NETFLIX

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1. Introduction to Netflix:

Video streaming services are becoming the heart of mainstream media. Everyone is moving towards more flexible entertainment experiences. Netflix, hulu, and Amazon prime are the pioneer of the mainstream media industry. According to Nielsen, in 2017, About 59 percent of the households have at least one subscription to these video streaming services. Netflix is the biggest contributor to forgo traditional cable network and it is crushing its competition by simply providing better quality and original content at economical price.

Netflix is leading provider of Video-on-Demand internet entertainment service with over 117 million members in over more than 180 countries. Netflix has 140 million hours of streaming media which includes Netflix's original series, documentaries and feature films. Netflix has attracted more than 23 million subscribers in United States and Canada with high definition video streaming. It is alone accounting for 29.7% of the peak downstream traffic in United States.

Netflix was founded by Reed Hastings and Marc Randolph in August 1997, when Hastings discovered an overdue rental copy of 'Apollo 13' in his closet. After paying his late fee, he began to ponder upon diverse ways and ideas to provide a home movie rental service with more satisfied customers. That led to Netflix's birth and began as selling and renting DVDs as video-on-demand services through Netflix's website and now it is a leading subscription provider for online movies and tv shows.

2. Introduction to Video-on-Demand:

Not long ago, “watching TV” meant sitting in front of the screen in your living room, waiting for a favorite program to come on at a set time. Today, the growth of video-on-demand (VOD) programming options where viewers can download or stream content from either a traditional TV package or an online source is creating extensive opportunities for consumers who have greater control than ever before over what they watch, when they watch and how they watch.

VOD was viewed as the marriage of pay per view programming combined with the internet downloading of entertainment, including movies and TV shows. Television VOD systems can stream content through either a set-top box, a computer or other device, allowing viewing in real time, or download it to a device such as a computer, digital video recorder (also called a personal video recorder) or portable media player for viewing at any time.

Netflix has started the development of VOD since the company’s inception. They have sorted the internet video into three groups.

1. Advertising-supported videos.
2. Digital file ownership.
3. Online video rental and pay TV.

Online Video at Netflix:

As Netflix was about to deliver online video to its customers, there were few challenges ahead of them.

1. The lack of customer base for online viewing feature.

2. Technology improvement required to deliver online content.

There were several alternatives thought to counter these challenges. They are:

1. Carrying out-licensing agreement through which the company would offer its proprietary recommendation system to cable providers seeking to enhance VOD offering.
2. Integrating online video streaming feature into their core offering.
3. Building stand-alone online video business system

Due to Netflix brand name and customer awareness, they have acquired the distinct advantage over many newer entrants.

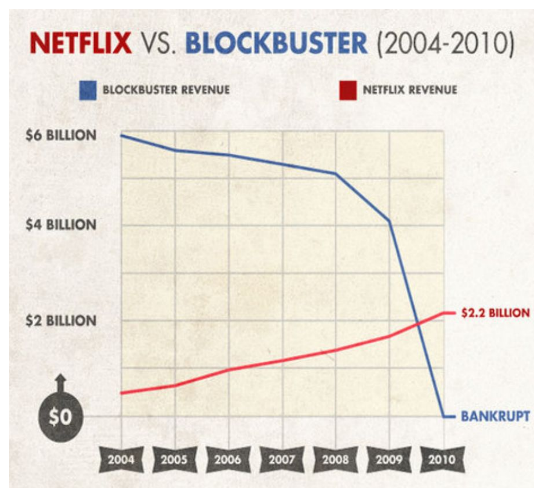
<u>3. Traditional Movie Rental Overview (companies, business model):</u>

Once upon a time, people used to rent DVDs and even VHS’s from brick-and-mortar video stores such as Blockbuster and Hollywood Video. These brick-and-mortar video stores offered a large selection of newly released and older movies available for customers to rent for a certain period of time. If the movies were returned after the initial period of time, they would incur a late fee.
Blockbuster opened in 1985 and, for the first 15 years or so of its operation, seemed to be a no-brainer choice for customers to rent movies from instead of purchasing movies at full price. Although the internet existed at the conception of Blockbuster and similar brick-and-mortar video stores, bandwidth and and streaming capabilities were not developed enough to be able to stream movies online.

As streaming capabilities increased, VHS's became extinct, and the idea of leaving one's home in order to acquire a movie that they would then watch at home began to become counterintuitive, companies such as Netflix began to capitalize on this opportunity. Netflix realized the unmet demand of sending customers' DVDs by mail, rather than having the customers come to them.

Had Blockbuster been able to stay ahead of its competition and offer a similar service to Netflix earlier in the game, perhaps they would be in better shape today than they are. It wasn't until Netflix had already been operating for six years that Blockbuster began to implement a similar movie-by-mail service. Instead of accepting defeat and making use of the company's remaining profits, the company "failed to fail", if you will. Blockbuster attempted to stay in business and, in return, went down on their sinking ship.

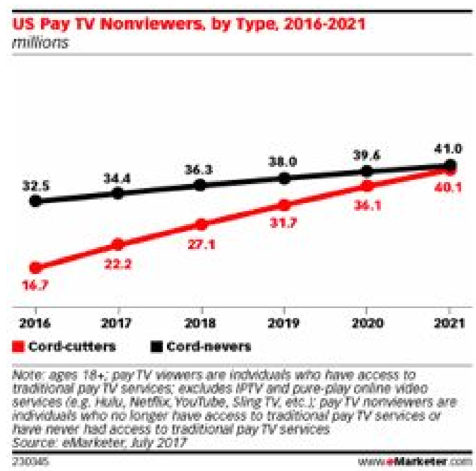
The CEO of Netflix, Reed Hastings, actually confronted Blockbuster in 2000 to propose a partnership where Netflix would manage all of Blockbuster's online brand and Blockbuster's physical stores would help to promote Netflix. As we all know now, Blockbuster clearly denied this deal, leading to Blockbuster going bankrupt in 2010 and Netflix now being a $28 billion company for capitalizing on this untapped market that was clearly so high in demand.



<u>4. Future Opportunities and Threats:</u>

Netflix's expansion into the video-on-demand market dynamically changes the direction of the company moving forward. As proven by Blockbuster's decline as the leader of video rental services, consumers are turning away from traditional brick and mortar stores and opting for VOD services. Through the introduction of an online video service, the company will present itself as a beacon for those who have chosen to leave the traditional forms behind.

Moving forward, Netflix will have the opportunity to further connect to the ever-growing market base of consumers who have turned their back on cable television and other conventional services. These individuals, given the term "cord-cutters", are expected to continue to significantly rise to an estimated 40.1 million in 2021. Furthermore, these statistics don't include "cord-nevers", individuals who have no prior connection to traditional media services and whose number is expected to match that of cord-cutters by 2021. Additionally, the majority of these consumers are younger millennials who will inherit most of the buying power in their respected economies.



Netflix also holds the opportunity to lead the industry in globalizing their video streaming services. Although it introduces higher upfront costs, developing greater customized content for new markets will further distinguish the company from its competitors. By introducing content developed specifically for the targeted culture or nation, Netflix will place themselves outright as the premier service in markets where competitors may not exist. This would allow them to gain market share quickly and hold the necessary image to retain it.

Proceeding into the future, Netflix will also have to face several emerging challenges in the market. As prior competitors, such as Amazon, continue to expand and new platforms, such as SlingTV, enter into the market, Netflix will have to find new ways to retain their current subscribers. Moreover, as production studios and cable companies create their own video streaming services, Netflix may lose rights to films in their library in addition to subscribers who prefer the new platforms. These potential losses in subscribers can be mitigated through the continuing development of proprietary content within Netflix's own studios and continuing the relationships formed with major producers like Disney.

5. CASE DISCUSSION QUESTIONS:

1. **Would you have been long or short Blockbuster stock at the time of the case? How about Netflix? Why?**

- At the time of the case, we would have been short on Blockbuster stock because of the expected decline in their consumer base. In contrast, we would have been long on Netflix. This is due to the fact that in 2007 Blockbuster was still a relatively powerful company within the movie rental market with a stock price that had not yet reflected the changing culture. Netflix, on the other hand, was at the forefront of this shift in technology and investing early would allow us to profit as the market adapted.

2. **Did Netflix do the same jobs for consumers that Blockbuster did? How did this evolve over time?**

- Netflix initially offered a completely new service to consumers than Blockbuster did. At the time of Netflix’s conception, Blockbuster solely offered video rentals through Brick and Mortar stores. After Netflix began its initiative to mail consumers DVDs, Blockbuster attempted to follow suit and offer a video mailing service as well. By the time Netflix rolled out it’s online video streaming service, Blockbuster was too far behind to keep up with their competition. Netflix was able to identify a changing demand of customers and stay ahead o f the competition.

3. **Compare Blockbuster's and Netflix's profit models. How might the differences affect the respective company's strategies?**

- For Netflix, the best part of Netflix’s profit model is customer rating and recommendation system. That enabled customers to find better movies and for Netflix, enabled to rent out their old movies which were cheap compare to new and expensive movies. This system played a significant role in Netflix’s profit model as Netflix had more old movies compared to the new ones. With the partnership of studios, they could provide lesser known movies at cheaper price that led to more customer satisfaction and attracted new customers.

- For Blockbuster, the key part of profit model was “late fee”. In 2004, these fees represented over 600 million for Blockbuster, which was 10% of its revenue. However, Netflix changed it model from “late fee” to “all you can watch”. That led to more satisfied subscribers.

4. **As you examine each major shift in Netflix's strategy, what might have been an assumptions checklist that they might have used at each stage? What assumptions checklist might you use for VOD?**

- Assumptions checklist that Netflix might have used at each stage:
    1. Using Internet to renting DVDs
    2. Being more consumer oriented
    3. Removing late fee and introducing monthly rental program which could be easily canceled
    4. Providing personalized recommendations of movie
    5. Opening more distribution center to deliver movies over night
- Video-on-Demand:
    1. Providing movies to customers without going out.
    2. Removing extra charges for consumers

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