Viacom (VIA.B) Earnings Report: Q1 2015 Conference Call Transcript

The following Viacom conference call took place on January 29, 2015, 08:30 AM ET. This is a transcript of that earnings call:

Company Participants

- Jim Bombassei; Viacom; SVP - IR
- Philippe Dauman; Viacom; President, CEO
- Wade Davis; Viacom; EVP, CFO Strategy, Corporate Development
- Tom Dooley; Viacom; Senior EVP, COO

Other Participants

- Michael Nathanson; MoffettNathanson; Analyst
- Alexia Quadrani; JP Morgan; Analyst
- John Janedis; Jefferies; Analyst
- Doug Mitchelson; UBS; Analyst
- Ben Mogil; Stifel Nicolaus; Analyst
- David Bank; RBC Capital Markets; Analyst
- Brian Wieser; Pivotal Research Group; Analyst
- Barton Crockett; FBR Capital Markets; Analyst
- Vijay Jayant; Evercore ISI; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Good day, everyone. Welcome to the Viacom first-quarter 2015 earnings release teleconference.

Today's call is being recorded.

At this time I'd like to turn the call over to Senior Vice President of Investor Relations, Mr. Jim Bombassei.

Jim Bombassei (SVP - IR):

Good morning, everyone,. Thank you for taking the time to join us for our earnings call for our December quarter. Listening from Los Angeles is our Chairman, Sumner Redstone; and joining us in New York are Philippe Dauman, our President and CEO; Tom Dooley, our Chief Operating Officer; and Wade Davis, our Chief Financial Officer.

Please note in addition to our press release we have slides and trending schedules containing supplemental information available on our Web site. I want to refer you to page number 2 in the web presentation and remind you that certain statements made on this call are forward-looking statements that involve risks and uncertainties. These risks and uncertainties are discussed in more detail in our filings with the SEC.

Today's remarks will focus on adjusted results. Reconciliations for non-GAAP financial information discussed on this call can be found in our earnings release or on our Web site.

And now I'll turn the call over to Philippe.

Philippe Dauman (President, CEO):

Thank you, Jim. Good morning, everyone. Thanks for joining us to discuss the first quarter of our 2015 fiscal year.

Viacom once again had a solid quarter. We drove revenue growth across all our business, and continued to evolve and adapt to meet the opportunities of an increasingly digital and multiplatform landscape. We also maintained our strong balance sheet, while continuing to return capital to our shareholders.

Let's take a quick look at our first-quarter financial performance. Revenues increased 5% to $3.34 billion due to growth across-the-board. All of our major drivers -- affiliate fees, advertising, theatrical distribution, and home entertainment -- saw increases in the quarter.

Adjusted operating income was flat for the quarter at $959 million. Adjusted net earnings were $538 million, and adjusted diluted earnings per share increased 8% to $1.29, the highest ever for a December quarter.

These results are a reflection of our commitment to produce great multiplatform content while efficiently and effectively managing our operations. This commitment has been fundamental to our success and will drive our growth in the future.

It is no secret that there are far-reaching shifts taking place in our industry. As the industry evolves, it is more important than ever to focus on Viacom's significant strengths.

Viacom has an unmatched portfolio of iconic and powerful brands and is a leading creator of the content that drives the industry ecosystem. Viacom's current distribution partnerships are strong, with most extending well into the future, and the ranks of new entrants are increasing rapidly.

Viacom's global footprint is broad and growing. Viacom is leading the rapid evolution to new measurement and monetization models that will unlock significant value, for us in particular.

We produce distinct, high-end video for screens of all sizes, content that drives greater consumer engagement and is highly valued by advertisers. We invest billions in original programming year in and year out. Included in our programming for this year in the US alone are well over 200 freshly produced series and events.

Turning back to the results, worldwide Media Networks revenues increased 4%, with a 6% increase in affiliate revenues. Domestic affiliate fees rose 8%, consistent with our annualized guidance of high single to low double digit increases going forward.

While we have recently seen a lot of posturing and positioning in affiliate negotiations across our industry, Viacom's distribution pipeline has never been stronger. We have long-term carriage agreements with every major distributor who is committed to a vibrant video business and most of the emerging players, including Google and Sony.

We deliver great value to our partners, and we are committed to helping them grow. Compared to other programming groups, Viacom networks are the leaders: number one in viewers 18 to 34 and viewers 18 to 49, based on Nielsen measurement. And we believe they account for an even greater proportion of non-Nielsen measured digital consumption.

As I've previously said, 70% of our subscriber base is covered by deals extending to 2018 and beyond, giving us significant visibility well into the future. As I mentioned on our last call, in the first quarter we successfully concluded carriage agreements with Verizon and Frontier Communications, and we are currently in productive discussions on other renewal deals.

We are also pleased that we renewed our affiliate agreement with DISH for our networks in Mexico. That deal includes the launch on DISH of the Paramount Channel next month to 2.2 million subscribers, bringing Paramount Channel's total distribution in Latin America at this early stage to 20 million subscribers.

We are also adding networks around the world, particularly in high-growth markets like India, Latin America, and Africa, but also in the UK, Continental Europe, and other parts of Asia. Our international business is growing rapidly and is very profitable -- not some day, but today.

New digital entrants are providing expansion opportunities as well as sparking industrywide innovation. In the first quarter, we renewed and expanded our agreement with Hulu. This month EPIX signed a multiyear renewal with Amazon, and we are looking forward to the launch of Sony's digital service in the coming months.

We are looking to tomorrow and the promise of innovation, bringing our programming to audiences where they want it, including mobile. Yesterday, for example, we added 24 Viacom networks to Verizon's FiOS mobile app, which brings TV Everywhere functionality to FiOS TV.

Also, in March our Nickelodeon group will launch a new direct-to-consumer subscription service. We believe this innovative service, which will have a distinct brand and will target the fast-growing mobile market, will be very attractive for parents and children. Nickelodeon will provide more details and announce the brand name at its upfront presentation next month.

Turning to advertising, Viacom's revenues grew 3% in the quarter. Domestic ad sales at our Media Networks declined 6% compared to last year, due primarily to lower C3 ratings. This was the first full quarter of results for Channel 5, which drove a 60% increase in international ad revenues.

Industrywide declines in ratings are generating debate about ways to close the gap between currently accepted ratings and actual consumption. It is an important secular issue. Inadequate measurement undermines innovation and disproportionately impacts those leading programmers, like us, who effectively provide the multiplatform experiences that viewers demand.

While it is currently a reality of our business, at Viacom we are not waiting for change. We are working with other major parties in the advertising ecosystem, bringing together data scientists and industry experts, whether at Nielsen or elsewhere, to create new measurement and monetization tools.

As an example, we are in specific discussions with several media agencies to enhance our capabilities to target and plan campaigns with even more precise and comprehensive measurement. To get there, we are bringing together data on engagement and behavior from a range of sources including set-top boxes, smart TVs, and other digital devices. We are confident that these new tools will allow us to distribute video in a more strategic way, unlocking significant revenue potential.

These opportunities are not limited to the US market. In tests in Norway, we have found that 12-to-24 ratings on MTV increased in the low teen percentages when viewing on other devices as measured. In general, we continue to develop ways to convert reach to revenue and monetize non-Nielsen-measured viewership as we grow this category from 30% of total ad sales to 50% in the next three years.

Earlier this week, Snapchat launched its Discover platform, which included Comedy Central and MTV International. Snapchat has 100 million global active users, most of whom are in the demographic sweet spot for Viacom .

This is another example of our non-Nielsen monetization strategy, enabled by the rich native content of our brands that resonates on social platforms and drives hundreds of millions of video streams and even more engagements per month. This is a meaningful expansion of our monetization opportunities, adding Snapchat to relationships with Twitter and Tumblr, among others.

These key attributes and initiatives as well as the creative spirit that drives our Company are what give us great confidence as we manage through this transition. We are rapidly adapting our processes and businesses as well as human, financial, and technological resources to increase focus on new, high-potential areas.

We have teams dedicated to content creation with a focus on more and better original programming that monetizes on all screens, dedicated to expansion and innovation on emerging mobile platforms, dedicated to the rapid rollout of innovative, integrated marketing and audience data capabilities, dedicated to building a thriving television studio at Paramount, dedicated to rolling out new brands in international markets with high growth potential, and much more.

It is clear that this transition will require some organizational realignment as well as rationalization of content that no longer meets our goals. We have identified specific areas where we can work more efficiently while focusing better on the evolving needs of our customers and audiences.

These changes are well underway and will result in substantial net cost savings throughout our organization, while at the same time increasing our focus and investment in areas with the highest growth potential. We expect to have more news about these ongoing efforts in the months ahead.

In addition, we continue to supplement our organic growth with disciplined strategic expansion. Following our successful acquisition of Channel 5 in the UK, we are looking at targeted investments that will press our advantage in key areas. We have concluded an agreement to acquire five regional television channels in India, which we will own along with our existing partner in India, Network 18, and shortly expect to receive our final regulatory approvals.

We are also negotiating another acquisition that would add to our scale in an important part of our business. Together, these two acquisitions involve about $400 million.

Taking advantage of these compelling opportunities does not detract from our steadfast, long-term commitment to returning capital to our shareholders while we grow our business. Through stock repurchases and dividends, Viacom returned almost $900 million to shareholders in the quarter.

In addition, we continued to effectively manage our debt, successfully accessing the markets for $1 billion at very attractive rates. We are on track to buy $750 million of our stock in this quarter.

We expect to decrease the pace of our buyback for the second half of the year, to stay at or below our leverage ratio target of 3.0. We will provide an update on our next earnings call.

Now let's talk briefly about our divisions. While the industry measurement issues continue to cause concern, Nickelodeon closed the calendar year as the top basic cable network with kids and total viewers. Nick is premiering more new content than ever, meeting the demands of kid audiences that are craving more new episodes and fewer repeats.

In the quarter, the sneak preview TV movie of Nickelodeon's new series, 100 Things to Do Before High School, ranked number one in its time period across all television and drove double-digit gains with key demos. This gives us great confidence when the series kicks off with new episodes in April. The movie Santa Hunters also premiered to strong ratings, scoring as the top kids' television telecast for the week.

Nickelodeon's tentpole shows also continue to be a force. The reimagined 2014 Nickelodeon HALO Awards captured the show's biggest audience ever with kids, tweens, and total viewers and was the number-one TV telecast for the night with kids. Coming up, the mega-tentpole Kids' Choice Awards will air in March, followed by the second annual Kids' Choice Sports Awards this summer.

Additionally, in early December, we launched the Nick Jr. app, which quickly topped the ranks in the US iTunes app store and was selected as the Editors' Choice in Apple Spotlight on the Best Apps of 2014. Looking ahead, Nickelodeon will air more than 150 new episodes and specials in the second quarter, with a focus on adapting to their viewers' changing tastes.

We have already found success with Bella and the Bulldogs, which drew 40% more viewers than our previous live-action launches. And of course, Teenage Mutant Ninja Turtles, which has become a dominant video, movie, and consumer product brand, wrapped up a very strong Christmas season as the number-one selling toy in the country for calendar 2014 according to NPD Group.

Comedy Central also has more original programming in the current quarter, with new seasons of returning series such as Workaholics, Broad City, and Kroll Show. Of course, the biggest news has been the successful launch of The Nightly Show with Larry Wilmore, which carries on Comedy Central's tradition of innovating in late night and has already joined The Daily Show with Jon Stewart in staking out a prime position in the cultural discourse.

And speaking of discourse, coming soon we'll be shooting and airing the Comedy Central roast of Justin Bieber. Mark your calendars; you won't want to miss it.

On Spike, we will be bringing fans the pop hit and viral phenomenon Lip Sync Battle, hosted by LL Cool J, which will premiere in April. On each episode, celebrities will go head-to-head in an outrageous lip-synch contest.

MTV also remains strong and resonant with its audience, placing Awkward and Faking It among the top 15 cable series in the quarter in the 12-to-34 demo. Through Always On, MTV builds a real-time conversation on all of their platforms -- on-air, online, mobile, and social -- in a way that no other brand can. In fact, MTV has doubled its unique digital visitors over the past year to a total of nearly 50 million in December.

In the second quarter, MTV premiered its new scripted thriller Eye Candy, and is launching Broke Ass Game Show next month, a funny, edgy show with man on the street dares that are perfect for digital sharing. MTV also returned several successful series in the second quarter, including Catfish, The Challenge, Teen Mom, and Ridiculousness.

We are also focusing on several high-quality big-event programs across our networks, and I'd like to update you on two of those. Next month, BET will launch its first-ever event miniseries, The Book of Negroes, a six-part historical drama. The television event will run over the course of three consecutive nights in February.

Spike is also in production on the epic series Tut, featuring Sir Ben Kingsley, about the boy king who ruled Egypt during the 18th Dynasty.

Moving to our newest brand, I'm proud to say that the integration of Channel 5 with our international operations is going extremely well and performance has quickly improved during this transition. Channel 5 is the only major free-to-air UK commercial network to grow share in 2014, and this December Channel 5 had its best Christmas week ratings in seven years.

And 2015 has started with a bang. Celebrity Big Brother launched with an audience of 3.6 million in early January, and the reality series delivered its highest-ever weekend ratings later that month. In addition, Channel 5 and MTV UK's first major joint commission, 10,000 BC, will begin airing on both channels in February.

Paramount's first quarter started where the previous one left off, building on the theatrical success of Teenage Mutant Ninja Turtles, which pulled in more than $477 million at the global box office. We acquired the Turtles in 2009 for $60 million, and the brand has already generated more than $2.5 billion at retail on consumer products, movie tickets, and home entertainment.

Our major new release in the quarter, Interstellar, was one of the year's most talked about films and a box office success, with box office to date of more than $660 million.

Paramount Pictures started the current quarter with the wide release of another movie that we're all very proud of. Nominated for a Best Picture Oscar, Selma brings to life an important part of our history.

Of course we are all looking forward to next week's release of the SpongeBob movie, Sponge Out of Water. The first title from Paramount Animation is taking one of the world's most iconic characters to a place, both literally and figuratively, he has never been before.

And just announced this week, Paramount has moved up the opening of proven franchise Mission: Impossible 5 to the end of July 2015. Nickelodeon and Paramount are also close to completing Paramount's first television production this year with School of Rock, which is set to air on Nickelodeon in the fiscal fourth quarter.

To conclude, we are pleased with our powerful position, particularly in this changing industry landscape. Viacom is dealing head-on with industry challenges, and we are positioning our operations for success.

We continue to be optimistic about the growth opportunities for our brands and the video content we produce, not only here in the US but particularly in international markets, where we see significant upside. Viacom has the assets, the commitment, the people, and the creative culture to succeed. We are innovating, investing, and unleashing our human and financial capital to take full advantage of these exciting opportunities, all of which puts us in an excellent position to continue to deliver outstanding content, deeper audience connections, and greater returns for our shareholders.

Thank you, and now I'll turn it over to Wade.

Wade Davis (EVP, CFO Strategy, Corporate Development):

Thanks, Philippe. Before I take you through our operating results, I want to note that our earnings release and web presentation summarizing the results for our December quarter are available on our Web site.

Now let's take a look at our segment results. At our Media Networks segment, revenues in the quarter were up 4% compared with the prior year. Domestic revenues were up slightly, while international revenues grew 25%.

Foreign currency headwinds had a 6 percentage point negative impact on international revenue. Channel 5 contributed 5 percentage points of revenue growth in the quarter. Page 10 of our web deck provides a breakdown of our Media Networks revenue performance.

In terms of advertising, worldwide revenues were up 3% in the quarter. Domestic revenues were down 6%, and international revenues increased 60%. The growth in international advertising revenues reflects the acquisition of Channel 5 as well as continued growth in the European marketplace. Foreign exchange losses had a 7 percentage point impact on international advertising growth and a 1 percentage point impact on worldwide advertising growth.

In terms of affiliate revenues, domestic revenues were up 8% year-over-year while international revenues declined 2%. Foreign exchange had a 7 percentage point unfavorable impact on international revenue growth and a 1 percentage point unfavorable impact on worldwide affiliate revenue growth.

Excluding the impact from the timing of product available under certain distribution agreements, domestic affiliate revenues grew high single digits in the quarter. Excluding the impact of foreign exchange, the growth in international affiliate revenue was due to new channel launches, increases in subscribers, higher rates, as well as the timing of product available under certain distribution agreements.

Expenses increased 9% in the quarter. Within operating expenses, programming expense grew 15% while distribution and other expenses increased 7%. SG&A expense was flat in the quarter.

Excluding the impact of Channel 5, programming expense increased 6%, while both distribution and other expenses and SG&A expense declined. The decrease in SG&A expense was driven by lower incentive-based compensation.

Media Networks adjusted operating income was down 1%, while the adjusted operating income margin declined to 42%. Channel 5 contributed about 3 percentage points of operating income growth in the quarter. The margin decline was driven by the 9% growth in expenses, which was partially offset by top-line revenue growth of 4%.

Moving to Filmed Entertainment, Filmed Entertainment revenues were up 6% in the quarter principally due to growth in home entertainment revenues. Page 12 of the web presentation provides a breakdown of Filmed Entertainment revenues.

Theatrical revenues increased 6%, primarily driven by carryover revenues from Teenage Mutant Ninja Turtles, which were partially offset by lower revenues from the current-quarter releases.

Home entertainment revenues grew 16% in the quarter. The increase reflects the performance of the current-quarter releases of Teenage Mutant Ninja Turtles and Hercules, while there were no titles released in the December quarter of last year.

License fees declined 9% in the quarter due to the mix of available titles. Filmed Entertainment generated an adjusted operating loss of $60 million in the quarter as compared to a loss of $74 million last year.

Now moving beyond the segment results, Other Items reflects a loss of $18 million due to foreign exchange losses. In terms of taxes, the adjusted effective tax rate was 32.3%, reflecting a 120 basis point improvement as compared to the prior year. The reduction in the adjusted effective tax rate was principally driven by the mix of domestic and international profitability.

With that, I'd like to turn the call over to Tom.

Tom Dooley (Senior EVP, COO):

Thanks, Wade. I'm going to talk about our cash flow, our debt, and the return of capital to our shareholders. I'll also cover seasonal factors impacting our 2015 fiscal year.

For the quarter, we generated $57 million in free cash flow compared to $278 million last year. Page 5 of the web deck presentation provides the components of free cash flow.

The decline in free cash flow in the quarter was principally due to higher working capital utilization. Working capital was negatively impacted primarily by production spending for our upcoming film releases, including Terminator Genisys.

Now moving to our debt, it remains principally fixed rate, with an average cost at quarter end of 4.5%. During the quarter, we took advantage of favorable market conditions and issued $1 billion of senior notes and debentures in a combination of 5- and 20-year maturities. Part of the issuance proceeds will be used to repay the $600 million of outstanding of our 1.25% senior notes that come due in February. The new debt was issued at an average rate of 4%.

In terms of our short-term funding, to the extent we have incremental borrowings, we are funding this in the commercial paper marketplace at an annual rate of approximately 35 basis points. At quarter end, we had no variable-rate borrowings.

In terms of our leverage, we ended the quarter with $13.8 billion of debt and capital leases outstanding. We had $1.2 billion of cash and cash equivalents.

Our leverage ratio at the end of the quarter was 3.2 times. Taking into consideration the February repayment of the $600 million of our senior notes, our leverage ratio is close to 3 times, which is within our targeted range. At December 31 our $2.5 billion bank revolver was undrawn.

During the quarter, we continued to return capital to our shareholders. Between our buyback and dividend programs, we returned a total of $887 million of capital back to our shareholders; and we ended the quarter with 407 million shares outstanding.

For the March quarter, we are on pace to purchase approximately $750 million of our stock, which means that for the first six months of the year we will have returned a total of approximately $1.8 billion to our shareholders.

Now let's turn to some of the factors impacting the remainder of our fiscal year. In terms of affiliate revenue, we continue to see annual growth in the high single-digit to low double-digit range. Quarterly affiliate revenue will fluctuate given the timing of transactions and the recognition of revenue related to certain distribution agreements which are tied to product availability.

For the March quarter, we anticipate that affiliate revenues will grow mid single digits as compared to the prior year.

For the full year, we expect that the organic growth rate for Media Networks programming expense will be in the mid single digits. However, reported programming expense will grow in the mid-teens, factoring in the acquisition of Channel 5. In terms of nonprogramming expense, we will continue to drive efficiencies throughout the organization in order to preserve our margins.

In Filmed Entertainment, we are excited about our upcoming slate, which includes SpongeBob, Terminator Genisys and Mission: Impossible 5. We continue to expect growth in profits to be weighted in the back half of the fiscal year, as the studio benefits from its summer theatrical releases as well as the availability of titles in the pay-TV and home entertainment marketplaces.

For 2015, we are now forecasting a book tax rate of 32.3%. We will continue to refine this as we go through the year and get a better sense of domestic versus international profitability mix.

Looking ahead at Paramount's production and development pipeline, the studio is currently in production on Paranormal Activity: The Ghost Image and Daddy's Home, which stars Will Ferrell and Mark Wahlberg. They will begin production shortly on Ben Hur, which is a coproduction with MGM; The Ring 3; and a comedy which stars Tina Fey that is being produced by Lorne Michaels. The studio is in development on a number of projects including sequels to Star Trek, World War Z, Teenage Mutant Ninja Turtles, and GI Joe.

In terms of TV production, Paramount continues to make great progress, having sold five more projects, to bring the total number of projects sold to 11. They currently have an additional 10 projects in development.

In summary, we remain focused on growing our businesses organically and investing in our brands and franchises. While we are experiencing a challenging ratings environment, we are working with our partners to more effectively measure consumption of our content, and we are developing ways to monetize viewership where measurement is currently unavailable.

We continue to generate strong growth in affiliate fees, and will manage our cost structure and drive greater efficiencies throughout the organization in order to preserve our core margins. From a capital structure standpoint, we continue to take advantage of the current interest rate environment, locking in long-term financing at very attractive rates. And we remain focused on returning excess capital to our shareholders.

Now I'd like to turn the call over to your questions.

QUESTIONS & ANSWERS

Operator:

(Operator Instructions) Michael Nathanson, MoffettNathanson.

Michael Nathanson (Analyst - MoffettNathanson):

Thanks. I have one for Philippe, and then one for Wade or Tom. For Philippe, I know you're confident about your ability to negotiate affiliate fees going forward. I know you've said 70% of the footprint is under contract through 2018.

But I wonder, looking out, given that some of your biggest MVPD partners are consolidating and some others are making more aggressive noises, do you think this means that Viacom has to get some more scale going forward, as those deals come up in the back end of the next five-year period?

Philippe Dauman (President, CEO):

Thank you, Michael. Yes, we have, as I mentioned in my remarks, the number-one position even on current Nielsen measurement in key demographics. I mentioned a couple of them: 18 to 34, 18 to 49. So we have the biggest scale, biggest reach in the demos that are particularly important when our distribution partners are trying to sell a variety of services to those same demos.

We are working closely with our affiliates to provide more value, even in the absence of affiliate renewals, as witness the announcement yesterday by Verizon FiOS for TV Everywhere capability. And we provide great value for all the reach that we provide; pound for pound, our programming fees are lower than many of the other programming families with much lower reach than we have.

So we continue to be very confident. We have successfully renewed on attractive terms for ourselves and our partners all of our major affiliate agreements, and certainly with all of those who are committed to their video business. So we continue to remain confident, and we feel we have the ability to manage our affiliate revenue stream as we now stand, successfully, as we go into the future. And we have demonstrated that.

Michael Nathanson (Analyst - MoffettNathanson):

Okay, thanks. Then for Tom or Wade, going back to the comments about potential restructurings, I know you want to save the actual numbers for when you do do the restructurings. But can you give a sense of just the range of how big the restructuring costs could be?

Or as Tom said, your goal is to maintain margin. Should we think about it that way, that margins will stay steady and costs will come down to maintain those margins?

Tom Dooley (Senior EVP, COO):

Look, Michael, as a Company, we've always been very focused on margins and improving them wherever we can. What we are contemplating right now -- we're not going to get into that and the magnitude of it at this point, but it will be something that focuses the business on the future business environment that we see coming down the pike. We are very confident that we can move there relatively quickly and be able to discuss it more comprehensively at the next call.

Michael Nathanson (Analyst - MoffettNathanson):

Okay. The next call you'll be able to give numbers on the size of this?

Tom Dooley (Senior EVP, COO):

Yes, sir.

Michael Nathanson (Analyst - MoffettNathanson):

Okay, thanks.

Operator:

Alexia Quadrani, JP Morgan.

Alexia Quadrani (Analyst - JP Morgan):

Thank you. Just two questions if I may. The first question is: any color you can provide on just domestic advertising trends in the March quarter?

And then the follow-up question. Is there a way you can quantify or give us just a general sense of how much of your ad revenue right now comes outside of the linear TV model? And I guess, where can that go, I guess, in a few years? Do you think you can make up any softness one can continue to see in TV, in the digital mobile world?

Philippe Dauman (President, CEO):

Thank you, Alexia. In terms of the current quarter, we see demand in the scatter market being quite strong. We are seeing pricing being, for us anyway, being in the teens, up from upfront pricing.

Our issue, based on the current Nielsen measurement in the quarter, is availability of impressions for us to sell. We currently look at domestic advertising in this quarter to be in a comparable range to what we reported for the last quarter, and we are looking to improvement in the back half of the year in domestic ad sales performance, with three principal drivers.

One is that we are, with new programming and better delivery of impressions, to increase the number of impressions that we are able to sell. Two, we are looking and working hard to better monetize the impressions that are not being properly monetized.

And three, we are continuing to work very closely with the agencies and our customers to drive value through better integrated marketing efforts. We have unique capabilities in that regard, use of reach data and engagement data through Viacom Velocity and Viacom Echo.

So as far as the movement toward better monetization of those impressions, we have a number of initiatives. I've described them in my remarks and in the prior call.

And when we talk about the proportion of our ad revenues, which in the last year were 30% non-Nielsen-dependent and over the next three years we expect that to grow toward the 50% mark, that growth will be driven by monetizing all these impressions that you have on our dot.coms, our apps, all the mobile impressions that we will continue to grow very rapidly, including through some of the new services that we will be launching with our telco partners.

Tom Dooley (Senior EVP, COO):

Alexia, there's really no crisp distinction between linear and digital. At this point in time, many of our deals allow us to provide delivery or fulfillment of the advertising commitment across both platforms. So that is providing us with great flexibility and, as we said earlier, beginning to allow us to monetize the broader consumption that we realize is taking place out there.

I think that's a trend. We are early in the cycle. The amount of digital consumption continues to grow; but as it does we are working, as Philippe said, really closely with our advertising partners and getting great momentum and great cooperation with the advertisers and the agencies to evolve the model.

Alexia Quadrani (Analyst - JP Morgan):

Thank you very much.

Operator:

John Janedis, Jefferies.

John Janedis (Analyst - Jefferies):

Thank you. Philippe, you talked about the hires on data and measurement. But can you talk more about how you're using data to promote viewership and to what extent it can increase the success rate of new programming, conceptually maybe to what Netflix has done?

Philippe Dauman (President, CEO):

Well, essentially -- particularly when we have programming on our mobile and other digital platforms, we have first-party information. We get very high CPMs, by the way, because we have great visibility on what kind of viewers are watching it. We are delivering a targeted audience to our advertisers.

And the more we increase our presence in those platforms where we can deliver and dynamically insert ads to very desirable audiences, not only will we have more impressions to sell but we will be able to sell them at higher CPMs than are otherwise available in less well-measured venues.

John Janedis (Analyst - Jefferies):

Maybe sticking with that theme then, you started to talk about the 30% sold away from Nielsen last quarter, on the way to 50%. Is that going to be a couple percent each quarter, or is there may be some sort of step function higher at certain points in time?

Philippe Dauman (President, CEO):

Well, there will be step functions along the way. There is going to be a steady progression.

That is certainly growing at strong rates. And then when you get new services that are launched, especially over the next few years, you're going to see a tremendous increase in mobile video distribution. So when these new services are launched and utilized by consumers, you're going to see some step changes along the way.

By the way, I don't want to shortchange the progress that Nielsen will also be making during this period. We are working very closely with them to improve the ability that Nielsen has, with its distribution partners, to better measure consumption, or to measure in the first place, consumption that is taking place, on streaming our networks on the variety of devices in the home and out of the home. During this time period, you will see improvement in that measurement as well.

John Janedis (Analyst - Jefferies):

Great. Thank you.

Operator:

Doug Mitchelson, UBS.

Doug Mitchelson (Analyst - UBS):

Thanks so much. A couple questions, Philippe. You talked quite a bit about the transitions taking place in Media. Can the Company maintain margin through all these changes when you look out over seven years? And can it and should it sustain this level of capital return? And then one more question after that.

Philippe Dauman (President, CEO):

As Tom talked about in his remarks, we are committed to maintain our margins. Technology is also giving us opportunities to improve the efficiency of operations.

Remember, we have a global footprint. And as we grow in all of our businesses around the world, in the US and around the world, we have an opportunity to look at how we do business.

As we have more programming throw weight we can look at how we procure programming, how we move it around the world, how we deal with our suppliers. So we are always finding very significant opportunities to increase our efficiency, as we continue to improve what appears on all of the screens on which our content appears and serve our viewers better.

So we are always focused on maintaining our margin, and we are taking a number of steps and at the same time investing for the future.

And we are committed for the very long-term, on the second part of your question, to return capital to our shareholders. At the same time, we want to maintain our strong financial position.

As you know, we target our 3.0 leverage ratio. We try to keep it at or below that level over the long run. We manage to that while meeting our capital needs.

That allows us the flexibility, given our strong cash flow generation, to return capital to shareholders -- which, by the way, along the way as we buy back shares is quite accretive to our bottom line.

Doug Mitchelson (Analyst - UBS):

I was hoping you would give us a little bit more detail on the over-the-top Nick service that you announced. Why just Nick and not something broader? What are your goals?

Is Nick programming going to be on the service? Is it global? What will pricing be?

Anything that you are willing to share would be helpful. Thank you.

Philippe Dauman (President, CEO):

Well, as I mentioned in my remarks, first of all, it's not going to be branded Nick. It's going to be a distinct brand, and Nickelodeon will unveil it at the upfront presentation to our advertisers.

And I certainly do not want to steal their thunder, as it will be a very great service. It will be geared to young viewers, quite young viewers. And their parents will, I think, very much welcome the availability of this premium subscription service that Nickelodeon will be offering.

So we are quite excited about it, and there are number of initiatives that we are working on. Again, we want to satisfy the demand that's coming from the viewers out there. They want more programming; they have an insatiable appetite for great content; and they want to be able to view that content on every device that they own.

So we are working with our distributors very closely, who also want to satisfy that demand. And we are looking at other opportunities that we have to both launch new services, find new ways to monetize the content we produce for existing services. And there is a lot of exciting opportunity as we move into that future, which, remember, is premised on people spending more and more time consuming entertainment and we are going to be a big part of their lives wherever they are viewing that content.

Doug Mitchelson (Analyst - UBS):

Thank you very much.

Operator:

Ben Mogil, Stifel.

Ben Mogil (Analyst - Stifel Nicolaus):

Hi, guys. Good morning and thanks for taking the question. So, just two quick questions. Probably the first one for Philippe. Any update that you can give us on some of the tests that you've done on dynamic ad insertion?

And then the second one, when you are talking about the flat margins at the Media Networks, are we talking reported, or are we talking excluding Channel 5?

Philippe Dauman (President, CEO):

Dynamic ad insertion, I'm glad you brought that up because as we continue to work with our affiliates on the video-on-demand side, dynamic ad insertion provides a great incremental opportunity for us at high CPMs for ourselves. And incidentally, given that the distributors also have a share in that, just as they do on the local minutes on the linear advertising for -- that's where they derive their local advertising revenue from -- it is a growing opportunity, and we over-index on this video-on-demand viewing.

So the ability to dynamically insert ads for advertisers -- I've used the example before: on a Thursday when somebody is watching a VOD and you can insert a movie ad for a movie that is opening that weekend, the CPMs on that are very high. So it's a great and growing opportunity and the way our tests and our results -- we're actually starting to derive some revenue from that -- are proving the point.

I'm sorry, what was your second question, Ben?

Ben Mogil (Analyst - Stifel Nicolaus):

Just on the Media Networks, the flat margins you were talking about, expectation this year. Are we talking on a consolidated basis or is that excluding Channel 5?

Philippe Dauman (President, CEO):

Obviously, Channel 5 is a lower-margin business.

Ben Mogil (Analyst - Stifel Nicolaus):

Sure.

Philippe Dauman (President, CEO):

As you know. And we're going to drive. Channel 5, by the way, is driving our overall business in the UK, and as we go forward will drive our business around the world, thanks to the great programming assets that it has. So we are very excited about the Channel 5 acquisition.

But yes, that is a lower margin business. And when we work on our margins in our international business and also in our domestic business, we look to maintain margins by finding efficiencies and growing our revenues, importantly.

Ben Mogil (Analyst - Stifel Nicolaus):

That's great, Philippe. Thanks for the color.

Operator:

David Bank, RBC Capital Markets.

David Bank (Analyst - RBC Capital Markets):

Okay, thanks. Philippe, we're really trying to get our arms around the measurement issue as the trajectory of consumer behavior changes. It's only likely going to accelerate with respect to cross-platform viewership and timeshifting.

So I think the issue that we wonder about is, it seems the advertisers have really defined the C3 parameter for measurement, and the advertisers have limited cross-platform measurement to that kind of identical spot load, which really hurts the headline rating numbers even if online impressions may be healthy.

So how much of this is about -- in changing the ratings metric and changing the ratings, how much of it is about a dialog with advertisers versus the measurement companies? Thanks very much.

Philippe Dauman (President, CEO):

It's both. Obviously we need to measure what people are viewing better. We need to improve even in C3. We need to improve just the C3 current measurement.

If you look at some of our shows across our networks, whether it's an Awkward or Faking It on MTV, or Drunk History on Comedy Central, or many of our other shows, there is a move just within the C3 universe from live viewing to viewing later on. So some of these shows are seeing as much as a 50% lift from the live viewing into C3.

And then you have a large proportion of viewing that's not being measured within that C3 window, and then viewing outside of the C3 window. So there has obviously been some talk over time about adding to the 3 number; but we're working very closely with the agencies and advertisers alike on more comprehensive measurement tools and working with them to take advantage of the reach we provide -- not just on the shows themselves, but in social media added on to our viewing, with special integrated marketing executions, sharing our data, sharing our research with them.

And we are getting a very receptive audience, and we are starting to see some movement there, which again will be a factor in improving our monetization going forward.

Tom Dooley (Senior EVP, COO):

David, one important thing to consider here is that -- one, the advertisers are the ultimate customer in terms of the purchases of our advertising. And different advertisers are moving down the digital road at different speeds, and the nature of their product defines the opportunity.

Car manufacturer who knows that an individual lease is coming up for renewal in three to six months, using that data combined with knowing what IP address that data, that person, is connected to would allow you to target ads as that person consumes content from Viacom or our competitors, is a very, very powerful tool in terms of targeting. That often is informed not only by the timing of that person's need or demand but also is informed by the kind of car they have and whether it's a luxury vehicle or a midsize or a compact.

People are just beginning to understand that and working with their advertising agencies and their partners, like Viacom , to better take advantage of that information and integrate that into a more informed buy, a much more targeted buy, a much more valuable buy to the advertiser. That's all taking place. That's what dynamic ad insertion is all about.

And there is just a plethora of data out there that adds to the value equation. Some advertisers, like the ones I just mentioned, are very sophisticated in beginning to use it; others are beginning to figure out ways and how it might apply to their product.

But as Philippe said earlier, we are in conversations across the industry with multiple agencies, dealing with multiple measurement metrics that reflect more appropriately that advertiser's targeting, defined targeted customer. And how -- and this is just the beginning of this whole evolution and whole understanding as to the metrics that are now available in the marketplace and how they'll begin to change this.

But the key thing is to get there, work with those advertisers, understand their products, and understand how we can bring -- connect them to consumers interested in consuming their products.

David Bank (Analyst - RBC Capital Markets):

Thanks, Tom; thanks, Philippe.

Operator:

Brian Wieser, Pivotal Research.

Brian Wieser (Analyst - Pivotal Research Group):

Great. Thanks for taking the question. First, putting aside the rating issues, do you get a sense that your core clients have more money in absolute terms to spend on TV this year versus last, but they just can't find the gross rating points? Or do you see those advertisers shifting spending to other media?

And a second question. I realize you don't want to talk too much the direct-to-consumer product for Nick. But can we read into the timing of when it will be announced at an upfront event that will have an ad-supported component?

Philippe Dauman (President, CEO):

On the latter question, again, I want to leave it to Nickelodeon to make the announcement at the upfront because they'll be -- they would not want me to take away their thunder, as I said before.

As far as client demand and where they might have spent on television, we are seeing strong demand. We had a very strong quarter in key categories like toys and movies in the last quarter, and we are seeing strong demand for the product we offer.

We do have a ratings delivery issue at the moment, which we hope will improve as the year progresses. But we are seeing good demand for television.

There is no better way to reach engaged audiences -- and particularly young audiences for toys, for movies, for electronics, for financial services aimed at young people, for cars, you name it -- there is no better way to reach them than on our networks. And that's why we continue to enjoy the demand and good pricing power.

Brian Wieser (Analyst - Pivotal Research Group):

So you see their general interest in using TV as still sufficiently healthy?

Philippe Dauman (President, CEO):

We are finding it healthy. We'd like to deliver more impressions.

Brian Wieser (Analyst - Pivotal Research Group):

Great. Thank you very much.

Operator:

Barton Crockett, FBR Capital Markets.

Barton Crockett (Analyst - FBR Capital Markets):

Thank you for taking the question. I wanted to ask you a broader question about consumer loyalty to your networks, which I think is really kind of the core driver of the value you are able to extract from distribution.

We've done some survey work which would suggest that on average, 15% of consumers could cancel or switch if some of your core networks were dropped from a big multichannel distributor. But you guys have some real life experience, and I was wondering what in your view is the percentage of people who would cancel or switch if Viacom networks were dropped based on data you've seen at maybe Cable ONE or DirecTV or your own kind of gut. How loyal do you think the subscribers are?

Philippe Dauman (President, CEO):

Well, we have, as you know, a great portfolio of brands, Barton, with people loyal to Nickelodeon, or MTV or a BT or a Comedy Central. So we have a broad scope of consumers who are loyal to various of our brands.

One of your fellow analysts who asked the question earlier put out a report recently using inquiries to other programmers, not us, about what happened in the Cable ONE situation, which is the small operator that didn't renew its affiliation agreement with us last April 1. And what he found from his checks was that based on the data that only went to sometime toward the end of 2014 -- it's not even current -- that expanded basic video customers had declined 18% since our networks were dropped.

So you have there an example of a company that is very rural that is facing on the video side very stiff competition from DISH and DirecTV and seems to be focusing mostly on the broadband business where it is not facing that kind of competition.

So it's an unusual situation, and we certainly -- we've had great success in renewing our deals with others who obviously have a strong commitment to all aspects of their business, including video. We provide great value for them to keep their customers. And to grow and attract new customers, a relationship with us is critically important.

Barton Crockett (Analyst - FBR Capital Markets):

Okay, great.

Jim Bombassei (SVP - IR):

Time for one more question.

Operator:

Vijay Jayant, Evercore ISI.

Vijay Jayant (Analyst - Evercore ISI):

Thanks. Philippe, you made some comments in your prepared remarks about something with Google. Can you talk about any opportunities with programming the YouTube type platforms that may be pretty attractive for your copyrights? Thanks.

Philippe Dauman (President, CEO):

Well, what I was referring to in my remarks was the Google fiber where we -- they are a good distributor of our channels. And they announced earlier this week, I believe, that they were expanding to three or four other cities.

And on YouTube, we have a number of clips that appear there for promotional reasons. There's some advertising revenue being generated there, relatively modest at this point. And we continue to look at opportunities for our content with them and all the other players out there.

We are always in conversations with all companies that are interested in utilizing video, and all of them are interested in talking to us. So it's a question of finding what the best form of partnership is, and that's always involving a model and one that will provide in the aggregate good growth opportunities for us.

Vijay Jayant (Analyst - Evercore ISI):

Can I ask one more please, which is talking about multiplatform; I think a lot of the distributors are incorporating SDKs to measure IP viewership.

Can you talk about the timeline of distributor platforms being ready and real measurement of IP viewership really coming into commercial value recognition?

Tom Dooley (Senior EVP, COO):

SDKs are being deployed right now, and we have them set up on a lot of our platforms and our services already. Nielsen is working very aggressively with all the major distributors to get those put in place. They are in place for a handful right now, but some of the larger ones still yet to be deployed. We hope and expect that they will be deployed within the next 3 to 6 months.

Vijay Jayant (Analyst - Evercore ISI):

Great. Thank you so much.

Jim Bombassei (SVP - IR):

We thank everyone for joining us on our earnings call.

Operator:

This concludes today's call.