Boyar

The Forgotten Forty

2018 Issue

Boyar research

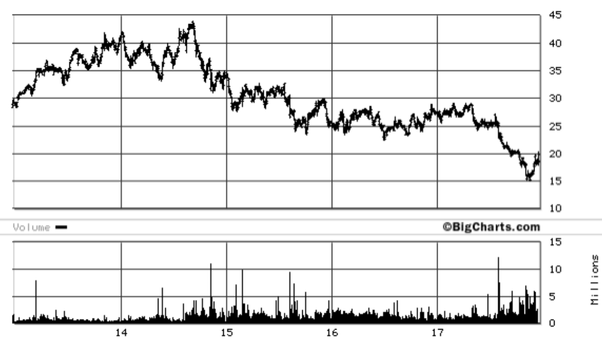
INVESTMENT RESEARCH SUMMARY
PRICED DECEMBER 14, 2017

Discovery Communications, Inc.

Capitalization Summary ($MM)	
Price	**$18.65**
Diluted Shares (MM)	**571.0**
Market Cap	**$10,649**
Total Debt	**$14,708**
Cash	**($6,994)**
Enterprise Value	**$18,363**

Share Ownership and Trading Data	
Average Daily Trading Volume (MM)	**3.6**
52-Week Price Range	**$14.99-$29.18**
Short % of Float	**27.0%**
Major Shareholders	**John Malone: econ. 3.5%, voting 28%**
	Advance/Newhouse: econ. 34%, voting 25%

DISCK
NASDAQ



Valuation and Misc. Stats ($MM) 9/30/17	
Book Value	**$5,740**
Price/Book Value	**1.9x**
Adjusted EPS (ttm)	**$2.13**
Price/Earnings	**8.8x**
Adj. EBITDA (ttm)	**$2,447**
EV/EBITDA	**7.5x**
Dividend Rate/Yield	**NA**

P&L Analysis ($MM)

Fiscal Year Ending December 31,	**2014**	**2015**	**2016**
Revenues	$6,265	$6,394	$6,497
Operating Income	$2,061	$1,985	$2,058
Margin	*32.9%*	*31.0%*	*31.7%*
EBITDA	$2,491	$2,398	$2,426
Margin	*39.8%*	*37.5%*	*37.3%*

Catalysts/Highlights

- Increased distribution with OTT providers and further Discovery GO (streaming) traction offer future growth opportunities
- The pending Scripps transaction deal offers meaningful synergies
- The 2018 Winter Olympics could help Eurosport bolster its direct-to-consumer and advertising ambitions
- Controlling shareholder/media mogul John Malone recently purchased nearly $9 million of DISCK shares at $19.75/share

INVESTMENT RATIONALE

Shares of Discovery Communications have faced significant selling pressure during 2017, declining by ~33% since last year's *Forgotten Forty* compared with an increase of nearly 18% for the S&P 500. This share price weakness likely reflects a number of factors, including investor concern over linear cable networks in general and the Company's adverse U.S. subscriber trends in particular, increased debt/leverage associated with its pending acquisition of Scripps, and a disappointing performance and outlook for its international business. Nevertheless, Discovery generates strong levels of free cash flow (~$1.5 billion; FCF yield: 14%), and we believe that it can continue to produce strong levels of FCF going forward.

Declines in subscriber counts for Discovery's U.S. networks (51% of total revenues) have accelerated throughout 2017 (5% decline in 3Q 2017). While the subscriber declines are concerning and worth monitoring, the Company's distribution revenue growth has actually been increasing (up 6% in 3Q 2017), reflecting rate increases and subscriber protections embedded in the Company's affiliate contracts. It should also be noted that DISCK's smaller networks are driving the decline, as the 3% 3Q 2017 sub decline in the Company's larger networks, which generate ~85% of segment revenues, was comparable with the decline seen in the prior quarter. DISCK is currently underpenetrated with OTT providers, but this underrepresentation could provide a nice source of future distribution growth considering that two of its key networks (Discovery Channel and Animal Planet) rank in the top 20 of channels that consumers would want included in an a-la-carte cable package, according to a recent TiVo study. Discovery's U.S. ad revenues (51% of segment total), which were up ~4% in 3Q 2017, should continue to be bolstered by the ongoing traction that DISCK is realizing with Discovery GO (streaming platform), where weekly streams have increased by about 50% from 1Q 2017 to 3Q 2017. The strong viewership on the GO platform (where consumers are tuning in longer) has a number of important implications, including driving increased advertising growth (expected to add over a point of U.S. ad growth during 2017 and strong growth in 2018), and reinforces the demand for the Company's content among the younger generation (~50% of GO users are aged 18-34).

Discovery's pending acquisition of Scripps also rattled and even frustrated investors because Discovery's leverage (net debt/EBITDA) levels will increase to nearly 5.0x from ~3.2x as a result of debt incurred to fund the $14.6 billion transaction (~70% debt and 30% equity), pausing DISCK's robust share repurchases with DISCK shares trading at 5-year-low levels. Discovery and Scripps generate strong levels of free cash flow (DISCK: ~$1.5 billion; SNI: ~$800 million), which is expected to enable DISCK to return to its targeted leverage (~3.25x) within 2 years of the deal's close (expected early 2018). Discovery is acquiring Scripps for just 8.7x EBITDA, factoring in the estimated $350 million in annual cost synergies, but revenue synergies are expected to be significant due to its increased scale (ability to attract higher affiliate fees from distributors), the potential to take SNI content to new international markets, and an opportunity to better monetize the combined businesses' strong viewership base (DISCK/SNI have 20% of viewership but less than 10% of industry economics).

Discovery's international networks business (47% of total) has disappointed investors with lower margins in the wake of the 2014 acquisition of Eurosport (23% during 3Q 2017 vs. ~40-45% pre-Eurosport). However, the international segment's margins are expected to improve going forward, with spending on sports rights—intended to bolster the network—expected to moderate going forward. The upcoming 2018 Winter Games, which is being broadcast on Eurosport for the first time, could go a long way toward boosting the Company's direct-to-consumer and advertising initiatives. Although DISCK recently reduced its outlook for international distribution growth in the near term (to a high single digit rate vs. low double digits)—reflecting, in part, subscriber declines in Latin America and Mexico due to economic challenges—the recent renewal of a number of key distributors in Europe should bode well from a longer-term perspective. We believe that multiple factors should continue to drive growth in the international networks segment from a longer-term perspective, including the still low international pay-TV penetration rates, the potential to offer its content to distributors on an exclusive basis, and the closing of the gap between Discovery's strong audience share in international markets relative to its advertising dollar share.

At current levels, DISCK shares trade at just 7.5x ttm EBITDA. In our view, this valuation is inconsistent with the Company's outsized profitability, strong and resilient free cash flow generation, and good growth prospects. Utilizing conservative assumptions, we estimate DISCK's intrinsic value (pro forma for the pending SNI deal) is upward of $40/share. We believe that there could be meaningful upside to our projection due to a number of factors, including the realization of greater-than-anticipated deal synergies, faster-than-expected deleveraging, improved U.S. sub trends and meaningful traction with new distribution platforms, and direct-to-consumer offerings. It should be noted that media mogul John Malone, who is one of DISCK's controlling shareholders, recently acquired ~$9mm Discovery shares via open market purchases at ~$19.75/share.

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The Madison Square Garden Company

Capitalization Summary ($MM)

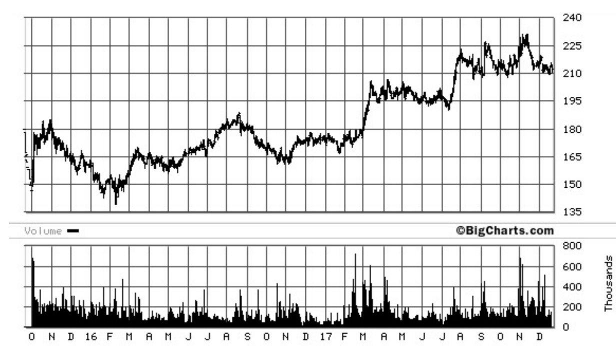
Price	**$209.87**
Diluted Shares (MM)	**23.6**
Market Cap	**$4,946**
Total Debt	**$105**
Cash	**($1,198)**
Enterprise Value	**$3,853**

Share Ownership and Trading Data

Average Daily Trading Volume (MM)	**0.2**
52-Week Price Range	**$231.44-$166.86**
Short % of Float	**3.0%**

Major Shareholder Dolan Family Group 22%, 71% voting

MSG
NYSE



Valuation and Misc. Stats ($MM) 9/30/17

Book Value	**$2,395**
Price/Book Value	**2.1x**
EPS (ttm)	NM
Price/Earnings	NM
EBITDA (ttm)	**$125**
EV/EBITDA	NM
Dividend Rate/Yield	NA

P&L Analysis ($MM)

Fiscal Year Ending June 30,	**2015**	**2016**	**2017**
Revenues	$1,072	$1,115	$1,316
Adj. EBITDA	$119	$68	$98
Margin	*11.1%*	*6.1%*	*7.4%*

Catalysts/Highlights

- Improved on-court performance of the Knicks could bolster MSG's sports segment
- Potential for monetization of valuable development rights due to strategic board appointment
- Two-year spin-off milestone has recently lapsed and could provide Dolans with the opportunity to take MSG private

INVESTMENT RATIONALE

Shares of MSG, which owns a portfolio of iconic sports teams (Knicks and Rangers) and venues (The Garden, LA Forum, etc.), performed well during 2017 (+21%) as its live sports and entertainment experiences proved resilient amid a difficult environment for many media-oriented companies. MSG sports (62% of FY 2017 revenues) experienced a 35% increase in revenues (+11% increase excluding $31 million of nonrecurring league distributions) thanks to growth in all of its main revenue categories (media rights, sponsorships, ticket sales, etc.) In addition, the ability of MSG's first-rate venues to attract nontraditional events also aided results as the Garden hosted both UFC (first-ever UFC event was the arena's highest grossing single-event ever) and eSports competitions. MSG Sports's long-term media rights deals, improved on-court performance of the Knicks (off to an encouraging start to the 2017/2018 season), and the signing of the Knicks' first-ever jersey sponsor (Squarespace) should help the segment sustain its momentum. MSG entertainment (38%) also posted strong revenue growth (+50%) primarily reflecting acquisitions (TAO and Boston Calling). However, event-related revenues at key venues, including the Garden and Forum, were up ~$20 million for the year as the number of events held at MSG's venues increased yet again thanks to MSG's ongoing strategy of attracting artists for multi-night and/or multi-venue engagements. The Christmas Spectacular enjoyed a banner year thanks to a ticket policy change that enabled MSG to capture margins previously ceded to ticket brokers (more direct sales to consumers). From a longer-term perspective, MSG's venue expansion strategy into select markets should provide future growth, and we note that a Las Vegas music/entertainment-focused venue is in the works.

MSG's ability to renew a number of its key corporate sponsors should also help it maintain its strong operating momentum. Not only has MSG renewed its first five signature partners that were up for renewal (multi-year, multi-million dollar agreements), but also each agreement, including a new 10-year deal with Delta, was substantially expanded. In our view, the strong rate of recent renewals suggests that sponsors recognize the value of MSG's live experiences, especially in today's fragmented media landscape. MSG is also making good progress on suite renewals at the Company's eponymous arena, having reached new deals with "solid built-in annual escalators" for the majority of suites up for renewal.

MSG continues to pursue growth opportunities, and FY 2017 was a busy year on this front, with investments in TAO (night clubs/restaurants) and Counter Logic Gaming (eSports). Although investors may be uneasy with the TAO deal, the business is already proving to be a nice strategic fit with MSG's recent signing of a major Fortune 500 company to an integrated entertainment/hospitality agreement (multi-year, multi-million-dollar) that includes access to MSG and TAO venues. Importantly, TAO also provides multiple new venues at which Chairman Dolan's band (JD & the Straight Shot) will be able to perform. Meanwhile, we believe that the eSports acquisition provides an opportunity for MSG to leverage its media rights and sponsorship expertise to capitalize on an increasingly popular and rapidly growing industry.

MSG owns significant development rights above Penn Station, and the recent appointment of Joe Lhota (formerly head of the New York MTA) to MSG's board could go a long way toward unlocking the value of this underappreciated asset. Meanwhile, MSG's investment in Azoff/MSG includes a number of investments in the entertainment business that are performing well, including the Oak View Group (venue management/services) and a global music rights business.

The recent abrupt resignation of MSG's well-regarded CEO Doc O'Connor has sent shares of MSG down about 10% over the past month. While the executive turmoil is disconcerting, we note that MSG has a strong board that includes noted activist investor Nelson Peltz. In addition, we would point out that Gregg Seibert, who serves as MSG's vice chairman, has been instrumental in a number of the value-creating moves at Dolan-related entities over the years (spin-offs, buybacks, dividends, etc.), including MSG's share repurchase initiatives, which has seen the Company buy back $263 million in MSG shares (1.55 million shares) at an average price of $170/share, 20% below MSG's current share price just since its 2015 spin-off. We believe that MSG will likely continue to be opportunistic with buybacks as it has ~$262 million remaining under its current buyback authorization and plenty of liquidity, including $1.2 billion in cash (just $105 million of total debt).

During 2017, the Houston Rockets (the 8th most valuable NBA franchise, according to *Forbes*) sold for $2.2 billion, representing a 33% premium to the most recent *Forbes* value. The transaction continues a longstanding trend whereby professional sports franchises routinely garner premiums to the prevailing *Forbes* value in acquisitions. Valuing the Knicks and Rangers (both rated as *Forbes*'s top-valued franchise in their respective leagues) at a similar premium results in a private market value for MSG of $327 a share, 56% above current levels. The 2-year spin-off milestone has recently passed, and the Dolans are flush with cash following their 2016 sale of Cablevision to Altice. Accordingly, we would not be surprised if they were to make a bid for MSG, which would go a long way toward narrowing the gap between MSG's public and private market value.

Kohl's Corporation

Capitalization Summary ($MM)	
Price	**$49.78**
Diluted Shares (MM)	**166.0**
Market Cap	**$8,263**
Total Debt	**$2,796**
Cash	**($736)**
Enterprise Value	**$10,323**

Share Ownership and Trading Data	
Average Daily Trading Volume (MM)	**4.1**
52-Week Price Range	**$55.19-$35.16**
Short % of Float	**19.6%**
Major Shareholder	**Insiders 1.2%**

KSS
NYSE

Valuation and Misc. Stats ($MM) 9/30/17	
Book Value per Share	**$30.30**
Price/Book Value	**1.6x**
EPS (ttm)	**$3.81**
Price/Earnings	**13.1x**
EBITDA (ttm)	**$2,285**
EV/EBITDA	**4.5x**
Dividend Rate/Yield	**$2.20/4.4%**

P&L Analysis ($MM)

Fiscal Year Ending Jan 28,	**2014**	**2015**	**2016**
Revenues	$19,023	$19,204	$18,686
EBITDA	$2,575	$2,487	$2,307
Margin	*13.5%*	*13.0%*	*12.4%*
FCF	$1,342	$784	$1,380
Margin	*7.1%*	*4.1%*	*7.4%*

Catalysts/Highlights

- After 2½ years of negative SSS, comps turned positive in 3Q 2017
- Management's numerous traffic driving initiatives, including 2 partnerships with Amazon.com and an upgraded loyalty program, should contribute to stronger SSS
- KSS's $250 million cost cutting initiative (over the next 3 years) should begin benefiting EPS in 2018

INVESTMENT RATIONALE

We view Kohl's Corporation as a brick-and-mortar retailer that can survive the "Amazon effect"—in fact, the Company recently partnered with Amazon.com on initiatives that we believe could boost SSS. Founded in 1988 in Wisconsin, KSS today operates 1,156 Kohl's stores in 49 states. It also has 12 FILA outlets and 4 Off/Aisle clearance centers. The Company sells moderately priced national brands (54% of revenues) as well as private and exclusive brands (46% of revenues) through its stores and website. National brands generally have the highest selling prices and the lowest gross margins, private brands generally have the lowest selling prices and the highest gross margins, and exclusive brands fall in the middle. KSS's 2016 revenues were split as follows: Women's (30%), Men's (20%), Home (19%), Children's (13%), Accessories (9%), Footwear (9%).

KSS management has two strategic priorities: (1) Improve operational excellence, and (2) drive increasing traffic into the stores. Regarding operational excellence, the Company is targeting $250 million in expense savings over the next 3 years. Management's traffic driving initiatives include a heavy emphasis on digital marketing, which is now KSS's largest marketing spend category. The Company increasingly delivers specific offers to consumers based on their past purchases. In addition, the Company recently introduced Under Armour products into all of its stores. The brand was a hit with Kohl's shoppers and contributed to the 20% growth experienced by the Activewear category (~15% of revenues) in 3Q 2017. In recent years, KSS made large investments to become best-in-class with respect to its omnichannel capabilities. Online sales grew by 15% in 3Q 2017, and 30% of online purchases were picked up by customers in KSS stores (saving them money on shipping). We believe that a well-executed omnichannel strategy can be a competitive advantage against e-commerce competitors. Accordingly, we believe that KSS's store base is one of its biggest assets, as 95% of its locations are in strip malls or are freestanding. Such destinations are not experiencing the traffic deterioration that malls are seeing. In recent quarters, some KSS stores saw traffic improve as a result of store closures by competitors. (For example, Macy's is in the midst of closing 100 stores.) We believe that KSS should continue to benefit as weaker retailers retrench. KSS is presently piloting the next evolution of its loyalty program, which has 30 million unique customers utilizing at least one element of the program. A company-wide rollout is expected in FY 2019. On the 3Q 2017 call, CEO Kevin Mansell stated that KSS management believes that "this next evolution has great opportunity to drive a step change in traffic and sales."

KSS's recent partnership with Amazon.com underscores the strategic value of its store base. In October 2017, KSS began two pilots with Amazon.com: (1) Amazon Smart Home Experiences, a dedicated area for Amazon gadgets and smart home devices, in 10 stores, and (2) Amazon Returns, a program under which Kohl's accepts returns of certain Amazon.com purchases, in 82 stores. We believe that Amazon Returns could prove to be particularly successful in introducing new customers to Kohl's and in bringing existing customers into Kohl's stores more often. A recent survey by JDA Software found that 70% of consumers prefer to return a product to a store whereas only 30% prefer returning items by mail. If the Amazon.com pilots prove successful at driving incremental traffic into KSS stores, a wide-scale rollout should follow.

SSS recently turned positive after 2½ years in the red. In recent quarters and years, SSS were 0.1% in 3Q 2017, (0.4%) in 2Q 2017, (2.7%) in 1Q 2017, (2.4%) in 2016, and 0.7% in 2015. Management's traffic driving initiatives bode well for rising SSS going forward, barring a recession. KSS's strong FCF (nearly $1.4 billion in 2016) has allowed it to return significant amounts of capital to shareholders. KSS began paying a dividend in 2011, and the dividend has grown by over 80% since then. KSS has also repurchased over 50% of its shares outstanding during the past decade. The firm's substantial real estate holdings further bolster its financial position. KSS owns 36% of its stores in addition to owning its corporate headquarters and the majority of its distribution centers. The owned stores alone could be worth over $6 billion (based on recent transactions), representing ~60% of the Company's enterprise value.

We have conservatively assumed that management's traffic driving initiatives merely offset rent and labor cost inflation, resulting in flat EBITDA going forward. After incorporating management's $250 million cost cutting program over the next 3 years, we project that EBITDA will grow by 3-4% annually out to 2020. We have assumed that KSS maintains its current dividend and that it uses FCF to pay down debt, resulting in a net cash balance of ~$1 billion at the end of 2020. KSS currently trades at just 2.8x our 2020 EBITDA estimate of $2.55 billion. Applying a 5.5x multiple to 2020 EBITDA, we estimate KSS's intrinsic value at $90 per share, offering 81% upside from current levels.