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*Democracy Dies in Darkness*

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## Disney's potential Fox acquisition shows radically different responses to Hollywood's Silicon Valley threat

By Steven Zeitchik

NEW YORK — At the 21st Century Fox annual meeting last month, a shareholder asked Lachlan Murdoch the question on many people's minds: "How," the man said, "do we keep up with Amazon, Facebook, Google and even Netflix?"

The Fox executive co-chairman avoided a direct answer. But his company has a very specific idea of how to deal with the challenge posed by the Silicon Valley leviathans who have stormed entertainment — double down on everything that isn't scripted entertainment.

That's a very different idea from rival Disney's. And it has made a potential deal between the companies a logical development — and a study in contrasts.



Signage is displayed for the FOX Galaxy Parking garage outside of 20th Century Fox Studios in Los Angeles. (Patrick T. Fallon/Bloomberg)

As Fox appears to be preparing an epic deal that would transfer many of its core assets to Disney, the two companies are pursuing similar goals: survive and emerge stronger after the current period of brutal change. But their respective

means of reaching them couldn't be further apart.

Disney, under Wall Street-darling CEO Robert Iger, seeks to fend off challenges from direct-to-consumer powerhouses like Netflix and Amazon by using the weapon of scale.

Amass as much entertainment content as possible, its thinking goes, then draw from it to populate an online streaming service.

Rupert Murdoch, the Fox impresario, looks to side-step many of those challenges entirely by building a focused legacy business of news, sports and non-scripted programming.

“Can a narrower 21st Century Fox satisfy Rupert Murdoch’s interests and allow for a more readily managed company?” said Brian Wieser, a senior analyst at N.Y.-based Pivotal. “That’s one of the questions,” he said, before adding, “Just one of them.”

Murdoch wouldn’t necessarily stop there, though. By potentially securing a huge amount of Disney’s stock, a seat on the board and a high-ranking position for son and scion James Murdoch, who would likely leave his family’s empire for a role under Iger, the deal would also enable Murdoch to plant a flag at Disney.

The deal, which analysts said could close in as soon as a few days, is the result of Fox’s months-long courtship with Disney and an occasional flirtation with Comcast Universal and Verizon. Neither Fox nor Disney would comment for this article.

Although details are known only to a few executives, the merger is believed to be a mostly stock transaction valued

as high as \$40 billion. If it passes regulatory hurdles, it would leave Murdoch primarily with a broadcast network (Fox), two cable-news destinations (Fox News Channel and Fox Business Channel) and a pair of sports networks (FS1 and FS2), which Murdoch would then potentially combine with print-media company News Corp. under son Lachlan.

Disney? It would boast the largest entertainment company in modern history by a wide margin, one that in addition to theme parks, Marvel Studios and Lucasfilm would now have the top-tier TV studio it has always craved and a film operation even bigger than the one it already runs.

A Disney film studio with Fox in its stable would have accounted for nearly 40 percent of U.S. box office revenue in 2016 – a far cry from just a few years ago, when dollars were roughly evenly split up among six studios.

**“This is a match made in deal heaven because it gives each side what they want,” said Lloyd Greif, an L.A.-based investment banker and mergers and acquisitions veteran who has no stake in either company. “But it’s still too early to say if it will work out the way they want.”**

For a long time, Fox was almost a true rival to Disney. In 2014, a year after it split off from the print-centric News Corp., it had \$31.9 billion in

annual revenue, in the same ballpark as Disney, which had \$48.8 billion in annual revenue.

Just three years later, though, the companies have gone in opposite directions. Fox has seen revenue shrink to \$28.5 billion. Disney’s, powered by mega-franchises like “Star Wars,” has grown to \$55 billion.

That has led to a rethink of how to handle the new challenges from Silicon Valley. Fox has essentially decided not to try. With a market cap of \$160 billion, however, Disney believes more assets could help it brush back players like Apple and Amazon, each with market caps over \$500 billion, that have entered the entertainment space.

Such scale would allow it to exert greater power over distributors, including cable providers and theater chains, as well as fill its own distribution pipeline before its streaming service launches in 2019.

Not everyone agrees this is a good idea. As the reports of a deal heated up this week, Disney’s stock price dropped 7 percent. Investors’ concern is that Disney would be trying to take on nimble competitors by adding even more infrastructure.

“It’s shocking, just poor strategic thinking,” said BTIG analyst Rich Greenfield, one of those naysayers. “Instead of investing money directly in

original content and building its direct-to-consumer business, it's tying itself further to a legacy ecosystem."

Fox's films, for instance, are often tied up in existing long-term deals with premium cable channels that prevent them from being sold directly to consumers.

Almost everyone agrees that a supersized Disney would benefit from Iger staying. The 66-year-old is scheduled to depart the company in 2019 — itself a deferral from 2018 — possibly to run for public office. But an integration after a long regulatory period could mean the executive would need to stay on until 2020, especially given the lack of successors.

Most experts dismissed the idea of James Murdoch fast-tracking to the top position at Disney, as a Financial Times report earlier this week suggested he could. Instead, the 44-year-old would take a job within the company, possibly running the combined outlets' international operations, and eventually make a run at the big job.

"I think Rupert realizes Iger is a good horse to ride," said George Geis, a professor at UCLA's Anderson School of Management who specializes in mergers and acquisitions. At the same time, he added that he "wouldn't be surprised if [James] Murdoch could get something out of this."

Murdoch's motives divided experts. Certainly, pocketing billions of dollars in stock to walk away from the scripted entertainment business looks a lot like an exit strategy. But a large stake in Disney, a potential board seat and a shot at a Murdoch family member running it all could be viewed as much an expansion of power as a shedding of it.

"Yes," laughed Wieser, when asked if Murdoch was getting out or further in.

These maneuverings could come with collateral damage for the tens of thousands of people Fox employs or works with as a combined company streamlines operations. One producer who makes movies with Disney said that "as a business person, I understand scale, but as a creative person, I worry about having one less buyer for material."

A creator with a project in development at Fox said he had an even more pressing concern. "I'm super-stressed right now," said the person, who spoke on the condition of anonymity to protect his professional relationships. Projects would inevitably be discarded as redundant or not deserving of resources, and he feared his would be among them.

Most in jeopardy are the areas where Fox's operations overlap with Disney's, such as animation and family-friendly

entertainment. The fate of Fox's elaborate offices in midtown Manhattan and the Westside of Los Angeles would also be in question as a combined company looked to cut costs.

**But cash savings is just one element of the deal. Analysts saw in the acquisition a battle for the future of two corporate giants and the titans who made them what they were. Iger is looking to build a Silicon Valley-proof machine, while Murdoch wants to ensure a strong family business long after he's gone, one that avoids the problems that have dogged Sumner Redstone's Viacom empire.**

**"This is two equals going at it," Greif said. "That's what makes the chess game so interesting."**