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PARA.OQ - Q3 2022 Paramount Global Earnings Call

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## PRESENTATION

### Operator

Good morning or good afternoon. My name is Adam, and I'll be the conference operator today. At this time, I would like to welcome everyone to Paramount Global's Q3 2022 Earnings Conference Call. (Operator Instructions). At this time, I would now like to turn the call over to Anthony DiClemente, Paramount Global's EVP, Investor Relations. You may now begin your conference call.

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### Anthony Joseph DiClemente - *Paramount Global - EVP of IR*

Good morning, everyone. Thank you for taking the time to join us for our third quarter 2022 earnings call. Joining me for today's discussion are Bob Bakish, our President and CEO; and Naveen Chopra, our CFO. Please note that in addition to our earnings release, we have trending schedules containing supplemental information available on our website.

I want to 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. Some of today's financial remarks will focus on adjusted results. Reconciliation of these non-GAAP financial measures can be found on our earnings release or in our trending schedules, which contain supplemental information and in each case, can be found in the Investor Relations section of our website.

And now I will turn the call over to Bob.

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### Robert Marc Bakish - *Paramount Global - President & Director*

Good morning, everyone, and thank you for joining us. Today, I'll share some highlights from our third quarter and give you my perspective on the road ahead. Naveen will then take you through the numbers, and then we'll open it up for questions. In the third quarter, Paramount continued to execute on our differentiated strategy to deliver compelling entertainment experiences for the world's consumers while creating value for our partners and shareholders. That strategy is firmly grounded in 3 key strengths: first, our broad range of popular content; second, our unmatched array of platforms; and third, our truly global operating reach.

I'm happy to report that our robust content engine fire on all cylinders in the quarter, producing a broad range of captivating stories with engaging characters and settings for lovers of content of all kinds. As the only media company with 5 different platforms, we've delivered this content to an exceptionally large consumer market. Our businesses include the #1 broadcast network, CBS; a portfolio of industry-leading cable networks, many of which are #1 across their respective demographics like Nickelodeon and BET; the #1 free ad-supported streaming TV service in the U.S., Pluto TV; a rapidly scaling subscription service, Paramount+; and a Hollywood studio with 6 #1 hits this year, Paramount Pictures. And for us, it's not just about the U.S. Our global operating footprint includes the largest number of broadcast homes in the world, content production capabilities across Latin America, the U.K., Europe, the Middle East, Africa and Asia Pacific, cable network reach in virtually every key market and deep commercial relationships. And once again, these assets delivered.

In the third quarter, we sustained our strength in TV, grew nicely in film and drove rapid growth in streaming around the world. That said, as I think everyone is aware, this is a complex environment and economic period, and our results for the quarter do reflect some macroeconomic headwinds that are affecting our industry. For us, however, managing through near-term volatility does not mean radically diverging from the strategy that is producing real momentum and positioning Paramount to win in the long run. As we execute, however, we are also taking aggressive precise actions to gain additional efficiency across our cable networks, streaming platforms, advertising sales, marketing and global operations. These will yield cost savings next year as well as long-term strategic benefits. And we're taking advantage of this current market to accelerate these efforts.

With that, let's take a closer look at the quarter and our plans ahead. It all starts with our world-class content with a powerful mix of scripted and unscripted originals, hit movies, news and live sports, we've got something for everyone in the household. Let's start with the incredible run at Paramount Pictures this year. I can't talk about producing great content without mentioning our theatrical releases, where Paramount Pictures has dominated with 6 #1 films.

That string of hits is led, of course, by Top Gun: Maverick. It's now the fifth largest domestic release of all time and the only film in history to be #1 on Memorial Day weekend and #1 on Labor Day weekend in the United States. It was the #1 title in the U.S. in digital home entertainment, its first week of release as well. And we know it will continue to draw big audiences once it comes over to Paramount+ later in the year.

And now our hard thriller, Smile, released at the end of September has hit it big as our sixth #1 box office film of the year. Made for just \$17 million, it's now on track to gross over \$200 million globally. Smile will also be the next example of our 45-day theatrical to streaming FAST follow strategy, which gives fans the chance to have the big screen experience before enjoying at home on Paramount+ and which gives us a very compelling return on investment.

Next, we'll move to broadcast and CBS. 2022's #1 broadcast network, whose fall season is off to a strong start. On the entertainment side, we have 7 of the top 10 shows and more shows in the top 30 than all other broadcast networks combined. This performance is seen in returning favorites were close to 11 million viewers tuned to the season 2 premiere of Ghost, for example, and is seen in new shows like Fire Country, the season's #1 new show.

Fall also means football. And for us, that means the NFL on CBS and on Paramount+. The 2022 season kicked off in September with viewership off to its best start on CBS since 2015, and its best start ever on Paramount+. College Football is off to a strong start as well. And in August, we announced Paramount will air big 10 football games on CBS and on Paramount+ that will kick off next season. That means the biggest and best in college sports will continue to call Paramount Home through the end of the decade.

We don't just have American football. We've got European football, too. In August, we extended the rights to air the UEFA Champions League keeping this marquee property on Paramount+ and CBS for the next 8 years. And I'm thrilled that we did. As so far this season, Paramount+ had dramatic growth in average audience in streaming minutes and in total households. So the outlook is strong, and we are excited that some of the best soccer in the world will keep kicking it on Paramount+ with more games and an expanded playoff format, the deal creates an even more efficient investment for many years to come.

Paramount+ also saw a strong acquisition in the quarter from our slate of original series like SEAL Team and from movie releases, including the psychological horror film, Orphan First Kill; and the triumphant return of our favorite losers in Beavis and Butt-Head Do the Universe.

This powerful array of popular content is the fuel that continued to drive growth in subscriptions across our streaming platforms in the third quarter. Total global direct-to-consumer subscribers rose to nearly \$67 million in the third quarter. And the key driver here was once again, Paramount+, which attracted 4.6 million new subscribers, reaching 46 million total subscribers for our flagship streaming service. In fact, year-to-date, Paramount+ has led the industry in U.S. sign-ups and gross subscriber additions according to Antenna's September 2022 report. Year-over-year revenue from Paramount+ grew 95%.

Importantly, these third quarter numbers only begin to reflect the impact of the exciting first-of-its-kind partnership with Walmart. As you probably know, we have a decade-long relationship with Walmart in merchandise and consumer goods. So when the world's largest retailer was looking to enhance its Walmart+ package with a streaming offering, we are thrilled they saw a natural fit with Paramount+. Starting in September, Walmart+ members could begin opting into a Paramount+ essential streaming plant at no extra cost.

Early results have been very encouraging. Paramount+ has great potential to accelerate Walmart+ growth and retention, and we expect the partnership to grow as the marketing program ramps up including an in-store presence for the more than 100 million retail customers who pass through Walmart in the U.S. every week. Innovative partnerships like this are an important element of our pursuit of the largest total addressable market and it's a strategy we've taken global.

In the third quarter, we joined forces with powerful partners to debut new streaming offerings in several international markets. We celebrated the Italian launch of Paramount+ in September in partnership with Sky Italia. And later this year, we'll introduce Paramount+ in Germany, Austria and Switzerland with Sky Deutschland; and in France with Canal+, and we continue to strike these kinds of innovative partnerships.

In the U.K., we are pleased to announce a new multiyear, multifaceted distribution agreement with Virgin Media. Under that agreement, Paramount+ will debut on Virgin TV in 2023. And Pluto TV will be more widely distributed on Virgin TV 360 and stream service. In the third quarter, we launched Sky Showtime, our joint venture with Comcast in Denmark, Finland, Norway and Sweden. For us, this partnership represents a capital-efficient way to go after smaller markets. For the viewers, it means access to the best entertainment from the entire Paramount family as well as from NBC and Universal Studios.

Pluto TV, already the top free ad-supported streaming TV service in the U.S. also continues to go global. In September, we announced that Pluto TV will launch in Canada on December 1. Here, too, we have joined forces with another long-standing partner, Corus Entertainment, who bring local content Canadian audiences love and a powerful local ad sales channel to drive monetization. Of course, we are all aware of the ongoing macroeconomic pressures that continue to affect our industry and the ad market in particular.

As we navigate this period, Paramount will continue to rely on the fiscally disciplined approach that has been our advantage in good times and bad. We have always been mindful of cost management as a company, and we are now taking additional steps to improve efficiency across our organization.

For example, we recently announced our intention to reorganize Showtime networks, Showtime OTT and Paramount Television Studios into other parts of the company. This will further align our studios network and streaming operations in ways that enable significant cost reductions and advance our strategic agenda. We're also doing work with respect to international operations, marketing and ad sales.

And speaking of ad sales, we know that advertisers see us as a cornerstone marketing solutions provider in the U.S. They want to be where the top hits are and even more so in complex economic times. And our combination of the #1 broadcast network, a rapidly growing streaming service and the #1 free ad-supported streaming TV service offer a reach and frequently proposition that no one else can match. In the end, what matters most to our advertisers is the same thing that matters most to our viewers, the product on the screen. That's why we couldn't be more excited about the sensational content coming to Paramount+ and our other platforms in Q4.

Of course, there is the much anticipated return of the biggest hit on television, Paramount Network's, Yellowstone. And through coordinated cross-platform marketing, we will capitalize on the excitement around the premier of the fifth season to help boost the launches of 2 new Taylor Sheridan creations on Paramount+. None other than Helen Mirren and Harrison Ford will lead 1923, the next installment of the thrilling origin story

of the Yellowstone Saga, and Sylvester Stallone is premiering in Tulsa King about Mafia Capo building a crew far really far from his old mob family. We're also excited to premier the revival of the popular FBI drama Criminal Minds this quarter, exclusively on Paramount+.

With the help of several members of the beloved original cast, we are looking forward to activating the franchise's large existing fan base, which we see paying big dividends for Paramount+. As I mentioned earlier, our big theatrical hit Smile and Top Gun: Maverick will come to Paramount+ in the fourth quarter. And everywhere Maverick goes, it just crushes. So we think that will be a big draw on Paramount+ as well.

All in all, we expect all these new titles and highly anticipated events will entice more and more subscribers to Paramount+ in the coming months. In closing, by delivering extraordinary experiences for our consumers, we will continue to demonstrate the long-term value of our broad multi-platform model. At the heart of it, that's the real proposition behind our strategy. And with the momentum we're seeing in the year and the quarter, it's clearly working. With that, I'll turn it over to Naveen to walk you through a more detailed look at our third quarter results, and I look forward to continuing the conversation in our Q&A.

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Thank you, Bob. Good morning, everyone. Our third quarter results demonstrate continued execution of our long-term strategy to create broad content for diverse audiences across multiple platforms on a global basis. It's a strategy that offers significant incremental opportunity relative to our traditional business in 3 important dimensions.

First, as we've noted previously, streaming offers a total addressable market, which is more than twice the size of linear, excluding China and India. And the incredible ease of consumption with a vast array of content available at home or on the go, in whatever format you want, ad-free or ad-supported means we can connect more consumers with Paramount content than ever before. Second, we expect streaming to be accretive to ARPU over time. In fact, streaming ARPU already exceeds linear ARPU in some international markets. For example, in the U.K. P+ ARPU in the current quarter is over 20% higher than our U.K. linear pay TV ARPU, and our total reach has grown relative to the linear-only world.

In the United States, it's worth noting that there are streaming services in the market today with ARPU comparable to or higher than the monthly revenue we generate per linear household. And we believe Paramount+ will achieve these levels of ARPU over time with the implementation of price increases and continued growth and engagement and advertising monetization. Third, we believe long-term operating margins in streaming will approach TV media margins as the benefits of our multi-platform strategy play out.

This strategy yields significant efficiencies in marketing expense where our linear networks provide a great promotional platform for Paramount+ and in content expense, where we monetize content like movies and sports across multiple platforms.

Our streaming content expense also benefits from a wealth of fully owned library content and world-renowned franchises that are a highly efficient driver of acquisition and retention. These cost efficiencies do not exist in a pure-play streaming business model. Of course, our investment in streaming does impact near-term profitability. But given the combination of a bigger market opportunity, incremental ARPU and compelling margins, we believe there is significant long-term shareholder value to be created, and we remain committed to this strategy despite the impact of near-term cyclical advertising headwinds.

Now let's get into our third quarter results, which reflect strong D2C growth and box office success, but also macroeconomic conditions and FX impacts on advertising revenue growth. Total company revenue grew 5% in the quarter. Affiliate and subscription revenue rose 8%, continuing to demonstrate that the ecosystem shift from Pay-TV to streaming yields net growth for our business. Theatrical revenue was also a significant contributor to total company growth in Q3. Licensing revenue declined 1% and advertising revenue declined 2%. FX was a headwind to advertising revenue in the quarter, resulting in a 300 basis point impact on the advertising growth rate.

On a constant currency basis, advertising revenue grew 1% in the quarter. In direct-to-consumer, we added 4.7 million global subscribers, which drove 59% subscription revenue growth. As of September 30, we had a base of 66.5 million global D2C subscribers, including 46 million Paramount+ subscribers. Paramount+ added 4.6 million global subs in the quarter. Note that our quarter end total subscriber count reflects the elimination of 1.9 million Paramount+ subs in the Nordics, following the launch of Sky Showtime in September, which replaced Paramount+ in that market.

Ubiquitous distribution remained a key theme for Paramount+ this quarter. Domestically, we became the video service for Walmart+. And in Europe, we launched Paramount+ in Italy, including a hard bundle offer with Sky Italia. These bundled distribution partnerships were both important contributors to Q3 sub growth. And despite a lighter slate of new original series in Q3 compared to Q2, other content formats, including sports like NFL and UEFA, movies such as Orphan: First Kill and core CBS programming were significant acquisition drivers.

In addition to healthy subscriber growth, Q3 also saw robust engagement among Paramount+ subscribers. Daily viewing hours and paid conversion were strong. Paramount+ domestic churn improved both sequentially and year-over-year. Paramount+ ARPU was up year-over-year in the quarter. As we've previously indicated, we are benefiting from a dramatic increase in international ARPU as we continue to expand the P+ subscriber base in higher ARPU international markets.

Subscriber additions, ARPU growth and improved retention helped Paramount+ deliver 100% subscription revenue growth.

Shifting to the advertising side of the D2C segment, Paramount+ benefited from robust impression growth, improving CPMs and consistently high sell-through rates. Pluto TV added 2.4 million global MAUs in the quarter bringing our global reach to 72 million MAUs and total viewing hours grew strong double digits year-over-year. In fact, Pluto TV became the first free ad-supported streaming service to represent a significant enough portion of monthly total U.S. TV viewing to be included in Nielsen's monthly gauge report. Together, Paramount+ and Pluto TV delivered total DTC advertising revenue growth of 4%. Advertising revenue was impacted by the macroeconomic environment.

But given the engagement trends across our D2C platforms, we are confident growth will reaccelerate when the digital ad marketplace improves. As a whole, the D2C segment delivered 38% year-over-year revenue growth, with total D2C revenue reaching over \$1.2 billion in the quarter. D2C OIBDA was a loss of \$343 million in the quarter, reflecting investments we're making in content, marketing and international expansion as well as the impact of macroeconomic advertising headwinds.

Moving to the TV Media segment. Revenue declined 5% in the quarter. TV media advertising revenue was flat on a constant currency basis. The combination of pricing growth and strength in local station advertising helped offset the impact of lower linear impressions and a softer scatter market. TV media advertising declined 3% on a reported basis due to 300 basis points of FX headwind. TV media affiliate revenue declined 5% in the quarter. Similar to last quarter, the trend in total affiliate revenue for TV Media was affected by the restructuring of international affiliate deals, which proactively shift revenue from our Pay-TV to D2C services.

TV media licensing revenue declined 9% year-over-year due to a lower volume of programs licensed relative to the year ago period. As we've noted in the past, licensing revenue in any given quarter can be lumpy based on the timing of program deliveries. TV Media OIBDA declined 11% in the quarter to \$1.2 billion, largely reflecting the flow-through of lower licensing revenue and the decline in affiliate revenue.

Our filmed entertainment results continue to benefit from the success of Top Gun: Maverick, which was a key contributor to a 48% increase in segment revenue and the delivery of \$41 million in segment OIBDA. Top Gun continues to deliver at the box office, was a huge hit in the home entertainment market and we expect will be a driver of subscribers on Paramount+ when the movie comes to the service later this year. On a total company basis, adjusted OIBDA was \$786 million in Q3, down 23% year-over-year, reflecting the investments we're making in streaming.

Turning to the balance sheet. We finished the quarter with \$3.4 billion of cash on hand and total debt of \$15.8 billion. We also maintain a committed \$3.5 billion credit facility that remains undrawn. Let's now turn to our outlook for Q4. Starting with D2C subscribers. We're enthusiastic about both domestic and international momentum at Paramount+ and expect to see healthy Q4 sub growth, driven by the combination of a powerful content slate, expanded partnerships and new market launches. We now expect to exceed our full year global D2C subscriber growth expectation of 75 million global subs, excluding the removal of subscribers to our services in Russia.

With respect to financials, we expect continued macroeconomic weakness, particularly in the advertising marketplace, will affect Q4 TV media and D2C OIBDA as we now anticipate the year-over-year rate of change in total company advertising in Q4 to be similar to what we reported in Q3. Longer term, while we continue to invest to support strategic growth, as Bob noted, we're also accelerating opportunities to improve efficiency in multiple parts of the business. In addition to reorganizing Showtime networks, we're taking steps to further align our U.S. and international operations, applying a more global mindset to content and platforms, which will yield both economic and strategic benefits.

On the marketing side, we're prioritizing resources and media spend to those segments with the highest growth potential. And finally, we are taking the next step in the evolution of our advertising sales organization, streamlining our relationships with the major holding companies to provide single-point access to our industry-leading array of advertising solutions. The financial expression of these changes will start to manifest in 2023 while also benefiting us in future years.

Bigger picture, our financial discipline, our unique asset mix, our differentiated strategy and the significant incremental opportunity presented by streaming give me confidence we can navigate the complex near-term macro environment while positioning the company to maximize long-term value. With that, operator, we can now open the line for questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) And the first question today comes from Michael Morris from Guggenheim Partners.

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**Michael C. Morris** - *Guggenheim Securities, LLC, Research Division - MD and Senior Analyst*

Bob, I'm wondering if you can share any updated thoughts on the Showtime service as compared to the Paramount+ service, maybe specifically how you feel about continuing to run them as separate businesses with the potential for a bundle versus having a more integrated service between the 2? Where -- what are you thinking about that going forward?

And if I could, Naveen, both you and Bob talked about a number of puts and takes going forward, including the potential for some more aggressive cost savings. Can you opine at all on how you're feeling about free cash flow into 2023, whether you think there's opportunity for any growth there with these savings or whether you think the -- you talked about peak losses at the D2C side next year, whether you expect that to be heavier.

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**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes. Sure, Michael. So I'll take the first part of that. As you know, we've been offering a Showtime, Paramount+ bundle for a while. That was initially a price bundle, and there we saw some nice churn benefit -- and now we have really early success with an integrated app bundle. It's definitely exceeded our expectations in terms of net adds and engagement. And the reason which we've proven over and over again is that broad works, and upgrading to Showtime inside of Paramount+ adds even more to that experience. And if you haven't, you really should check out that version of Paramount+. It's the version I use, and it's great.

Bigger picture, I think this next chapter of Showtime is going to be particularly compelling. As we mentioned, we have a set of in-process organizational moves, and that will see Showtime benefit from further integration with the rest of the company. It will potentially introduce new ways really to create incremental value for both consumers and for distributors. It's going to unlock some significant cost synergies.

And I think beyond that, what I'm excited about, too, is how this slate of content for Showtime is going to evolve. There's been some early conversations around that. Start with the fact that the Showtime brand will stand really more than ever for thought-provoking, kind of distinctive, often edgy content.

And that means that it will continue to be a home for creative ideas. But in parallel, I believe you will see us extract more from some core franchises. We know that franchises work, and we think that's a good play for Showtime as well. And there'll be some incremental benefit from broader Paramount IP. So the road ahead for Showtime is really exciting, and we'll keep you up to date along the way. Naveen?

**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Yes. So to the questions on free cash flow in 2023 and what to expect there. I'd note a few things. I mean, first of all, in terms of the broad trends that are influencing free cash flow. It's really about the ramp in production and marketing investments related to streaming. And then obviously, some of the macro impacts on the advertising marketplace, offset by improvements that we're making both with respect to the cost side of the equation as well as improvements that we're seeing in working capital. And that's an important point because we are very focused on ultimately driving improvements in both earnings and free cash flow.

And I think what you'll see in '22 and both in 2023 is that the changes in OIBDA don't necessarily reflect the changes in free cash flow, which is to say the changes in free cash flow are better or lower than the changes in OIBDA because we have made improvements from a working capital perspective. So while it's premature to put any specific numbers on that for '23, I would note that we are still focused on peak D2C losses next year and continuing to apply that formula of improved working capital and realizing the benefit of the cost reductions that we noted, all of which should put us in a position to ultimately improve cash flow and OIBDA trajectory.

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**Operator**

The next question comes from Bryan Kraft from Deutsche Bank.

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**Bryan D. Kraft** - *Deutsche Bank AG, Research Division - Senior Analyst*

I guess I want to ask you, first, on the Walmart partnership. Just can you comment on how optimum performance has been so far since the launch in September? Are you finding that there's high awareness among Walmart+ subscribers and any other color on that? And then also, I just wanted to ask you, I mean, given the success you've had with the wholesale distribution of Paramount+, combined with the macroeconomic pressure on advertising, how should we think about Paramount+ ARPU growth and the trajectory it's on going forward?

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**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes, sure, Bryan. So as I mentioned in my remarks, we really have a decades-long relationship with Walmart. It's a relationship that's rooted in consumer products and home video. And yes, we have an office in Bentonville. And so when they were looking to add a video offering, we were really thrilled that they saw Paramount+ is the right choice. And part of the reason there as they really described to us was that they see both brands, i.e., Walmart and Paramount, as representing all audiences. The cost, the center of the country, young, old, you name it.

And yet again, I think that's confirmation of the power of our broad positioning built on popular content. So we launched our Walmart Paramount+ partnership in September, and just for the room, any Walmart's customer can choose to opt into Paramount+, and that gives them access to the Paramount+ Essentials product at no incremental cost -- once they opt in, they become a Paramount+ subscriber, and we get paid.

Partnership is off to an excellent start. We really -- I have not seen a more collaborative relationship between 2 big companies than what we have here right now, and that's phenomenal. And we are exceeding our early objectives in terms of number of subscribers that have joined through Walmart+. I think the more important point is the partnership has a long multiyear road ahead of it. To date, we've only done limited marketing, really leveraging some e-mail lists they have and some of our media the full in-store Paramount+ presence, for example, which will reach, I believe it's 140 million-ish customers visiting a Walmart store in the U.S. every week has yet to kick off. And by the way, there 1.4 million employees also get access for the ability to opt into Paramount+. And so we look for this partnership to be driving not only Paramount+ subscribers, but importantly, Walmart+ subscribers as well as they get access to this great benefit for quite some time.

I'd note that we also plan to execute on a multi-platform basis around our IP, and that's things like in-store activations around -- I don't know, PAW Patrol and Turtles next year and many other great franchises. So this is a super powerful example of our belief in partnership. And again, we're thrilled with the early results.



**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

And I'll jump in on the ARPU side of that question. I think simply put, we are very bullish about the ability to continue to grow ARPU in the streaming business, particularly around Paramount+. As we've spoken about before, there are a number of elements to that, some of which you're already seeing and some of which you'll see in the future. So for example, as I noted in my remarks, we are already seeing the benefit of continued expansion in higher ARPU markets on an international basis, and that's already benefiting ARPU.

And as we go forward, we see continued ARPU growth through the combination of both expansion and ad monetization and pricing on the subscription side. And the ad monetization piece, while in the short term is impacted by the marketplace, the fundamental engagement metrics that we see there give us great confidence that increasing consumer engagement will ultimately drive improvements in ARPU as the market returns.

And then on the subscription pricing side of it, we definitely see opportunities to increase price on Paramount+, and you will see us do that in the future. I think it's fair to say that pricing is moving higher across the industry, you see that with a number of competing services. And we think that, that means we have room to increase price and ultimately drive ARPU while preserving our value position relative to others. And I think that's true both in the U.S. and in key international markets.

That of course will be smart about how and when we raise price because we'll be looking to do it in ways that minimize any sort of negative churn impact. And that means we'll definitely take advantage of our dual tier offering, which allows us to adjust pricing on each tier independently and means that the essential tier can continue to serve price-sensitive users while still generating compelling levels of ARPU through ad monetization. And we'll also think about pricing in conjunction with how it interacts with our content slate.

So we're, as I said, confident we can raise price and that's one part of the bigger ARPU equation that includes continued growth in ad monetization and sub growth in high-value markets.

**Operator**

The next question comes from Rich Greenfield from LightShed Partners.

**Richard Scott Greenfield** - *LightShed Partners, LLC - Partner and Media & Technology Analyst*

When you look at sort of the success of Top Gun and Smile, it clearly shows us that you made the right decision in pushing both or waiting for both of those titles, and putting them into the box office versus putting them directly on to the streaming service. I think when you talk about sort of scale and reach of theaters, that was a clear benefit to both of those titles. But if you shift gears and you look at something like Halo or 1883. I guess I wonder, would those titles have benefited from being on a platform with more scale than Paramount+, meaning something like Netflix, we just saw NBCU shift Girls5eva from Peacock over to Netflix. And I'm just wondering, how do you think about sort of the pluses and minuses tied to reach and scale when you're deciding whether to put a piece of content on to your own service versus sell it to a third party? And how do you make that decision?

**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes. Sure, Rich. Look, I actually think we and others have talked about this a number of times over the year because it's really -- in a way, it's the arms dealer question embedded in it. And I think it's fair to say people's view on that topic has moved around over time. So as you know, we have 2 objectives: producing cash flow and margins from traditional media; and simultaneously building scale in the most important growth sector in media, which is streaming, really the network for the 21st century.

So our strategy around film, to the first part of your question, which is really theatrical leading to streaming. It's absolutely the right call in general, and it certainly worked for those titles, TGM and Smile, because both titles really benefited significantly from the theatrical window, and that's both

financially and from a marketing franchise building perspective. And as you know, both are coming to Paramount+ this year, and I'm confident they will be significant drivers, which will really continue our momentum as we scale streaming.

So that goes to your second point. If we're going to build scale streaming assets, which, as you know, we believe is fundamental in the long run. As I said, streaming is the network for the 21st century, and networks always had incremental economics to studio, and they will again. So if we're going to do that, we obviously need to leverage great content. So titles like 1883 and Halo, frankly, they need to be on Paramount+. And by the way, they've both proven very effective on the platform in terms of subscriber acquisition and engagement.

So they are working. In that case, the objective is not about maximum reach. They're key to creating asset value in streaming. And again, we believe that's the superior strategy from a long-term shareholder value perspective versus being a studio-only operation. And that's really the studio only operation is the path you be on if you started moving those to other places. So bottom line, we remain committed to traditional, including theatrical and streaming including through titles like 1883 and for that matter, our films. And we believe that's one of our advantages in the pursuit of shareholder value.

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## Operator

Next question is from Brett Feldman from Goldman Sachs.

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### **Brett Joseph Feldman** - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

So first, Naveen, thanks for giving us some help and some of thinking about the relationship next year between cash flow and EBITDA. For this year, you're essentially breakeven on cash flow through the first 3 quarters of the year. What are the key swing factors we need to be thinking about for the fourth quarter because sometimes nailing down working capital for us can be a little bit difficult.

And then you've had a lot of momentum and you expect to still have some momentum in the Paramount+ subscriber base, leveraging the new distribution in the new markets you're in. I'm wondering at what point you're going to -- you expect to be fairly fully distributed, whether it's through partnerships or geographic such that the incremental driver of subscribers is going to increasingly be about driving greater penetration through your content delivery in those markets? Is that something we should be thinking about in 2023? Or do you still think you've got a lot of distribution opportunities as we move into next year?

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### **Robert Marc Bakish** - *Paramount Global - President & Director*

Naveen, do you want to start with the Q4 thing, and then I'll take the streaming one?

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### **Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Sure. So on expectations for Q4 cash flow, I'd mention a few things. Again, just going back a little bit to what's driving cash flow in Q3, which as I noted earlier, is really about the ramp in production spend and marketing and international launches. And I think of those as sort of negative working capital drivers. Q4 will obviously improve relative to that because we'll get past some of those needs. Now some of that improvement, I expect will be offset by the macroeconomic factors affecting Q4 OIBDA as some of that obviously will flow to cash flow.

And therefore, I think it's probably most helpful to think about free cash flow on a full year basis. And when you look at it through that lens, as I said earlier, you'll see that the year-over-year change in free cash flow will be significantly smaller than the year-over-year change in OIBDA, which again reflects the progress that we're making in improving working capital, which is very important to us.

We're highly focused on the importance of generating free cash flow while we continue to invest in growth. So hopefully, that gives you a little bit of sense of how to think about the full year.

**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes. And as to your second question on subscriber growth, et cetera, start at the high level. We have absolute confidence in our subscriber growth potential and really the length of the runway here. And it's not just an opinion. It's really informed by data. Remember, we led the U.S. in 2022 in subscriber additions as we simultaneously expanded globally, notably this year to Western Europe. And with respect to the streaming opportunity, we really have a double benefit. Start with the market is large and it is still growing. And then add to that, we're clearly taking share. You see that in '22 unquestionably through the numbers. I'd also point out, it's not just about sub growth for us. We see real ARPU growth, and Naveen commented on that a bit already.

So in general, we feel good. Now when you unpack it and you look at streaming and you look at the drivers, and you start to think about 2023 and beyond, it's really -- and it sounds simplistic, but it's content, what's your slate doing? What are you doing in terms of market expansion and then how you think about partnerships? So our content slate continues to build. It's Killer in Q4. We could talk about that some, if you want, and that's going to run right into '23, and that's not just in the U.S., that's on a global basis. So we feel very good about that. And obviously, we have a longer-term content plan where we continue to build series, Paramount movies, et cetera.

If you look at market expansion, we're ending '23 with the completion really of Western Europe, which means that's going to drive -- we're ending '22, sorry, with the completion of Western Europe, and that's going to drive '23. We're going to do some stuff in terms of additional market expansion in '23, and we haven't talked about that yet. So put a pin in it. But I also want to point out that just because you launched in a market, that doesn't mean you get all the subs right away. Take the U.K. as an example. Sure, we launched with Sky in hard bundle, and that's performing very well. We're happy, our partners happy, et cetera. We've also launched in channel stores and direct D2C.

And then now today, we announced that Virgin is going to put Paramount+ on Virgin TV. So these markets will build over time. So it's not just about the entry point. It's about deepening your participation market by market. And by the way, including in the U.S. benefiting from both your content slate and incremental partners. So again, big picture, we feel very good about the size of this market. We feel very good about our ability to take share. We're doing that today. And we feel very good about the road ahead. This is going to be one of the cornerstone services for the world's consumers, and we are most certainly on that path.

**Operator**

The next question comes from Douglas Mitchelson from Credit Suisse.

**Douglas David Mitchelson** - *Crédit Suisse AG, Research Division - MD*

Bob, so a multipart question on advertising. So Bob, any further context around advertising trends you're willing to offer? Are you seeing broad weakness or certain categories pulling back? Anything on how that softness is sequencing in 4Q. Some companies are saying they're seeing stabilization the declines, others are saying, continues to weaken. So anything there?

And then Naveen, you talked about improving advertising monetization. One of the big debates for streaming and free TV recently, obviously is what level CPMs can be achieved, especially as targeting has improved. And I think some of the premium, the CPM goals out there for some of the newer services are well above what you guys might be getting currently. So I'm just curious, what are the ad monetization efforts? When do they start to layer in? And specifically, what kind of upside do you see as your targeting efforts improve?

**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes, sure. So look, as I said in my remarks, a difficult macroeconomic environment is certainly impacting ad sales in the quarter. It is a function of what we're seeing in the scatter market, where there is softness, more so on the digital side versus television. Worth noting that as you know, TV

has the additional benefit of a large upfront base. And our audience share growth or the performance of our brands, notably CBS in the broadcast year allowed us to take more dollar volume in the upfront, something I'm very happy about sitting here today.

In terms of categories, we're seeing travel is good, Electronics are good. Auto still hasn't moved. But I would point out, auto is a very interesting study because -- they've been building all the cars. They're just missing the last chip or maybe a couple of chips. And once those chips show up, there are zillions of cars out there that are going to have to move. So I don't know when that's going to happen, but when it does, it's going to be very good for the ad market, which goes to the broader point.

And look, I'm not an economist, but I think history can be instructive here. If you look back, we've had 3 down out ad cycles since 2000, right? We had one coming out of 9/11, one in 2008 and then one more recently in COVID in 2020, and they're all different, but the similarity is they all lasted a few quarters. It was all when there was negative GDP growth and each of those cycles led to a number of quarters with particularly robust ad growth coming out. So yes, we do have some macro-driven softness and all the people are talking about it.

But as it always does, this market will turn. And that's when you'll see real benefit from our positioning as a market leader with, the #1 broadcaster, cable group that includes leaders in young and diverse audiences, the #1 FAST service in the U.S., Pluto; rapidly scaling streaming service to Paramount+. It's all wrapped around compelling content that people want to be associated with and available more so than ever with what we're doing right now through a single point of access for the holdcos and clients with best-in-industry creative support and ad tech. So it's powerful positioning. It will really show itself again as this market turns, which is inevitably will.

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

And Doug, with respect to ad monetization, a few comments. First of all, I would say the main drivers of ad monetization from sort of an ARPU perspective, I mean, obviously, on the top line subscriber growth plays into it. But from an ARPU perspective, for us, it's really engagement driven. And I would say that we're really just getting started despite a lot of the great metrics that we're already pointing to in terms of consumption, both on P+ and Pluto and all of those trends moving up very positively. -- and churn continuing to come down.

I think we have a lot of headroom to continue to drive engagement, which will ultimately result in higher levels of advertising monetization. Second thing I would note is that with respect to CPMs and you asked about sort of how realistic some of the expectations may be out there, I would note that we've been in this business for a long period of time. We're in it at scale.

Our D2C businesses today are sort of at \$1.5 billion advertising run rate. And what that means is that we have been very focused on what is the largest part of that market. We're not necessarily going for the very premium CPMs. We don't think that's where the biggest pool of dollars exist. And that means that we are focused on 2 things: number one, continuing to drive scale and we price our advertising in order to achieve that; and number two, we're focused on packaging. And that's one of the big differentiators that we bring to the equation is the ability to package multiple types of D2C inventory, streaming inventory along with the full spectrum of both cable and broadcast inventory, which is ultimately, I think, the answer that advertisers are looking for.

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**Operator**

The next question comes from Ben Swinburne from Morgan Stanley.

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**Benjamin Daniel Swinburne** - *Morgan Stanley, Research Division - MD*

Just to pick on a couple of topics, you guys have already covered a bit. Naveen, should we expect a restructuring charge or charges in the fourth quarter, just given the cost activity you talked about any sizing of either that or what kind of magnitude of savings you guys are sort of targeting as you look into next year? I know it's probably early, but figured I'd ask. And then for either of you, just continuing on advertising, the linear business is holding up pretty well relative to digital. And Naveen to your last point on engagement, engagement was up a lot at Pluto, I think strong double digits, not sure what that means quantitatively but that sounds pretty strong.

But we're seeing the ad revenues really slow.

Why do you guys think linear is holding up better than digital? Is that all in the upfront? Or are there other factors -- and Bob, do you have a perspective on how Netflix launch, which I think is this week and Disney coming impacts your business and how you position your inventory and your ad tech as those guys now come to market and compete for ad dollars?

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Yes. Ben, it's Naveen. I'll start on the cost side and then turn it over to Bob to take the advertising side of that question. So I guess, first, just to the specifics, and then I'll talk a little bigger picture on what we're doing from a cost perspective. As I said, the benefit of the moves that we're making on the cost side will mostly manifest in 2023. I do think that there's a potential for a restructuring charge in Q4. We'll see depending on exactly the timing of finalizing some of these decisions.

I'm not going to put any specific numbers on those cost savings, but I would say that -- these are meaningful and sizable. They are things that we think not only have an economic benefit to us, but frankly, help put us where we want to be strategically in terms of both how we want to operate and where we want to focus our resources. And we shared some of the examples of what that looks like. It includes both labor and nonlabor expenses. It spans a lot of different parts of the business. And I'd point out that incremental to the ongoing work that we've spoken about previously that helps drive efficiencies on the linear side of the business. So it is meaningful, and I think it can be a helpful contributor to 2023, particularly in light of some of the macroeconomic challenges that exist right now.

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**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes. And Ben, on the ad market, you're right, the TV side has held up better than the digital side. I think there are a variety -- a couple of reasons for that. One is, yes, upfront base. And remember, our strategy in the upfront because we didn't know what the market was going to be like, but we had some concerns that things could soften -- and we were in a place where we had taken, I think, 18 points of broadcast share year-to-year. So we decided to have a volume upfront versus a price upfront. And we did business at high singles, but we took significant volume, and that was a good thing, and that's certainly helping TV for us. Second, and somewhat related to that, you always have a place where TV has limited supply. Broadcast, obviously, the most limited supply than cable. But effectively, those vehicles are sold out, and that supply pool is not getting any bigger, let's say, and add to that, you've got proven effectiveness.

If you're an advertiser with either product or servicing certainly in the United States and you want to make an impact on a national level there really is no better demonstrated media than television and people know that. So when they have to make choices, TV still is relatively well positioned in that. More broadly speaking, the market at the moment is a bit demand constrained. And that definitely works against the digital side. That's kind of the flip side of the television. There is digital supply out there. When you have strong demand market, you can really benefit, and you've seen us benefit. But when there's demand constraint, that tends to be rougher.

I would point out that based on the numbers I've seen reported, our D2C number of plus 4 actually compares quite favorably with some other large digital guys and what they've put on the table. So at least that's good, and we're happy about that. But at the moment, there's definitely some demand constraints we're working through. As to your question on Netflix I'd say 2 things. I'd say I'd start with the fact that new entrants going into the ad sports streaming, it's really validates again what we've long believed that adds our critical component of a broad streaming model. We see that as -- as you know, we have a totally free product in Pluto, and we have a lower priced product in Paramount+ Essentials.

Those are enabled by ad sales, and they broaden consumer access and consumers make choices. Some pay more, some pay less, and ad helps you do that. So again, validation of our strategy. When you talk to advertisers, they really care about the content, and they want to be wrapped around popular content, but they want to also get the right mix of reach and frequency. It's not just reach, it's also frequency. And we have an integrated server that lets us deal with that. That's part of what Naveen was talking about when he said the value ultimately of our multi-platform strategy. People like our diverse collection of content, entertainment, sports, news.

They like our track record in working with clients, integrated advertising. We're doing a lot in the advanced space. In fact, the fourth quarter is the first quarter ever where all the holding companies had at least one piece of business on non-Nielsen guarantees. So we're working with them on that. And we're dependable. We have a long track record of partnership. So yes, there's new entrants. The ad market has always been competitive. We feel great about our position. We've been there for decades. We have an industry unique portfolio.

No one else has broadcast network, FAST and a high-growth subscription streaming service, all wrapped around really the suite of content we have. So it's not about a new entrant. I think in the near term, it's really about the state of the market that's going to -- the whole thing is going to pivot on. But we're not surprised they're joining the market, and we're happy to compete with them.

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Operator, we have time for one last question.

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**Operator**

Our final question today comes from John Hodulik from UBS.

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**John Christopher Hodulik** - *UBS Investment Bank, Research Division - MD, Sector Head of the United States Communications Group and Telco & Pay TV Analyst*

On the media side, yes, we've hit the advertising piece. How about on the affiliate side. I guess for Naveen, can you quantify the impact that the reclassification of Sky had on the acceleration and the affiliate declines in the quarter, maybe what you're seeing in terms of cord cutting? And then just any outlook you could provide on that line item. That would be great.

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Yes. John, thanks for the question. I'd start by saying that with respect to the affiliate and subscription side of the business, particularly in TV media, I actually don't think that the Q3 rate of change is a particularly helpful indicator of what we expect to see longer term. And the reason for that is that there are a number of kind of nonorganic factors that affect the year-over-year comps. It includes the suspension of our linear channels in Russia.

There's a fairly sizable FX impact. There's differences in the number of pay-per-view events in the comp quarters. And as I mentioned, there's ongoing restructuring of primarily international affiliate deals that moves revenue from TV Media segment into the direct-to-consumer segment. I'm not going to size each of those independently, but I can tell you that if you adjust for sort of that group of inorganic items, TV media affiliate revenue would have been down 3% in the quarter versus the 5% reported. And I think that 3% is probably a better indicator of the underlying trend that we see on the linear affiliate side.

That being said, I think the real important takeaway here is that the better number to focus on is total company affiliate and subscription revenue, which as we noted in our remarks, grew 8% in the quarter. That's an important number because it demonstrates that the growth we're seeing in streaming is more than offsetting the declines that we're seeing in the linear ecosystem. And we expect that, that trend will continue.

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**Robert Marc Bakish** - *Paramount Global - President & Director*

Yes. Look, I'd just like to close by saying I understand there are concerns about the macro environment impacting the financials. But again, they're cyclical, they will inevitably turn. And more importantly, our world-class content engine is driving unquestionable momentum across our platforms. By that, I mean streaming, television and theatrical. We're really putting points on the board in all of them, and we're going to continue to lean into this momentum as we execute our differentiated strategy. We continue to feel this is the best path to value creation.

Of course, we'll always look at any option, but we will continue to do that as we execute and we look forward to getting the dialogue with all of you as we do. Thank you for your support. Have a great day.

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**Naveen Chopra** - *Paramount Global - Executive VP & CFO*

Thanks all.

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**Operator**

This concludes today's call. Thank you very much for your attendance. You may now disconnect your lines.

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