Fox Corporation

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Bryan Kraft: OK, welcome, everyone. I'm pleased to introduce for our second fireside of the day John Nallen, who's the Chief Operating Officer of Fox Corporation. John, welcome.

John Nallen: Thanks, Bryan. Thanks for having us.

Bryan Kraft: Thanks for joining us. Maybe to start off, it's been five years almost to the day since FOX completed the sale of most of its assets to Disney and created new FOX. Since then, the industry's gone through quite a bit of change, with cord-cutting and the shift in consumption towards streaming. How do you see video distribution evolving from here? How will it impact FOX's networks and content? And how is FOX positioning itself for that future?

John Nallen: There's a lot to unpack there.

Bryan Kraft: There is.

John Nallen: And so, we'll start with the five years. I mean, it's been remarkable that, in this five-year period, the focus of the company has maintained itself on principally news and sports during that period.

And during that five years, we've renewed a significant amount of our -- virtually all of our sports rights. We renewed once, maybe twice, our major affiliate deals during that period. On-screen, I think we've just done a fantastic job, news, sports and local. Tubi was an acquisition we made during that period, which is a growth engine I'm sure we'll talk about today. And from a capital allocation standpoint, we returned a substantial amount of capital during that period to the shareholders in the form of buybacks and dividends.

So we're set up. We had a great five years. We're not taking a victory lap, by any means. We've got -- a lot of it was about establishing ourselves for the next five and 10 years. And to focus on your question about video distribution, I firmly believe that, looking forward, we sit here five years from now having this same conversation, the biggest distributors of our product will still be the biggest distributors we have today. The Pay TV system will be the most important revenue stream for us from an affiliate revenue standpoint.

Now, a lot will happen in between. There'll be a lot of direct-to-consumer products out there addressing the market that's outside of Pay TV. There'll be a lot of self-bundling that people will be doing outside. But as they do that, there'll be an eye back to Pay TV to see is that a more efficient consumer buy for them.

But there's just no question that the largest revenue stream on our distribution side will still be from the major names, many of which you'll have here today. And we'll evolve. We'll put products into the market that will be responsive to that market that's outside of Pay TV because, otherwise, you can run a valuation on FOX where, if we didn't do that, you would just take the Pay TV universe, run a DCF, put a terminal on the end, and say, OK, that's FOX. But that's not the way we're going to run and grow the company. It will be to address the bigger market that's out there from a distribution standpoint.

Bryan Kraft: One of the ways you're going to address it was the recent announcement with Disney and Warner of the plan to introduce the sports bundle later this year. Tell us about the strategic calculus behind your decision and what are the benefits to the business, what are the risks and potential unintended consequences, for example accelerating Pay TV declines, impacts on affiliate renewals, that sort of thing. Could you maybe talk about that a bit?

John Nallen: Yes. There's obviously been a lot talked about and written about the platform since we announced it a few weeks ago. You've written a piece, as well.

I firmly believe that the platform is not a catalyst for accelerating Pay TV declines. Whatever will happen in the Pay TV universe will happen independent of the D2C product we're putting out on this platform. This platform is addressed to a market that's unserved right now, entirely the cord-cutters and cord-nevers that are outside of Pay TV. Come back to a point I just made, Pay TV is just too important to our business for us to be disruptive to it by introducing products that will accelerate Pay TV declines.

So it's a niche product. You will have heard last week Lachlan mentioned our expectation is in 4.5 to 5 years to have five million subs in this product. It will be a premium product. And I think once -- people said, well, it's an incomplete product. How is that going to serve the consumer? Well, I come back to this point of self-bundling, that that will occur. But as it occurs, the consumer has to be mindful about the Pay TV environment and see do they have a much more efficient buy by staying in or moving into Pay TV.

So, importantly, as I say, I don't see it as a catalyst. Pay TV will -- we're running about 8%, 8.5% declines on Pay TV subs now. I'm hopeful that that will ameliorate itself so we get to a core Pay TV universe that's focused primarily on news and sports, and that we will serve the independent market of Pay TV through other products. Otherwise, I come back to my valuation point.

Bryan Kraft: Yes. Do you think the sports bundle may end up just highlighting the value of some of the virtual MVPD services that are out there. When you think about $45 to $50 for the sports bundle versus $73 for the low end of the virtual MVPD products, which are pretty complete, it just seems like the value lies much more in the virtual realm.

John Nallen: Yes, you're right. Perversely, when you add up a number of these D2C products, you come back -- YouTube TV is the example you're giving at that price level, which has all of our products, not only the products that are in the platform but those that are offered by our peers and competitors. So there's a perverse way of looking at this that, in fact, promotes Pay TV by looking at the value equation.

The people that have left that are cord-cutters, cord-nevers, I just think they have left the system forever. And they will look for different ways to accumulate their entertainment, sports and news product. And this was just one solution to that market. But it may be a moment for it to be a stickier opportunity for Pay TV when you look at the pricing in the D2C world.

Bryan Kraft: Right. You mentioned Tubi in your opening remarks for the first question. That's been a significant driver of engagement and ad revenue growth for FOX ever since the acquisition in 2020. I think what investors are really trying to understand is how large that Tubi ad revenue pool could ultimately become, what will steady-state profitability be like for Tubi, and will Tubi's role within FOX change over time as the distribution landscape kind of continues to evolve.

John Nallen: I think taking the last one first, I don't think there's a dramatic change in what Tubi will be for FOX. It's an AVOD service. It's number one, Nielsen has it, and now at 1.5% TV viewing on Nielsen Gauge. It serves an audience, 60% of which are cord-cutters and cord-nevers, so advertisers are able to get to a segment that they would be unable to reach through traditional advertising means. Its secret sauce is obviously its user interface, its algorithms; but, more importantly, its library. There's 240,000 episodes and films on there. We just did a deal recently with Warner Brothers to bring DC films and some of their television product to the market.

So, I don't see it evolving into ad-free tiers or an SVOD. It's just like -- its sweet spot and its growth spot is around AVOD.

Steady-state, our expectation is you're at 20% to 30% margins off of this business. Right now, in the library, about 95% of the library is revenue share. There’s balance in licensed and original content. Having said that, the viewing is a little more disproportionate. We have a third of the viewing from licensed and original content, two-thirds from revenue share. But obviously, in a revenue share model, your margin is starting at a 50% margin off of the revenue, and then working your way down.

So, we think a 20% to 30% margin contribution is a substantial contribution by that business, which will be one of the growth engines at FOX. If you look out as to where FOX is headed, the investment we're making in Tubi will turn to become a real contributor to the business, longer-term.

Bryan Kraft: Maybe to follow up on that for a second, how do you get from where you are now on margins to where you want to be? Is it a matter of just better leveraging that licensed content and improve the margin on it? Or are there other areas of investment that are diluting the margins today that will scale or just become less over time?

John Nallen: Well, I think it's more about the growth of the top line and contribution of original and licensed product and the disproportionality of the viewing represented by a disproportionality of the content acquisition that we make. So I think once -- it's a business where engagement is extraordinarily high, the revenue has not yet caught up to the engagement, given some of the pressures out in the market.

But this business, there's been talk about it being a $1 billion revenue business shortly, and I wouldn't debate that. And it's grown from virtually nothing to be a $1 billion revenue business. So to get to those margins, it's all about top line growth. We're not spending disproportionately on either content marketing promo, subscriber acquisition, where that's an area where we'd have to focus on cost reductions. It's really about top line growth.

Bryan Kraft: Understood. Maybe to shift gears a little bit, can you talk about what you're seeing in the ad market? It'd be great if you could talk about different areas of the market that your business is focused on, sports, national news, local and general entertainment, where I know you have less exposure.

John Nallen: Yes. There's a lot there, a lot to talk about. Clearly, it's a nuanced market overall. But if you look at the place where we play the most, two-thirds of our advertising revenue is generated from Sports and News. And that is the area where it's healthiest right now, particularly in Sports. So if we unpack it a bit, Sports, we had a superb post-season in the NFL. We had a bit -- just a rocky schedule early on in the regular season that contributed to ups and downs but the post-season, incredibly strong. Obviously, we didn't have the Super Bowl this year, but it was a record Super Bowl. And we quite like that, because that Super Bowl gets handed to us for next year.

If we look, the other place where there was just great momentum and I think an inflection point in viewing last year, and will continue, is college football. I mean, for us, the Ohio State-Michigan game peaked at 23 million viewers. And I think everybody's dealing on college football was just extraordinary last year. And our Big Game Saturday represented a real contribution to growth of viewing against where we were. And we just see that continuing.

Staying with Sports, it's quieter now for us, so we have NASCAR, which is going fine. Daytona 500, we had a rain delay, moved it from one day to the other so that impacted ratings. I don't want to say, surprisingly, but baseball is extraordinarily healthy for us right now in early bookings. Season begins the end of the month. But what we're seeing a bit anecdotally is some RSN money moving up nationally. And that's contributing to the health there.

On the News side, national is still great. Pricing is strong. I'm sure we'll talk about ratings as we go through this. The place where we were impacted in Q1 and Q2, much less so now in Q3, is direct response pricing. It's just a lot of pressure on direct response pricing.

On the local side, there's a lot of pluses and minuses when you look at year-on-year -- Super Bowl, political, number of games. When you cut through it all, the local market for us is about flat year-on-year. And clearly, what we're all pointed to and focused on is the upcoming political season. We've got five battleground states inside of our footprint in Georgia, Wisconsin, Arizona, Michigan, Pennsylvania. Those are all really big targeted spends. We've got 16 Senate races inside of our markets. There's big down-ballot issues and races that are going on. And I know some spending, at least on the Presidential side, has started already.

The piece we missed, quite frankly all of us, is the primaries. There wasn't much spending, and obviously nothing on the Democratic side, and less so on the -- not less so, but less than expected on the Republican side. So locally, what we'll look forward to is some time July, August, a real kick-in of spending in what could be a record Presidential and Senate race, going forward.

Tubi, if you look at that advertising, we were up 17% in Q2 on Tubi growth. We're pacing at or above that still. So the Tubi machine continues to do quite well.

Then the entertainment side. You said it's a much smaller piece of our business. But that's probably the most challenged in the market, is entertainment viewing, entertainment pricing. Right now that's the most difficult, but it's a small piece of our business.

Bryan Kraft: Right. You mentioned direct response, which has obviously been a focus. Is that pricing kind of just at this level that it's been for a long time, or is it actually starting to tick up? I'm wondering if you could comment on that.

John Nallen: Yes. We're seeing slight improvements in direct response. So we're down, i n the first couple of quarters, we were down high teens, 20s as far as pricing. Comparable year-on-year we're down, high single digits now. It's come back. And sequentially, the pricing has moved up. It's not just a comp year-on-year. It's also a sequential improvement.

I should mention, one of the focuses on the national side, one of the areas or categories that we talked about before. And it's just interesting because pharma is now such a big spend on the national side. We had 50 brands that came to market last year. Obviously, none of them are falling off patent, so they'll continue to spend next year. Auto, there's 60 million units scheduled for the current year, up from where it was a year ago, so that's continued to be healthy. And surprisingly, travel. You've experienced it yourself just watching television. There's a lot of travel ads, both for states and cruises and trips, which is benefiting the market.

On the local side, auto continues strong for the same reason as at national. And retail home improvement is a category we've seen doing quite well. The one that's consistently negative now in the local side, which was a boon for us, is wagering, because that has now moved to a national level because it's a much more efficient buy for those betting companies to be buying nationally as opposed to locally.

Bryan Kraft: In this category, are you even or up on that when -- is just a shift from your local business to your national business?

John Nallen: Well, the shift to national is helpful because it's a better buy. It's a more expensive buy for us. So I'd say, overall, if I look at our whole book of business on advertising, we're up in wagering because they are spending more on a national level. And particularly, given what I described earlier, the sports success we had in the fall, a lot of money was put toward wagering there.

Bryan Kraft: OK. Maybe we can talk about affiliate revenue for a moment. Can you talk about the affiliate revenue outlook, both on the MVPD and on the station side? I think you just completed a renewal cycle. Maybe if you could talk about what you achieved there and when we'll see the full impact on results, and just any color on when the next renewal begins, the cycle begins.

John Nallen: Yes. So our business -- I remember being back in the Investor Day five years ago, trying to have everyone appreciate how simple our business really is now. I mean, half our -- directionally -- half our business is advertising, and half our business is distribution. And I remember the complexities of the News Corp business. I've been around for 30 years where I had to deal with a lot of other issues, but it's a much simpler business.

So the half that's distribution we obviously have a lot of focus on. What we've seen, as I said earlier, is a consistent decline of 7%, ticking up to 8%, ticking up to 8.5% in volume coming down. Yet through that, what you've seen in our, sequentially, last few quarters' results is holding serve, or an increase to our affiliate revenue. And that speaks to the power of the focused FOX channels, particularly in Sports and News.

They’re part of every Pay TV bundling --, they’re must-have -- I'll give an illustration later about FOX News dominance, but they're just important to the Pay TV system, those channels. So in the renewals that we've completed, they've all been, importantly, quiet. There hasn't been -- you haven't heard FOX out there going dark, a lot of noise, marketing, us against them, them against us. It just hasn't happened. The discussions have been very clear, very intense, no question about that, but also constructive as to what FOX can deliver for the Pay TV bundle.

We're through. For fiscal '24, we finished our renewals for the year. We don't have any left. We'll continue again in the autumn next year with about a third of our portfolio renewing there. But that's the way you should really think about our business now, going forward, we'll roughly have 25% to a third of our affiliate revenue renewing every year. That's really just the cadence that we're onto. These deals are normally around three years. Some extend to four. But you just now get in a rhythm of every three years having a third of your book renewing at that point.

But we feel -- look, we feel great with the rights we have secured, with the ratings that we've got. It's a constructive conversation that we have on the affiliate side.

Bryan Kraft: As you worked through this current cycle, did anything change relative to the last one as far as terms or structure of the agreements, just broadly speaking?

John Nallen: Not really. I think there's been more attention after the Disney-Charter discussion around two things. One is long-tail networks and their importance, or lack thereof, in distribution and affiliate pricing. And the second is D2C products and what rights the pay subscriber has over D2C products that the content company's offering independently in the market.

Luckily for us, we don't have long-tail networks. And up until recently, we haven't had a D2C product other than FOX Nation that's out there. So the construct has been pretty traditional, and again, we're focused on the success of the Pay TV bundle because it's just -- it's so vitally important to our business.

Bryan Kraft: Yes. You mentioned FOX Nation. That's been at the center of the news streaming strategy. Based on Steve's comments on your earnings call, it sounds as though maybe you're pulling back somewhat on investment there. I don't know if it's the right read, but I just wanted to ask you, I guess, what is happening at FOX Nation? What have you learned about the consumer appetite for the service? Is it turning out to be more niche than you expected? And what's the future of that business?

John Nallen: So I wouldn't have read, or we shouldn't read Steve's comments as being any de-emphasis of FOX Nation. FOX Nation is vitally important, complementary product for the avid FOX News fan. And we are not pulling back materially investment in FOX Nation. In fact, we've got a programming suite looking forward to revitalize what's being offered inside of FOX Nation.

Now, clearly, we had a decline in engagement when Tucker Carlson left FOX Nation because we used to do separate programming there, but that engagement has ticked right back up with new programming that we've put into it. There's been commentary that FOX Nation has sub base around two million subscribers. I wouldn't dissuade you from that.

That's generally where we are. And we're looking for growth in that sub base, not maintenance of it.

But it's hovered around that level for 18 months or so, recognizing that there is a core group of FOX News fans that will take this service, and not every FOX News fan is going to take this service independently. But it's a vital part. Clearly, if we ever go D2C in FOX News, which I'm not here to announce we're doing that by any means, having the FOX Nation engine of subscription, video, search, everything else, is quite helpful in being able to launch a product like that.

Bryan Kraft: Maybe we could talk about programming a bit. Over the past year, there've been a lot of changes to the FOX News prime time schedule, as you alluded to a second ago with Tucker leaving. How's the current schedule performing? What have ratings been like? Do you foresee additional adjustments to programming at FOX News this year?

John Nallen: So we changed the programming in July. And if I look at this over the last three quarters, year-on-year, Q1 we were down high teens ratings, primetime. Q2, similarly. Right now, in January and February, we're about even with where we were a year ago. So a really market improvement in the primetime schedule ratings that have occurred.

I think the strength of FOX News you can illustrate from two recent events. Last week's State of the Union speech, the number one channel in America for viewing of that speech was FOX News. Every broadcast, cable, whatever, it was FOX News had the number one viewing. In addition, a couple weeks earlier with Super Tuesday, FOX News out-rated CNN and MSNBC combined on coverage then. So oftentimes, you've raised it in the past with me, when we see change of administrations, people question what will happen to FOX News. Here we have an administration that you would question whether it's a FOX News fan, yet the biggest viewing of the State of the Union speech was by FOX News fans at that point in time.

So, I think FOX News continues to go from strength to strength. Suzanne and her team are focused on the schedule, but there's no changes that are in discussion that I'm aware about.

Bryan Kraft: Yes. I guess, I mean, given what you said, it sounds like you should see strong -- if you sustain current ratings, you should see strong growth in the September quarter as the comps get easier.

John Nallen: Well, exactly. Well, plus, we have -- for us, we're looking at two Super Bowls this year, right? We've got the football Super Bowl, but we've got the election Super Bowl, going forward. So from FOX News, the coverage is just going to dial up beyond the incredible coverage they've had covering Ukraine, Middle East, all those issues. But we've got a big '25 ahead of us when you look at those two big events.

Bryan Kraft: Yes. Shifting to Sports, over the past year you've opted not to renew WWE. You did renew NASCAR with a trimmed-down schedule. Is the FOX Sports rights portfolio complete at this stage? Could you envision adding any new rights over the next few years? And conversely, are there any current rights that you have that maybe don't make sense or aren't as must-have in the future as those renewals come up?

John Nallen: I don't want to keep using this five-year history, but during that period, beyond the ones you described, we trimmed our -- we transferred our U.S. Open Golf contract. It was the only golf we had. Didn't make sense for us to continue to do that. And obviously got out of Thursday Night Football even a year earlier than expected when we transferred that -- or when Amazon acquired that contract.

But I think we've renewed our foundational rights, as we refer to them. The NFL contract goes out another 10 years, MLB to 2028. NASCAR, we just did a seven-year renewal. College Football takes us out till the mid-2030s. We've got just a strong portfolio to look forward to, and there's no big renewal for us of our foundational rights on the horizon.

There are other product that's out there. I mean, clearly, there's a lot of talk about the NBA. We've never been in the NBA business other than when we had the RSNs, so there shouldn't be an expectation that we'll be players in the NBA renewal.

But no, if you look at our sports portfolio, I don't think it's lacking. And when we look at the schedule, the calendar for the year, it's hard to figure out where you would put some of these events because we've got big FOX, FS1, FS2, and they're pretty full with sports events through the calendar. So it'd be a bit of a challenge for us.

And when we look at sports rights, clearly we're looking at the advertising revenue. But we're also looking to., can we incrementally drive affiliate revenue, incremental to what we're getting either in retrans or in the affiliate fee. And Thursday Night Football was a great example, where a Sunday package is what was driving the affiliate revenue that we were getting from distribution. And incrementally, having Thursday wasn't as much of an impetus to that as Sunday alone would be. So the loss of Thursday wasn't as big an impact to us on retrans, given that we had the marquee product on Sunday.

Bryan Kraft: Right. How about on the general entertainment side of the business, whether it's on the FOX network or on Tubi? How's the programming performing? Any major changes for next season? And maybe if you could just elaborate on how the incremental Tubi investment is being deployed.

John Nallen: So on the Entertainment side, Rob Wade and his team were just doing an incredible job. We have the number one series in Next Level Chef, 18 to 49. Four of the top five new series on the network are on the network. FOX has got four of the five. You can look up the names. Some of them are odd, Krapopolis and Grimsburg and others like that. But they're doing fine. And we'll continue to announce new products. Our Upfront is May 13, so you've been in there in the past, Bryan. You'll see announcements around what next year's schedule will hold.

At Tubi, where we're focused really is on originals, but don't get concerned, because when people talk about originals off-network, they think about the SVOD-type spending into original entertainment, which is not what we do. But up until recent change in leadership, we spent an amount on originals that was based on volume. So they were less expensive, but a lot, as that were put out there. And we were able to determine, based on the information we have on users, what kind of originals to make, because you know what the viewing habits are, and you want to pump more toward it.

What we're doing now is taking the same dollar investment in originals but concentrating it on slightly bigger swings, something that we can get behind and promote and market, and that will have a longer shelf life to it than the originals that we have. So, again, at the Upfront, you'll hear us announce a calendar of new originals for Tubi that you'll notice are bigger swings but, again, nothing in the context of what you'd see the SVOD players spending for their originals.

Bryan Kraft: Got it. What should we expect in terms of growth in content amortization expense for FOX this year?

John Nallen: It's a mixed, confusing spreadsheet when you have to go through it, because--.

Bryan Kraft: --We just want to look to the bottom of it.

John Nallen: Yes. Well, I can just kind of parse through, because we had the Super Bowl last year. We don't have it this year. Number of playoff games differed year-on-year. So that's just pollution in there. But when you cut through it and look at what the near-term impacts of it are, in the current year it's the step-up in our new NFL deal. That's at the heart of our step-up in costs this year.

From there, you'll see a more normalized cost increase, going forward, but first-year step-ups for all of us are really the thing we look to absorb and then monetize as we go out further. So there's not a big increase in entertainment costs. There's not a big increase in news costs if I look across the company. Tubi will have some increase in costs related to programming. But the sports step-up is the most notable one out of our portfolio.

Bryan Kraft: Got it. We're running short on time, so I'm going to try to re-prioritize a little bit. I think one question that I really wanted to hit on is, and I don't know what you're going to say in response to it is, but a lot of people want to know just what the appetite is for FOX to participate in industry consolidation if the opportunity presented itself. I think there's a lot of people out there who believe the argument for doing so is becoming more compelling for FOX as the Pay TV industry base continues to shrink and this sort of could be the right time.

John Nallen: Yes. Well, I think I can capture a number of thoughts in thinking about our response for that. Capital allocation, valuation, consolidation are probably all part of it. And there's no one more frustrated on the valuation side than me, given what we've achieved. You look at the value of Tubi, the Lot, our betting assets, our tax assets, some of the others where you parse that away and look at the fundamental value and trading multiple of our assets, and it's just frustrating, I think, which therefore is relevant to consolidation. Because if we were -- and we are very interested in increasing the growth of the business through acquisition. But our currency, from an equity standpoint alone, is highly undervalued in order to do that consolidation using equity currency.

Our balance sheet is incredibly strong. The cash flow generation of the business is very high. Our debt levels are incredibly manageable. We just paid $1.250 billion in January/February back, and our cash flow just continues to accrete to the balance sheet. So in lieu of finding a consolidation or M&A opportunity that's so accretive to us, I come back to the undervaluation of the stock where we've plowed $5.2 billion into buybacks, because that's the best return our shareholders can get right now on deploying that capital. But I'm hopeful that the remaining shareholders, net of a buyback, are going to enjoy a lift in valuation and a lift in growth either through organic investment, M&A, or other deployments of capital.

But yes, we're not closed to opportunities in the industry. We just are frustrated that we from a currency and that we haven't found anything so compelling and so accretive that we would turn and say this is where we're headed.

Bryan Kraft: What about from the other perspective as maybe a seller?

John Nallen: I was about to say we're not good sellers, but five years ago we were good sellers.

Bryan Kraft: Great seller.

John Nallen: It hasn't crossed our minds. There's been no inbound about it. I'm not suggesting that we're open for business on it, but we're much more focused on growing the business than we are in selling the business.

Bryan Kraft: Just about out of time, so it's a great place to wrap up. Thank you, John, appreciate it.

John Nallen: Thanks so much.