

I'd like to talk about a very simple business today.

After a long haul listening to very thorough presentations and detailed financial analysis, we are going to try to make this one relatively easy.

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This will be the most challenging slide of the day.

Please read it carefully.





In addition to siting and contributing to the development of Disneyland in Southern California and of Walt Disney World in Central Florida, his clients included Six Flags, World Fairs, Knott's Berry Farm and SeaWorld.

Today, I'd like to talk to you about SeaWorld which has a rich history dating back to 1959, when Busch Gardens Tampa, shown here, first opened. The park's second location in Williamsburg followed in the 70s.



Our research began shortly after in these very short and a little too snug shorts.



The company was later purchased by Anheuser-Busch in 1989. In 2008, BUD was acquired by InBev. New management slashed capital expenditures and began soliciting bids for non-core assets like Busch Entertainment Corporation.

One year later, Blackstone acquired Busch Entertainment for \$2.7 billion – not too far from the stock’s recent enterprise value. Blackstone took SeaWorld public in April 2013 at \$27 per share and the stock closed its first day of trading up 25%. The good news stopped shortly after.

This is a good business suffering from temporary challenges. It’s a simple business. So I’d like to spend my time today reviewing those challenges and explaining why we think the market is overreacting. If you believe the brand is not permanently impaired (we do), fair value is significantly greater than today’s price. Let’s take a look.



This is a great white shark. Along for the ride are remoras. Remoras use the shark for transport, protection and also feed on the crumbs left behind.

We think of SeaWorld as the remora of the amusement park industry, feeding on the crumbs left behind by Disney and Universal. There's a lot of money to be made as the number three player in this business. It's not a zero sum game.

Of course, this was also true when the stock traded near \$40, so it's important to understand what has changed since then and determine the impact, if any, on value.





This is an easy way to think about the IPO. High expectations allowed Blackstone to sell their shares at a premium. Wall Street pitched investors a compelling story.

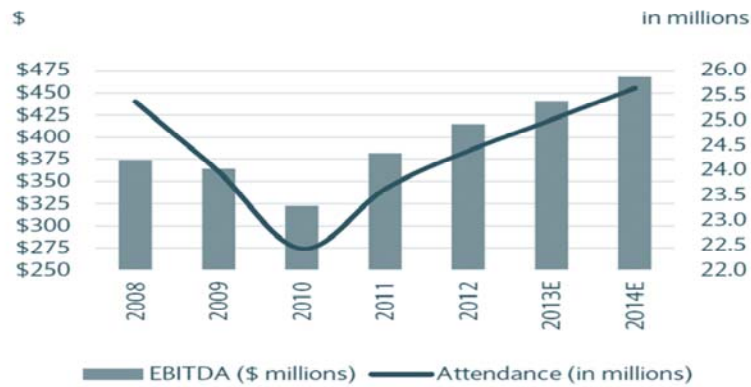
Public investors bought the story and the shares. Reality turned out somewhat differently, leading to disappointment.



## Attendance Estimates Were Too High

Consensus assumed a rebound in attendance and pricing

Adj. EBITDA and Attendance



The next two slides illustrate the street's expectations at the time of the IPO. You can see here that consensus projected a rebound in attendance and pricing.

This wasn't an outrageous assumption considering that attendance in 2012 was still a million below prior peak levels and the company was in the "early innings" of its dynamic pricing strategy.

## CapEx Estimates Were Too Low

Consensus assumed a normalization of capital expenditures

Historical and Projected Capex

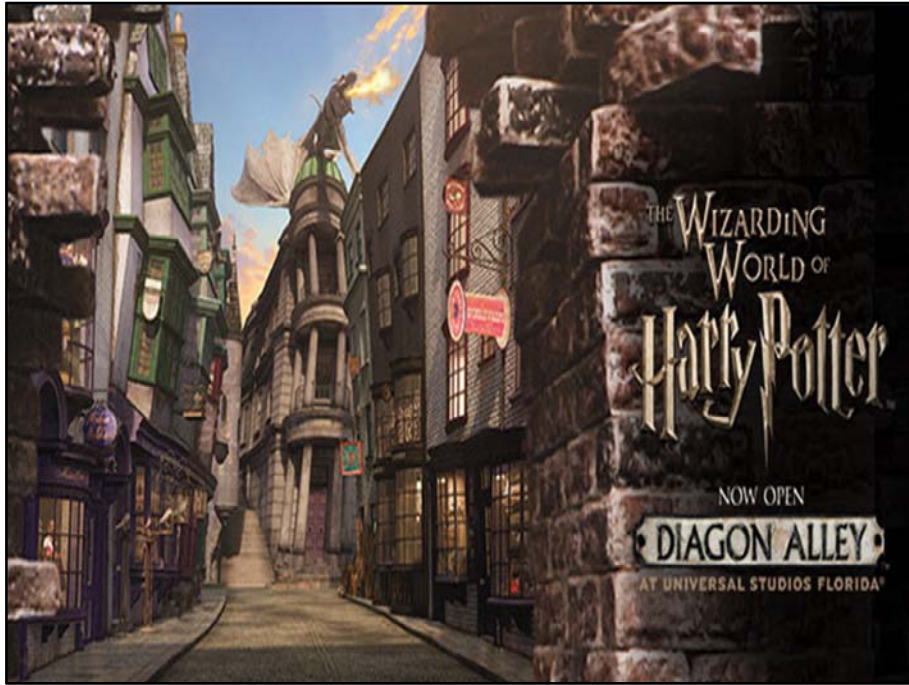


They also assumed that capital expenditures would normalize. Again, this appeared to be a reasonable assumption as capital spending was elevated for years under Blackstone after being cut by InBev. This was a big reason to be long the stock as these dollars would have dropped straight to the bottom line.



Instead, the company was faced with a series of unfortunate events driving a large gap between initial expectations and reality. First and foremost, Blackfish premiered at the Sundance Film Festival in January 2013 and was picked up by CNN for wider release.

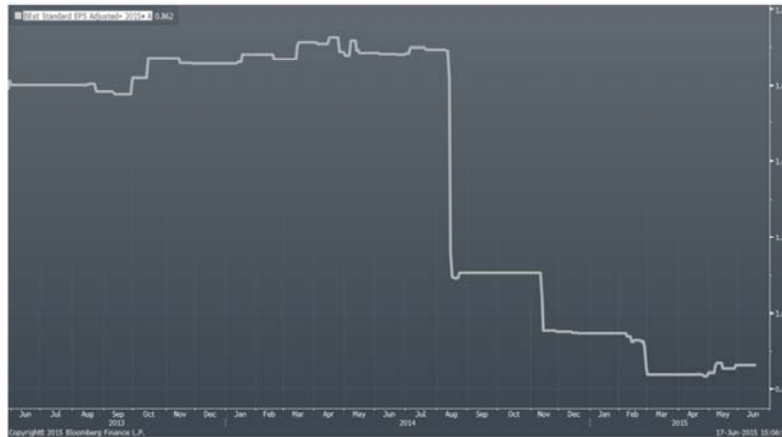
Management was slow to get in front of the film and essentially ignored the impact until it was too late. Attendance declines accelerated in 2014.



In addition, Universal launched a follow-up to the Wizarding World of Harry Potter last year. If you have kids, you know how big of a deal this is.

## Earnings Expectations Reset Lower

The former investor base capitulated and threw in the towel



As a result, management missed targets and guided lower. Investors capitulated and threw in the towel. Expectations collapsed along with the stock on its highest volume in history.

It's easy to understand why consensus is so bearish on the stock today. To recap:

1. Blackfish has tarnished the brand.
2. Disney and Universal are firing on all cylinders.
3. And the company's strategy is unclear.

We'll take each point in turn.



### **Consensus:**

Consumers tastes are evolving and Blackfish permanently impaired SeaWorld's brand

### **Our View:**

Animals provide a rare educational experience and SeaWorld is past the point of "Peak Blackfish"

Let's start with Blackfish. This was a very difficult movie to watch. It was extremely emotional which makes for a very good film. It also makes it very easy to jump to conclusions and overstate its impact, which we think is temporary.



Some history may be useful for perspective. PETA has been campaigning to free orcas since 1998. The Blackfish broadcasts on CNN injected new life into its SeaWorld campaign.

In 2012, they actually sued SeaWorld on behalf of captive orcas arguing that the orcas deserved protection under the 13th Amendment, which prohibits slavery. They lost the case. And in 2013, when SeaWorld sponsored a float in Macy's Thanksgiving Day Parade PETA stood along the route to protest.





Despite all the attention, more than 7 out of 10 people believe PETA is too extreme.

Can you see why?

## "BLACKFISH" BACKLASH

a trainer...Dawn would not have remained a trainer at SeaWorld for 15 years if she felt that the whales were not well cared for."

Brancheau Family



This is a very emotionally charged issue.

But as always, there are two sides to the story.

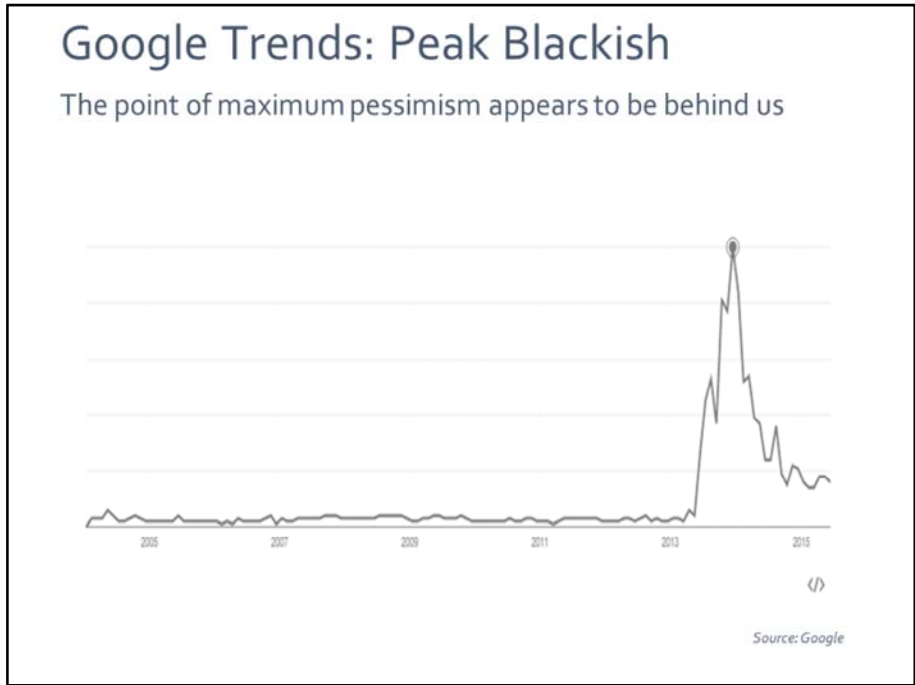
## Over 175 million people visit zoos

More visitors than the NFL, NBA, NHL and MLB combined



I think the average American still enjoys going to the zoo or the aquarium. The empirical evidence supports this assumption. Over 175 million people visit zoos annually – more than the NFL, NBA, NHL, and MLB annual attendance combined.

Zoos have been around for a very long time. They provide kids with an educational experience that is impossible to get anywhere else. SeaWorld serves a very similar role. It is a unique place.



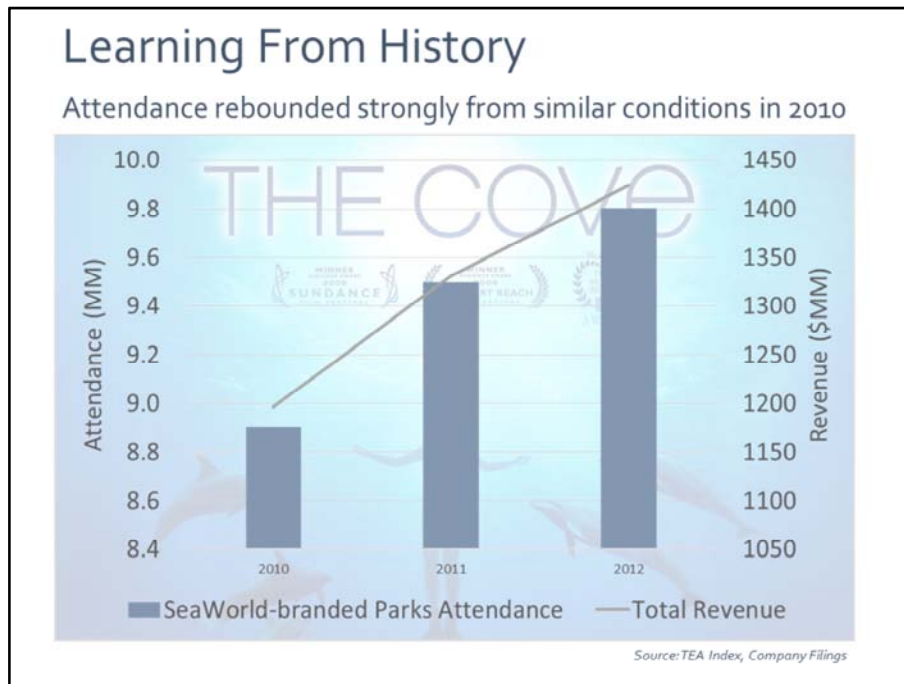
So we think the maximum impact from Blackfish is behind us.

You can see this in Google Trends.



You can also see this in San Diego where park revenues appear to be bottoming. This chart shows SeaWorld's monthly rent payments to the city which are a function of sales at the park.

You can clearly see the decline in revenues during 2013 which accelerated in 2014. You can also see (if you look hard enough) what appears to be a recent trough. Comps should get easier as SeaWorld anniversaries Harry Potter and Blackfish.



We can also learn from prior experience. Blackfish was not the first documentary to negatively impact SeaWorld. A similar film, The Cove, was released in 2009, and had an equally negative impact on park attendance.

There were other similarities between 2009 and 2014 as well. In addition to negative PR centered around the death of a SeaWorld trainer, Universal opened Harry Potter attractions in both years. In many ways 2010 was actually worse than 2014. But it also provides us with a good baseline for expectations.

As shown here, attendance at both Orlando and California SeaWorld parks rebounded strongly from the 2010 trough. Revenues followed. We see no reason to believe this time is different.



### Consensus:

Consumers tastes are evolving and Blackfish permanently impaired SeaWorld's brand

### Our View:

Animals provide a rare educational experience and SeaWorld is past the point of "Peak Blackfish"

Bottom Line. We think the maximum impact from Blackfish is behind us.

Let's move on to Harry Potter and the competition.





### **Consensus:**

Impossible for SeaWorld to compete with Disney and Universal

### **Our View:**

This is not a zero sum game; the remora should continue to benefit from the efforts of the shark

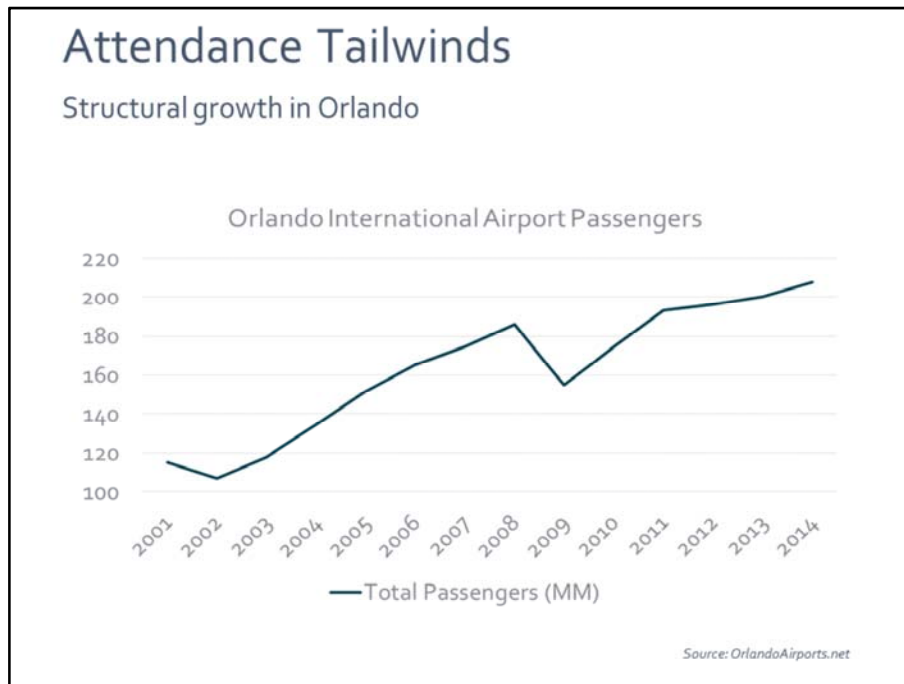
As a rule of thumb in the amusement park industry, operators spend roughly 10% of sales to maintain the parks, invest in new attractions and drive attendance. If you're Disney, 10% of sales is a lot of money!

Obviously, SeaWorld cannot compete with Disney and Universal dollar for dollar. We don't disagree with consensus on this point. We just don't think the remora needs to compete at all.



SeaWorld has competed in the same markets as Disney for decades. They haven't survived by competing head on. I can promise you that if this kid plays the conventional way, he will fail conventionally. I can also promise you that if SeaWorld attempts to compete head to head with Disney and Universal, they will fail conventionally.

It is impossible for them to match these giants dollar for dollar. But they don't have to. Instead, they've survived by playing their own game. The rides and animal encounters offered at SeaWorld create a unique experience for families. Since its inception, SeaWorld has successfully used educational entertainment to connect its guests with the natural world. This experience is invaluable.

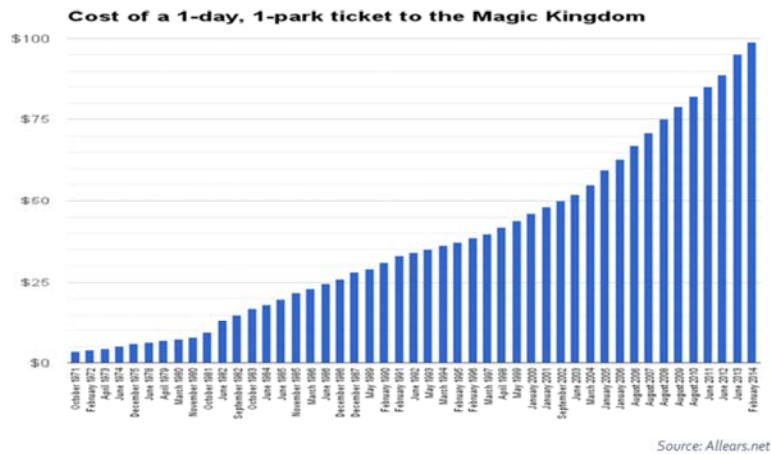


**Let's go back to the remora for a minute.** Think about how easy these guys have it. These guys just piggy back off the shark all day. They let the shark do all the heavy work and they enjoy all the scraps.

Sharks leave lots of scraps behind. So does Disney. Look at the passenger traffic into Orlando over the years. That's a lot of potential park visitors.

## Competition Has Its Benefits

SeaWorld has plenty of cover to raise ticket prices



Disney and Universal provide additional benefits to SeaWorld. In addition to attendance, they provide plenty of cover in terms of pricing.

Take a look at ticket prices at the Magic Kingdom over the years. Disney cost about \$50 just ten years ago. Today it costs twice that in addition to the obscene amounts of money you spend once in the park.

Let's think about this for a second. If Disney continues to raise prices at 6% annually, in ten years the price of admission at Disney would be almost 2x that of SeaWorld (assuming the same starting point). Even if SeaWorld raised prices at half the rate as Disney, its tickets would still be a third cheaper in ten years.



### **Consensus:**

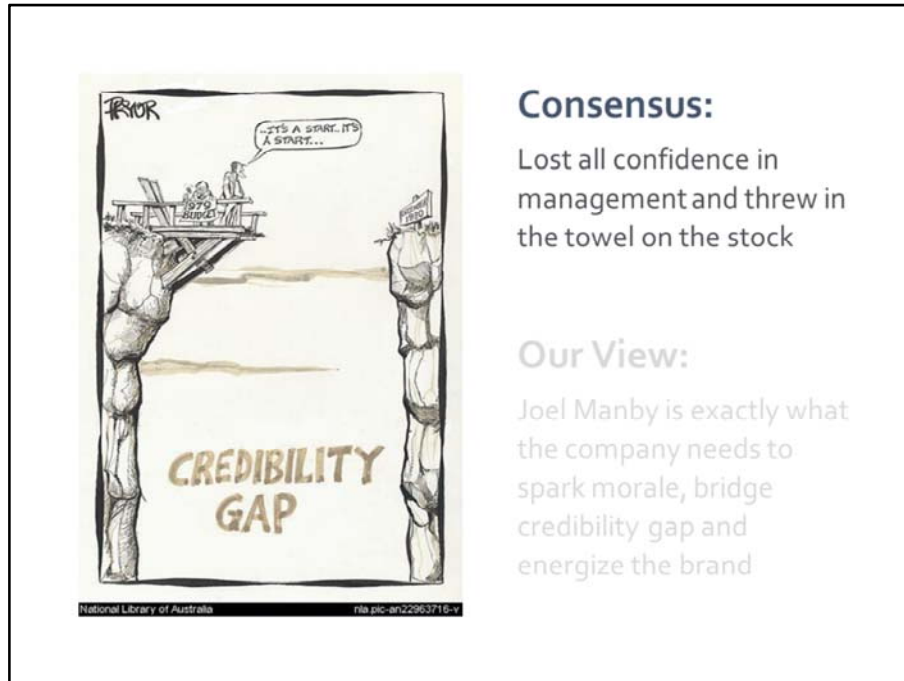
Impossible for SeaWorld to compete with Disney and Universal

### **Our View:**

This is not a zero sum game; the remora should continue to benefit from the efforts of the shark

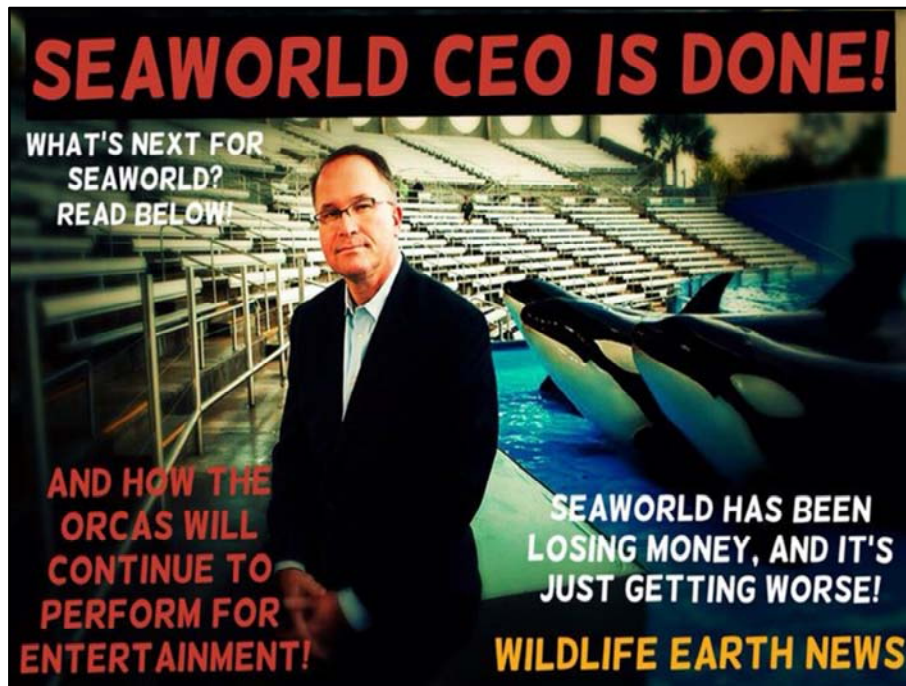
Bottom Line: Attendance and pricing may be challenged in the short term, but both are headed higher in the long run. Being the remora has its benefits. There is plenty of money to be made as the small fish in a big pond.

Let's move on to the most recent change at the company before wrapping up with our napkin valuation.



SeaWorld's former CEO, Jim Atchison, started working at Tampa's Busch Gardens parking cars when he was 16.

The company's management team had an average tenure of almost three decades in the industry. It's amazing how fast perception changes.



SeaWorld's prospectus listed its proven management as a core competitive advantage. Given the company's performance and prior management's complete loss of credibility, I'm not sure I would agree.

That being said, we invested in the stock based on its discount to asset value and despite this "proven" team. Since then, the company has replaced its CEO and announced an "interim" CFO.

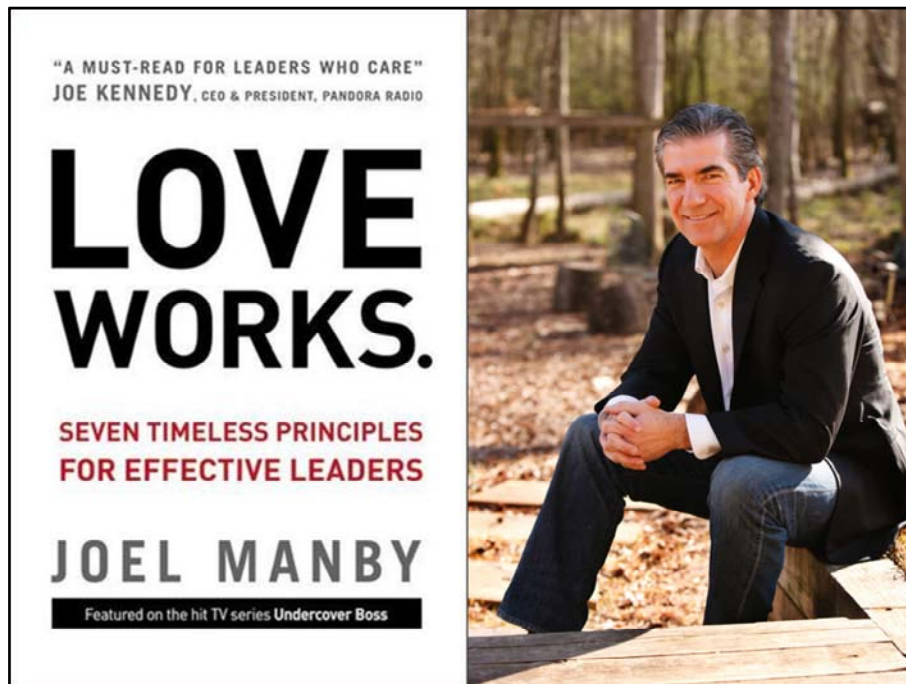




Meet Joel Manby. The new Sheriff in town. Manby was featured on the first season of Undercover Boss. It is still one of their most popular episodes and for good reason. People love this guy. They love working for him and they love watching him succeed.

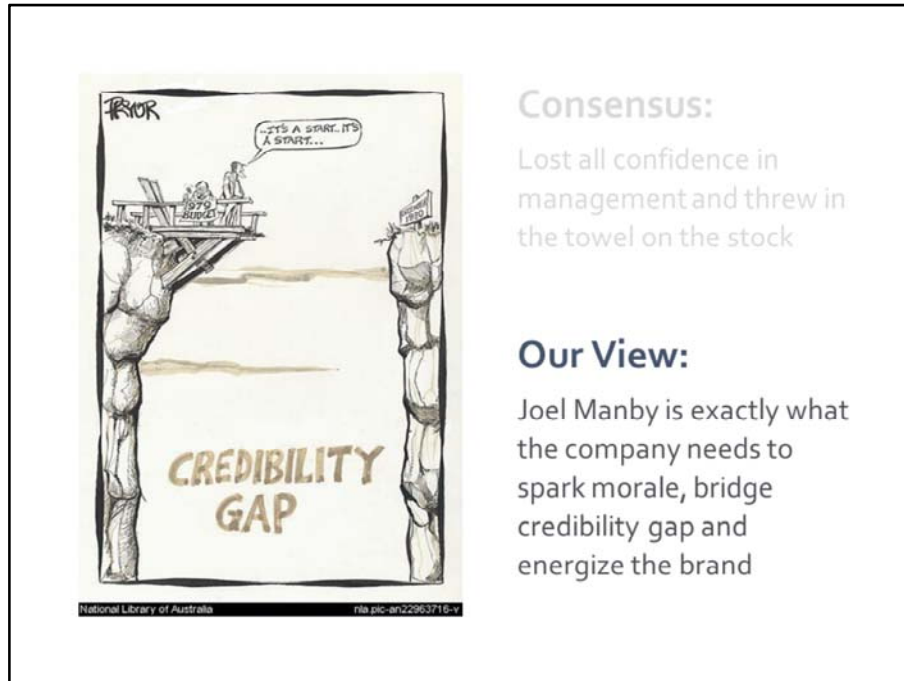
Prior to joining SeaWorld a few months ago, Manby was CEO of Herschend Family Entertainment. He grew Herschend from a family owned park business into the largest privately owned theme park company in the US.

It's valued at roughly \$1 billion thanks largely to Manby's hard work. In his time there, he grew the business to 26 parks compounding sales at 7% annually.



We think Manby is a home run for SeaWorld. After reading his book, I couldn't comprehend why this guy would have ever left Herschend to go work for a private-equity-owned business, given the relationship he formed with the family, the employees and the customers.

But our conversations with operators in the industry have provided us with insight and reinforced our initial impressions. Manby understands SeaWorld's situation. He appreciates the board set up and understands the risks. He did his diligence and he was ready for a change. He couldn't pass on the opportunity to rebuild this historic brand and we think he is the guy to do it.



### Consensus:

Lost all confidence in management and threw in the towel on the stock

### Our View:

Joel Manby is exactly what the company needs to spark morale, bridge credibility gap and energize the brand

Bottom Line: Manby has his work cut out for him, but we think he's the right jockey to be riding this seahorse. We've bought more stock since we climbed aboard.

Let's take a look at what SEAS is doing to address its challenges.



The company launched a new national TV campaign which started in April.



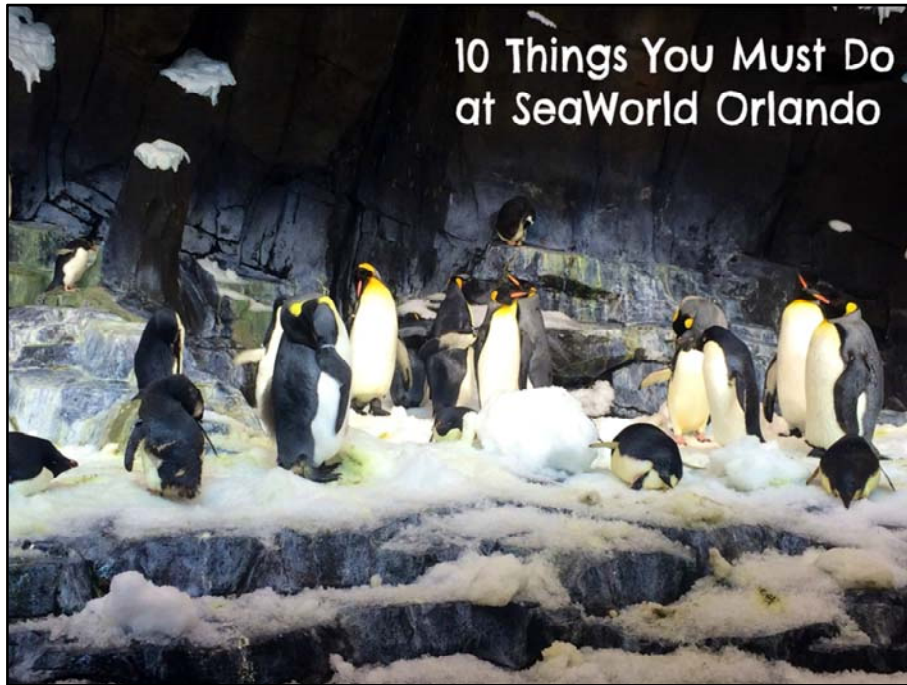
They are answering the difficult questions.



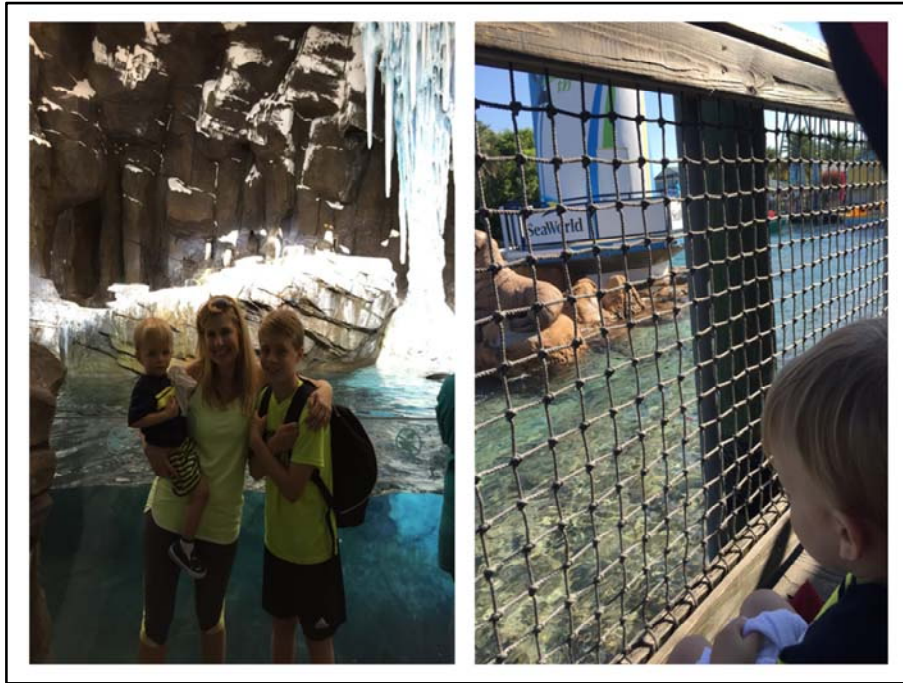
And they are highlighting decades of accomplishments in rescue and conservation. We think it is important to educate the consumer on SeaWorld's culture.

The company is now taking the right steps to present their side of the story.





At the same time, taking the attention off the Orcas and highlighting other attractions at its parks probably won't hurt.



Antarctica drove traffic back to the parks in 2013. The ride itself is not all that exciting but the exhibit is pretty amazing.

We were there in April and couldn't drag my two-year-old son, Lucca, out of the room despite the fact that it was 32 degrees and he was wearing shorts and a tee shirt.





We didn't get to meet Leon - Sea Lion High was not open yet during our visit - but we did manage to ride the Manta a few times.



This thing is awesome. But what makes it unique is SeaWorld's ability to combine a zoological experience with a fantastic ride.



This is what you are walking through while waiting in line. Super cool.



Next year, the company is launching Mako – Orlando's tallest and fastest coaster. Mako will be a massive attraction around the shark exhibit.

We think what they are doing is unique and contrasts with rides and experiences at Disney and Universal, which are looking more and more like each other.

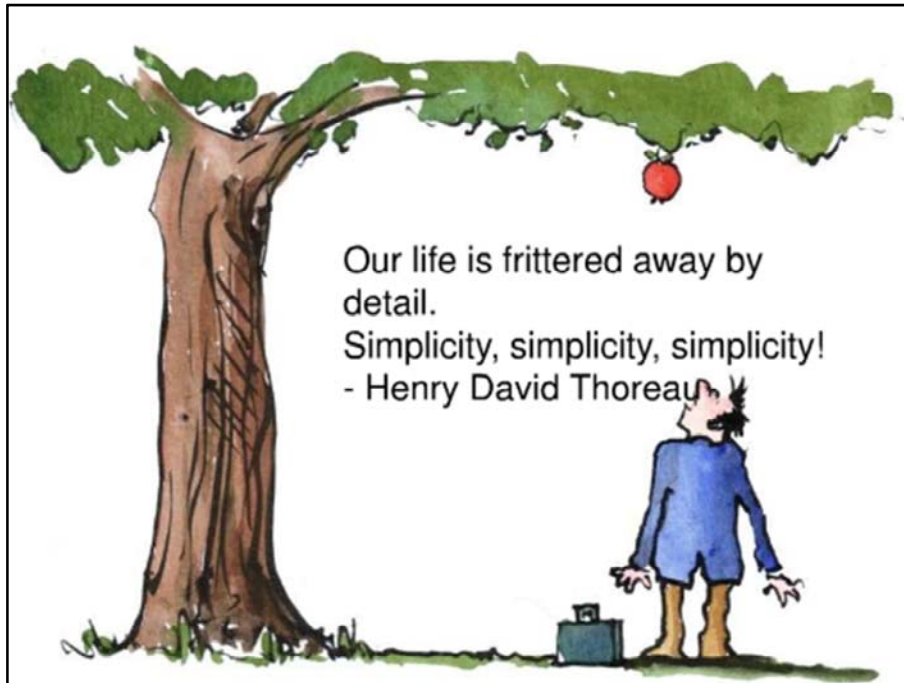


But the biggest development by far is construction of the Blue World Project which begins in San Diego next year.





The new facility is planned to have a total water volume of 10 million gallons and a surface area of nearly 1.5 acres, providing guests with the world's largest underwater viewing experience of killer whales.



Bottom Line: We think the company is taking the right steps to get people back in the parks. If we are correct, a good chunk of increased attendance should drop to the bottom line given high operating leverage and initiatives in place to reduce the company's cost structure.

We'll wrap up with over over-simplified valuation work on the stock.

## First Assumption: Attendance

How Many People Are In The Parks?



Revenues are driven by two factors. The first is how many people are in the parks. Attendance was north of 24 million in 2008-2009 and 2011-2012.

No reason we can't get back there.



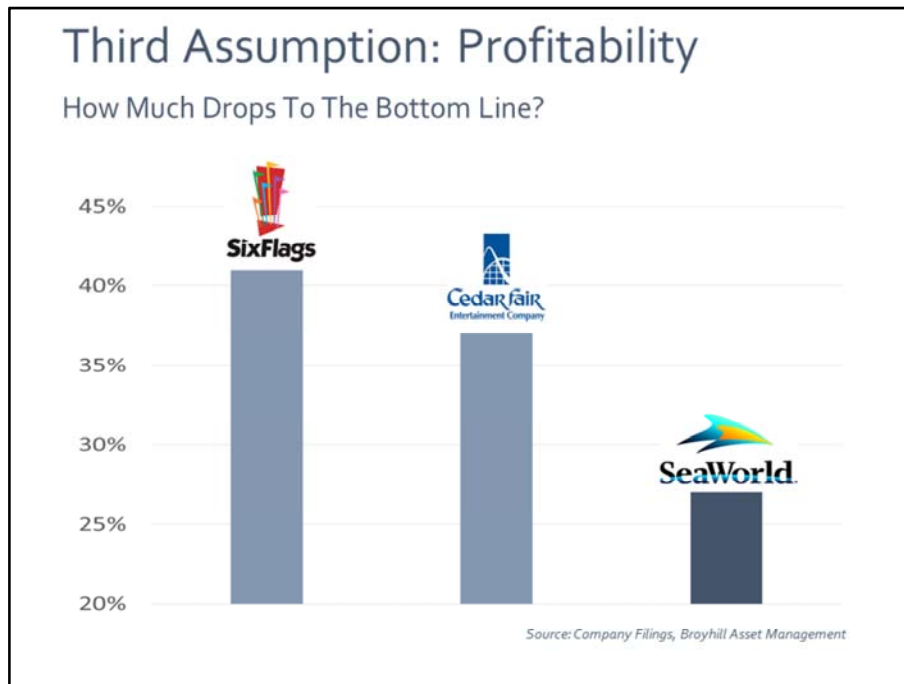
## Section Assumption: Spending

How Much Are People Spending Once They Are There?



Source: Company Filings, Broyhill Asset Management

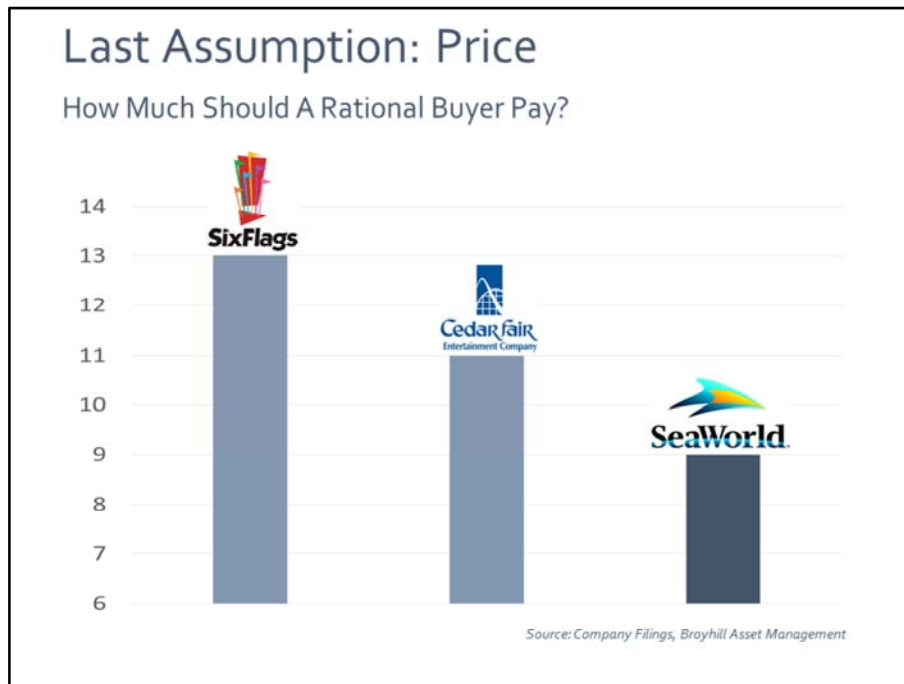
The second factor is spending at the parks. Beyond the next year or two, where management may be more aggressive on price to drive traffic, pricing should continue to rise over time. Putting these two together we should get back to \$1.5 billion in sales pretty easily.



Next, we need to make some assumptions about margins. We think last year is likely to mark a trough for the company. And despite these challenges, the company still generated \$350 million in EBITDA in 2014.

That puts margins at about 25% - more than ten points below the regional parks. Some of this gap is structural. It costs more to feed an orca than a rollercoaster. But we don't think it should cost ten points more.

We think Manby will close some of this gap. Assuming he gets us back to 30% would put EBITDA at \$450 million.



Mr. Market is currently valuing SEAS at a trough multiple on trough earnings. We think that's a mistake. SIX is trading at 13x EBITDA. FUN is at 11. SEAS traded at a premium to these guys at IPO. We are not implying it deserves a premium but we do think it's pretty short sighted to assume sentiment will remain this depressed.

And we think we have plenty of downside protection with the stock trading near levels where it was last taken out. The replacement cost on these assets is estimated at \$5 billion. Even if we cut that number in half, we have plenty of asset coverage. We think fair value is closer to \$30 just assuming a normalization in attendance with upside to \$40 over time.



Buffett likes good businesses with deep and defensible moats. No need to make it more complicated than that. We like moats too – particularly when they are defended by sharks and killer whales!



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