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Will Warner Bros. Discovery have too much debt and not enough content?

Article

The news: **Warner Bros. Discovery** reported its earnings on Thursday, missing some of analysts' expectations.

- Revenue fell 8% to **$9.82 billion, trailing expectations of $10.36 billion** per Refinitiv estimates. Its revenue was also 8% down from one year ago.
- WBD **added 2.8 million streaming subscribers in Q3**, bringing it to 94.9 million direct-to-consumer customers—but revenue in that business unit fell to $2.3 billion, down 6%.
- Discovery experienced an 11% drop in advertising across its TV networks.

How we got here: It's been a challenging half-year since **David Zaslav**'s cable programming empire **Discovery Inc.** combined with **WarnerMedia** last April. WBD has been harmed by a massive debt load and a demoralized workforce, both of which are affecting its strategy.

Money matters: WBD's $47.5 billion in net debt is a tough pill to swallow. To put things in perspective, its net leverage ratio is roughly 5:1, higher than most other media companies.

- According to an October SEC filing, WBD anticipates paying $3.2 billion to $4.3 billion in pre-tax restructuring costs tied to its merger.
- With that debt, it's likely that WBD may make some decisions against its long-term interests. Case in point: Holding on to TNT's NBA rights will be challenging when they expire after the 2024—2025 season, with the NBA all but certain to demand a significant hike over the more than $1 billion TNT currently pays to carry games.
- In order to prepare for the merger of the **HBO Max** and **Discovery+** services the following year, WBD has trimmed or eliminated dozens of titles from the former. It also plans to discontinue making HBO Max originals in a number of European nations.
- Highly anticipated programming like "Demimonde" from producer J.J. Abrams and the "Batgirl" film have been canceled, even after completing production, for tax credits.
- Six upcoming animated shows, including Bruce Timm's "Batman: Caped Crusader," intended to expand upon his highly acclaimed 1990s "Batman: The Animated Series," have been canceled by HBO Max. A number of other projects that have been halted will be pitched to competitors.

Reason to hope: On the bright side, during the company's Q2 earnings call, WBD revealed that the company would consider the possibility of launching a free, ad-supported streaming TV (FAST) service.

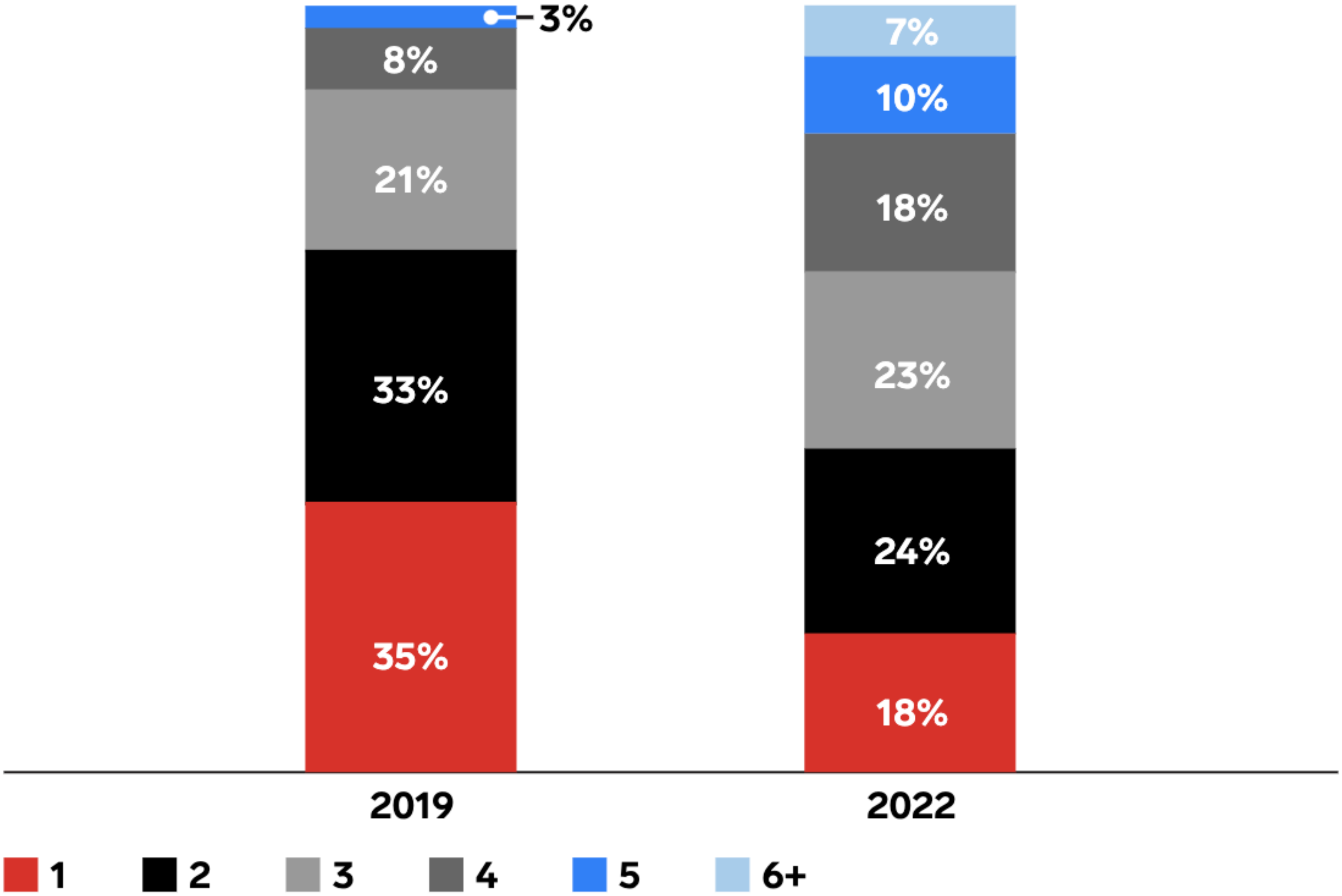
- A service akin to **Pluto,** operated by **Paramount Global**, and **Tubi** (**Fox** Corp.) would bring in incremental ad dollars in the same way it has for those two competitors.

- The service is expected to launch after the merger of HBO Max and Discovery+, which isn't expected until spring 2023, according to an update from the company's earnings call. So those FAST dollars aren't exactly right around the corner.

Our take: WBD has made its position clear: It won't overpay on programming to increase the subscription numbers for its streaming services. That position of austerity isn't exactly *wrong* for our current inflationary times, but is it *right*? With consumers concerned about the number of streaming services they're willing to pay for, does WBD really want to give them a reason to cut theirs?

Number of Paid Streaming Services Among US Paid Video Subscribers, 2019 & 2022

% of respondents



Source: Nielsen, "State of Play," April 6, 2022

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