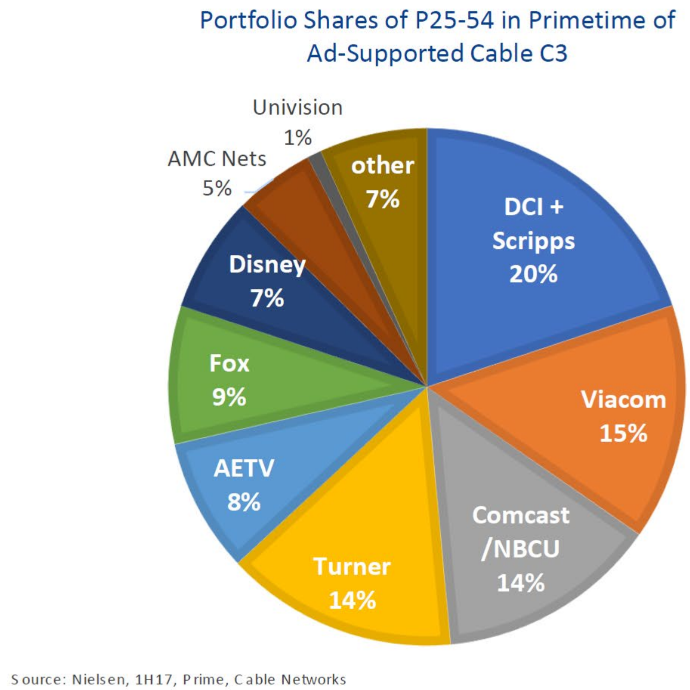
Source: Variety 2015 survey, https://pmcvariety.files.wordpress.com/2015/06/digitalsmiths-unbundling-survey.jpg

The combined company will have 5 out of the top 20 networks that consumers would want to include in their own a-la-carte TV bundle according to a 2015 Variety survey

INVESTMENT PROCESS

Business Quality: Competitive Advantage

20% Share of P25-54 Ad-Supported Viewership



Source: Discovery 2017 Scripps Merger presentation

Combined Audience Share (ad supported C3)

21.6% of W25-54 Primetime

19.2% of P2+ Primetime

18.8% of P25-54 Total Day

The combined company will have **substantial scale and bargaining power with distributors**

INVESTMENT PROCESS

Business Quality: Competitive Advantage

Discovery's Broad Global Distribution Platform…

HIGHLIGHTS

- **3** Billion Subscribers
- **220+** Countries & Territories
- **77** Local Offices
- **8** Networks per Country (average)
- **170** Million Viewers Reached
- **47** Languages
- **40 MM+** O&O Unique Visitors
- **3.5BN+** Monthly Video Views

U.S. & Canada	
802	Million Subscribers
2	Countries

U.K. & Ireland	
191	Million Subscribers
5	Countries

Eurosport	
238	Million Subscribers
101	Countries

Latin America	
370	Million Subscribers
48	Countries

CEEMEA	
612	Million Subscribers
111	Countries

Southern Europe	
284	Million Subscribers
9	Countries

Nordics	
66	Million Subscribers
9	Countries

Asia Pacific	
674	Million Subscribers
37	Countries

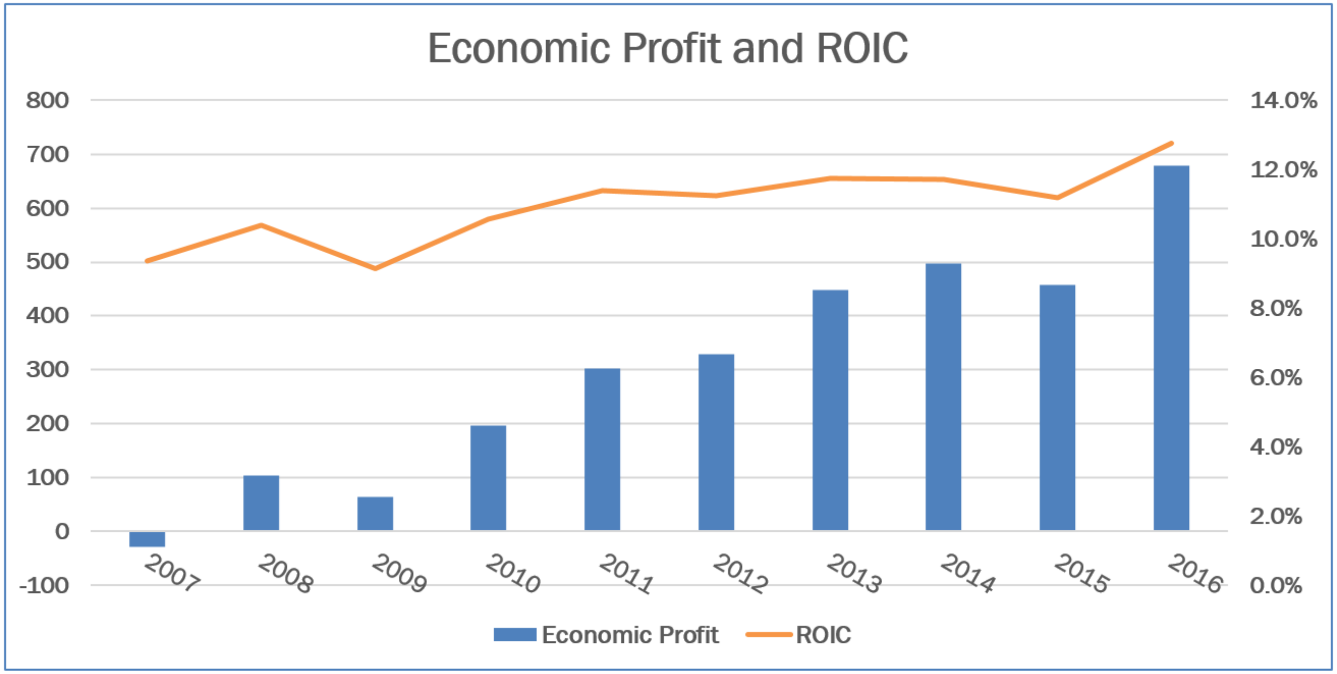
Note: Viewer numbers including non-controlled joint ventures and are as of June 30, 2017 according to The Nielsen Company in the U.S. and internal data review and external sources outside of the U.S.

Source: Discovery 2017 Scripps Merger presentation

Discovery has **unrivaled global distribution**, which it can use to monetize some of the acquired Scripps Networks' content internationally.

INVESTMENT PROCESS

Business Quality: Validation



Source: Company Reports

- It is important to compare our qualitative analysis against historical financial metrics
- The company's high and growing Economic Profit and high Return on Invested Capital corroborate our analysis that this is a high quality business

<u>Conclusion</u>: Discovery has a **sustainable competitive advantage** due to its **brands, content library and global distribution** and is an **Above Average** quality business.

INVESTMENT PROCESS

Management Quality

What Determines Management Quality

1. Track-record of a) operating the business b) capital allocation
2. Alignment of incentives with shareholders

Discovery's Management: Track Record

- Current CEO responsible for meaningfully growing the company's economic profit over the last decade
- Management increased the international distribution for its channels through a sustained program of investment
- Maintained and grew key brands (e.g. Discovery and Investigation Discovery), but a couple of networks (TLC and Animal Planet) remain in turnaround mode
- Capital allocation track record is too early to assess as not enough time has passed from the recent deals

Discovery's Management: Alignment

- Large direct share ownership: CEO owns $60M
- John Malone is on the board and controls a substantial minority of the vote, increasing confidence in capital allocation
- Compensation metrics (sales, EBITDA and FCF) are imperfect as they don't include ROIC or Economic Profit.

Conclusion: Management Quality is Above Average

INVESTMENT PROCESS

Balance Sheet Quality

What Determines Balance Sheet Quality

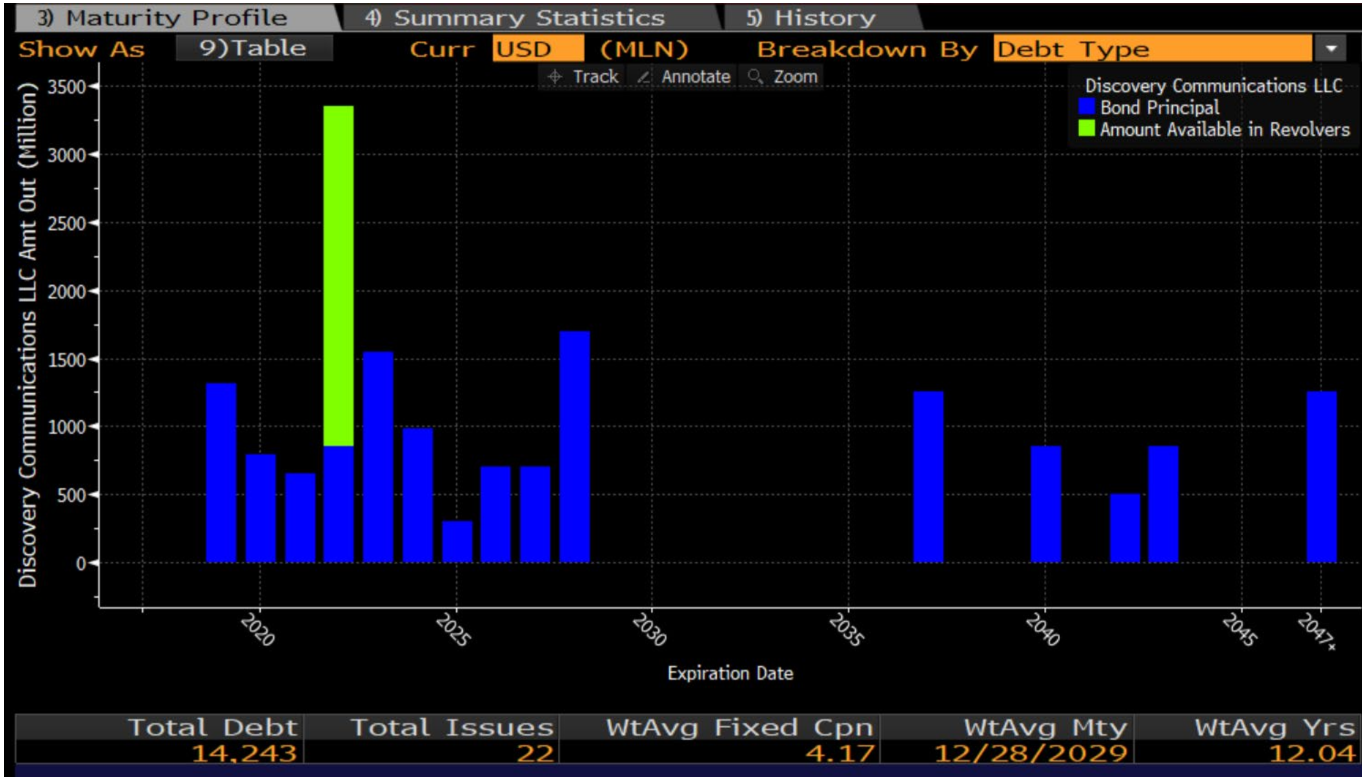
1. Ability to withstand temporary adversity without needing to raise capital
2. Appropriate leverage relative to profitability that doesn't necessitate the use of Free Cash Flow to reduce debt

Balance Sheet Quality

- Pro-Forma for the SNI acquisition, Debt/EBITDA is ~ 5x
- Debt/EBITDA should decline to 4.7x and 4x by the end of 2018 and 2019 in my Base Case
- Debt/EBITDA would be at 5x and 4.5x by the end of 2018 and 2019 in my Worst Case
- Debt covenants are at 5.5x, stepping down to 5x a year and to 4.5x two years from deal close
- Interest Coverage (EBITA/Interest) is 4.8x at its trough in my Worst Case
- Management was able to lock in a very low cost of debt (~4%) for very long-term maturities
- For example, the company's longest maturity is 2047 with a 5.2% coupon and a spread of 2.5% at issue and ~ 2.3% currently to US Treasuries

INVESTMENT PROCESS

Balance Sheet Quality



Source: Bloomberg

- **The company's debt maturities are very well distributed, lessening liquidity risk**
- I estimate Discovery will generate $1.5B+ of FCF in each of the next 5 years in the Worst Case

<u>Conclusion</u>: Balance Sheet Quality is Below Average, but improving and expected to reach Average in 2 years.

INVESTMENT PROCESS

Security Research and Valuation

Step 2

Analysis of Key Economic Variables

- Identify key economic variables most likely to materially impact the long-term business outcome
- Establish a range of reasonable values for each variable under different scenarios

If we could only know 5 or fewer things about the business 10 years from now, what would they be?

1. Domestic subscription revenues
2. Domestic advertising revenues
3. International subscription revenues
4. International advertising revenues
5. Cost of content

INVESTMENT PROCESS

Key Economic Variables – Domestic Subscription Revenue

	Q1 '16	Q2 '16	Q3 '16	Q4 '16	Q1 '17	Q2 '17
Cable basic video subs*	53,302	53,046	52,951	52,845	52,658	52,412
DBS subs*~	33,474	33,449	33,495	33,477	33,186	32,743
Telco TV subs*	12,732	12,244	11,862	11,524	11,200	10,913
Combined video subs*	99,508	98,739	98,308	97,846	97,044	96,068
*Combined net adds**	*(162)*	*(768)*	*(432)*	*(462)*	*(802)*	*(976)*
y/y % change, combined video subs	*-1.2%*	*-1.3%*	*-1.3%*	*-1.8%*	*-2.5%*	*-2.7%*

As of August 2017.

*Includes residential and commercial subscribers.

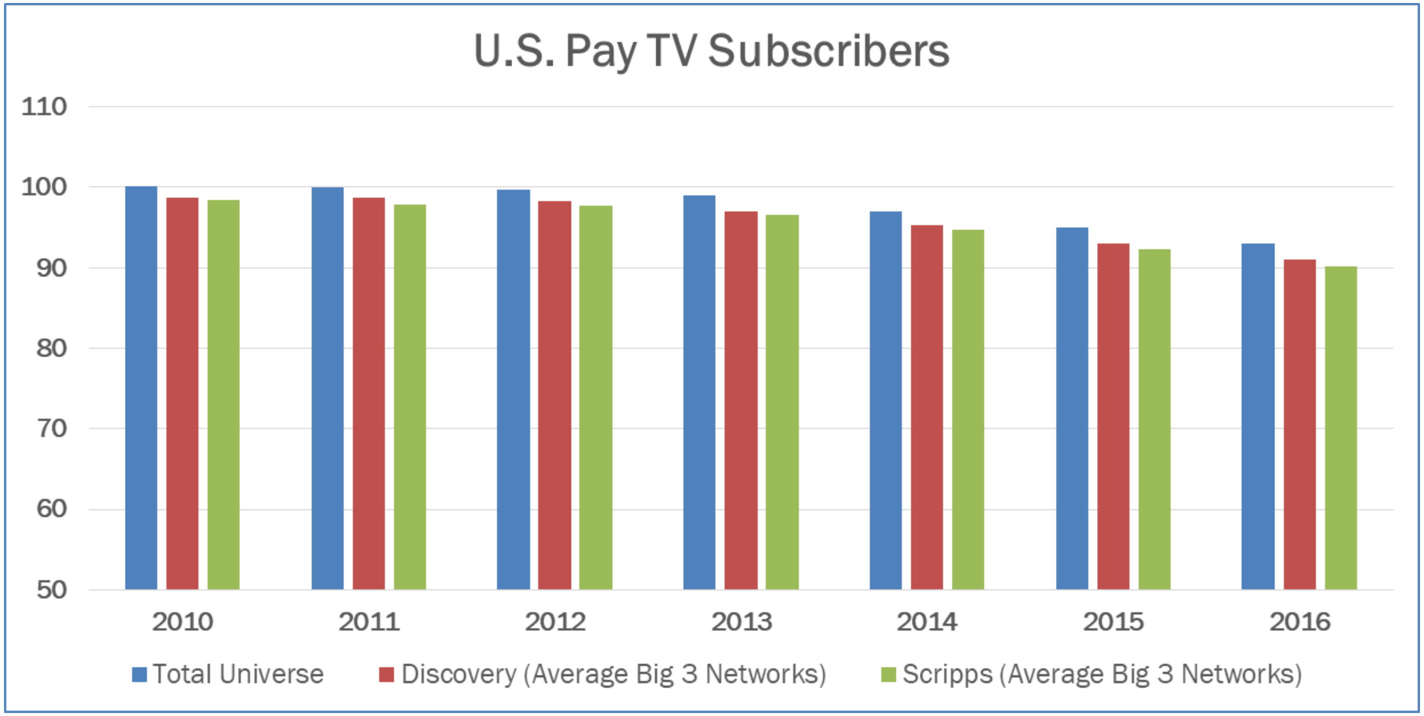
~DBS subscribers employ Kagan estimate of DISH subscribers excluding estimated 1.45 million Sling TV subscribers as of Q2 '17. DBS also excludes 491,000 DIRECTV NOW subscribers.

Source: SNL Kagan and Cowen and Company estimates

- Video subscriber losses for traditional distributors are approaching 3% per year

INVESTMENT PROCESS

Key Economic Variables – Domestic Subscription Revenue

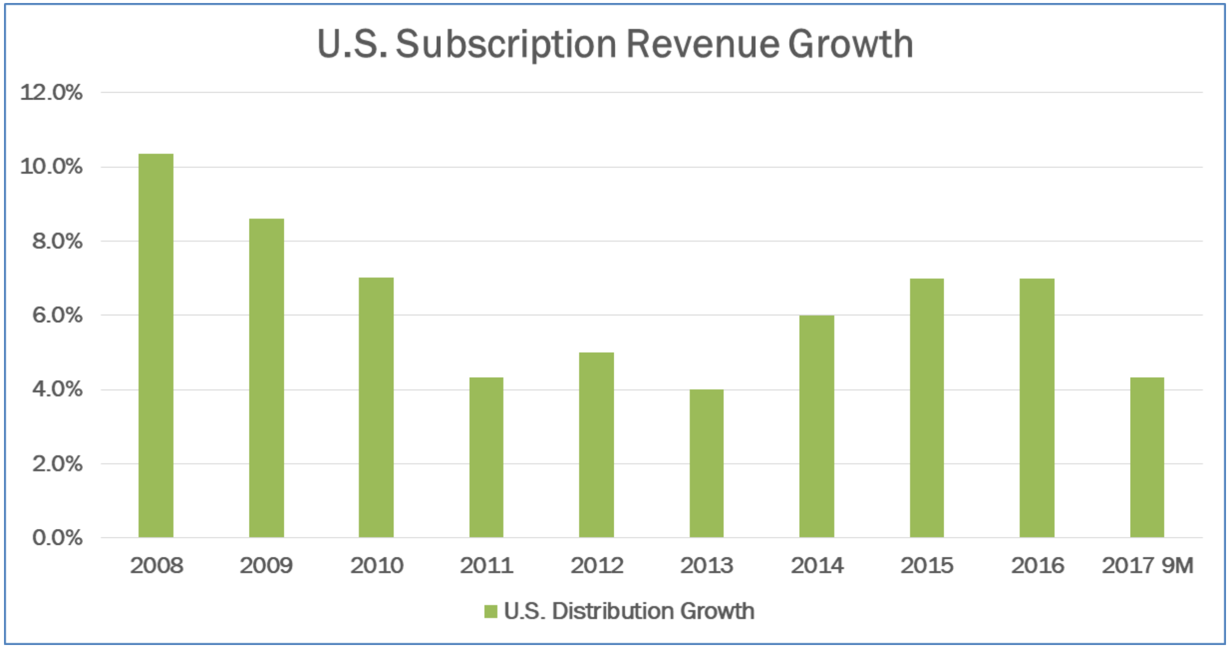


Source: Forms 10-K of TWX, SNI, DIS, DISCK and CMCSA; Calculated as maximum of any major channel in a year

- Cable network distribution has been declining ~ 2%-3% in recent years
- Discovery and Scripps have seen their main networks decline at similar rates
- On the Q3 2017 earnings call Discovery said the core networks declined ~ 3% while all networks decline ~ 5%, suggesting that the marginal networks are losing distribution at rate of 7%+

INVESTMENT PROCESS

Key Economic Variables – Domestic Subscription Revenue

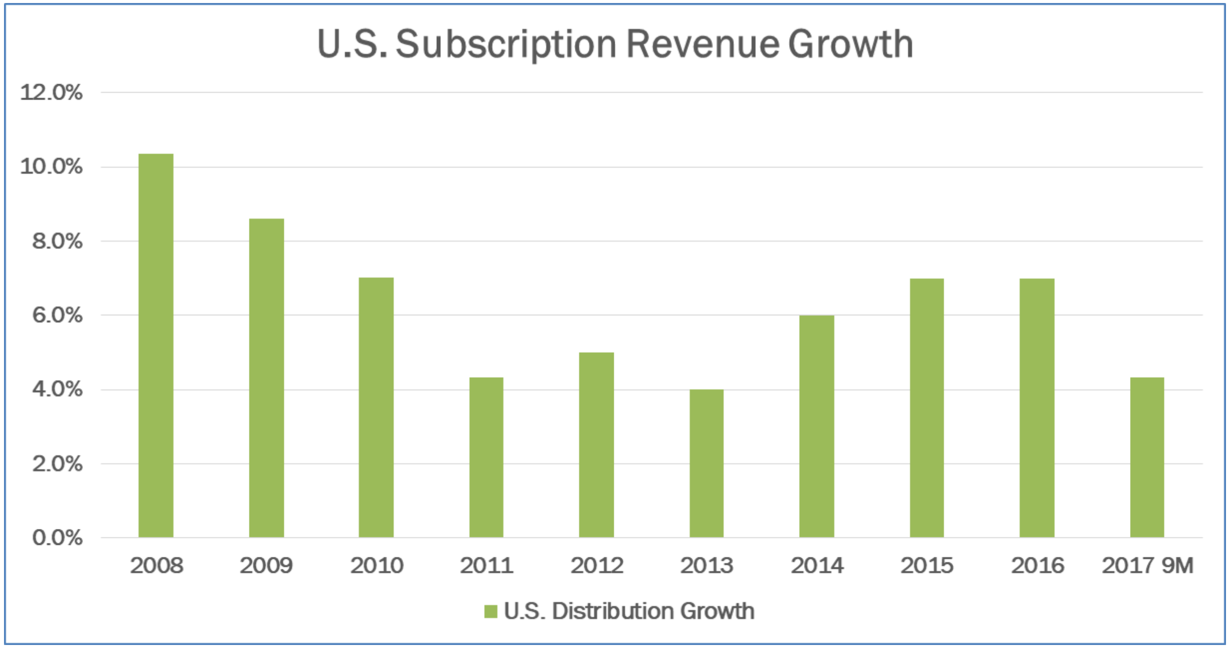


Source: Company Reports

- Despite declines in the number of subscribers the company has maintained subscription revenue growth due to pricing
- Annual price escalators are contractually in the high single digits, consistent with the pricing implied in the YTD results
- Deals are long-term, typically 5+ years
- Discovery's content is inexpensive – less than 35c per network per month

INVESTMENT PROCESS

Key Economic Variables – Domestic Subscription Revenue

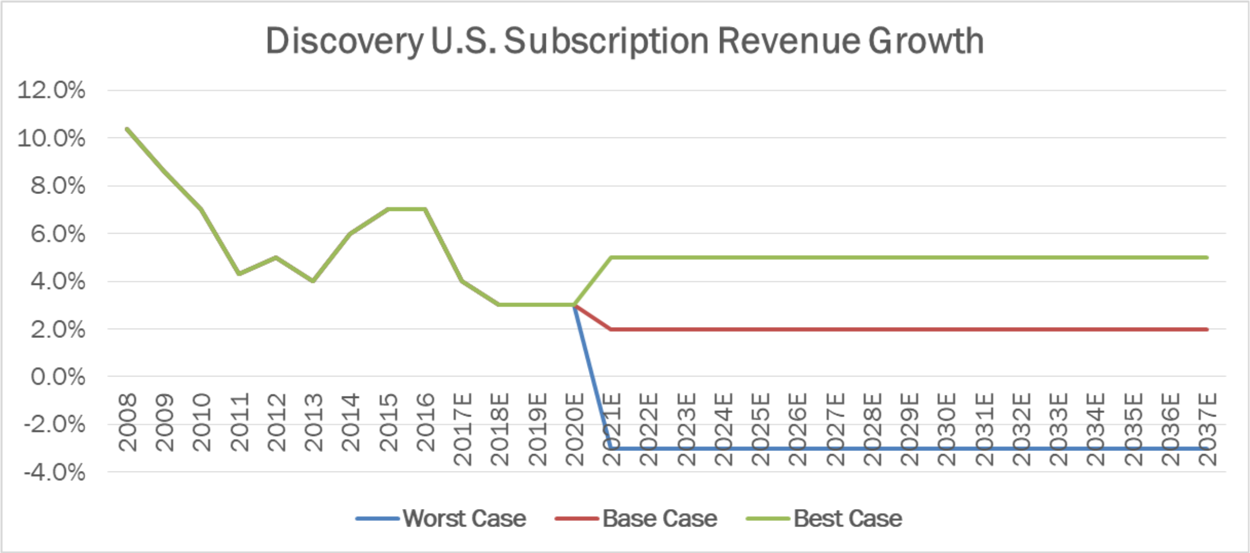


Source: Company Reports

- Despite declines in the number of subscribers the company has maintained subscription revenue growth due to pricing
- Annual price escalators are contractually in the high single digits, consistent with the pricing implied in the YTD results
- Deals are long-term, typically 5+ years
- Discovery's content is inexpensive – less than 35c per network per month

INVESTMENT PROCESS

Key Economic Variables – Domestic Subscription Revenue

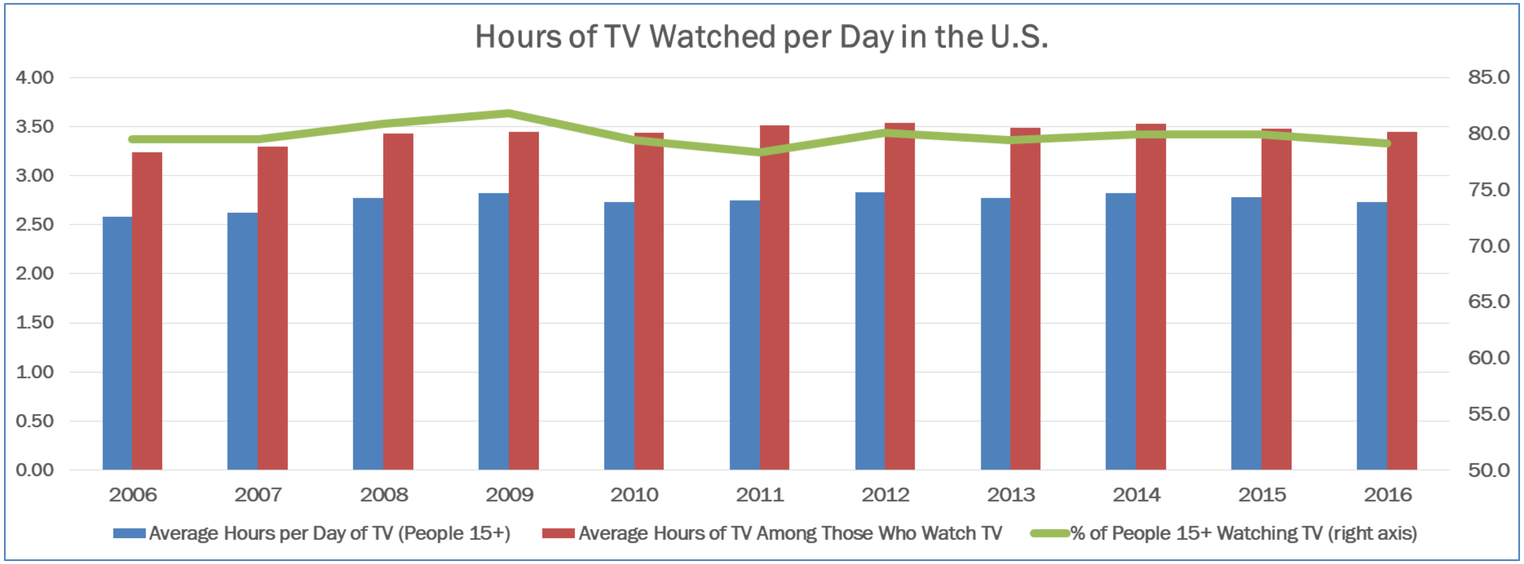


Source: Company Reports, Silver Ring Value Partners estimates

- **Base Case:** U.S. subscription revenue grows ~ 2% per year (-3% volume, +5% price)
- **Worst Case:** U.S. subscription revenue declines ~ 3% per year (-5% volume, +2% price)
- **Best Case:** U.S. subscription revenue grows ~ 5% per year (-2% volume, + 7% price)

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

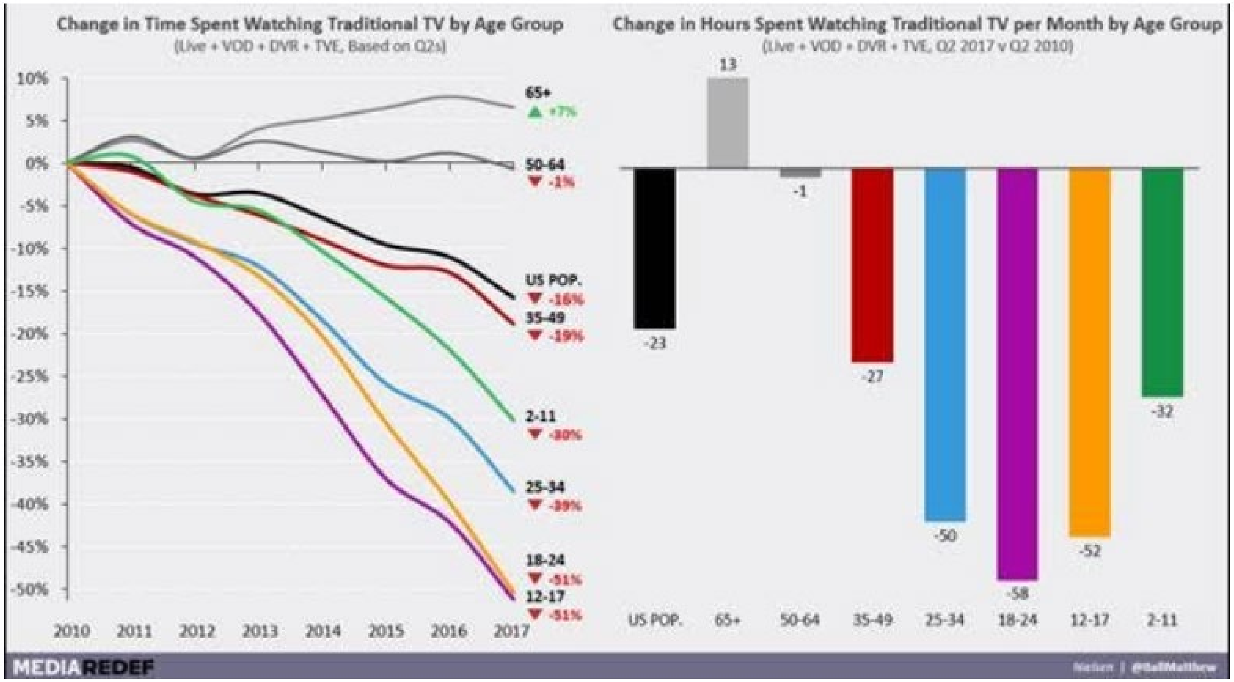


Source: BLS.gov

- Despite increased usage of the internet, mobile apps ands social media, there has not been a material decline in the amount of time spent watching TV
- The percent of people watching TV has also been stable

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue



Source: Morgan Stanley

- However, the amount of time spent on *traditional TV* has declined
- This decline is particularly pronounced among younger people
- The likely cause is viewing of new, internet-based services such as Netflix, which allow viewing of older library content

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

Quarterly Average Y/Y Ratings Trends (C3, TD TH)

	Q1'16	Q2'16	Q3'16	Q4'16	Q1'17	Q2'17	Average
ESPN	-11%	-7%	-19%	-15%	1%	-9%	-10%
FOX Sports 1	14%	8%	7%	57%	7%	-9%	14%
TNT	-9%	-4%	-9%	-22%	-15%	-15%	-12%
TBS	-12%	-5%	-7%	-17%	-11%	-11%	-10%
USA	-15%	-15%	-16%	-12%	-14%	-17%	-15%
Spike TV	-5%	-11%	-10%	-12%	-5%	-11%	-9%
AMC	-1%	-10%	-24%	-16%	-13%	-2%	-11%
History	-15%	-12%	-9%	-9%	1%	-5%	-8%
Food Network	1%	-2%	-8%	-1%	-2%	-7%	-3%
Travel Channel	8%	7%	0%	4%	-2%	-2%	3%
DIY Network	12%	13%	12%	10%	5%	-5%	8%
Cooking Channel	5%	8%	1%	7%	10%	-4%	5%
Great American Country	25%	16%	6%	6%	-2%	-10%	7%
National Geographic	-10%	5%	-1%	-6%	-2%	-20%	-6%
HGTV	14%	2%	3%	0%	-3%	-3%	2%
Average (comparable nets)	**0%**	**0%**	**-5%**	**-2%**	**-3%**	**-9%**	**-3%**
Discovery Channel	-7%	-3%	-20%	-17%	-8%	-19%	-12%
American Heroes Channel	-16%	-16%	-18%	-16%	-11%	-18%	-16%
TLC	-11%	-12%	-22%	-14%	-9%	7%	-10%
Investigation Discovery	4%	2%	6%	12%	11%	12%	8%
Animal Planet	2%	10%	3%	1%	-1%	-15%	0%
Oprah Winfrey Network	-1%	7%	-1%	0%	0%	-1%	1%
Science	-1%	2%	5%	7%	-13%	-10%	-2%
Destination America	-12%	-7%	-12%	-8%	0%	-8%	-8%
Average (DISCA nets)	**-5%**	**-2%**	**-7%**	**-4%**	**-4%**	**-6%**	**-5%**

Note: We used average quarterly C3 Total Day, Total Households (HH) as part of our year-over-year analysis. Sources: The Nielsen Company and Wells Fargo Securities, LLC.

Source: Wells Fargo, 7/2017

- The company's US ratings have been declining on average in the mid single digits

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

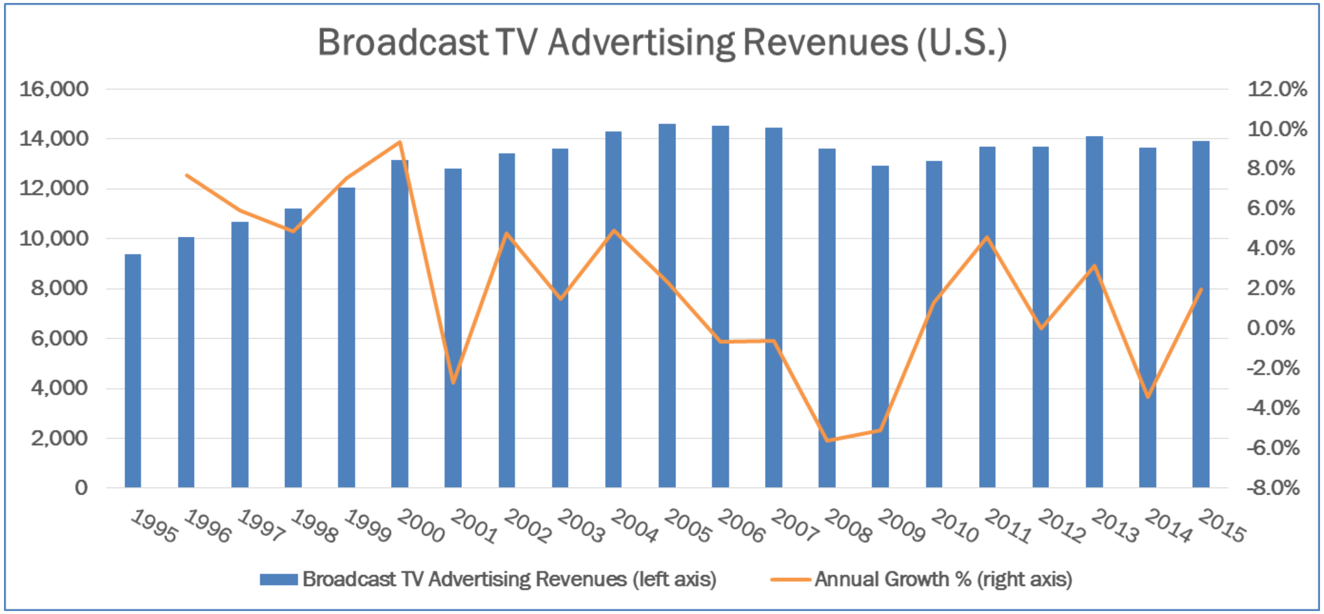
Over The Top Video Providers: Analysis of Impact on Cable Network Ratings		
		Comment
Netflix 2014 Global streaming Subscribers (millions, avg)	49.7	Source: Netflix quarterly reports
Netflix 2014 Total Streaming Hours (millions)	29,000	Source: Netflix Q4 2015 quarterly report
Netflix 2014 Global Average Hours per Subscriber per Day	1.6	
Netflix 2015 Global Streaming Subscribers (millions, avg)	67.9	Source: Netflix quarterly reports
Netflix 2015 Total Streaming Hours (millions)	42,500	Source: Netflix Q4 2015 quarterly report
Netflix 2015 Global Average Hours per Subscriber per Day	1.7	
Assumed Ratio of U.S. Subscribers Daily Hours as a % of Global Average	110%	My assumption based on international market launch lagging U.S. launch
Netflix 2014 U.S. Average Hours per Subscriber per Day	1.8	
Netflix 2014 U.S. Streaming Subscribers (millions, avg)	37.1	Source: Netflix quarterly reports
Netflix 2014 U.S. Streaming Hours (millions)	23,781	
Netflix 2015 U.S. Average Hours per Subscriber per Day	1.9	
Netflix 2015 U.S. Streaming Subscribers (millions, avg)	42.9	Source: Netflix quarterly reports
Netflix 2015 U.S. Streaming Hours (millions)	29,526	
Netflix Increase in U.S. Netflix Annual Hours Streamed between 2015 and 2014 (millions)	5,745	
2014 U.S. Pay TV Basic Cable Networks Subscribers (millions)	97.0	Source: Analysis of 10-K filings for major cable network companies
Average Daily Hours of TV Consumption, Adults 18+	3.9	Average of 2.8 hours from BLS for people 15+ and the 5 hour Nielsen estimate for people 18-55
Total 2014 U.S. Pay TV Annual Time Spent Viewing by Basic Cable Subscribers	138,080	
Increase in U.S. Netflix Hours Streamed % 2014 Total TV Viewing Time	4.2%	
Amazon Prime TV and Hulu % of Netflix Impact	50%	My rough estimate as Amazon Prime TV data is unavailable
Total Over The Top Internet Video Providers Impact on 2015 Cable Networks Ratings	**6.2%**	
Estimated Future Impact on Cable Network Ratings from OTT Video		
Netflix 2020 Average U.S. Hours per Subscriber per Day	2.2	
Netflix 2020 U.S. Subscribers (millions)	65	47.5M as of Q3 2016, with long-term management guidance of 60M-90M, current run-rate of 4M net adds per year
Netflix 2020 U.S. Streaming Hours (millions)	51,897	
Increase Over 2015	22,371	
Netflix Cumulative Additional Impact 2015-2020 on Cable Network Ratings	**17.3%**	
Impact on Ratings per Year	**3.5%**	
Amazon Prime TV and Hulu % of Netflix Impact	60%	My assumption is that Hulu and Amazon slightly close the gap vs. Netflix in 5 years
Amazon and Hulu Cumulative Additional Impact 2015-2020 on Cable Network Ratings	**10.4%**	
Impact on Ratings per Year	**2.1%**	
Total Annual Over The Top (OTT) Video Providers Negative Impact on Cable TV Ratings per Year	**5.5%**	

Source: Silver Ring Value Partners Analysis, Netflix Quarterly Reports, BLS, Nielsen

- Direct to consumer offerings such as Netflix likely to hurt ratings by ~ 5% per year

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

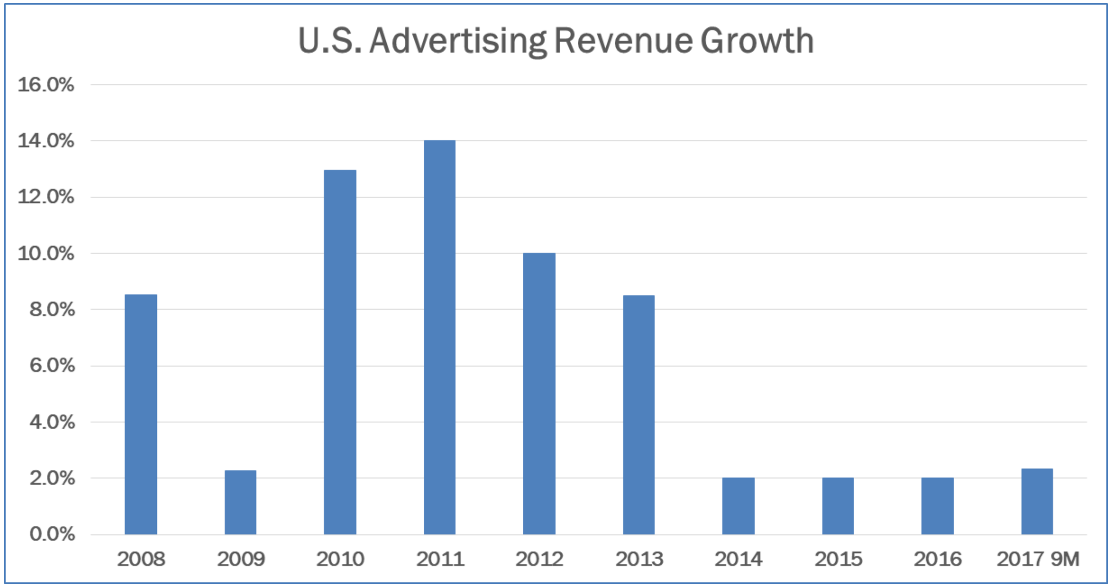


Source: J.P. Morgan, MAGNA

- An analog for what is happening in the Cable TV industry is what happened to the Broadcast TV industry over the last 15 years
- Despite declining ratings, advertising revenue grew low single digits
- This was due to *pricing power* as advertisers value share of voice vs. competitors more so than absolute reach

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

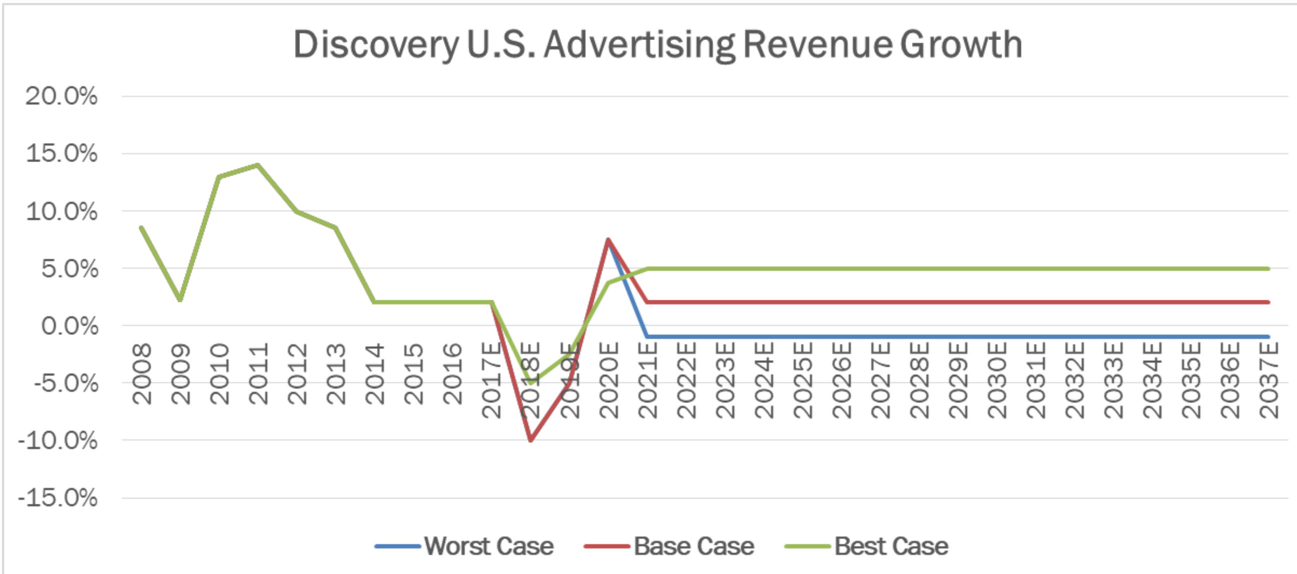


Source: Company Reports

- Despite mid single digits ratings declines over the last two years, advertising revenue grew ~ 2% per year
- This shows initial evidence that cable networks have *pricing power* given their unique medium (targeted mass video)

INVESTMENT PROCESS

Key Economic Variables – Domestic Advertising Revenue

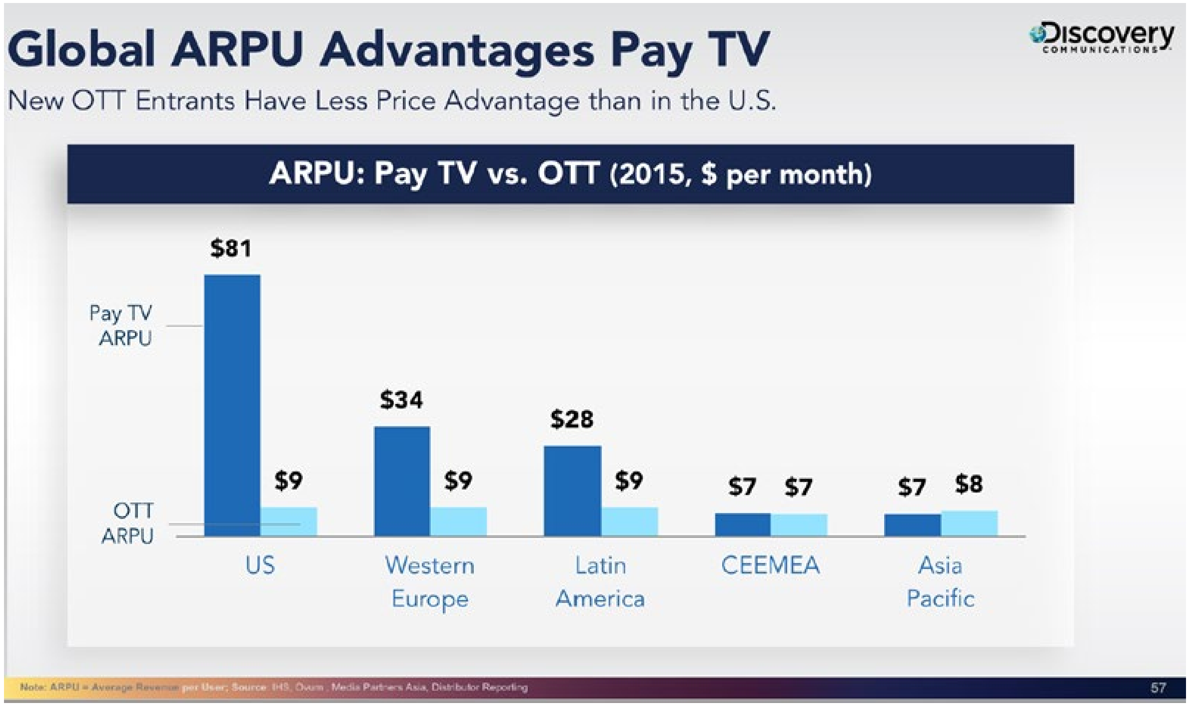


Source: Company Reports, Silver Ring Value Partners estimates

- **Worst Case:** Immediate advertising recession followed by -1% declines
- **Base Case:** Immediate advertising recession (to be conservative given where we are in the economic cycle), followed by 2% growth
- **Best Case:** Mild economic recession followed by 5% growth
- All scenarios assume ratings continue to decline
- **Market participants underestimate Cable TV's pricing power**

INVESTMENT PROCESS

Key Economic Variables – International Subscription Revenue



Source: Discovery 2015 Investor Day presentation

- Outside the US, services such as Netflix are less compelling as an alternative to traditional TV due to a smaller price differential

INVESTMENT PROCESS

Key Economic Variables – International Subscription Revenue

Source: Company Reports

- International markets are earlier in their development stage and have more room for additional Pay TV penetration and subscriber growth
- Discovery has grown all of its major networks internationally at high single digit annual rates or better over the last 5 years

INVESTMENT PROCESS

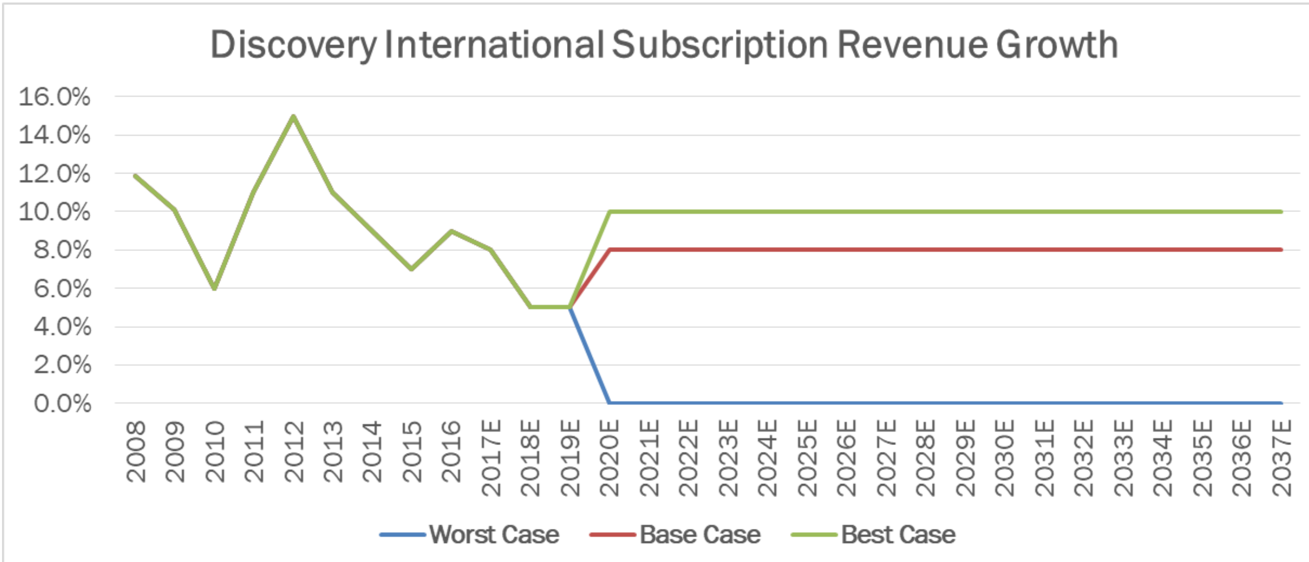
Key Economic Variables – International Subscription Revenue

Source: Discovery 2015 Investor Day presentation

- Company is investing in EuroSport by aggregating inexpensive sports rights
- Inelastic consumer demand for sports improves bargaining power
- EuroSport Player has interesting optionality if it gains scale
- Company is willing to sacrifice short-term revenue to build a customer base (e.g. recently put Bundesliga soccer rights only on the direct to consumer offering)

INVESTMENT PROCESS

Key Economic Variables – International Subscription Revenue

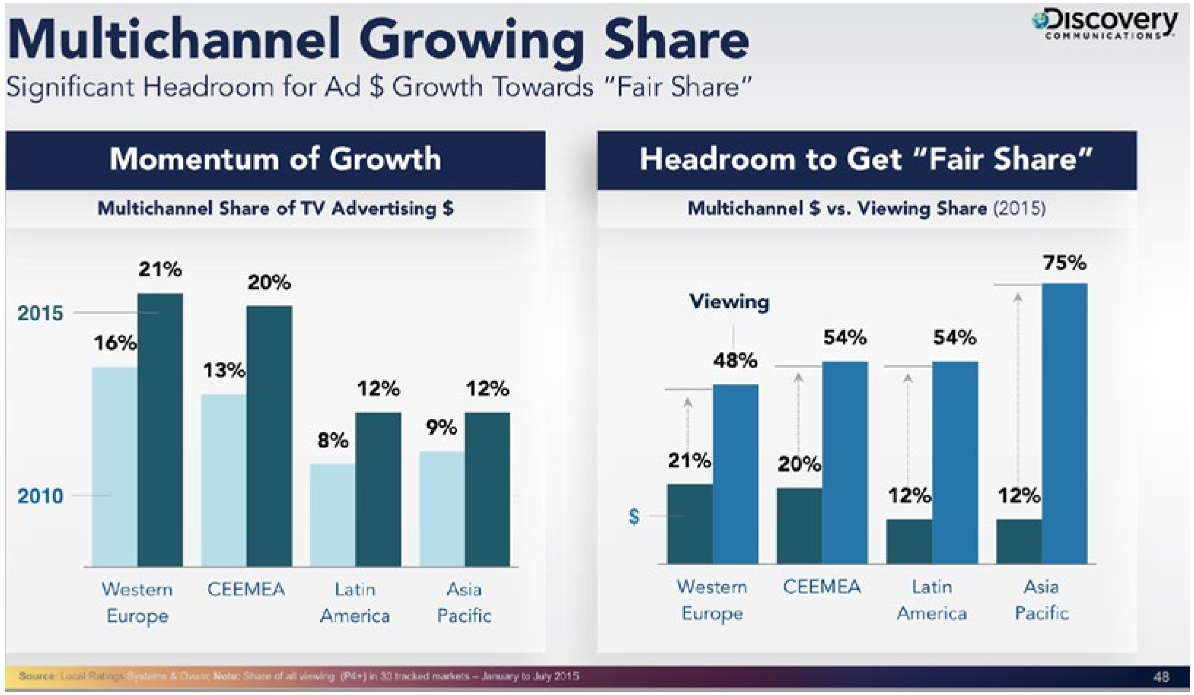


Source: Company Reports, Silver Ring Value Partners estimates

- **Worst Case:** Growth drops to 0% starting in 2018
- **Base Case:** Long-term growth at 8% driven by both subscriber growth and price
- **Best Case:** Long-term growth at 10% driven by subscriber growth and price

INVESTMENT PROCESS

Key Economic Variables – International Advertising Revenue



Source: Discovery 2015 Investor Day presentation

- International Cable TV advertising still growing at healthy rates and has room to continue to grow

INVESTMENT PROCESS

Key Economic Variables – International Subscription Revenue

Source: Company Reports, Silver Ring Value Partners estimates

Recent deceleration in organic growth in part driven by:

- Economic recession in parts of Latin America (e.g. Brazil)
- Pricing pressure in Asia where company lacks sports rights
- Natural disasters in Puerto Rico and Caribbean

INVESTMENT PROCESS

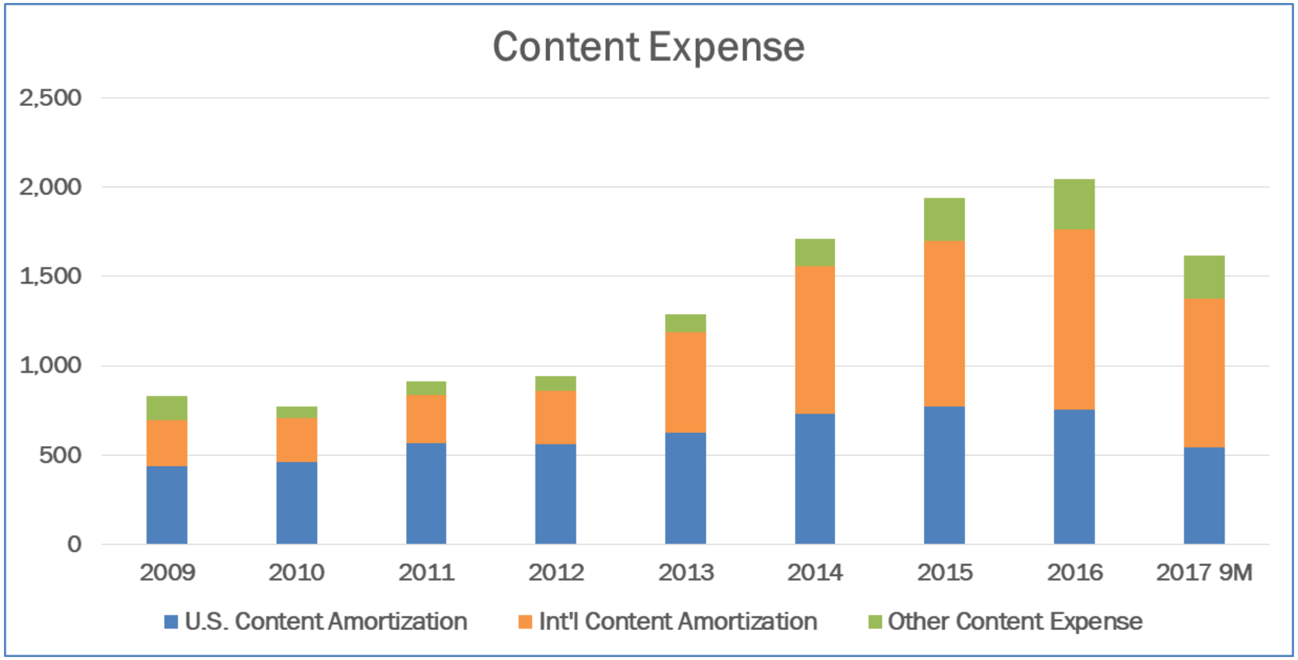
Key Economic Variables – International Advertising Revenue

Source: Company Reports, Silver Ring Value Partners estimates

- Modeling advertising recession in 2018/2019 (-10%/-5%) given where we are in the cycle, but not because of any particular view on the timing
- **Worst Case:** Long-term growth of 0%, due to negative ratings offset by pricing
- **Base Case:** Long-term growth of 4%, due to LSD ratings growth + pricing
- **Best Case:** Long-term growth of 10%, due to MSD ratings growth + pricing

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

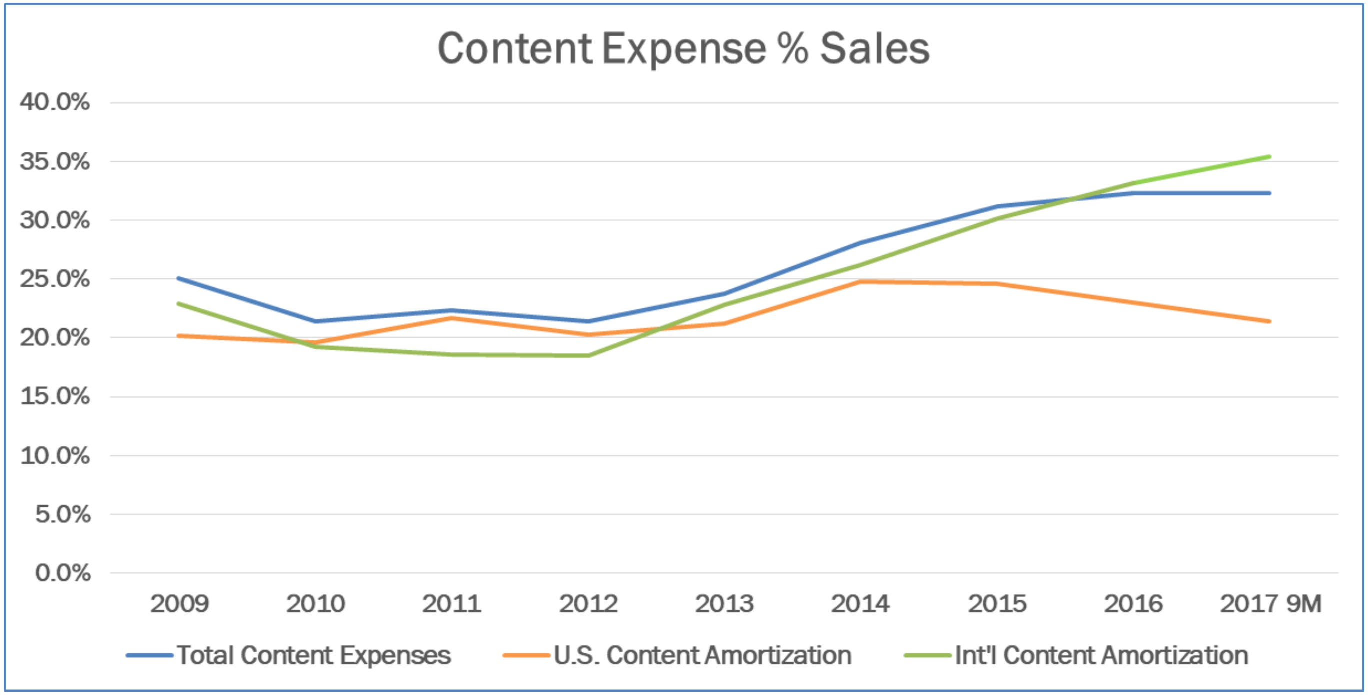


Source: Company Reports, Silver Ring Value Partners estimates

- Content costs grew at a ~14% compounded rate 2009-2016
- US costs grew at ~ 8%, while International costs (which included acquisitions) grew at a 21% rate)
- Some of the split between U.S. and International is artificial as the same content is frequently repurposed globally

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

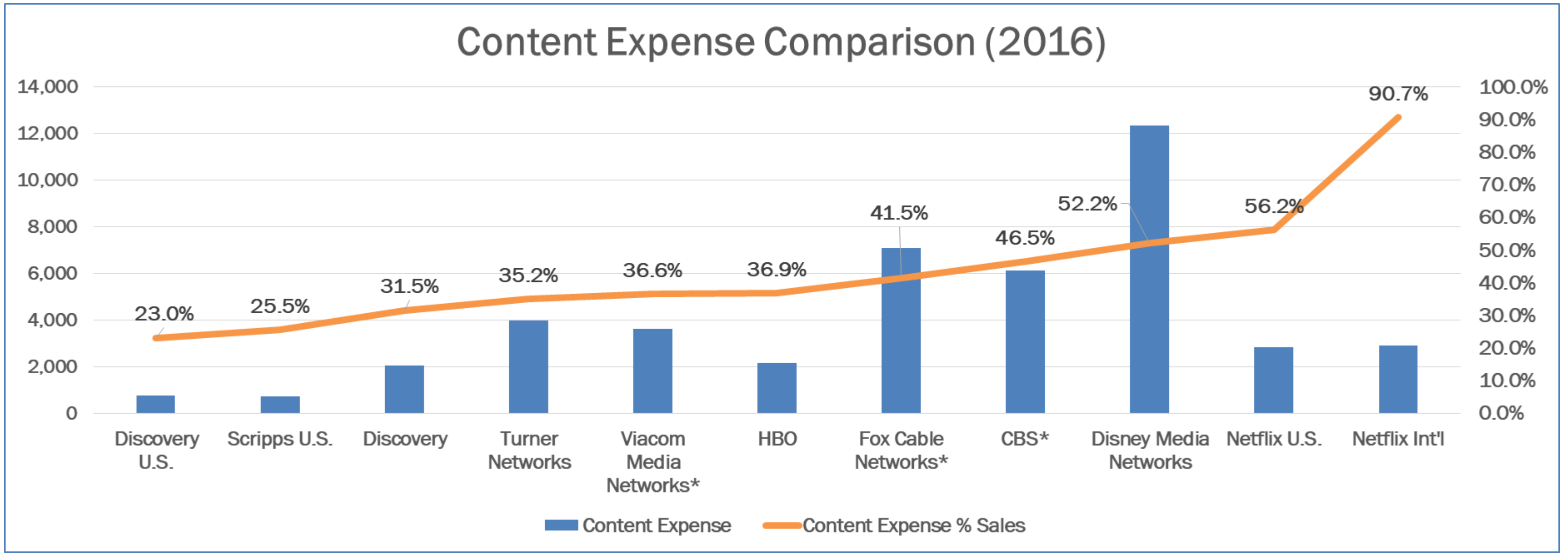


Source: Company Reports, Silver Ring Value Partners estimates

- U.S. content expenses have stayed in the low 20% range of sales
- International content expenses have increased substantially due to:
    - Acquisitions with smaller scale
    - Investment in sports rights (e.g. Bundesliga, Eurosport)

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

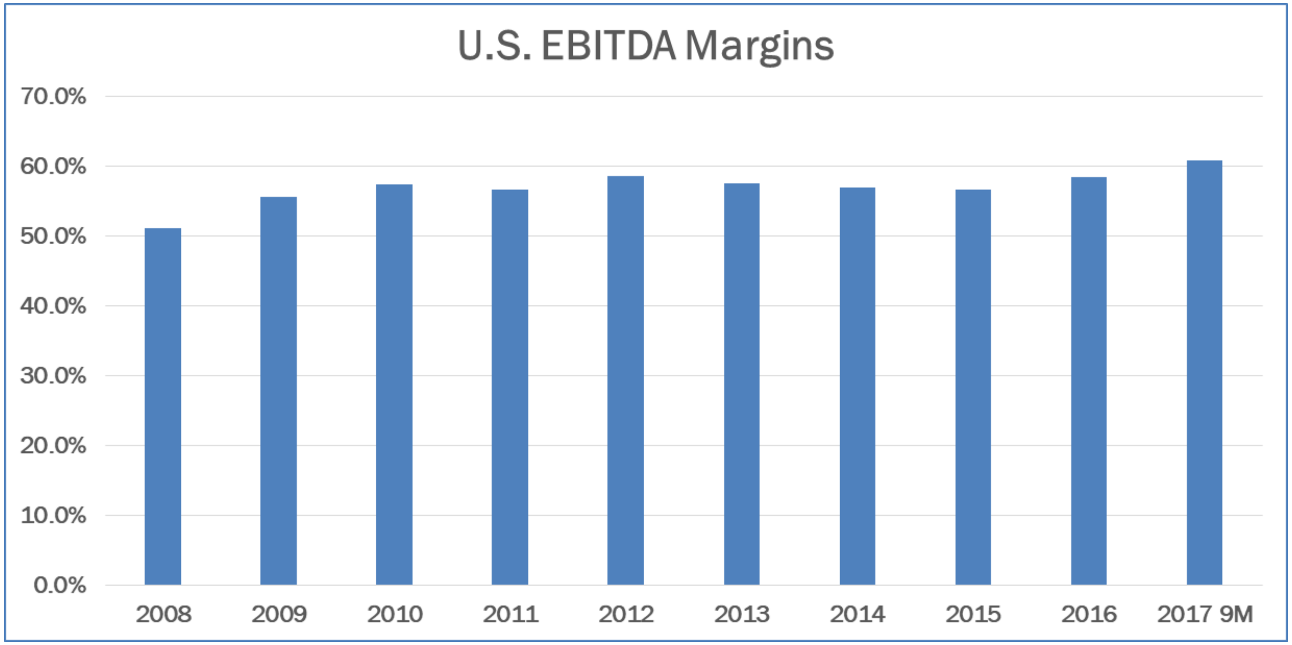


Source: Company Reports, Silver Ring Value Partners estimates
** = Silver Ring Value Partners estimate based on partial company disclosures*

- Discovery and Scripps have a structurally lower-cost model due to the nature of their content (no expensive talent or sports rights)
- Combined the two companies spend almost ~ $3B per year – an amount that gives them substantial scale

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

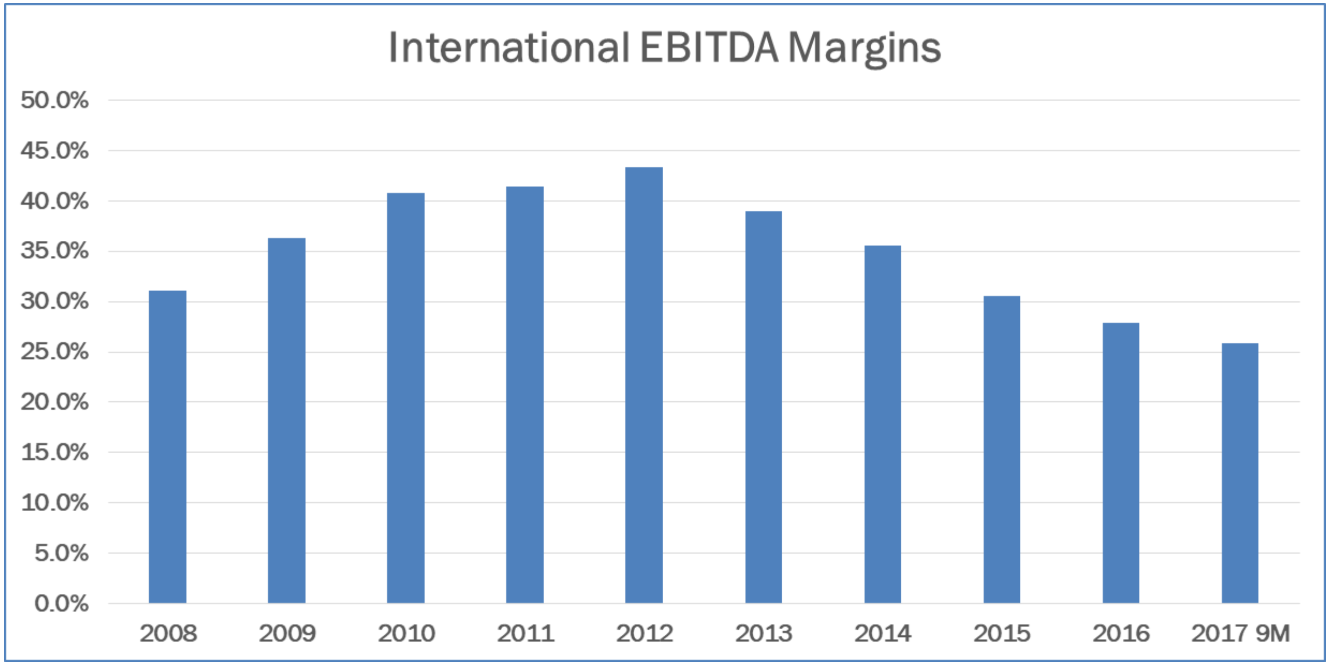


Source: Company Reports, Silver Ring Value Partners estimates

- U.S. margins have been high and stable

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

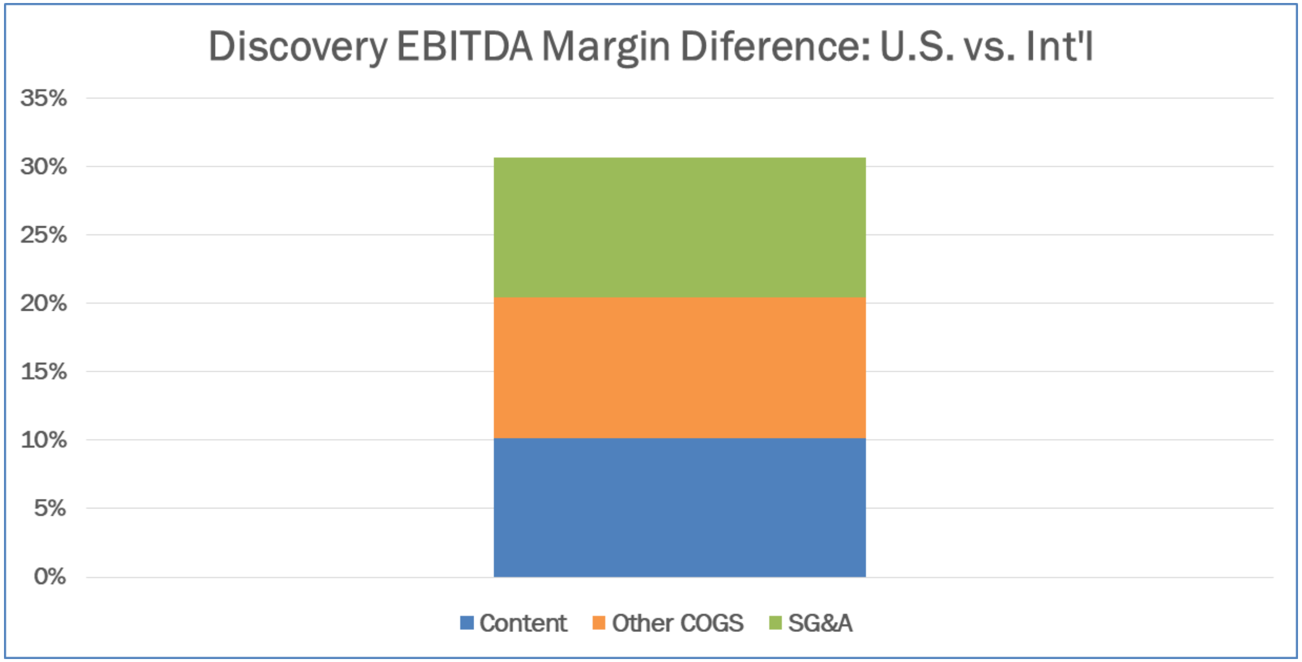


Source: Company Reports, Silver Ring Value Partners estimates

- International margins have been falling due to:
  - Acquisitions (e.g. SBS) which had lower margins
  - Sports rights investment (e.g. Olympics, Bundesliga soccer)
  - Investment in the Direct to Consumer EuroSport Player

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

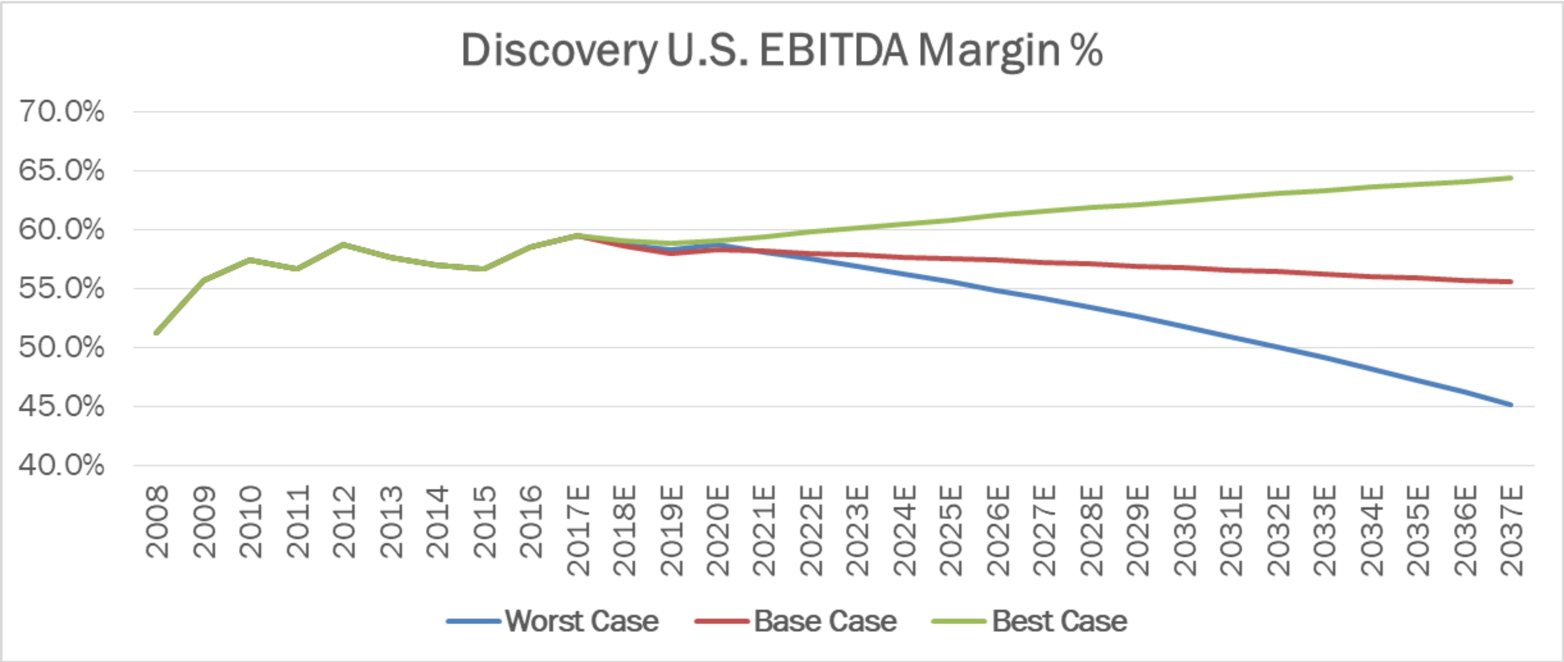


Source: Company Reports, Silver Ring Value Partners estimates

- The ~ 30% difference between the 2016 margins of the two segments was evenly divided between Content, Other COGS and SG&A leverage
- Some of the difference is structural (e.g. deleverage from operating in multiple countries)
- Some of the difference is temporary (e.g. high sports content investment)

INVESTMENT PROCESS

Key Economic Variables – Cost of Content

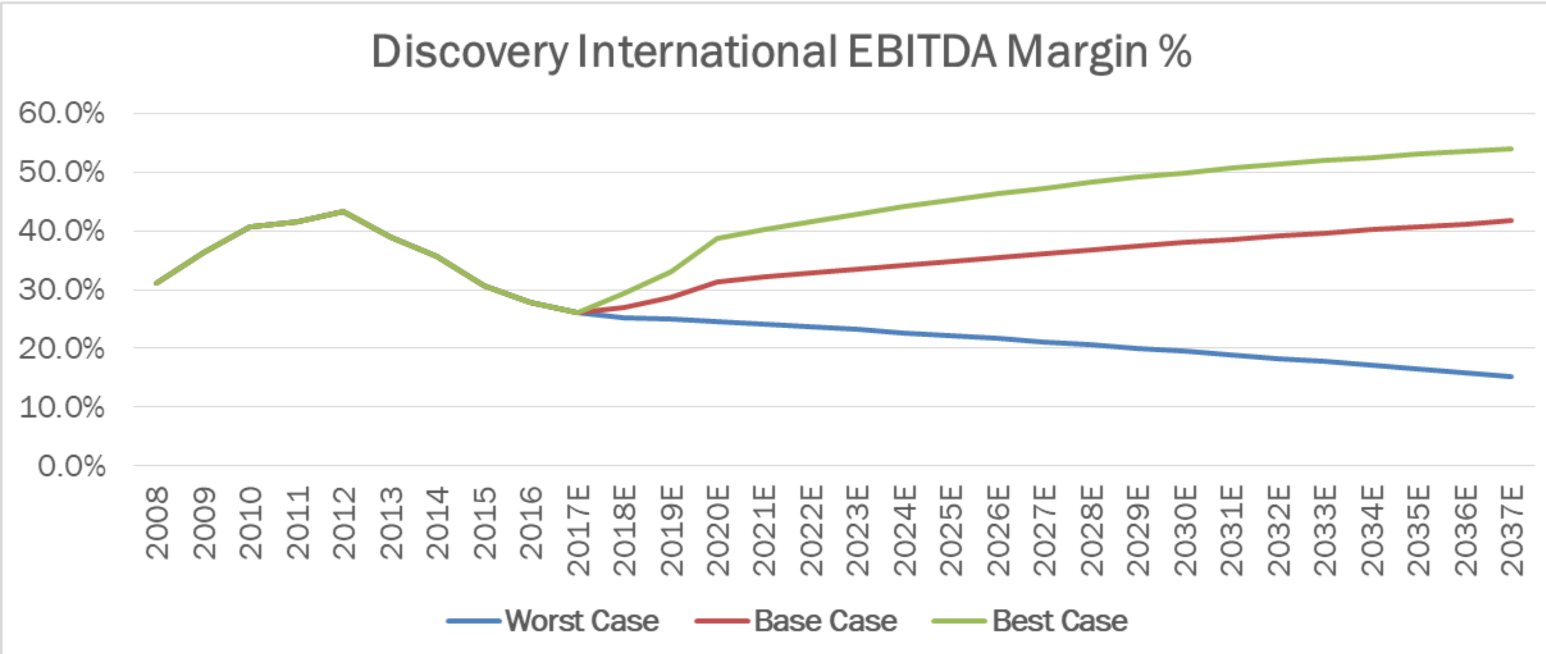


Source: Company Reports, Silver Ring Value Partners estimates

- **Worst Case:** Margins decline substantially due to deleverage from declining sales and rising content costs
- **Base Case:** Margins decline slightly due to rising content costs
- **Best Case:** Margins increase slightly due to positive leverage from rising sales

INVESTMENT PROCESS

Key Economic Variables – Cost of Content



Source: Company Reports, Silver Ring Value Partners estimates

- **Worst Case:** Margins continue to decline due to rising content costs
- **Base Case:** Margins increase slowly as rising sales more than offset continued investment in content, including sports
- **Best Case:** Margins increase substantially due to positive operating leverage and moderate growth in content spending

INVESTMENT PROCESS

Security Research and Valuation

Step 3 **Financial Modeling**

Use the analysis from Steps 1 and 2 to model the company's income statement, balance sheet and cash flow statement, and create 3 scenarios:

- *Worst case*, where each key economic variable has its *worst* likely outcome
- *Base case*, where each key economic variable has its *most* likely outcome
- *Best case*, where each key economic variable has its *best* likely outcome

INVESTMENT PROCESS

Financial Modeling

Key Assumptions: Base Case	
U.S. Distribution Growth (LT)	2.0%
U.S. Adveritising Growth (LT)	2.0%
International Distribution Growth (LT)	8.0%
International Adveritising Growth (LT)	4.0%
One-time Decline in SNI Advertising	-5.0%
Advertising Recession Magnitude	-10.0%
Tax Rate	26.0%

- Scripps deal synergies of ~ $350M vs. management's $350M target
- Assume deal revenue dis-synergies from culture/integration issues cause a one-time 5% advertising decline for the legacy Scripps business
- Immediate advertising recession of 10% in 2018 and another 5% in 2019
- Half of the benefits of the newly-passed lower US corporate tax rate competed away and passed through to customers, half retained

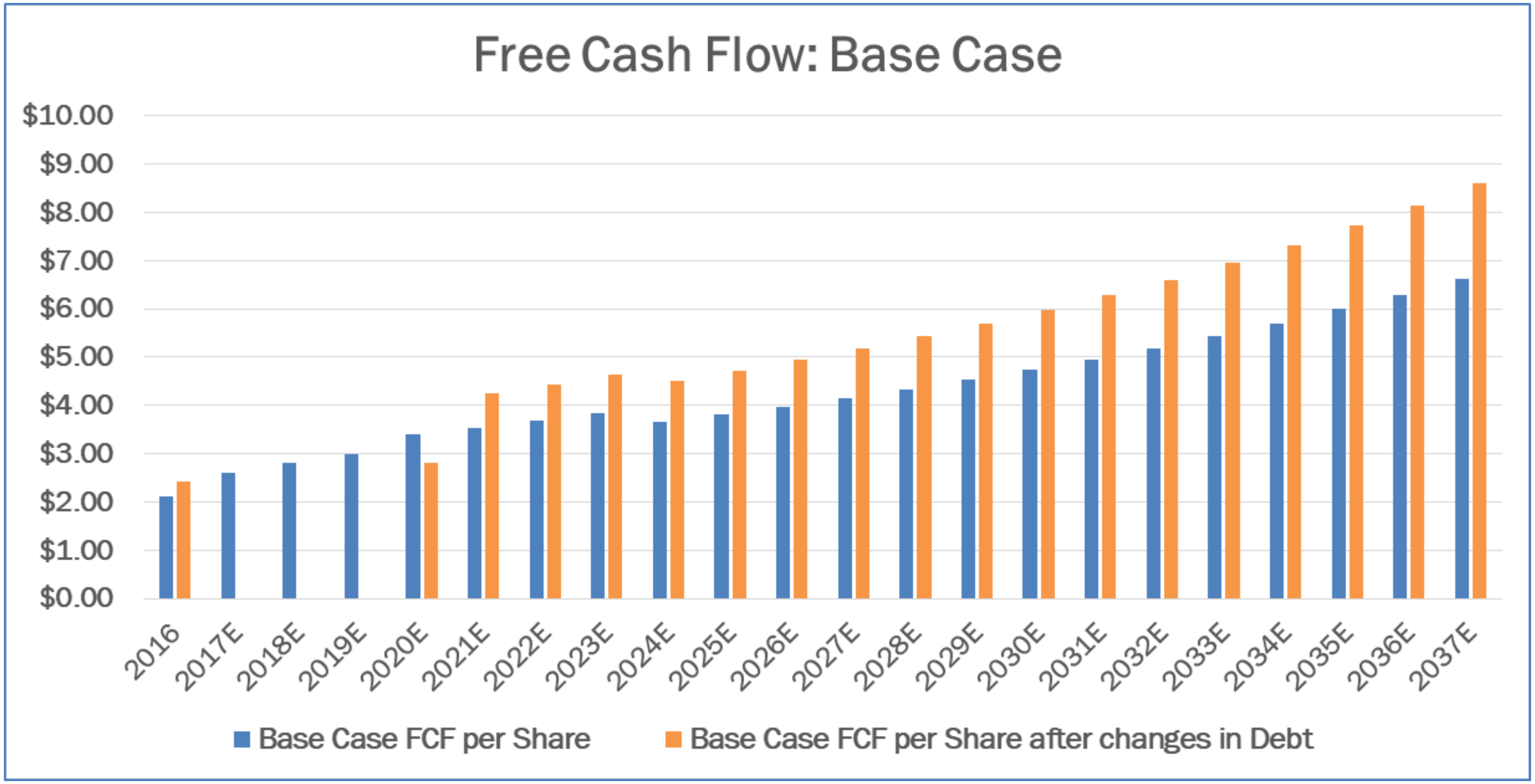
INVESTMENT PROCESS

Financial Modeling

Discovery/Scripps Pro-Forma Model: Base Case																									
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	5yr CAGR	10yr CAGR	20yr CAGR
Sales	9,753	10,135	9,639	9,565	10,100	10,466	10,851	11,257	11,685	12,138	12,616	13,121	13,655	14,221	14,820	15,455	16,129	16,843	17,602	18,408	19,264	20,175	1.4%	2.6%	3.5%
U.S. Networks	3,285	3,380	3,255	3,227	3,388	3,455	3,523	3,592	3,663	3,735	3,808	3,883	3,959	4,037	4,117	4,198	4,280	4,365	4,451	4,539	4,628	4,719	0.8%	1.4%	1.7%
Distribution	1,532	1,593	1,641	1,690	1,741	1,776	1,811	1,848	1,885	1,922	1,961	2,000	2,040	2,081	2,122	2,165	2,208	2,252	2,297	2,343	2,390	2,438	2.6%	2.3%	2.1%
% Growth		4.0%	3.0%	3.0%	3.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%			
Advertising	1,690	1,724	1,551	1,474	1,584	1,616	1,648	1,681	1,715	1,749	1,784	1,820	1,856	1,893	1,931	1,970	2,009	2,050	2,091	2,132	2,175	2,219	-0.9%	0.5%	1.3%
% Growth		2.0%	-10.0%	-5.0%	7.5%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%			
Other	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	0.0%	0.0%	0.0%
Scripps U.S. Networks	2,871	2,968	2,668	2,594	2,739	2,793	2,847	2,903	2,960	3,018	3,077	3,138	3,199	3,262	3,326	3,392	3,458	3,527	3,596	3,667	3,739	3,813	-0.8%	0.6%	1.3%
Distribution	786	802	818	834	851	868	885	903	921	939	958	977	997	1,017	1,037	1,058	1,079	1,100	1,122	1,145	1,168	1,191	2.0%	2.0%	2.0%
% Growth		2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%			
Advertising	2,029	2,110	1,794	1,704	1,832	1,868	1,906	1,944	1,983	2,022	2,063	2,104	2,146	2,189	2,233	2,278	2,323	2,370	2,417	2,465	2,515	2,565	-2.0%	0.0%	1.0%
% Growth		4.0%	-15.0%	-5.0%	7.5%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%			
Other	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	0.0%	0.0%	0.0%
International Networks	3,040	3,213	3,172	3,208	3,413	3,633	3,868	4,121	4,391	4,681	4,993	5,326	5,684	6,069	6,481	6,924	7,399	7,909	8,458	9,047	9,680	10,360	3.8%	5.2%	6.0%
Distribution	1,681	1,815	1,906	2,002	2,162	2,335	2,521	2,723	2,941	3,176	3,430	3,705	4,001	4,321	4,667	5,040	5,444	5,879	6,349	6,857	7,406	7,998	6.8%	7.4%	7.7%
% Growth		8.0%	5.0%	5.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%			
Advertising	1,279	1,317	1,186	1,126	1,171	1,218	1,267	1,318	1,370	1,425	1,482	1,541	1,603	1,667	1,734	1,803	1,875	1,950	2,028	2,110	2,194	2,282	-0.8%	1.6%	2.8%
% Growth		3.0%	-10.0%	-5.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%			
Other	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	0.0%	0.0%	0.0%
Scripps International Networks	557	574	543	535	559	585	612	641	671	704	738	774	812	853	896	942	991	1,042	1,097	1,155	1,217	1,283	1.3%	3.0%	4.1%
Distribution	109	114	123	133	144	155	167	181	195	211	228	246	266	287	310	335	361	390	422	455	492	531	8.0%	8.0%	8.0%
% Growth		5.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%			
Advertising	387	399	359	341	355	369	384	399	415	432	449	467	485	505	525	546	568	591	614	639	664	691	-0.8%	1.6%	2.8%
% Growth		3.0%	-10.0%	-5.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%			
Other	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	0.0%	0.0%	0.0%
EBITDA	3,839	3,928	3,824	3,930	4,280	4,435	4,598	4,772	4,955	5,150	5,358	5,578	5,812	6,061	6,326	6,609	6,910	7,231	7,574	7,940	8,331	8,749	3.2%	3.6%	4.1%
% Sales	39.4%	38.8%	39.7%	41.1%	42.4%	42.4%	42.4%	42.4%	42.4%	42.4%	42.5%	42.5%	42.6%	42.6%	42.7%	42.8%	42.8%	42.9%	43.0%	43.1%	43.2%	43.4%			
% Growth		2.3%	-2.6%	2.8%	8.9%	3.6%	3.7%	3.8%	3.9%	3.9%	4.0%	4.1%	4.2%	4.3%	4.4%	4.5%	4.6%	4.6%	4.7%	4.8%	4.9%	5.0%			
U.S. Networks	1,922	2,011	1,907	1,872	1,975	2,009	2,043	2,078	2,113	2,149	2,185	2,222	2,259	2,297	2,336	2,375	2,414	2,455	2,495	2,537	2,579	2,622	0.3%	1.0%	1.3%
% Sales	58.5%	59.5%	58.6%	58.0%	58.3%	58.1%	58.0%	57.8%	57.7%	57.5%	57.4%	57.2%	57.1%	56.9%	56.7%	56.6%	56.4%	56.2%	56.1%	55.9%	55.7%	55.5%			
Scripps U.S. Networks	1,413	1,445	1,347	1,385	1,472	1,497	1,522	1,547	1,573	1,599	1,625	1,652	1,679	1,706	1,734	1,763	1,791	1,820	1,850	1,880	1,910	1,941	1.0%	1.3%	1.5%
% Sales	49.2%	48.7%	50.5%	53.4%	53.8%	53.6%	53.4%	53.3%	53.1%	53.0%	52.8%	52.6%	52.5%	52.3%	52.1%	52.0%	51.8%	51.6%	51.4%	51.3%	51.1%	50.9%			
International Networks	848	836	858	918	1,071	1,166	1,270	1,381	1,502	1,633	1,774	1,926	2,091	2,269	2,462	2,670	2,894	3,137	3,399	3,682	3,988	4,318	8.7%	8.7%	8.6%
% Sales	27.9%	26.0%	27.1%	28.6%	31.4%	32.1%	32.8%	33.5%	34.2%	34.9%	35.5%	36.2%	36.8%	37.4%	38.0%	38.6%	39.1%	39.7%	40.2%	40.7%	41.2%	41.7%			
Scripps International Networks	100	113	133	134	149	157	166	176	187	198	210	222	236	251	266	283	301	320	340	362	386	411	8.0%	7.0%	6.7%
% Sales	18.0%	19.7%	24.5%	25.0%	26.6%	26.9%	27.2%	27.5%	27.8%	28.1%	28.4%	28.7%	29.1%	29.4%	29.7%	30.0%	30.4%	30.7%	31.0%	31.4%	31.7%	32.0%			
Corporate	(444)	(477)	(420)	(379)	(387)	(395)	(403)	(411)	(419)	(427)	(436)	(445)	(453)	(463)	(472)	(481)	(491)	(501)	(511)	(521)	(531)	(542)	-3.3%	-0.7%	0.6%
% Sales	-4.6%	-4.7%	-4.4%	-4.0%	-3.8%	-3.8%	-3.7%	-3.6%	-3.6%	-3.5%	-3.5%	-3.4%	-3.3%	-3.3%	-3.2%	-3.1%	-3.0%	-3.0%	-2.9%	-2.8%	-2.8%	-2.7%			
EPS		$2.60	$2.81	$3.00	$3.39	$3.54	$3.68	$3.83	$3.66	$3.82	$3.98	$4.15	$4.33	$4.52	$4.73	$4.95	$5.19	$5.44	$5.71	$5.99	$6.30	$6.63	7.3%	4.8%	4.8%
FCF		1,893	2,047	2,186	2,474	2,585	2,687	2,795	2,673	2,784	2,901	3,026	3,159	3,301	3,451	3,612	3,784	3,967	4,162	4,371	4,595	4,834	7.3%	4.8%	4.8%
% Net income		100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%			
Debt		18,608	16,561	14,375	13,947	14,467	15,019	15,605	16,228	16,890	17,595	18,346	19,145	19,996	20,904	21,872	22,906	24,009	25,188	26,447	27,794	29,235	-4.2%	-0.1%	2.3%
Target Debt/EBITDA			3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Actual Debt/EBITDA		5.11x	4.66x	3.93x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Target Change in Debt			(2,047)	(2,186)	(428)	520	552	586	623	663	705	750	799	851	908	968	1,033	1,103	1,179	1,260	1,347	1,441			
FCF including Changes in Debt			0	0	2,047	3,104	3,239	3,381	3,296	3,446	3,606	3,777	3,958	4,152	4,359	4,580	4,817	5,070	5,341	5,631	5,942	6,275	69,713		
% Net income																									

INVESTMENT PROCESS

Financial Modeling



- Assumes leverage is maintained at 3.5x Debt/EBITDA

INVESTMENT PROCESS

Financial Modeling

Key Assumptions: Worst Case	
U.S. Distribution Growth (LT)	-3.0%
U.S. Adveritising Growth (LT)	-1.0%
International Distribution Growth (LT)	0.0%
International Adveritising Growth (LT)	0.0%
One-time Decline in SNI Advertising	-10.0%
Advertising Recession Magnitude	-10.0%
Tax Rate	32.0%

- Scripps deal synergies of ~ $250M vs. management's $350M target
- Assume deal revenue dis-synergies from culture/integration issues cause a one-time 10% advertising decline for the legacy Scripps business
- Immediate advertising recession of 10% in 2018 and another 5% in 2019
- All of the benefits of the newly-passed lower US corporate tax rate competed away and passed through to customers
- No terminal value after 20 years

INVESTMENT PROCESS

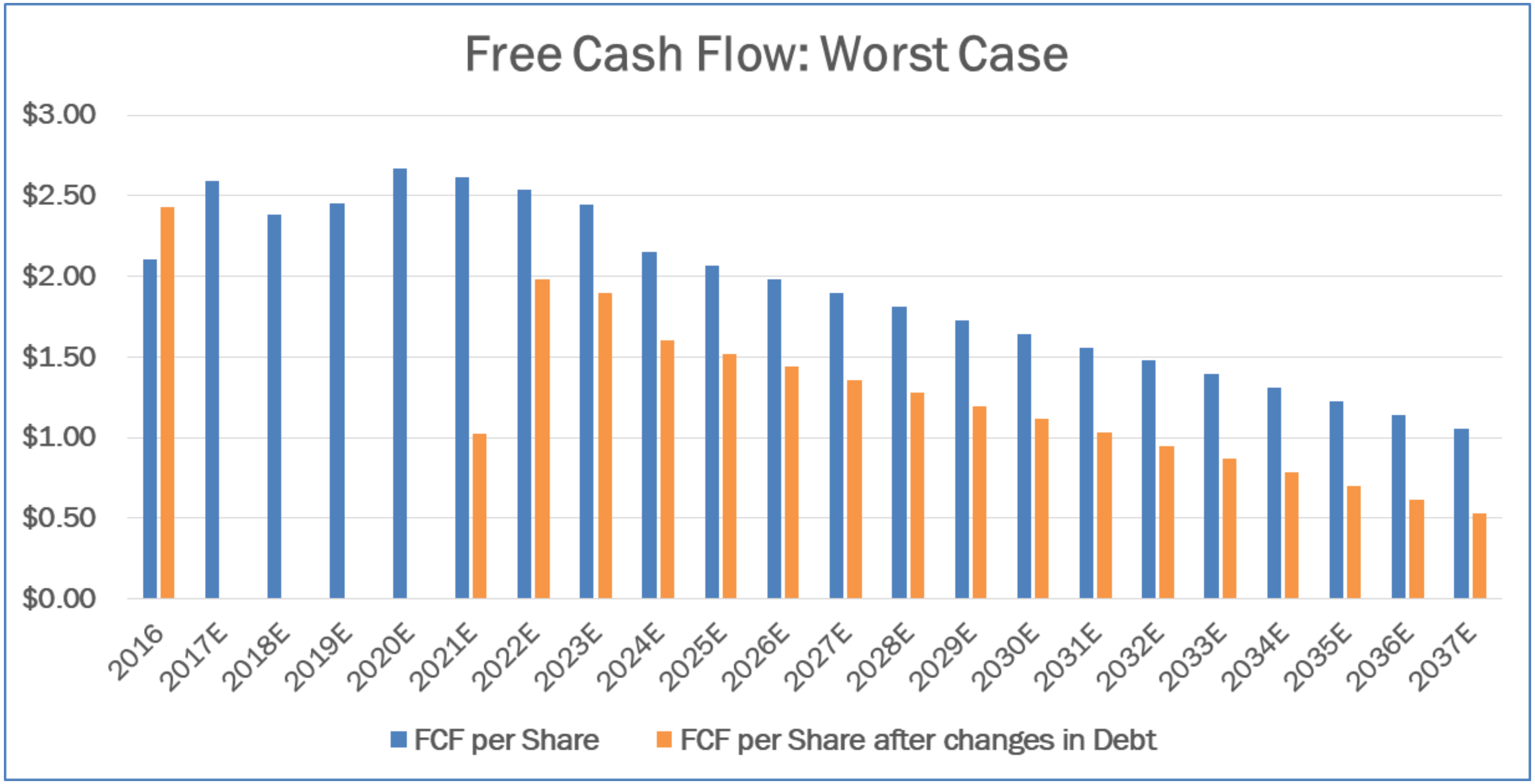
Financial Modeling

Discovery/Scripps Pro-Forma Model: Worst Case

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	5yr CAGR	10yr CAGR	20yr CAGR
Sales	9,753	10,135	9,527	9,452	9,751	9,640	9,532	9,426	9,323	9,222	9,124	9,028	8,935	8,843	8,754	8,667	8,581	8,498	8,417	8,337	8,260	8,184	-1.2%	-1.1%	-1.1%
U.S. Networks	3,285	3,380	3,255	3,227	3,388	3,320	3,254	3,189	3,126	3,065	3,005	2,946	2,889	2,834	2,780	2,727	2,675	2,625	2,576	2,528	2,481	2,436	-0.8%	-1.4%	-1.6%
Distribution	1,532	1,593	1,641	1,690	1,741	1,689	1,638	1,589	1,541	1,495	1,450	1,407	1,365	1,324	1,284	1,245	1,208	1,172	1,137	1,103	1,069	1,037	0.6%	-1.2%	-2.1%
% Growth		4.0%	3.0%	3.0%	3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%			
Advertising	1,690	1,724	1,551	1,474	1,584	1,569	1,553	1,537	1,522	1,507	1,492	1,477	1,462	1,447	1,433	1,419	1,404	1,390	1,376	1,363	1,349	1,336	-2.1%	-1.5%	-1.3%
% Growth		2.0%	-10.0%	-5.0%	7.5%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%			
Other	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	0.0%	0.0%	0.0%
Scripps U.S. Networks	2,871	2,968	2,562	2,494	2,631	2,588	2,547	2,506	2,466	2,427	2,388	2,351	2,314	2,278	2,243	2,209	2,175	2,142	2,110	2,078	2,047	2,017	-3.0%	-2.3%	-1.9%
Distribution	786	802	818	834	851	825	800	776	753	730	709	687	667	647	627	608	590	572	555	539	523	507	0.0%	-1.5%	-2.3%
% Growth		2.0%	2.0%	2.0%	2.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%	-3.0%			
Advertising	2,029	2,110	1,688	1,604	1,724	1,707	1,690	1,673	1,656	1,640	1,623	1,607	1,591	1,575	1,559	1,544	1,528	1,513	1,498	1,483	1,468	1,453	-4.3%	-2.7%	-1.8%
% Growth		4.0%	-20.0%	-5.0%	7.5%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%			
Other	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	0.0%	0.0%	0.0%
International Networks	3,040	3,213	3,172	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	3,208	0.0%	0.0%	0.0%
Distribution	1,681	1,815	1,906	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2,002	2.0%	1.0%	0.5%
% Growth		8.0%	5.0%	5.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%			
Advertising	1,279	1,317	1,186	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	1,126	-3.1%	-1.6%	-0.8%
% Growth		3.0%	-10.0%	-5.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%			
Other	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	0.0%	0.0%	0.0%
Scripps International Networks	557	574	538	523	523	523	523	523	523	523	523	523	523	523	523	523	523	523	523	523	523	523	-1.8%	-0.9%	-0.5%
Distribution	109	114	117	121	121	121	121	121	121	121	121	121	121	121	121	121	121	121	121	121	121	121	1.2%	0.6%	0.3%
% Growth		5.0%	3.0%	3.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%			
Advertising	387	399	359	341	341	341	341	341	341	341	341	341	341	341	341	341	341	341	341	341	341	341	-3.1%	-1.6%	-0.8%
% Growth		3.0%	-10.0%	-5.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%			
Other	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	0.0%	0.0%	0.0%
EBITDA	3,839	3,928	3,632	3,632	3,800	3,676	3,553	3,430	3,309	3,188	3,069	2,949	2,831	2,713	2,595	2,478	2,361	2,245	2,129	2,012	1,896	1,780	-2.0%	-2.8%	-3.9%
% Sales	39.4%	38.8%	38.1%	38.4%	39.0%	38.1%	37.3%	36.4%	35.5%	34.6%	33.6%	32.7%	31.7%	30.7%	29.6%	28.6%	27.5%	26.4%	25.3%	24.1%	23.0%	21.8%			
% Growth		2.3%	-7.5%	0.0%	4.6%	-3.3%	-3.4%	-3.4%	-3.5%	-3.6%	-3.8%	-3.9%	-4.0%	-4.2%	-4.3%	-4.5%	-4.7%	-4.9%	-5.2%	-5.5%	-5.8%	-6.1%			
U.S. Networks	1,922	2,011	1,911	1,881	1,990	1,930	1,872	1,815	1,758	1,703	1,649	1,595	1,542	1,490	1,439	1,389	1,339	1,290	1,242	1,194	1,147	1,101	-1.4%	-2.3%	-3.0%
% Sales	58.5%	59.5%	58.7%	58.3%	58.7%	58.1%	57.5%	56.9%	56.2%	55.6%	54.9%	54.1%	53.4%	52.6%	51.8%	50.9%	50.1%	49.2%	48.2%	47.2%	46.2%	45.2%			
Scripps U.S. Networks	1,413	1,445	1,244	1,239	1,323	1,284	1,245	1,207	1,169	1,131	1,094	1,057	1,020	984	948	912	877	841	806	772	737	703	-2.9%	-3.1%	-3.5%
% Sales	49.2%	48.7%	48.5%	49.7%	50.3%	49.6%	48.9%	48.2%	47.4%	46.6%	45.8%	45.0%	44.1%	43.2%	42.3%	41.3%	40.3%	39.3%	38.2%	37.1%	36.0%	34.8%			
International Networks	848	836	802	805	790	775	760	744	728	712	695	678	661	644	626	607	589	570	550	531	510	490	-1.9%	-2.1%	-2.6%
% Sales	27.9%	26.0%	25.3%	25.1%	24.6%	24.2%	23.7%	23.2%	22.7%	22.2%	21.7%	21.1%	20.6%	20.1%	19.5%	18.9%	18.4%	17.8%	17.2%	16.5%	15.9%	15.3%			
Scripps International Networks	100	113	95	87	84	81	78	76	73	70	67	64	61	57	54	51	47	44	41	37	33	30	-7.1%	-5.6%	-6.5%
% Sales	18.0%	19.7%	17.7%	16.5%	16.0%	15.5%	15.0%	14.4%	13.9%	13.3%	12.8%	12.2%	11.6%	11.0%	10.4%	9.7%	9.1%	8.4%	7.7%	7.1%	6.4%	5.6%			
Corporate	(444)	(477)	(420)	(379)	(387)	(395)	(403)	(411)	(419)	(427)	(436)	(445)	(453)	(463)	(472)	(481)	(491)	(501)	(511)	(521)	(531)	(542)	-3.3%	-0.7%	0.6%
% Sales	-4.6%	-4.7%	-4.4%	-4.0%	-4.0%	-4.1%	-4.2%	-4.4%	-4.5%	-4.6%	-4.8%	-4.9%	-5.1%	-5.2%	-5.4%	-5.6%	-5.7%	-5.9%	-6.1%	-6.2%	-6.4%	-6.6%			
Interest Rate		4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%			
Tax Rate		32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%			
EPS		$2.59	$2.39	$2.45	$2.67	$2.62	$2.54	$2.45	$2.15	$2.06	$1.98	$1.90	$1.81	$1.73	$1.64	$1.56	$1.48	$1.39	$1.31	$1.22	$1.14	$1.06	-0.4%	-3.1%	-4.4%
FCF		1,890	1,741	1,791	1,945	1,908	1,851	1,784	1,568	1,506	1,444	1,383	1,322	1,260	1,199	1,138	1,077	1,016	955	893	832	771	-0.4%	-3.1%	-4.4%
% Net income		100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%			
Debt		18,608	16,867	15,077	13,132	11,968	11,562	11,159	10,759	10,363	9,968	9,576	9,186	8,798	8,412	8,026	7,642	7,259	6,877	6,495	6,113	5,731	-9.1%	-6.4%	-5.7%
Target Debt/EBITDA			3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Actual Debt/EBITDA		5.11x	4.98x	4.45x	3.71x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Target Change in Debt			(1,741)	(1,791)	(1,945)	(1,164)	(406)	(403)	(400)	(397)	(394)	(392)	(390)	(388)	(387)	(385)	(384)	(383)	(382)	(382)	(382)	(382)			
FCF including Changes in Debt			0	0	0	745	1,445	1,381	1,168	1,109	1,050	991	932	872	813	753	693	633	572	511	450	389			

INVESTMENT PROCESS

Financial Modeling



- Assumes the need to pay down debt to remain at 3.5x Debt/EBITDA
- No free cash flow after 20 years

INVESTMENT PROCESS

Financial Modeling

Key Assumptions: Best Case	
U.S. Distribution Growth (LT)	**5.0%**
U.S. Adveritising Growth (LT)	**5.0%**
International Distribution Growth (LT)	**10.0%**
International Adveritising Growth (LT)	**10.0%**
One-time Decline in SNI Advertising	**0.0%**
Advertising Recession Magnitude	**-5.0%**
Tax Rate	**21.0%**

- Scripps deal synergies of ~ $400M vs. management's $350M target
- Assume no deal revenue dis-synergies from culture/integration issues
- Immediate advertising recession of 5% in 2018 and another 2.5% in 2019
- All of the benefits of the newly-passed lower US corporate tax rate retained by the company

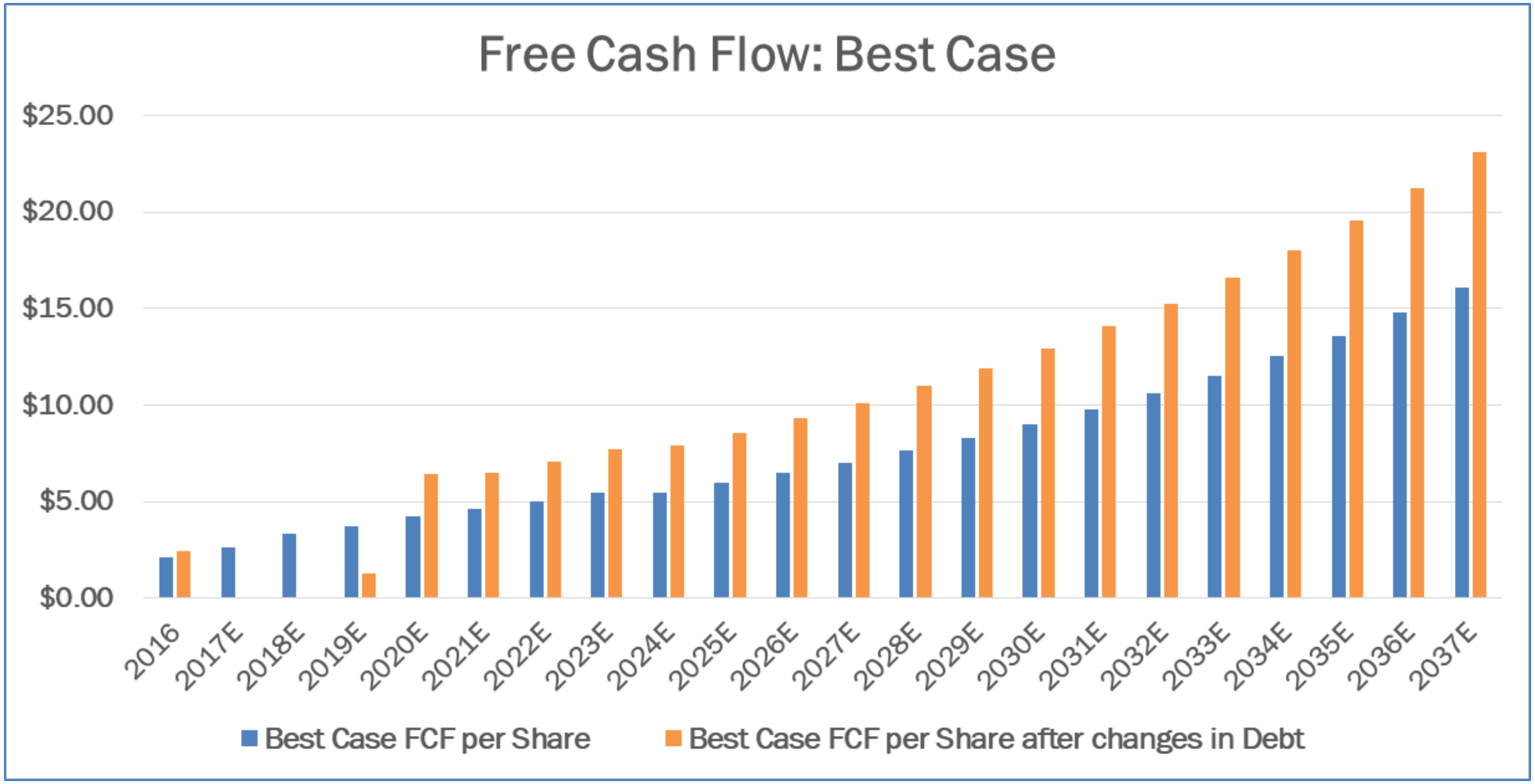
INVESTMENT PROCESS

Financial Modeling

Discovery/Scripps Pro-Forma Model: Best Case																									
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	5yr CAGR	10yr CAGR	20yr CAGR
Sales	**9,753**	**10,135**	**9,938**	**9,943**	**10,504**	**11,215**	**11,981**	**12,807**	**13,698**	**14,661**	**15,700**	**16,824**	**18,038**	**19,352**	**20,775**	**22,315**	**23,984**	**25,792**	**27,754**	**29,882**	**32,192**	**34,700**	**3.4%**	**5.2%**	**6.3%**
U.S. Networks	**3,285**	**3,380**	**3,342**	**3,350**	**3,461**	**3,630**	**3,809**	**3,996**	**4,193**	**4,399**	**4,616**	**4,844**	**5,083**	**5,334**	**5,597**	**5,874**	**6,165**	**6,470**	**6,790**	**7,126**	**7,479**	**7,850**	**2.4%**	**3.7%**	**4.3%**
Distribution	1,532	1,593	1,641	1,690	1,741	1,828	1,919	2,015	2,116	2,222	2,333	2,450	2,572	2,701	2,836	2,978	3,127	3,283	3,447	3,619	3,800	3,990	**3.8%**	**4.4%**	**4.7%**
% Growth		**4.0%**	**3.0%**	3.0%	3.0%	**5.0%**	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%			
Advertising	1,690	1,724	1,638	1,597	1,657	1,739	1,826	1,918	2,014	2,114	2,220	2,331	2,447	2,570	2,698	2,833	2,975	3,124	3,280	3,444	3,616	3,797	**1.2%**	**3.1%**	**4.0%**
% Growth		**2.0%**	**-5.0%**	**-2.5%**	**3.8%**	**5.0%**	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%			
Other	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	63	**0.0%**	**0.0%**	**0.0%**
Scripps U.S. Networks	**2,871**	**2,968**	**2,879**	**2,845**	**2,935**	**3,079**	**3,230**	**3,389**	**3,555**	**3,730**	**3,914**	**4,107**	**4,309**	**4,522**	**4,745**	**4,980**	**5,226**	**5,484**	**5,756**	**6,041**	**6,340**	**6,654**	**1.7%**	**3.3%**	**4.1%**
Distribution	786	802	818	834	851	893	938	985	1,034	1,086	1,140	1,197	1,257	1,320	1,386	1,455	1,528	1,604	1,684	1,768	1,857	1,950	**3.2%**	**4.1%**	**4.5%**
% Growth		**2.0%**	**2.0%**	2.0%	2.0%	**5.0%**	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%			
Advertising	2,029	2,110	2,005	1,955	2,028	2,129	2,236	2,348	2,465	2,588	2,718	2,853	2,996	3,146	3,303	3,468	3,642	3,824	4,015	4,216	4,427	4,648	**1.2%**	**3.1%**	**4.0%**
% Growth		**4.0%**	**-5.0%**	**-2.5%**	**3.8%**	**5.0%**	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%			
Other	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	56	**0.0%**	**0.0%**	**0.0%**
International Networks	**3,040**	**3,213**	**3,172**	**3,208**	**3,521**	**3,865**	**4,243**	**4,660**	**5,118**	**5,621**	**6,175**	**6,785**	**7,455**	**8,193**	**9,004**	**9,897**	**10,878**	**11,958**	**13,146**	**14,453**	**15,890**	**17,471**	**5.7%**	**7.8%**	**8.8%**
Distribution	1,681	1,815	1,906	2,002	2,202	2,422	2,664	2,930	3,224	3,546	3,900	4,291	4,720	5,192	5,711	6,282	6,910	7,601	8,361	9,197	10,117	11,129	**8.0%**	**9.0%**	**9.5%**
% Growth		**8.0%**	**5.0%**	5.0%	**10.0%**	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%			
Advertising	1,279	1,317	1,186	1,126	1,239	1,363	1,499	1,649	1,814	1,995	2,195	2,414	2,656	2,921	3,214	3,535	3,888	4,277	4,705	5,176	5,693	6,262	**2.6%**	**6.2%**	**8.1%**
% Growth		**3.0%**	#####	**-5.0%**	**10.0%**	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%			
Other	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	80	**0.0%**	**0.0%**	**0.0%**
Scripps International Networks	**557**	**574**	**546**	**540**	**588**	**641**	**699**	**762**	**833**	**910**	**995**	**1,088**	**1,191**	**1,304**	**1,428**	**1,564**	**1,715**	**1,880**	**2,062**	**2,262**	**2,482**	**2,724**	**4.0%**	**6.6%**	**8.1%**
Distribution	109	114	125	138	152	167	184	202	222	244	269	296	325	358	393	433	476	524	576	634	697	767	**10.0%**	**10.0%**	**10.0%**
% Growth		**5.0%**	**10.0%**	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%			
Advertising	387	399	359	341	375	413	454	499	549	604	665	731	804	885	973	1,070	1,178	1,295	1,425	1,567	1,724	1,896	**2.6%**	**6.2%**	**8.1%**
% Growth		**3.0%**	#####	**-5.0%**	**10.0%**	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%			
Other	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	61	**0.0%**	**0.0%**	**0.0%**
EBITDA	**3,839**	**3,928**	**4,155**	**4,428**	**4,895**	**5,312**	**5,763**	**6,251**	**6,778**	**7,349**	**7,967**	**8,636**	**9,361**	**10,147**	**10,998**	**11,922**	**12,923**	**14,010**	**15,190**	**16,471**	**17,862**	**19,374**	**8.0%**	**8.2%**	**8.3%**
% Sales	**39.4%**	**38.8%**	**41.8%**	**44.5%**	**46.6%**	**47.4%**	**48.1%**	**48.8%**	**49.5%**	**50.1%**	**50.7%**	**51.3%**	**51.9%**	**52.4%**	**52.9%**	**53.4%**	**53.9%**	**54.3%**	**54.7%**	**55.1%**	**55.5%**	**55.8%**			
% Growth		**2.3%**	**5.8%**	**6.6%**	**10.6%**	**8.5%**	**8.5%**	**8.5%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**	**8.5%**			
U.S. Networks	1,922	2,011	1,974	1,971	2,042	2,157	2,277	2,404	2,537	2,677	2,825	2,980	3,143	3,315	3,496	3,686	3,886	4,097	4,318	4,551	4,796	5,053	**2.5%**	**4.0%**	**4.7%**
% Sales	58.5%	59.5%	59.1%	58.8%	59.0%	59.4%	59.8%	60.1%	60.5%	60.9%	61.2%	61.5%	61.8%	62.2%	62.5%	62.8%	63.0%	63.3%	63.6%	63.9%	64.1%	64.4%			
Scripps U.S. Networks	1,413	1,445	1,522	1,606	1,661	1,753	1,850	1,951	2,059	2,172	2,290	2,415	2,546	2,685	2,830	2,983	3,144	3,313	3,491	3,678	3,874	4,081	**5.1%**	**5.3%**	**5.3%**
% Sales	49.2%	48.7%	52.9%	56.4%	56.6%	56.9%	57.3%	57.6%	57.9%	58.2%	58.5%	58.8%	59.1%	59.4%	59.6%	59.9%	60.2%	60.4%	60.6%	60.9%	61.1%	61.3%			
International Networks	848	836	929	1,061	1,363	1,554	1,766	2,000	2,259	2,545	2,861	3,210	3,595	4,020	4,488	5,006	5,576	6,205	6,898	7,662	8,505	9,433	**16.1%**	**14.4%**	**12.9%**
% Sales	27.9%	26.0%	29.3%	33.1%	38.7%	40.2%	41.6%	42.9%	44.1%	45.3%	46.3%	47.3%	48.2%	49.1%	49.8%	50.6%	51.3%	51.9%	52.5%	53.0%	53.5%	54.0%			
Scripps International Networks	100	113	150	169	217	244	273	306	343	383	427	476	530	590	655	728	808	896	994	1,101	1,219	1,349	**19.3%**	**15.5%**	**13.2%**
% Sales	18.0%	19.7%	27.6%	31.3%	36.9%	38.0%	39.1%	40.2%	41.1%	42.1%	42.9%	43.8%	44.5%	45.2%	45.9%	46.5%	47.1%	47.7%	48.2%	48.7%	49.1%	49.5%			
Corporate	(444)	(477)	(420)	(379)	(387)	(395)	(403)	(411)	(419)	(427)	(436)	(445)	(453)	(463)	(472)	(481)	(491)	(501)	(511)	(521)	(531)	(542)	**-3.3%**	**-0.7%**	**0.6%**
% Sales	-4.6%	-4.7%	-4.2%	-3.8%	-3.7%	-3.5%	-3.4%	-3.2%	-3.1%	-2.9%	-2.8%	-2.6%	-2.5%	-2.4%	-2.3%	-2.2%	-2.0%	-1.9%	-1.8%	-1.7%	-1.7%	-1.6%			
EPS		**$2.60**	**$3.35**	**$3.73**	**$4.24**	**$4.61**	**$5.02**	**$5.46**	**$5.47**	**$5.95**	**$6.47**	**$7.02**	**$7.63**	**$8.29**	**$9.00**	**$9.77**	**$10.62**	**$11.53**	**$12.52**	**$13.60**	**$14.77**	**$16.04**	**14.1%**	**10.5%**	**9.5%**
FCF		**1,895**	**2,446**	**2,722**	**3,090**	**3,361**	**3,660**	**3,982**	**3,992**	**4,340**	**4,716**	**5,124**	**5,566**	**6,046**	**6,566**	**7,130**	**7,743**	**8,409**	**9,133**	**9,919**	**10,774**	**11,704**	**14.1%**	**10.5%**	**9.5%**
% Net income		**100%**	**100%**	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%			
Debt		**18,608**	**16,162**	**14,369**	**15,961**	**17,351**	**18,857**	**20,488**	**22,256**	**24,172**	**26,249**	**28,502**	**30,944**	**33,595**	**36,471**	**39,593**	**42,984**	**46,667**	**50,668**	**55,018**	**59,747**	**64,890**	**0.3%**	**4.4%**	**6.4%**
Target Debt/EBITDA			**3.50x**	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Actual Debt/EBITDA		5.11x	4.20x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x	3.50x			
Target Change in Debt			#####	(1,793)	1,593	1,390	1,506	1,631	1,768	1,916	2,077	2,252	2,443	2,650	2,876	3,122	3,390	3,683	4,002	4,350	4,729	5,143			
FCF including Changes in Debt			**0**	**928**	**4,682**	**4,751**	**5,165**	**5,613**	**5,760**	**6,256**	**6,793**	**7,376**	**8,009**	**8,696**	**9,442**	**10,253**	**11,134**	**12,092**	**13,134**	**14,269**	**15,503**	**16,847**	**168,769**		
% Net income																									

INVESTMENT PROCESS

Financial Modeling



- Assumes leverage is maintained at 3.5x Debt/EBITDA

INVESTMENT PROCESS

Security Research and Valuation

Step 4 **Valuation**

- Estimate the range of intrinsic values for the business using Discounted Cash Flow (DCF) analysis
- Perform sanity checks on each part of the range by checking other valuation metrics, such as normalized P/E, EV/EBITA, and Price to Book (P/B) ratios

INVESTMENT PROCESS

Valuation

Discovery Communications (DISCK) Valuation - Pro-forma for SNI				
	Worst	Base	Best	LFY
DCF Value	**$8**	**$48**	**$103**	
Price	$22.30	$22.30	$22.30	
Price % Value	**280%**	**47%**	**22%**	
Expected Return	**-64%**	**113%**	**360%**	
IRR	**-1%**	**15%**	**25%**	
Implied P/E on Normalized EPS	3.6x	17.0x	29.3x	
Current P/E on Normalized EPS	10.1x	8.0x	6.4x	9.4x
Implied EV/EBITA (2018E)	7.1x	14.7x	23.5x	
Current EV/EBITA (2018E)	10.1x	9.6x	8.8x	9.4x
12/26/2017				

- Primary valuation tool is a DCF of equity cash flows using a 10% discount rate
- Worst case has no terminal value; Other scenarios assume 3% terminal growth rate
- Another way of looking at the Base case is that if we were to buy the company today and own it forever and are right on our cash flow forecast, we would get a 15% IRR

INVESTMENT PROCESS

Valuation

Valuation Checks						
	Base Case Normalized	DISCK 5yr Avg	TWX Acquisition	Disney - Fox Deal	FOXA Current	DIS
P/E	17.0x	15.3x	16.5x		16.8x	17.4x
EV/EBITA	14.7x	12.5x	11.7x	12.0x	11.3x	12.5x

Source: Company Reports, Bloomberg, Silver Ring Value Partners estimates

- Valuation implied by the Base Case is reasonable, but slightly higher than some of the valuation checks
- This makes sense as:
  - Last 5 year history is affected by the negative sector sentiment of the last few years
  - Some of the EV/EBITA valuation checks were prior to US tax rate change

<u>Good News:</u> At either the current price of ~ $22 or when I increased DISCK to a ~ 10% position ($16.75), if I am correct that the company is likely to earn ~ $3/share in EPS/FCF in a couple of years at a sustainable capital structure and grow from there, then the stock is really undervalued and **has a large margin of safety**.

INVESTMENT PROCESS

Valuation – Sensitivity Analysis

Additional Sensitivity Analysis			
Key Assumption Change	**Change in Base Case Value**	**New Base Case Value**	**New Price % Value**
U.S. Business Goes Away after 5 years	$25	$22	97%
No Benefit to FCF from Increasing Debt Inline with EBITDA	$6	$41	53%
1% Decrease in the International Business's LT Growth Rate	$4	$43	50%
1% Decrease in the U.S. Business's LT Growth Rate	$4	$43	50%
No Benefit from Lower US Tax Rate	$4	$44	51%
Additional 20% Immediate Decline in Scripps Advertising Sales	$3	$44	51%

- Hard to make reasonable changes to assumptions to make the stock *unattractive* at the current price

INVESTMENT PROCESS

Security Research and Valuation

Step 5 **Behavioral Checklist**

- Ask a series of questions to guard against behavioral biases before finalizing the analysis
- Checklist includes questions such as:
  - Have the most recent developments – positive or negative – colored the analysis of the company's prospects disproportionately to their long-term significance?
  - If the markets closed and I couldn't sell this security for five years, would I be comfortable owning it?
  - Do I have emotions – positive or negative – towards this investment?

In this case, there are three specific potential behavioral biases:

- *Anchoring* – I owned the position for a long time before increasing it to 10%
- *Base-rate Neglect* – Large deals such as the acquisition of SNI have a track record of destroying value
- *Overconfidence* – Both mine and the management team's

INVESTMENT PROCESS

Behavioral Checklist

How I addressed the potential behavioral biases:

Anchoring – I re-underwrote the investment from scratch, including brand new models built without reference to the old models. I also spent a substantial amount of time analyzing financial leverage and secular industry issues in the context of new data.

Base-Rate Neglect – I assumed a meaningful (5%) revenue loss from culture issues at the acquired company, Scripps. These are the kind of issues that typically cause such deals to underperform. The implied equity IRR on the deal in my Base Case is ~ 9%, implying moderate value destruction.

Overconfidence – Management only highlights the positives and does not like to talk about the negatives in a balanced fashion. I sought out negative information and opinions, including performing a 'devil's advocate' exercise with another knowledgeable investor.

INVESTMENT PROCESS

Behavioral Checklist

SNI Acquisition Economics

Cost	10,730
Cash	8,400
Stock	7,039
Debt @ 3.5x Leverage	4,709
IRR (Base)	**9.3%**
FCF Yield (2020)	**7.8%**
EV/EBITA (2020)	**11.8x**

Base Case SNI Contribution

	2018	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**	**2033**	**2034**	**2035**	**2036**	**2037**	**TV**
EBITA	1,133	1,221	1,314	1,347	1,380	1,414	1,447	1,482	1,517	1,552	1,589	1,627	1,666	1,706	1,748	1,791	1,835	1,881	1,929	1,980	
EBITDA	1,181	1,260	1,345	1,373	1,401	1,431	1,462	1,493	1,526	1,560	1,595	1,632	1,670	1,709	1,750	1,793	1,837	1,883	1,931	1,981	
Debt	5,499	4,957	4,709	4,805	4,905	5,008	5,115	5,226	5,341	5,461	5,584	5,712	5,845	5,983	6,126	6,275	6,429	6,590	6,758	6,932	
Leverage	4.7x	3.9x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	3.5x	
Interest Rate	**4%**	4%	4%	4%	4%	4%	4%	4%	4%	4%	**6%**	6%	6%	6%	6%	6%	6%	6%	6%	6%	
Interest Expense	220	198	188	192	196	200	205	209	214	218	335	343	351	359	368	376	386	395	405	416	
Taxes	238	266	293	300	308	315	323	331	339	347	326	334	342	350	359	368	377	386	396	407	
Tax Rate	**26%**	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	26%	
FCF	**676**	**757**	**833**	**854**	**876**	**898**	**920**	**942**	**964**	**987**	**928**	**950**	**973**	**997**	**1,021**	**1,046**	**1,073**	**1,100**	**1,128**	**1,157**	**16,685**
FCF including changes in Debt	**135**	**508**	**929**	**954**	**980**	**1,005**	**1,031**	**1,057**	**1,083**	**1,111**	**1,056**	**1,083**	**1,111**	**1,140**	**1,170**	**1,201**	**1,233**	**1,267**	**1,302**	**1,157**	**16,685**

INVESTMENT PROCESS

Portfolio Construction

Quality Assessment:

- Margin of Safety comes from considering the combination of the quality of the company and the discount to intrinsic value.
- The goal is to avoid below-average businesses, as it is too hard to estimate their value accurately.
- The minimum required expected IRR is 12% for the highest quality businesses and increases to 15% for average businesses.

PURCHASE GUIDELINES

	Business Quality		
	Average	Above Average	Excellent
Price as % of base case value	<55%	<65%	<75%

- Discovery Communications clearly qualifies for purchase as my Business Quality assessment is ‘Above Average’ and the stock is priced at less than 65% of Base Case value

INVESTMENT PROCESS

Portfolio Construction

Position Sizing:

Three principles are used to size positions within the portfolio:

- Portfolio at Risk (PaR) – PaR is the position size multiplied by the downside to the worst case value estimate. As an example, a 10% position with worst case downside of 30% would have a PaR of 3%. PaR will typically not exceed 5% at purchase.
- Risk of permanent capital loss declines as company quality increases. Increasingly higher quality parameters are a prerequisite for larger positions in the portfolio.
- No position size should be so large that a complete loss, however improbable, would result in capital loss that the rest of the portfolio would be unable to overcome.

POSITION SIZING GUIDELINES

	Position Size		
	Small (5%)	Medium (10%)	Large (15%)
Price as % of Base case value	<75%	<75%	<75%
Business quality	Average+	Average+	Above Average+
Balance Sheet quality	Any	Average+	Above Average+
Management quality	Any	Average+	Above Average+
Downside to Worst case	Any	<35%	<35%

INVESTMENT PROCESS

Portfolio Construction

Three potential problems with the investment:

1. *Financial Leverage* – the company is taking on a fair amount of debt (almost 5x leverage) at a time that I believe to be well past the mid-point of the economic cycle. This contributes to the large downside of the Worst case which would eliminate the company from consideration for a Medium or Large position.
2. *Deal Integration Risk* – the company is about to attempt to digest another large company, which entails a risk of a culture clash or distraction leading to poor results.
3. *Secular Headwinds, Especially in the U.S.* – It is far better to have secular trends be a tailwind than a headwind. There is always the possibility that I am wrong and that the U.S. Pay TV ecosystem unravels faster than I expect and the company is unable to make the transition to a direct-to-consumer model.

INVESTMENT PROCESS

Portfolio Construction – Discovery Communications Position Sizing

Position Size Based on Position Sizing Guidelines as of 11/22/2017							
Position Size	Price	Price % Base Case Value	Expected Return to Base Case	Downside to Worst Case	Expected Return to Best Case	Portfolio at Risk (PaR)	Portfolio Contribution at Base Case
5.0%	$16.77	38.5%	160%	-53%	436%	-2.6%	8.0%

- Based on the position sizing guidelines, Discovery would only have qualified as a small position (5%), due to its downside to Worst Case being greater than 35%

Position Size with Hedge (Put Option) Based on Position Sizing Guidelines as of 11/22/2017							
Position Size	Price	Price % Base Case Value	Expected Return to Base Case	Downside to Worst Case	Expected Return to Best Case	Portfolio at Risk (PaR)	Portfolio Contribution at Base Case
Discovery Stock (DISCK)	$16.77						
Put Option (Jan 2020, Strike = $15)	$3.24						
10.0%	$20.01	45.9%	118%	-25%	349%	-2.5%	11.8%

- By hedging this position with a 2020 Put Option, we can substantially reduce the downside and therefore take a much larger position
- Usually, such hedging is too expensive over the foreseeable time horizon of the investment
- However, in this case most of the important negative developments are likely to be known in the next 24 months (e.g. SNI deal integration risk, ability to de-lever from high financial leverage without tripping debt covenants), so this is a one-time hedge
- We will also have two more years' worth of information about the pace of the secular issues facing the Pay TV ecosystem, allowing us to update our assumptions and re-assess

Bottom Line: Discovery hedged with a 2020 Put option presented an attractive investment with moderate risk. Investment is still attractive today despite the stock having risen to $22.

INVESTMENT PROCESS

Portfolio Construction – Discovery Communications at the Current Price

Position Size with Hedge (Put Option) Based on Position Sizing Guidelines as of 12/27/2017							
Position Size	Price	Price % Base Case Value	Expected Return to Base Case	Downside to Worst Case	Expected Return to Best Case	Portfolio at Risk (PaR)	Portfolio Contribution at Base Case
Discovery Stock (DISCK)	$21.74						
Put Option (Jan 2020, Strike = $15)	$2.18						
10.0%	$23.92	50.3%	99%	-37%	329%	-3.7%	9.9%

- Investment still offers attractive returns and risk/reward at current prices
- Downside protection is reduced
- Current Base/Best cases ~ 10% higher due to U.S. tax rate change

Position Size with Hedge (Put Option) Based on Position Sizing Guidelines as of 12/27/2017							
Position Size	Price	Price % Base Case Value	Expected Return to Base Case	Downside to Worst Case	Expected Return to Best Case	Portfolio at Risk (PaR)	Portfolio Contribution at Base Case
Discovery Stock (DISCK)	$21.74						
Put Option (Jan 2020, Strike = $20)	$3.83						
10.0%	$25.57	53.8%	86%	-22%	301%	-2.2%	8.6%

- At current prices, changing the strike price of the Put option from $15 to $20 would achieve moderate downside with a still significant amount of expected return
- I am using the mid-price for the Put options here – in practice the bid/ask spread is very wide and your results could deviate from the above to some degree

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