

Analysis of the Walt Disney's acquisition of 21st Century Fox

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Abstract. The film and television entertainment industry is a rapidly evolving industry, which must launch products in a short amount of time to cater to the audience. Otherwise, audience loss and a decline in profitability may result. Therefore, acquisition is a crucial business decision for film and entertainment companies, as it expedites the establishment of a production chain. This paper focuses on a series of implications for both companies and the film and entertainment industry as a result of Walt Disney's acquisition of 21st Century Fox. The impact of Disney's acquisition of Fox to launch the streaming service Disney+ on Disney's business position is analyzed in terms of financial data, box office revenues, and other aspects. According to the analysis, Disney has benefited from the acquisition. This acquisition has placed Disney at the top of the U.S. box office and given it the ability to compete with streaming companies like Netflix in the streaming service industry. However, there are also limitations and deficiencies, e.g., it may make the market less diverse. Therefore, in addition to a discussion of the limitations and flaws, this study offers substantial recommendations to allow Disney to simultaneously protect its intellectual property and expand its audience to increase viewership and prevent box office losses.

Keywords: Disney; 21st Century Fox; Acquisition; Streaming.

1. Introduction

The entertainment and media industry is a rapidly evolving and expanding sector. To meet customer demand for high-quality material on the Internet, the media market must reorganize, and businesses are urged to digitally alter their products [1]. For this reason, it is crucial for the film and entertainment industry to rapidly improve a company competency or expand a business field. Therefore, merger and acquisition are an efficient business strategy for entertainment and media industry acquisitions and mergers. The reason is that it allows companies to have a mature technology or product production chain directly to meet market demand, while solidifying their business value and position. Acquisition is a business technique used to integrate the competitive advantages of two or more companies into a single corporate entity. As a result, it hopes to create the "one plus one is greater than two" impact and ultimately achieve better stock market performance [2].

The Walt Disney Company (henceforth referred to as Disney) completed the acquisition of Pixar in 2006. The benefit of Pixar animation is the industry-leading 3D animation production technology. TinToy, an animated short made by Pixar in 1988, received the Academy Award for best animated short film. The rate of development has accelerated since then. When Pixar used 3D technology to make animation works throughout the rise of the global market, Disney sensed the technological disparity. Disney and Pixar inked a deal to make three animated feature films in May 1991. According to the agreement, Disney is responsible for the distribution of animation produced by Pixar, and the two companies divide production costs and box office proceeds. Clearly, the teamwork was exceptional, as the first animated feature film "Toy Story" grossed \$362 million worldwide in 1995. Previous collaboration demonstrated the viability of Disney's acquisition of Pixar. After the completion of the merger and acquisition, the method of short-term window analysis created a scenario in which Pixar shareholders reaped greater gains, totaling \$48 per share in anomalous returns on the day of the transaction [3]. At the same time, Pixar also took a high amount of box office for Disney. The 2007 release of Total Food Story took in \$205 million. These data demonstrate that the acquisition has created beneficial synergies.

The primary objective of this paper is to investigate whether acquisitions are a viable strategy for film and entertainment companies to quickly broaden their business direction and strengthen their

market position. This paper begins by discussing the background, how, and why of Disney's acquisition of Fox. It then analyzes the impact of the acquisition on the two companies, their competitors, and the market through the ROA, EPS and other indicators. Finally, it will conclude with recommendations for similar acquisitions and a pertinent conclusion.

2. Case Descriptions

2.1. Background

On March 20, 2019, Disney finalized its USD 71 billion acquisition of 21st Century Fox, Inc.'s (henceforth referred to as Fox) entertainment holdings [4]. Disney now owns the majority of 21st Century Fox's entertainment holdings, including 20th Century Fox, FX, National Geographic, and Fox's 30% stake in Hulu, as a result of the acquisition. This transaction occurred at a time when the entire industry was struggling [5]. According to IMDbPro's Box Office report, the annual domestic box office in the United States declined by 4.8% in 2019 compared to 2018. Additionally, it is the steepest fall in the previous five years. This is attributable to Netflix's growing market share as a streaming platform [5]. People choose streaming services that are less expensive than movie tickets since they may view movies for less money. Therefore, Disney hopes to gain a significant position in the streaming industry through the acquisition of Fox in order to launch competing streaming services to Netflix. On November 12, 2019, Disney announced a streaming service in the United States called Disney+ [4]. Bob Iger, the CEO of Disney, stated that Disney+ was a family-oriented streaming service featuring original programming containing every classic Disney film [4].

2.2. Acquiring Motivations

For Disney aspect, multimedia objects may necessitate more storage space and transmission bandwidth than conventional Web content. Consequently, performance enhancements such as streaming proxy caching and multicast delivery are desirable for reducing the impact of streaming workloads on the Internet [6]. Consequently, streaming services play a crucial role in the contemporary film and entertainment industries. The acquisition of Fox provides Disney with the ability to expand its streaming services throughout Europe and Asia and have the ability to compete with Netflix, which is a giant in the streaming industry.

For Fox aspect, as a result of digitalization, billions of people can now stream entertainment virtually anywhere and at any time. With the development of YouTube, Netflix, Amazon Prime, HBO, and others, physical video distributors such as Blockbuster collapsed. Shortly thereafter, theatres and television networks witnessed a drop in their audiences and income, which had a profound effect on film production firms [7]. In recent years, Fox's revenue has stagnated and dropped. Fox has the opportunity to appease its less profitable business section through the sale of significant assets. Fox has the potential to realign its business because internet advertising and streaming pose less of a threat to the content of its properties [7]. Fox did not want to lose its movie characters, and Disney provided the opportunity for Fox to maintain its reputation.

3. Analysis

3.1. The Positive Impact of Acquisition on Disney

The horizontal merger between Disney and Fox reduces the number of potential "Big Five" corporations that dominate the U.S. audiovisual market from six to five [8]. Besides, it enabled Disney to gain about 40% of the overall market share. With around 38% of domestic movie ticket sales in 2019 (seen from Fig. 1), Disney and Fox films dominated the box office. The eight highest-grossing movies at the box office were produced, released, or co-produced by Disney. With 13.8% of the U.S. market, Warner Bros. is Disney's primary competition [9].

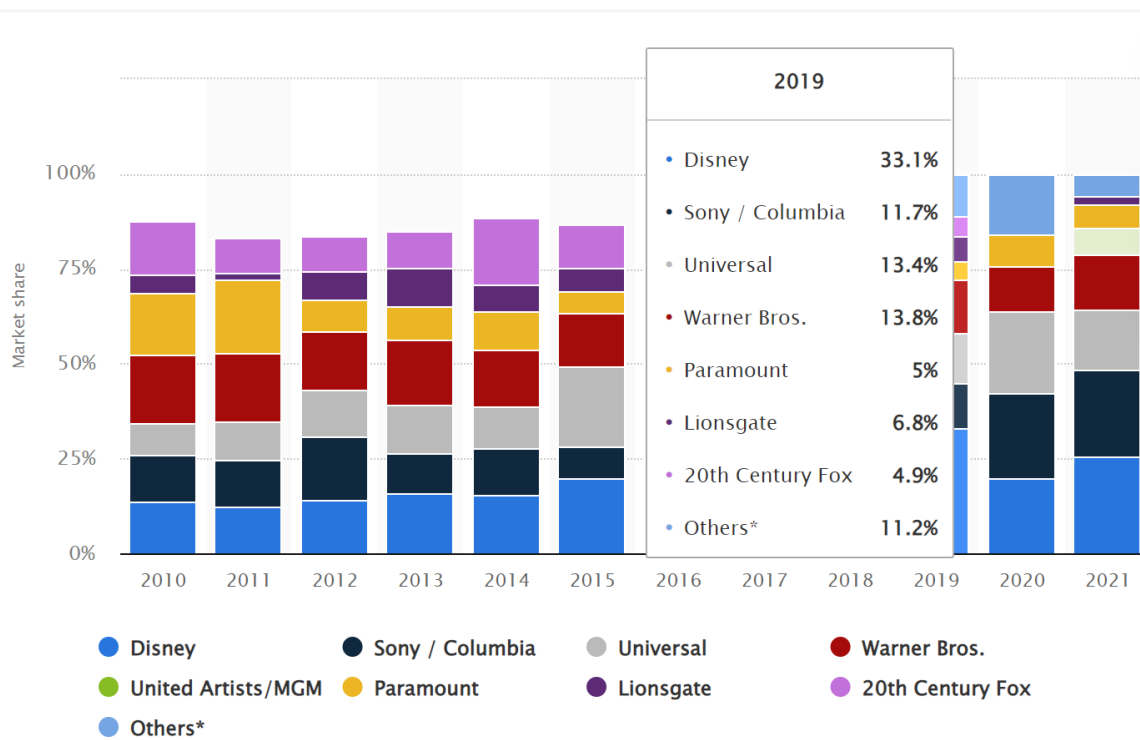


Fig. 1 U.S. Hollywood studio box office share (Source: Statista).

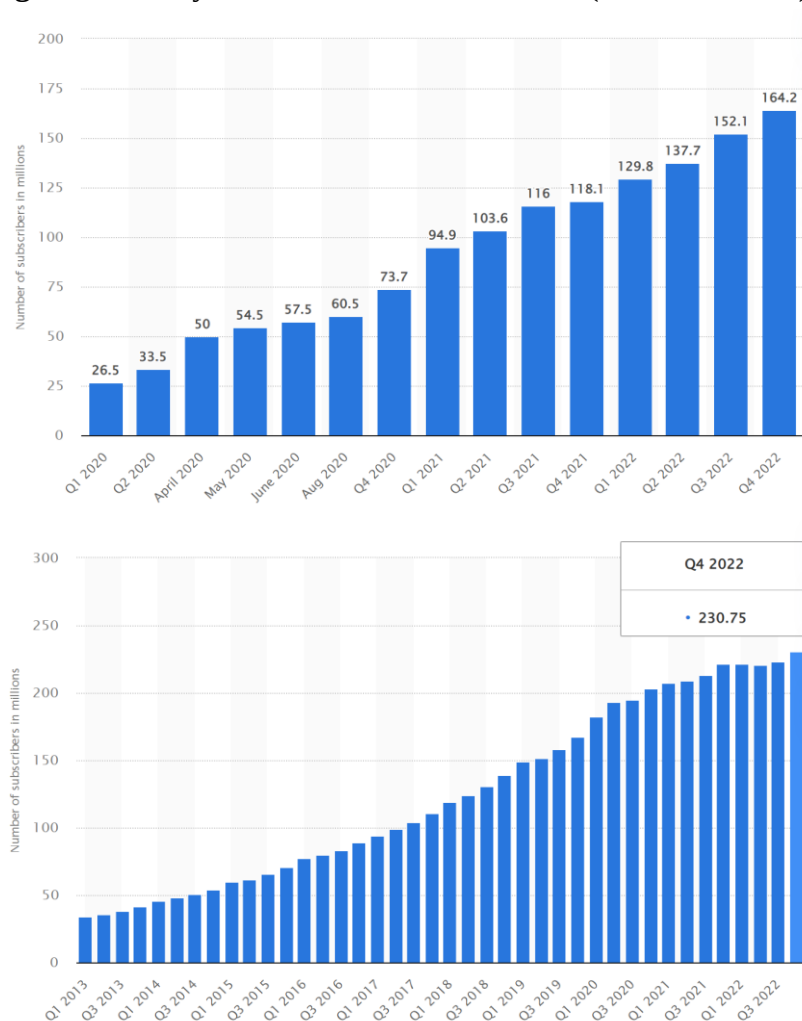


Fig. 2 Number of subscriptions of Disney+ (upper) and Netflix (lower) (Source: Statista).

Disney got a 60% controlling interest in the popular streaming service by acquiring Fox's Hulu share and successfully launched Disney+ streaming service. As depicted in Fig. 2, the number of subscriptions to Disney+, the streaming service Disney created after acquiring a stake in Fox's Hulu, has nearly matched the number of subscriptions Netflix in just two years. This guarantees Disney's commercial position in the emerging streaming service industry.

3.2. Financial Analysis of Disney

As shown in Fig. 3, in the five years prior to and after Disney's 2019 acquisition of Fox, Disney's revenue reached higher levels. Therefore, this acquisition decision is a positive impact for Disney's profitability.

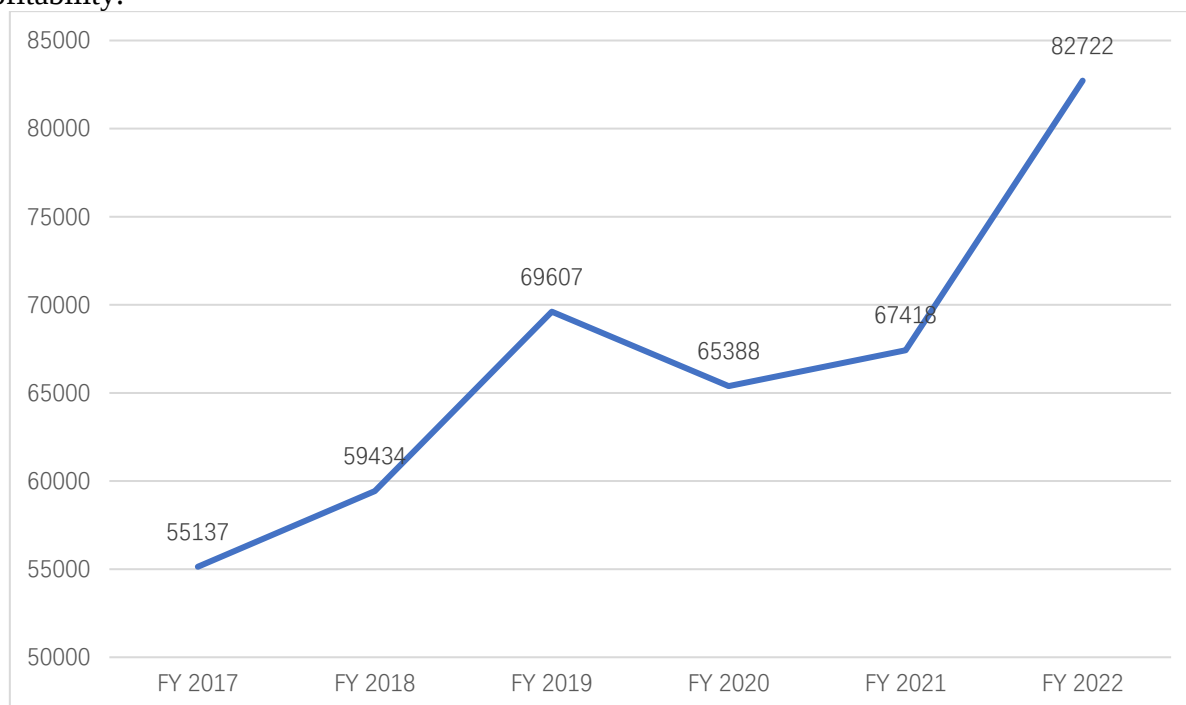


Fig. 3 Disney revenue before and after acquisition of Fox (Millions of USD).

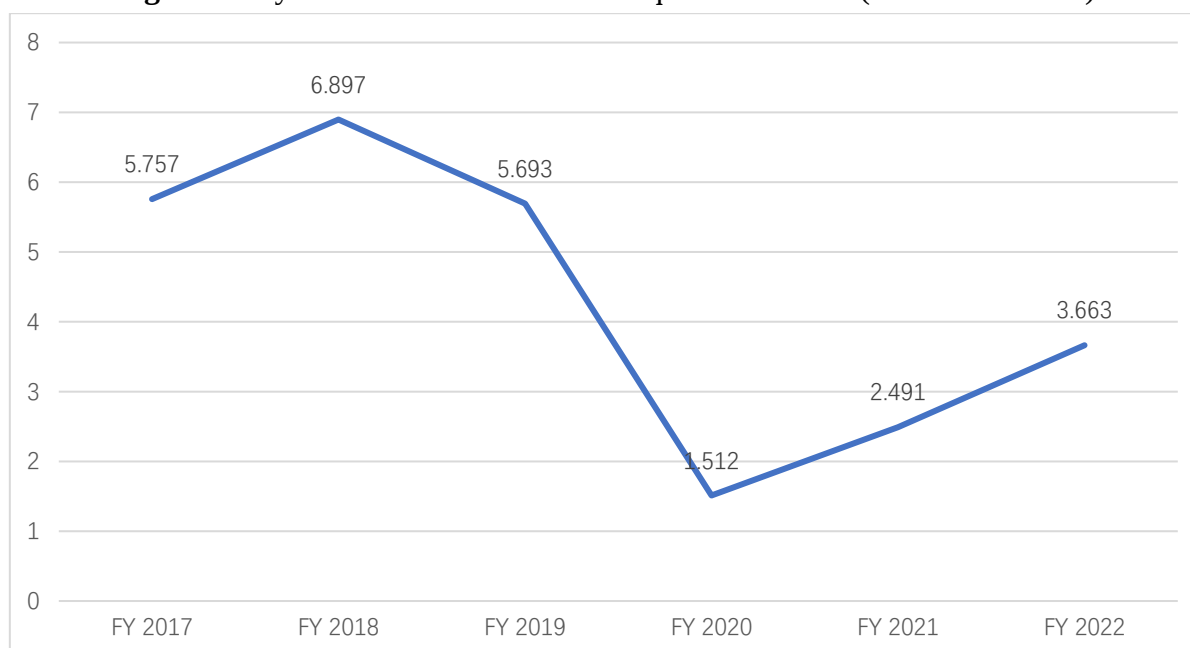


Fig. 4 Disney EPS before and after acquisition of Fox (Millions of USD).

As illustrated in Fig. 4, Disney's earnings per share decreased following the Fox acquisition. There are two potential causes for this occurrence. One is that Disney issued 307 million shares on the day

of the acquisition, resulting in a fall in earnings per share due to the increase in outstanding shares. Since Disney purchased 21CF with its considerable debt, the cost of debt has considerably grown. Therefore, despite strong revenue increase, the company's net income would be badly affected.

4. Limitations of the Acquiring

Initially estimated at \$52.4 billion, Disney's acquisition of Fox was ultimately completed for \$71.3 billion, a premium of approximately 26.51%. Therefore, the choice to purchase Fox could have a negative effect on the firm's stock price, as investors would wonder if the premium acquisition was warranted and would add value to the company. Specifically, investors question that the synergies promised by the premium paid will be realized and that the merged company's value will be preserved or increased [10]. Disney's acquisition of Fox, as opposed to working with Fox, necessitates that Fox-produced movies be reviewed and authorized by Disney prior to distribution, which could limit the inventiveness of Fox filmmakers and make the movies less consumer-friendly [11].

5. Suggestions

Disney has acquired Pixar, Marvel, Fox, and other studios, owns a large number of characters and intellectual property, and is now the owner of the Disney+ streaming platform; therefore, Disney must protect its intellectual property, particularly to regulate illegal downloading of streaming media. Despite Disney's acquisition of Fox and the launch of the Disney+ streaming service, competition in the streaming service industry remains fierce, particularly with Netflix, and Disney's audience consists primarily of children and families, a smaller demographic than Netflix [11]. Disney can attempt to produce more films for adolescents and adults.

Additionally, it can be seen in Fig. 3 that Disney's revenue in 2020 has decreased, which may be due to COVID-19 disrupting Disneyland's business and reducing ticket sales. Therefore, Disney can create an online Disneyland via streaming to prevent shutdowns for a variety of reasons and reduce the revenue impact of factors like force majeure. For Fox, Disney is a world-famous film distributor with a strong commercial reputation, so it is an excellent opportunity to distribute quality films that will draw audiences and improve their financial value.

6. Conclusion

In summary, Disney's acquisition of Fox was a successful business move. The acquisition of Fox by Disney has yielded excellent box office results, a large market share, and more well-known film and television intellectual properties to appeal to a wide range of consumers. It also established a commercial presence in the film and entertainment industry and developed a business in the emerging streaming services industry. However, the company's decision to acquire at a premium may raise questions among investors. In addition, the debt-financed acquisition increases debt risk and expense, and the issuance of additional shares reduces earnings per share. Besides, Disney's acquisition of Fox should be as far as possible to avoid a single type of film to prevent audience loss. The competition in the streaming industry is still fierce, Disney needs to consider broadening the audience. For Fox, it needs to seize this opportunity to produce popular and in-depth films to expand its popularity. Nevertheless, it should be noted that this study has some shortcomings, e.g., this paper focuses on the effects of the acquisition of two entertainment film and television industry giants on the acquired company, whereas smaller film and entertainment company acquisitions may not be applicable to this analysis. For further study, the acquisition cases of smaller companies in the film and entertainment industry can be chosen to analyze to see if the acquisition is also a good business strategy for small companies. Overall, these results offer a guideline for analyzing the impact that M&A will have on film and entertainment companies.

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