Speaker 4
0s

Welcome to the Netflix Q2 2025 earnings interview. I'm Spencer Wang, VP of Finance, IR, and Corporate Development. Joining me today are Co-CEOs Ted Sarandos and Greg Peters, and CFO Spence Neumann. As a reminder, we'll be making forward-looking statements, and actual results may vary. We'll take questions submitted by the analyst community, and we will begin with our results and our forecast. The first question comes from Steve Cahill of Wells Fargo. The question is, since the revenue increase in your forecast is primarily FX-driven, we're curious about the components of the constant currency increase. Is this due to a better underlying revenue growth, or are there specific expenses that are coming in better, like content amortization?

Speaker 3
50s

I will take that one. Thanks, Steve. As you saw in the letter, we increased our full-year revenue guidance to $44.8 billion-$45.2 billion. That's up from the prior guide of $43.5 billion-$44.5 billion, so up about $1 billion at the midpoint of the range and a tighter range. you noted, it primarily reflects the FX impact from the weakening dollar relative to most other currencies. The good news is we're also seeing strength in our underlying business. We've got healthy member growth, and that even picked up nicely at the end of Q2, a bit more than we expected. We think that'll carry through with our strong back half slate. We're reflecting that in our latest forecast. We're also seeing nice momentum in ad sales. Still off a pretty small base, but good growth, and it's on pace to roughly double our revenue in the year. It's a bit ahead of beginning-of-year expectations. When we carry all that through to operating margin, our operating expenses are essentially unchanged, which is part of your question. They're basically unchanged forecast to forecast. We're largely flowing through the expected higher revenues to profit margin. That's why our updated target full-year reported margin is up a point from 29% to 30%.

Speaker 3
2m 0s

That 50 basis point increase in FX-neutral margin is really just that revenue lift from stronger membership growth and ads relative to prior forecast flowing through to margin.

Speaker 4
2m 10s

Thank you, Spence. We'll take our next question from Barton Crockett of Rosenblatt Securities. Why is operating margin guidance for the full year only 30% after the upside in Q2 and a forecast of 31.5% for the third quarter? Is there a timing issue, FX issue, or is there a new level of spending that will continue beyond the fourth quarter of 2025?

Speaker 3
2m 38s

This is really mostly timing. Thanks, Barton. As a reminder, we primarily manage to full-year margins, and we expect our content expenses will ramp in Q3 and Q4. We've got many of our biggest new and returning titles and live events in the back half of the year. Q4 is typically and generally almost always a heavier film slate. I'm sure we'll talk about, I expect we'll talk about more of this on the call. We'll also be marketing to support that heavier slate. We're continuing to aggressively build out our ad sales infrastructure and capabilities through the year. All of that is to be expected. We can manage to it. We manage to those margins. Even with that back half ramp in expenses, we expect operating margins to be up year over year in each quarter, including Q4. As just noted, we expect to deliver strong full-year margins as we just took up our guide to 29.5% FX-neutral, 30% reported.

Speaker 4
3m 36s

Great. Thanks, Spence. The next question comes from Tom Champion of Piper Sandler. How has your view of the consumer and the macroeconomy changed over the last 90 days?

Speaker 1
3m 49s

Similar to last quarter, we're carefully watching consumer sentiment in the broader economy. At this point, there's really nothing significant to note in the metrics and the indicators that we get directly through the business. Those are retention that remains stable and industry-leading. There have been no significant shifts in plan mix or plan take rate. The price changes we've done since the last quarter have been in line with expectations. Engagement also remains healthy. Things all look stable from those indicators. Big picture, entertainment in general and Netflix specific have been historically pretty resilient in tougher economic times. We also think that we are at incredible entertainment value, not only compared to traditional entertainment, but if you think about other streaming competitors, when we start at $7.99 in the U.S. and you think about all the entertainment you get, we have a belief and expectation that the demand for not only entertainment, but for us specifically, will remain strong.

Speaker 4
4m 43s

Thanks, Greg. I think it's a nice follow-up to this question will be on advertising. So from Ben Swinburne of Morgan Stanley, can you share any data points around your upfront negotiations?

Speaker 1
4m 57s

Yep. As we noted in the letter, our U.S. upfront, it's nearly complete. We've closed the large majority of deals with the major agencies. Those results have generally been in line or slightly better than our targets and consistent with our goal to roughly double the ads business this year. What are advertisers excited about? Growing scale is something we definitely hear. Also, a highly attentive and engaged audience. Bigger audience, but also an audience that's more engaged relative to our peers. The rollout of our own ad tech stack, which helps deliver a bunch of features. Our slate is generally amazing and includes a growing number of live events that advertisers are excited about.

Speaker 4
5m 37s

Great. Follow-up question on advertising from Vikram of Baird. How have advertisers in the U.S. responded to the Netflix ad suite rollout since the April launch? What features and capabilities are attracting the most interest? How is the initial feedback in other regions outside of the U.S.?

Speaker 1
5m 59s

We've completed the rollout of our own ad tech stack and the Netflix ad suite to all of our ad markets now. We are fully on our own stack around the world at this point. That rollout was generally smooth across all countries. We see good performance metrics across all countries, and the early results are in line with our expectations. Now we are in this phase of learning and improving quickly based on the fact that being live everywhere means that you get a bunch of feedback about what we can do better, which is great. As we mentioned before, the most immediate benefit from this rollout is just making it easier for advertisers to buy on Netflix. We hear that benefit, that ease from direct feedback, talking to advertisers. They tell us that it is easier. We see it in our overall sales performance. We've seen an increased programmatic buying. All of these are consistent with what we are expecting both qualitatively and from a metrics perspective. We're also, I guess, worth noting that we're going to roll out additional demand sources like Yahoo! That'll further open up the market for us. Long-term, being on our own stack, that improves the speed of our execution to deliver this pretty significant roadmap of features that we have in front of us.

Speaker 1
7m 7s

It's things like improved targeting and measurement. There's also leveraging advertiser and third-party data sources, which we definitely hear demand for as well. It will ultimately allow us to improve the ad experience for our members, which is critically important. That means better ads personalization. The ads that I see are increasingly different from the ads that, let's say, Ted would see. They're more relevant for each of us, which is good for us as users, and it's good for the brands. We're also going to be introducing interactivity in the second half of the year. That's exciting. This is a pretty significant milestone for us, one we're super excited to get behind us because now we can shift into this steady release cycle where we're dropping new features all the time, both for advertisers and for members. That's the development and release model that we have in other parts of the business. It's fun to be able to get to that point.

Speaker 4
7m 56s

Thanks, Greg. I'll move us along now to a set of questions around content as well as engagement. This one comes from Ben Swinburne of Morgan Stanley. 1% engagement growth year over year suggests engagement is down year over year on an average per-member basis. How do we reconcile that with engagement growing on a per-member household basis, if that's still accurate?

Speaker 1
8m 21s

Total view hours did grow a bit in the first half of 2025, and that's despite a particularly back half-weighted slate. To your point on engagement on a per-member basis, we've mostly been focused for the last few years on measuring engagement on what we call an owner household basis. This takes out the borrower effect. We obviously think this is the best way to assess our engagement per member because it removes the tricky comparison impacts from paid sharing. That metric, per-owner household engagement, has been relatively steady over the past two and a half years throughout the rollout of paid sharing and amidst increasing competition for TV time as more viewing moves to streaming and gets this on-demand benefit. We're glad to have held that normalized engagement level, but we clearly also want to increase it. To that end, we're optimistic and expect that our engagement growth in the second half of this year will be better than in the first half given our strong second-half slate.

Speaker 4
9m 22s

Thanks, Greg. Great segue to Doug Neumann's question from JP Morgan. The content in the back half of the year looks strong with Squid Game 3 already the third most popular non-English series ever and Wednesday and Stranger Things releasing in the coming months. You often say that no single title drives more than 1% of total viewing. How do you think about the business currently as being "hit-boosted" or "hit-driven"? Are you confident that both original and licensed content momentum can continue in 2026?

Speaker 2
9m 57s

Yeah, I'll take that. Thank you, Doug. On the first part of your question, we're definitely riding this long-term trend of linear to streaming, and that has a natural adoption curve. We can accelerate our growth with big hits. As you said, each one of them, even in success, is going to drive about 1% of total viewing. You need a lot more than just a big hit every once in a while. To your point, it's not about the single hit. What it is, is about a steady drumbeat of shows and films and soon-enough games that our members really love and continue to expect from us. By way of example, we had 44 individual shows nominated for Emmys this year. That's what quality at scale looks like. We ended the quarter with a huge return to Squid Game. Thanks for acknowledging. Go into the second half with the return of Wednesday and Stranger Things and a really strong slate of supporting titles and favorites and new shows. Like next week, we've got this week we've got Eric Bana's Untamed. Next week, we have Leigh-Anne's new comedy show, Leigh-Anne. Both look really great. And that's just to name a few.

Speaker 2
11m 0s

The back half of the year also has perhaps the most anticipated slate of new movies that we've ever had. That starts on the 25th with Happy Gilmore 2, followed by a new Knives Out film. We have new films from Noah Baumbach, from Guillermo del Toro, from Catherine Bigelow. It does not stop there. It does roll right into 2026. That's the second part of your question. We're looking forward to movies like The Rip from Ben Affleck and Matt Damon, Shirley Starr on a new movie called Apex, which is a phenomenal action movie. Millie Bobby Brown is back in Enola Holmes 3. Recall that in 2023, Enola Holmes 2 was our biggest movie. We're looking forward to that new sequel. Greta Gerwig's Narnia is going to be phenomenal. On top of that, we talk about return of Bridgerton, One Piece, Avatar: The Last Airbender, all three huge successes around the world. The Gentlemen, Four Seasons, Point Break, I'm sorry, Running Point, sorry, Beef, which, as you recall, in 2023, won just about every award imaginable and was a gigantic success for us. It's back for a new season in 2026. Three Body Problem, Love Is Blind, Outer Banks, and not just from the U.S., from France, we have Lupin, from Spain, we have Berlin.

Speaker 2
12m 21s

We have a new season of A Hundred Years of Solitude from Colombia. Big hit returning shows and new series from each of our regions around the world. The new stuff we've got coming up, like Man on Fire, reimagining of Little House on the Prairie. The Duffer Brothers from Stranger Things have a brand new show, The Burrows. We've got Human Vapor from Japan, Operation Saffron Cigar from India, Kendis Love Bee Translated from Korea. Again, popular programming new and returning from all over the world in 2026. Unscripted shows like the reboot of Star Search. We've got Into the Doll Universe with Wonka's Golden Ticket, which we're really excited about. In our live, we've got a few surprises for you next year. Of course, we have our NFL Christmas Day doubleheader that we're really thrilled about too. We're really incredibly excited about the back half of this year and confident that it keeps rolling in 2026.

Speaker 4
13m 17s

Thank you, Ted. We'll take the next question from Rich Greenfield of Lightshed Partners, who asks, "Are you concerned by the stagnation in your viewing share domestically?" I think Rich is probably referring to the Nielsen Gauge data. Do you need to spend more on programming or spend differently to materially move your viewing share higher?

Speaker 2
13m 38s

Yeah, thanks, Rich. Look, our goal continues to be to continue to grow our share over the long term. Over the past few years, you're right, we've been able to maintain our share even as we've worked through a growing number of TV-based streaming services, some free, some paid. The impact of paid sharing that Greg mentioned earlier, as well as this 2025 slate that was more back half-weighted than we typically have in previous years. Over the long term, we tend to keep growing as the other 50% of TV viewing migrates from linear to streaming. We'll do that by doing what we've always done, continuously improve the service. Keep in mind, since 2020, our content amortization has grown more than 50%, from under $11 billion to more than $16 billion that we expect to do this year. Over that same time period, we definitely saw increased spending, but also increased engagement, increased revenue, increased profit, and increased profit margin. That is our model in action. It is our objective to sustain healthy revenue growth, reinvest in the business to improve on all aspects of the service. That includes growing content spend, strengthening and expanding the entertainment offering, and to drive that positive flywheel of growth by adding value to our members and all the while growing engagement, revenue, and profit around the world.

Speaker 4
15m 7s

Great. Thank you, Ted. I'll move to Alan Gould from Loop Capital next. Can you provide more information on the TF1 partnership? Why did you choose to add TF1 in France as opposed to other broadcasters as your first partner? Why is now the right time to create such a partnership? Should we anticipate similar partnerships in other countries?

Speaker 1
15m 34s

Yeah, perhaps just start with the rationale for the partnership. You would think with that long list of amazing titles that Ted just rattled off, we would have enough to satisfy every person on the planet. It turns out we actually consistently hear from our members that they want more. They want more variety, more breadth of content. The fundamental purpose for this TF1 partnership is all about that goal of expanding our entertainment offering. How do we enhance the value we deliver to members? We want to provide more content, more variety, more quality. Just as you've seen us do with licensing and production, this is just another mechanism to expand that offering. In this case, it's specifically about highly relevant local-for-local content in a country that has strong demand for that local content. This is an accelerated way to satisfy that need. Why now? Why was this time the right time? We have invested a lot in a bunch of enabling capabilities that are either required or highly leveraged by this deal. You can think live, ads, the new UI, among other things. Why TF1 versus some other partner? We know each other really well. We wanted our first partner to be in a big territory.

Speaker 1
16m 44s

We wanted to pick the leading local programmer. We wanted to be highly aligned in terms of the deal and the shape of the partnership and the values that we thought we could generate mutually by working together for our customers. We both look at this as an opportunity to learn, to figure out how do we scale the local content that TF1 is producing to more customers in France. We are looking forward to seeing what consumers think. You never really know until you get out there and get the real reactions. Obviously, we'll factor that into our plans going forward.

Speaker 4
17m 17s

Thanks, Greg. From Robert Fishman of MoffettNathanson, with reports suggesting Apple is now in the driver's seat for F1 rights. Haha, pun intended, I guess. Plus UFC and MLB still looking for new deals, and the NFL may be looking to come to market a year earlier. Can you share updated thoughts on how you are approaching sports rights for Netflix and where you draw the line on something that can move the needle?

Speaker 2
17m 47s

Thanks for that, Robert. Remember, sports are a subcomponent of our live strategy. Our live strategy goes beyond sports alone. Our live strategy and our sports strategy are unchanged. We remain focused on ownable, big breakthrough events because our audiences really love them. Anything we chase in the event space or in the sports space has got to make economic sense as well. We bring a lot to the table, and the deals that we make have to reflect that. Live is a relatively small part of the total content spend. We have about 200 billion view hours. It is a pretty small part of view hours as well right now. That being said, not all view hours are equal. What we have seen with live has outsized positive impacts around conversation, around acquisition, and we suspect around retention. Right now, we're very excited where we sit. We're very excited with the existing strategy. We're excited about the Canelo Crawford fight in September and the SAG Awards and our weekly WWE matches. The NFL, of course, is a great property. We're happy to have the Christmas Day doubleheader, which includes Dallas versus Washington and Detroit versus Minnesota. Today, our live events have all primarily been in the U.S., keep in mind.

Speaker 2
19m 4s

Over time, we're going to continue to invest and grow our live capabilities for events around the world in the years ahead. We're excited, but the strategy is unchanged.

Speaker 4
19m 14s

Thanks, Ted. Good follow-up question on that one from Steve Cahill of Wells Fargo. What investments have you made to increase your capabilities in producing live events? What have you been able to do in-house in 2025 that you couldn't do last year? How long will it take before you have the capability to produce large-scale events like NFL games?

Speaker 2
19m 36s

Yeah, thanks, Steve. I'd say, remember, when we started original scripted programming, we had zero production capability. House of Cards was, in fact, thinking about our first three years of original programming, all of those shows were produced by others. You have to go three years later, we've produced Stranger Things in-house. Today, we still have shows that are produced by others. Universal, 20th Television, which is Disney, Paramount, Lionsgate, Warner Television. There's lots of available infrastructure to produce TV. That is true of live events and sports as well. When we do more and more, we may choose to bring some of that in-house. We've already produced a few. We're just as likely to continue to use partners with existing production infrastructure and work to make sure that those productions are bespoke and they feel like they could only be on Netflix. You shouldn't think about the mix of partnerships and self-producing as a, we think about it as a scaling tool, not backfilling some lack of ability in some area of the company. I should note, by example, CBS is a phenomenal partner producing the NFL games with us. We're thrilled to work with them again this year on Christmas Day.

Speaker 1
20m 53s

Maybe take this opportunity just to make some commentary on the general capability we've been building with live. When we start something new, we pretty much expect that we're not going to be brilliant at it at the beginning.

Speaker 4
21m 6s

What?

Speaker 1
21m 7s

Yeah, that's true, unfortunately. We don't have any real reason to believe that. We don't let that stop us from kicking off initiatives that we believe have a strong strategic rationale, even though we know we need to develop that capability. Of course, our job is to get out there and learn by doing and get world-class as quickly as we possibly can. If you look at our current capabilities around live, we are in just a completely different place today compared to when we first started. As a good example that just happened last Friday, we had our first concurrent pair of live events. We had Taylor versus Serrano globally delivered alongside WWE SmackDown, which was delivered ex-U.S., both events at scale and delivered with extremely high quality. It's great progress we've seen. We've got a great roadmap of features ahead of us to continue to enhance those experiences for folks.

Speaker 4
21m 55s

Thank you both. Last question on the content side or the topic of content comes from Ben Swinburne of Morgan Stanley. What are the learnings from the success of K-pop Demon Hunters? More animated musicals with fictional bands, perhaps?

Speaker 2
22m 11s

Man, that is a question from a man who probably has that movie playing on repeat in their home, if I'm guessing correctly. K-pop Demon Hunters is a phenomenal success out of the gate. One of the things that I'm really proud of the team over is original animation, not sequel, not live-action remake. Original animation feature is very tough and has been struggling for years. I think the fact that our biggest hits now, Leo, Sea Beast, and now K-pop Demon Hunters are original animation. We are super thrilled about that. The mix of music and pop culture, getting it right matters. The storytelling matters. The innovation in animation itself matters. The fact that people are in love with this film and in love with the music from this film, that'll keep it going for a long time. We are really thrilled. The next beat is, where does it go from here? We put in the letter just how successful the music has been and continues to be. We think that'll drive fandom for this fictional K-pop bands that we have, but more importantly, for the song Golden and for the song Soda Pop. These are enormous hits. They all come from a film that's available only on Netflix.

Speaker 2
23m 23s

We are really excited that we can pierce the culture with original animated features, considering that folks have been poking us on it.

Speaker 4
23m 33s

Let's do it again later in the year with In Your Dreams, right, Ted?

Speaker 2
23m 36s

Absolutely. In Your Dreams is another very funny one and also completely original.

Speaker 4
23m 39s

Yep. Great. I'll move us on now to a few questions on plans as well as product. From Michael Morris of Guggenheim, he asks, Netflix continues to broaden content genres, notably with live sports and the recently announced TF1 partnership. Is there a path to additional tiers of service based on types of content available, or will Netflix always make all content available at the ad-free/ad-supported price points?

Speaker 1
24m 9s

I've learned to never say never. I would say we remain open to evolving our consumer-facing model. I think we've got a few important principles that we're carrying with us that I don't see changing significantly. One is we want to provide members choice, right? How do we have a different set of plans, a different price point, different features that allows folks to opt into what is the right Netflix for them? Also, how do we provide good accessibility to new members around the world? We want to grow. That means making sure that we've got accessible price points. Finally, the plans we offer have to ensure that we're having reasonable returns to the business based on the entertainment value that we delivered. We're hoping to grow those, and those returns would grow as well. Obviously, the reason to do that is we can continue to reinvest in adding more entertainment and building a better experience. Maybe one other thought, too, is there is a component of complexity and choice stacks that we have to consider in how we think about our offering is structured. Having said all that, though, I think we believe that the bundle is a great value for members.

Speaker 1
25m 11s

It allows members around the world to access a wide range of entertainment in a very easy way at a very reasonable price. I would expect that that will remain an important feature of our offering for the foreseeable future.A

Speaker 4
25m 22s

lot of value and simplicity, huh?

Speaker 1
25m 24s

Yeah.

Speaker 4
25m 25s

Great. From Rich Greenfield of Lightshed Partners, help us understand why your new UI/UX is so important as you expand live content. Beyond live, can you provide some color on what metrics have improved since the launch of the new UI, such as speed of users finding a title and change in failed sessions?

Speaker 1
25m 47s

Yeah, as we said previously, it's really hard for a new UI to immediately compete, be better than the UI that we've had for the past 10 years that's been iteratively evolved and improved. Now that we've actually rolled out this new UI to the first large wave of TV devices, we're actually seeing performance that's better than what we saw in our pre-launch testing. To some degree, that's expected because we made some improvements based on the results of that testing phase. It's exciting to see that those delivered actual better results. The rate of that change actually gives us increased confidence that this new experience will drive better performance by the variety of metrics we look at, some of which include the ones that Rich is mentioning in relatively short order. Maybe just a point on why did we build this and launch this new experience in the first place? Why was this so important? Bluntly, the previous experience was designed for the Netflix of 10 years ago. The business has evolved considerably since then. We got a wider breadth of entertainment options. We got TV and film, more of those, of course, from around the world, but now also games and live events.

Speaker 1
26m 57s

If you think about the discovery experience that's best suited for these new content types, it's inherently different. Helping our members understand that there's a really good reason for them to launch Netflix and tune in at 7:00 P.M. on a Friday night versus just showing up whenever they were free and wanted to be entertained, that's a totally different job. We really need a different user interface to do that job well. Add to that, we saw the opportunity to leverage newer technologies like real-time recommendations that respond dynamically to what you need from us in that specific moment. The Netflix you get on a Tuesday night is different from the Netflix you get on a Sunday afternoon. Put all of those rationales together and what we're seeing in terms of the performance so far, we're very confident that we've got a much better platform in this new user experience to build from, to continue to improve. That'll help us meet the needs of the business over the years to come.

Speaker 4
27m 51s

Thanks, Greg. The next question comes from Steve Cahill of Wells Fargo. YouTube is the only streamer that exceeds Netflix in terms of U.S. share of TV time. Do you see an opportunity to bring notable YouTube creators and their content exclusively to Netflix? How big could this opportunity be?

Speaker 2
28m 12s

Thanks, Steve. Look, we want to be in business with the best creatives on the planet, regardless of where they come from. Some of them are here in Hollywood. Others are in Korea. Some are in India. And some are creators that distribute only on social media platforms. Most of them have not yet been discovered. For those creators doing great work, we have phenomenal distribution, desirable monetization, brilliant discovery in our UI, and a hungry audience waiting to be entertained. Steve, I think I listened to you on a podcast where you talked about our business model and I believe on this very topic. We largely agree with you and believe that working with a wide set of content creators makes a lot of sense for us. As you said, if I'm remembering it right, not everything on YouTube will fit on Netflix. We couldn't agree with that more. There are some creators on YouTube like Miss Rachel that are a great fit. If you saw on the engagement report, she said 53 million views in the first half of 2025 on Netflix. She clearly works on Netflix. We're really excited about the Sidemen and Pop the Balloon, and a wide variety of creators and video podcasters that might be a good fit for us, particularly if they're doing great work and looking for different ways to connect with audiences.

Speaker 1
29m 28s

Maybe broadening this out for a second and taking that question to look at sort of all of the competitors that we face for our share of TV time. We've always said that the market for entertainment is very large. We face competition from all kinds of directions. Whether it's linear or streamers or video games or social media, it's also a very dynamic competitive market as we and all of our competitors seek to provide better and better options for consumers. One of those changes, one of those vectors of dynamicism has been that sort of steady, inevitable shift to streaming and on-demand as more services move to deliver their content in a way that we all know consumers want. That creates increasing competitive pressure for us that we've got to respond to. We also see free services as a form of strong competition. Free is very powerful from a consumer perspective. It is not surprising that some free services are growing in engagement. I think Ted said it well earlier in the call, not all hours are created equal. We have a different profit model from other services, a strong profit model. We are going to compete to win more moments of truth for sure, but especially compete to win those most profitable moments.

Speaker 1
30m 44s

Back to your specific question, it is worth remembering there is about 80% of total TV view share that neither Netflix nor YouTube are winning right now. We think that represents a huge opportunity for which we are competing aggressively. We aim to grow our share.

Speaker 4
30m 59s

vast majority of our money and attention is focused on that 80%. Thank you. Next question from Justin Patterson of KeyBank. Could you please talk about your generative AI initiatives? Where do you think Gen AI will be most impactful over time, revenue or expense efficiency?

Speaker 2
31m 21s

Let me start with Gen AI. We remain convinced that AI represents an incredible opportunity to help creators make films and series better, not just cheaper. There are these AI-powered creator tools. This is real people doing real work with better tools. Our creators are already seeing the benefits in production through pre-visualization and shot planning work, and certainly visual effects. It used to be that only big budget projects would have access to advanced visual effects like de-aging. Remember last quarter, we talked about Pedro Páramo. That is just no longer the case. This year, we had El La Tonata, a very big hit show for us from Argentina. In that production, we leveraged virtual production and AI-powered VFX. There was a shot in the show that the creators wanted to show a building collapsing in Buenos Aires. Our Eyeline team partnered with their creative team using AI-powered tools. They were able to achieve an amazing result with remarkable speed. In fact, that VFX sequence was completed 10 times faster than it could have been completed with traditional VFX tools and workflows. Also, the cost of it just would not have been feasible for a show on that budget. That sequence actually is the very first Gen AI final footage to appear on screen in a Netflix original series or film.

Speaker 2
32m 52s

The creators were thrilled with the result. We were thrilled with the result. More importantly, the audience was thrilled with the result. I think these tools are helping creators expand the possibilities of storytelling on screen. That is endlessly exciting.

Speaker 1
33m 8s

Maybe to cover a few of the other areas, the member experience is a place where we feel like there's tons of opportunity to leverage these new generative technologies to improve the experience. We've been in the personalization and recommendation business for two decades. Yet, we see a tremendous room and opportunity to make it even better by leveraging some of the more newer generative techniques. We're also rolling out, have piloted right now a conversational experience that allows our members to basically have a sort of natural language discussion with our user interface saying, "I want to watch a film from the '80s that's a dark psychological thriller." Get some results back. Maybe iterate through those in a way that you just couldn't have done in our previous experiences. That's super exciting. We see that all of the work that we do there essentially is a force multiplier to that large content investment that we're making. If we do a better job there, that means every dollar that we spend means more value back to our members by connecting them with the titles that they're truly going to love. Advertising is another really great area. We've seen it's a high hurdle to create a brand-forward spot in a creative universe of one of the titles that we're currently carrying.

Speaker 1
34m 23s

It is very compelling for both watchers and for those brands. We think these generative techniques can decrease that hurdle iteratively over time and enable us to do that in more and more spots. There's a bunch of places where we think we've got an advantage in terms of data and scale where we can leverage these new generative techniques to deliver just more benefits for our members and for our creative community.

Speaker 4
34m 45s

Yeah. If you do not mind me coming back for one second, I just rolled off Eyeline as if everyone knows what Eyeline is. I probably should clarify that Eyeline is our production innovation group inside of our VFX house at Scanline. They are doing a lot of this work with our creators. I just realized that I just threw that out there as if everyone knew.

Speaker 2
35m 3s

Thanks for clarifying, Ted. Let's see. Our next question comes from Brian Pitts of BMO Capital Markets. With your evolving gaming ambitions, including partnerships with Grand Theft Auto and the recently announced Roblox agreement, can you talk to near-term monetization opportunities within gaming?

Speaker 1
35m 22s

Sure. We look at the near-term monetization opportunity with games very similar to how we've looked at other new content categories. You can think of unscripted or film or on and on. That's essentially, if we deliver more value in our offering, we get increased user acquisition. We get increased retention. We get increased willingness to pay. It drives all of the sort core fundamentals of our business. We've seen those positive effects, albeit in a small way relative to the size of our overall business when it comes to members playing games on the service. We already have those positive proof points. We're going to ramp our investment in this area, which is currently quite small compared to our overall content investment, as we ramp the size of those positive effects. We want to remain disciplined in not investing too far ahead of demonstrating that we know how to translate that investment into value for our members. We've seen good progress, as you note, with licensed games like GTA. We've seen good progress with games we developed like Squid Game Unleashed. You will see more from us in both of those categories, as well as a whole new set of interactive experiences that we think that we are either in a unique or differential position to deliver.

Speaker 1
36m 35s

We are super excited to roll those out over the next year. We remain open to the core question. We remain open to evolving our monetization model. We have got to get to a lot more scale before that becomes a really materially relevant question. We are going to do that work first. It is probably worth restating, the TAM for this market is very, very large. We remain convicted about our strategic opportunity and excited to make more progress.

Speaker 4
37m 1s

Thanks, Greg. We'll take our last question from Jessica Reef Ehrlich of Bank of America Securities. Given your healthy balance sheet and what appears to be a coming wave of M&A in media globally, are there certain types of assets that would strengthen your moat, i.e., what is your view of owning successful IP or studio assets as they come to market?

Speaker 2
37m 25s

I'll take that one, Spencer. Thanks, Jessica. We agree continued consolidation of studio and network assets is likely. At least with respect to consolidation within legacy media, we do not think it materially changes the competitive landscape. As you also know, we have historically been more builders than buyers. We continue to see big runway for growth without fundamentally changing that playbook. You heard a lot of that today. We look at a lot of things. We apply a framework or a lens to those opportunities when we look. It is, is it a big opportunity? Does it strengthen our entertainment offering? Does it strengthen our capabilities? Does it accelerate our strategy? We look at all of that relative to the opportunity cost of distraction or other alternatives. We have been pretty clear in the past that we also have no interest in owning legacy media networks. That also kind of reduces the funnel for us. In general, we believe we can and will be choosy. We've got a great business. We're predominantly focused on growing that organically, investing aggressively and responsibly into that growth, and returning excess cash to shareholders through share purchase. I think you'll see us continue on that path.

Speaker 4
38m 40s

Great. Thanks, Spence. That will wrap up our Q2 earnings call. We thank you all for taking the time to join us. We look forward to seeing you all next quarter. Thank you.