Content, Cars, and Comparisons in the "Streaming Wars" — MatthewBall.vc

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33-42 minutes

If offered the opportunity to invest in one of the following two series, which would you pick?

- **Series 1:** $100MM series consisting of ten hour-long episodes set in a sci-fi universe
- **Series 2:** $100MM series consisting of ten hour-long episodes focused on a pair of lovestruck Portlanders

The risk and return profiles of each of these two series is pretty self-evident. Option two is too expensive, faces a lower ceiling, and has minimal potential for IP generation and ancillary monetization.

Let's take it further and say there were two flavors of the clear winner:

- **Series 1A:** A *Star Wars* spinoff
- **Series 1B:** A brand new space opera concept

Again, easy.

There are more elements one could add, too. What if I said we had two options for making 1A. The first is based on an idea from [not going to name names, but you can guess], while the second comes from Kevin Feige, the head of Marvel Studios. Another option: this show's development and production process could be managed by a team of former HBO execs or those of [not going to name names].

Putting aside how these choices are affected by IP rights or whether they obligate the content to, say, Disney+ or HBO, it's clear which of these series is likely to (1) build the largest audience; (2) have the greatest cultural impact; (3) be more highly valued by audiences; (4) generate the most rewatching; (5) generate the highest licensing fees, and so on. This is because we know all the "things" behind content — IP, talent, experience, development processes and so forth — are both highly variable and consequential. To believe otherwise is to argue against any form of creative execution, or at least to say that everyone has the same batting average.

At the same time, common analysis and accounting standards alike would treat every show above — and every permutation therein — as the same. Equivalent. Substitutable. Predictable. Like comparing the Dodge Ram 2500 to a Ford F250. Or the fleets of Hertz versus Avis with no consideration of utilization rates.

Consider, for example, the most common narrative of the "Streaming Wars": the enormity of spending. Nearly every "Streaming Wars" report, essay, or brief includes columnar charts designed to answer the who "spends the most" question — often several times! There are not just comparisons of total content spend but also sub-views focused just on total domestic spend or total spending excluding live sports, or excluding theatrically released films, or excluding live sports and feature films and international content, and so on.

It does make sense to focus on content spend. After all, this is not just the largest expense for an SVOD service, it's the core of what a consumer is "buying" from these services. But today's methodologies are deeply flawed, violate their own logic, and confuse rather than clarify.

Columnar content spending charts, by definition, treat content as a commodity. But if content is the core driver of the Streaming Wars, then it's also the front line of competition and, by definition, execution has to matter and all efforts can't be equal. The accounting standards designed to adjudicate the specific financial value of content investments are even worse. Return on content investments will obviously be affected by how "good" a service's content is, how routinely a service makes "good" content, and longer their "good" content remains popular. And thus, the decision to apply the same *standard* to all services means being generous to some and punitive to others.

It's not new that the media industry is based on hard-to-value art. However, the challenges of content valuation and comparisons are much greater in the OTT video era. In addition, the importance of and upside from hit content has increased considerably as we've moved from an industry bundle to standalone direct-to-consumer services. Sorting through these issues in detail might seem dry, but it's critical to understanding what both Hollywood and New Hollywood hope to achieve in the decade to come. But in short: content spend in the streaming era needs to be handicapped/adjusted for the ability of a network to create hits, as well as the rate at which this content "converts" into a library with durable value. As a result, the gap between the biggest and smallest spenders is tighter than the topline numbers suggest.

2 Hard 2 Value

There are three overarching challenges to content valuations and comparisons in the "Streaming Wars".

Value Signals

Historically, when a given network (e.g. NBC) would develop a show, there would be clear signals on its value, success and break-even. For example, a linearly scheduled network knew exactly (1) how many viewers it would need for a given timeslot, such as 8–9PM on a Wednesday, to generate a profit; (2) the specific market price of the ads bought against that airing; (3) how competitors performed in that same timeslot (including rough profit estimates); (4) how a replacement show might perform; and (5) how to optimize the investments through budgetary changes, new time slots, etc. In other words, a network always knew both the literal P&L and intangible "opportunity cost" of every program and programming decision. Third parties didn't have this same clarity, but there was still a substantial amount of data available and analysis possible.

SVOD services, however, don't have nor give off any of these signals. They rarely sell their content to third parties and never need to redetermine the market value of their library in order to compensate talent at a later date or pay royalties. Furthermore, there are no timeslots in SVOD and thus no finite capacity. Netflix and Hulu don't need to focus on having the 20 "most profitable" shows as possible. Instead, the goal is to continuously, but economically, grow per user engagement with more content. Added engagement, in turn, drives retention, pricing power, and so on.

According to *The Information* and *Reuters*, the above means that SVOD services judge the performance of any given content investment using only internal benchmarks and they base most of these measures on opaque attribution calculations. Examples here include "cost per viewing hour" for overall efficiency, or "cost per new subscriber" when considering how a title grew the overall subscriber base. This means content disappoints only by underperforming internal goals and averages. There is no bomb or failure, per se, nor even an opportunity cost (50% of things, after all, must be below median). This obviously makes external analysis even harder - but it also means that a service doesn't really know if it's optimized, either (let alone how it compares to peers).

This model produces unique oddities, too. Unlike in traditional TV or film, an SVOD service can't really "lose money" on its content investments, nor does wasteful/inefficient spending directly reduce profitability. Write-downs on content investments, for example, only happen in extreme cases. The last time Netflix publicly wrote down its content investments was in January 2018, when it recognized a $39MM charge after scrapping a film, comedy special, and half a season of *House of Cards* after the titles' leads were credibly accused of sexual misconduct.

The 2018 Netflix series *Seven Seconds* was originally intended to be a multi-season show but was ultimately cancelled before the first season premiered, rebranded a "limited series," and barely marketed. Although the show must have fallen well short of Netflix's pre-launch expectations, it was not written off. In fact, it was by third parties (e.g. analysts and the press) as standard "content spend", and amortized in the same fashion as *Stranger Things* S1. Keep in mind, too, that because *Stranger Things* S1 spawned subsequent seasons, the first continued to grow and receive significant rewatches.

In the event of substantial reshoots (e.g. *The Morning Show*, which essentially doubled its budget), new spend is counted and financially capitalized atop prior investment. Thus Apple's need to spend more money to correct mistakes means that on an accounting basis, its underlying content becomes *more* than was *originally planned*, and in the eyes of the press, Apple has become an even scarier spending giant. Amazon reportedly paid an enormous sum for the rights to make five seasons of a series based in the Lord of the Rings universe. Even if these are incredibly unpopular, fall short of internal expectations, and hit below-service averages for cost per hour watched, this spend is unlikely written down unless one or more seasons go unmade.

Compare any of the above examples to traditional media models. Not only does content have relatively black and white P&Ls, but there's a direct connection between the size of a miss and the size of a loss.

Kingmaker Hits

Making matters harder is the fact that the benefits of hit content have grown enormously in the digital era.

In the traditional TV era, the relationship between the popularity of a show and its economic value was relatively linear. If CBS' 8–9PM show reached 5MM homes instead of 4MM, it would generate roughly 20% more ad revenue. It would also help with carriage, but the effects here were pretty diffuse on a per show basis. Network distribution deals with the likes of Comcast or DirecTV, for example, ran several years and were for the entire network, not for a given show in a given timeslot for a brief period of time. A popular show would also help promote some other shows as well as increase the ratings for the show right before and after it. But overall, the total impact of incremental viewership for a single show was modest in the context of the network's yearly P&L. Even for hit shows.

In the SVOD era, the returns to success have become exponential not just exaggerated. A "homerun" like *Game of* Thrones or *The Mandalorian* isn't linearly more valuable than a hit; it can mean the difference between having and not having a subscriber in the first place — and thus the difference between generating revenue or not generating revenue. In addition, having a tentpole will lift a services' entire portfolio (e.g. if show X leads you to open service Y, you end up watching more of service Y). No one gets hooked on content on a service they don't watch or subscribe to in the first place. This means that tentpole content doesn't just drive acquisition revenue, it drives the efficiency (and fans) of all other content investments as well.

It's important, too, to broaden the definition of a hit or even a tentpole beyond pure audience size (the classic definition). What SVOD services need is behavior-changing titles. In the time of "Peak TV", with some 600+ new original scripted series airing annual and on-demand access to thousands more, everyone has heard of shows they "must watch" or would "love". If that doesn't drive them to seek out and subscribe to a service, or actually watch the show on a service they already have, these endorsements and awareness don't matter much.

Similarly, content that's watched but does not meaningfully affect future behavior is essentially "bought" engagement. It's generally understood that retaining subscribers requires a certain volume of engagement relative to a price — say, 20 hours per month for a $10 subscription. Driving additional viewing hours helps ensure that an active customer (i.e. someone who already "bought" this month) will make the decision to keep their service for the next month. But ideally, a service wants to get out of the treadmill-like process of having to fight for x hours per month every month lest a consumer churn.

The best way to do this is through a recurring cadence of intensely valued, must-have content. Shows like *Star Trek: Picard*, *Game of Thrones*, or *The Mandalorian*, for example, are so important that they alone can deliver one-to-two month subscriptions for millions of customers even if nothing else is

watched. And if a service can assemble enough of these series, a year-long subscription is possible. Disney, for example, is targeting two Marvel Cinematic Universe and one Star Wars TV series per year. This doesn't mean that no other programming is necessary or valuable. But in this case, their engagement drives pricing power.

Of course, IP alone isn't critical. The quality (and reliability) of execution matters too. The Marvel Cinematic Universe turned also-ran characters into the biggest video franchise in history. And not only has it lasted longer and done better than expected, but it broke the axis on what was believed to be possible. When it launched its "Phase 1" slate, the MCU released 1.2 films per year. In "Phase Three", the MCU released three films per year and grossed close to 50% more per year. 2021 will see the MCU move to four films per year plus two series. Conversely, the DC Extended Universe struggled to achieve half of the early MCU's results and sputtered after only a few entries. But note that this comparative analysis is possible specifically because this content existed in theaters, not SVOD. As a result, we both know how these two franchises performed.

The Importance of Stock

Perhaps more important than the ability for a hit show to drive a subscriber addition or raise overall viewing is the idea of library accumulation. This again is uniquely important versus historically precedent.

Traditionally, a television network was in a process of constant regeneration. Every year, it would optimize for a finite number of linear "slots" (e.g. 8–9PM Wednesdays) by cancelling many of its current shows and replacing them with new ones. Thus, after enough time passed, its entire slate — the core of what a network like CBS "sold" to customers — would be different. The popularity of the shows CBS had in years prior still helped, but only in the sense that these shows helped finance and launch the new ones. Indeed, CBS would rarely even re-air these shows after a year and, in most cases, didn't own them in the first place. Instead, they were "rented". This meant a network's programming spend was essentially all an operating expense; content investments never accrued, nor did old content investments generate ongoing revenue.

SVOD could work this way. Netflix and Amazon could rent their exclusives and licenses for a year or two then continually refresh them to keep their service feeling new. However, this strategy makes little sense. Traditional TV networks only "rented" content because they had finite programming time (e.g. 48 half-hour slots per day) and could only air one thing at a time. Their goal, therefore, was to maximize potential viewership in each of these slots. This meant the biggest networks would focus on airing new or recently new high-budget shows, rather than reruns with lesser appeal. Accordingly, it rarely made sense to "buy" long-term rights, when they could instead rent them short term. And after these airings, smaller, less profitable networks would then "rent" these rights as hand-me-downs, and smaller, less profitable networks (or time slots) would "rent" them even later on. This rotation process represented the efficient allocation of content: as it became less valuable, it went to less valuable networks targeting less valuable viewing.

But an SVOD service can offer all of its content to all of its consumers all of the time. There is no finite capacity, no limits to when a consumer can watch what, and everything can be aired at the same time (so to speak). This means that an SVOD service can go after all consumers, all viewing time, and all content, always — and that "rotating content" down to other services means giving away consumers and viewing time, too.

Accordingly, each of the major SVOD services is now focused on investing in content that it can own exclusively and in perpetuity, rather than renting or rotating it. In aggregate, these services hope to amass an enormous library of already-paid-for content that would not just help rebuff competition but would also allow for margin expansion even if prices stayed flat and the amount of content offered to consumers continued to grow.

Consider, for example, Netflix's 2012 content spend of $2B. This meant that in 2012, consumers could access roughly $2B in content (at 2012 prices) and no more. In those days, 100% of this spend was a license from third parties, meaning all of this content had to be "repurchased" in 2013 or it would go away. Thus, if Netflix spent an incremental $2.5B in 2013, the incremental content available to consumers grew only $500MM, not $2.5B.

In 2019, Netflix will spend around $15B in content, about 60% of which will stay on the service indefinitely as they are owned, self-produced originals. This means that in 2020, Netflix consumers will not just have $18B in 2020 content spend, but they will also have access to the $8.5B or so of content produced in 2019. In fact, they get more than $15B when one includes almost all the Netflix originals

owned to date (such as *Stranger Things*). In other words, Netflix's total content offering is growing at several times the rate of its actual content spend.

This library accumulation also helps defend against "free" (i.e. bundled at no incremental cost) and lower cost competitors. If Netflix is outspending Amazon by $5B a year, it'll have an incremental $25B in content after five years. Compared to Apple, Netflix will have $60B more content in 2025. Sure, the perceived value of content may be depressed by ecosystem subscription giveaways, but access to the world's largest ever library of content for $15 a month is still a lot of value irrespective of whether one can cobble together some equivalent portion for free via Amazon Prime and by buying an iPhone.

Summarizing the Spend

The truth about content spend in the streaming era is it needs to be handicapped or adjusted for the ability to create hits as well as the rate at which this content "converts" into a library with durable value.

Consider, for example, the bizarre criticism that Disney's $1–2B original content budget is insufficient in today's Streaming Wars. This $1–2B is arguably several times more impactful per dollar than $1–2B that would be spent by Netflix, Amazon, or Hulu. Disney+'s *The Mandalorian,* for example, is one of the most expensive shows ever made, but it has created more value than almost any other show ever, too. It will also be rewatched more and over a longer period. The value of *The Mandalorian* (which cost $104MM) is probably as impactful a half dozen (or more) series from Amazon, Showtime, or Starz.

HBO is another interesting question. Its $1.5B in original programming is modest compared to Netflix's $10B. But HBO's spend generates perennial Emmy nominations, dominates IMDb traffic, and *seems* to have an enormous cultural influence. It may spend 85% less than Netflix, but the comparative impact feels much tighter. Consider, for example, that HBO and Netflix have held comparable shares of Emmy nominations (though HBO dominates in wins) for years, even though HBO produces far fewer shows. Furthermore, Netflix's original content spend has more than doubled over the past five years while nominations have shrunk. It will also be proven below that HBO's success with award bodies hasn't come at the cost of mainstream popularity. It's also intuitive that the library value of HBO's slates is enormously greater than those of long-time peers Showtime and Starz. But is it?

To analyze this, I want to use data from Parrot Analytics (a portfolio company). Parrot tracks the popularity of TV content by capturing "Demand Expressions" from 2B+ online users each day, with signals spanning search engines, social media chatter, fan and critic sites, social video views, piracy downloads, streaming traffic, downloads, and even traffic to Wikipedia and microblogging sites, all on a per title, per country basis. All signals are then weighted based on their correlation with intention (e.g. a Facebook page is worth far less than a digital rental or full stream) and summarized as a proprietary metric, "Demand Expression". Parrot's data is widely reported on and used by companies such as Amazon, Sky, and Disney. And while this data cannot be perfect, it gives a clear sense of how in-demand content from each service is, rather than just how many viewers it collects. This is, of course, distinct from the philosophical idea of "quality", which, as with all art, isn't calculable.

Launching New Original Series

All of the major "premium networks" substantially outperform the market average for in-demand content. This isn't a surprise given their added focus on quality, higher production values, and greater spend on talent. However, HBO's new series are on average twice as in-demand as those of Netflix and Amazon, and 40% greater than its typically defined peers, Showtime and Starz.

This is an enormous differential — especially in a town where, as the saying goes, "nobody knows anything". In addition, this differential adds up over time. The gap between 2.7x and 1.3x might be launching one more truly great show, for example. Over four years, this means having one more new tentpole season every quarter, and 10 extra library seasons overall.

The size of this differential is also a testament to the aforementioned role of creative expertise and execution. HBO has an infamously slow and deliberate development process (often losing projects as a result) and is incredibly selective. In recent years, HBO has produced and passed on pilots such as *The Corrections* (based on the Jonathan Franzen novel and starring Maggie Gyllenhaal, Ewan McGregor, Chris Cooper, and Greta Gerwig), as well as one of its *Game of Thrones* prequels (it's impossible to imagine another network passing on even a mediocre spinoff to one of the three biggest shows of the decade). In addition, the company's B2B brand means it's the "preferred network" to many of the most talented creators (a result of talent friendly deals, a strong working relationships, etc). This makes it easier for HBO to acquire the "best projects" in a competitive situation. The company's reputation for quality results in greater baseline demand/sampling from audiences, too.

Conversely, all of the streamers had to build their businesses from scratch. They had untested teams, no pre-existing talent or content pipelines, and no reputation. In addition, they often had little choice but to pick up shows other networks first passed over, or even un-cancel shows dropped by the traditional ecosystem. Accordingly, it's no surprise that the first seasons of new entrants Amazon and Netflix underperform, even though budgets are much higher.

Notably, though, this means that the average performance of these newer networks should increase over time. And to point, Amazon once underperformed even the average television network (a group that included the premium networks above, plus TBS, TruTV, Fox, AMC, etc.), but in 2019, it beat every network except HBO and Starz. Still, there remains a hugely consequential gap between HBO and long-in-operation Showtime and Starz. In addition, a single year of near parity is just a single year; success is demonstrated by the ability to reliably outperform.

Growing and Sustaining Old Original Series

However, the sustainability of a service depends not just on the popularity of its shows at launch, but also the durability and/or growth of viewership afterwards. This, too, can vary widely. *Friends* was the most watched show of 2000–2001, while *CSI* was the most watched show of 2001–2002. But 20 years later, *Friends* is still one of the most popular shows in the United States, while few watch or speak about *CSI*. In addition, Netflix has often spoken about how its recommendation algorithms help to build audiences over time. As a result, it's no longer necessary for a show to pop upon its initial release, let alone its premiere date. To this end, the streamer often points to how it multiplied the fan bases for series such as *Breaking Bad* and *You*.

True to Netflix's claims, its original shows (1) are the most likely to grow year-over-year; (2) will see the greatest growth when they grow; (3) and when they decline, they will tend to decline the least.

However, year-to-year change is an amplifier. On average, Netflix's series were the least demanded to begin with. As such, they need *far* greater growth to meet the performance of competing services, and the same *rate* of growth doesn't mean the same overall growth. To use a simple example, a 10% increase to 50 adds then a 6% increase in 100. To match HBO, Netflix would need 100% of its slate to double in demand, rather than see 30% grow 90%.

And here, it's important to reiterate that the value of hits grows non-linearly. A good way to think about this is through college GPAs: the difference between a 3.3 and 3.4 is much less significant and easier than moving from a 3.8 to a 3.9. On balance, Netflix has weak grades. Semester-to-semester improvements help, but the average remains low.

Cumulative Slates

Ultimately, analysis needs to return to the in-market reality of the Streaming Wars and "Peak TV", where networks didn't just have better and bigger shows, but they also had more of them. This last point is the final addition to programming an overall offering: there's the ability to launch a great show, the ability to grow or sustain it, and then the question of how many you make in the first place. The better a network does at each, the more an overall slate can 'average' up over time. And all SVODS, by definition, sell slates and services – not individual shows or hours of entertainment.

According to Parrot, Netflix released 16 "Outstanding or Better" seasons of TV in 2019 (this means "Demand Expressions" were >8x that of the average series, equivalent to the top 2.5% of all releases). This was more than any other video service. However, this is largely a result of the streamer's enormous output. Only 12% of Netflix's 135 2019 total releases qualified as "Outstanding or Better", while 55% (or 74) were average or below.

HBO released 14 "Outstanding or Better" seasons of television in 2019, two fewer than Netflix. However, it released 30 series compared to Netflix's 135. To this end, nearly 1 in 2 of HBO's releases were "Outstanding or Better" and only 20% were average or less. The difference in pound-for-pound punching power of these two networks is extraordinary.

Overall, HBO's 2019 series were more than 7x more in-demand than those of the average TV network (including History, ABC, Fox, History, etc.), or 12x when including *Game of Thrones*. This compares to 4.0x for Apple TV+ and Netflix, 5.6 for Amazon, Showtime, and Hulu, 5.8 for CBS, and 6.8 for Starz. And remember that in SVOD, the relationship between demand and value is non-linear; a show 8x more in-demand than the average is likely to be worth well more than 8x the average show. This matters beyond a single year (i.e. 2019), too. Over time, these titles aggregate into a library that every service hopes will drive future engagement at no additional cost.

This doesn't mean the goal of every series is to be a tentpole blockbuster. Many series are produced with far modest intentions and a lower viewership ceiling. But the goal of programming is to draw in, delight, and retain audiences. This means producing in-demand and valued content. That can be a show many people want, or one a few want very deeply. (Note, too, that HBO leads in both Emmys and demand.)

And in aggregate, a network needs its offering to be relatively more in-demand than its competitors, while also achieving the volume of shows necessary to support an ongoing subscription. Netflix does this quite effectively through its incredibly high output — and benefits from accounting treatment that doesn't penalize them for failure.

But as the Streaming Wars mature and the land-grab stage of competition ends, its profits will depend on the ability to efficiently produce enduring content. In addition, its competitors — namely HBO Max and Hulu — are substantially growing their output, too, and they are arguing their batting averages will be much higher. Netflix faces two other related challenges here. It has now lost several historical suppliers of original content (e.g. WarnerMedia, 21st Century Fox, Disney and, for the most part, NBCUniversal). In addition, it needs to build its library of "stock" much faster than its Old Media competitors, each of which inherits large ones. That said, it's also fair to argue that HBO Max will not be able to sustain HBO's averages and will also endanger the network's attractiveness to creative talent and its brand equity with audiences.

Taking a step back, the success of *The Mandalorian* is also instructive. The title was one of only four "Exceptional" releases in 2019, beating 99.75% of other 2019 series. Demand for the title (which cost roughly $100MM) was equivalent to the combined demand for all 11 of Apple TV+'s 2019 original series (which cost at least $1B) and nearly half of Netflix's 135+ new seasons. Most of these series were never intended to achieve tentpole popularity, but the aggregate cost is orders above that of *The Mandalorian*. In addition, most believe that Disney can reliably produce at least a few of these series per year. 2020, for example, is expected to include a second season of *The Mandalorian*, as well as two series based in the Marvel Cinematic Universe and starring its film franchise leads. The cost here will be up to $400MM, but it will probably by several times the demand generated by the slates of Showtime, Apple TV+, and Starz.

Obviously, *The Mandalorian* benefited from the fact it was based on globally popular IP in a genre that has a particularly high ceiling (per the start of this essay). However, it also reiterates the point that while IP is an asset, execution is paramount. The show was 43x more demanded than the average series in 2019, while Netflix's 2019 Marvel series *The Punisher* and *Jessica Jones* averaged 9x and 8x, while Hulu's Marvel Runaways achieved only 9x. (These series weren't made by Netflix or Hulu but by Marvel Television, which is distinct from Marvel Studios, maker of the MCU movies and forthcoming Disney+ MCU series. In 2019, it was shut down and folded into Marvel Studios.)

Starz' *Power* is another interesting example. Although the show receives limited press coverage, it's routinely one of the most watched series in cable. And it's even more in-demand, per Parrot Analytics. This is a reflection of both creative execution and the upside from focusing on specific, underserved segments (e.g. black Americans). Power's outsized success has also led to the creation of a franchise, too. Four spinoffs are reportedly in development.

Knowing When and Why A Rose Isn't A Rose

There are many drivers of success in the SVOD era: the quality of content, the volumes of it, a service's monetization model, and its overall scale. Each of these elements interact and must be considered together.

For example, Apple and Amazon invest in original content to differentiate their platforms. As a result, titles with limited demand, distinctiveness, or notability probably don't drive Prime renewals or iPhone purchases — and thus value — even if they're relatively well watched. In this sense, it might make sense not just to assess average demand for Apple and Amazon's slates as compared to TV overall and/or Netflix, but to do so while assigning zero value to titles that aren't meaningfully above average.

Netflix, meanwhile, is selling bulk entertainment to audiences (most estimates suggest the average account watches 60 hours per month). Of course, Netflix still benefits from increases in average demand and popularity, but even little watched and/or barely enjoyed shows would drive some value, in contrast to the tech platforms. At the same time, these sorts of titles serve as little more than "OpEx" — they help keep current customers today but don't convert to library value or drive future/recurring viewership. And a greater share of Netflix's content spend is "OpEx" than any other network (though again, amortization rules are basically standardized across all players).

This is an important balance to the Netflix scale argument. Because content licenses are set by the market, rather than sold on a per subscriber basis, Netflix pays the same for a license like *Seinfeld* or *Big New Sci-Fi Epic A* as services such as HBO or Hulu, which have half as many subscribers. This means that the per subscriber cost of these licenses are much lower, and, in turn, it's much easier for Netflix to achieve break-even viewership than its competitors. Similarly, Netflix's larger customer base means that, on average, it will see greater viewership for its "B+" titles than others will with even their "A-grade" series. These are powerful advantages. (Put another way, would *The Witcher* have been as big if it were on CBS All Access? Would *Tiger King* become a cultural sensation on a network other than Netflix?)

On the other hand, Netflix is also investing far less efficiently than HBO (perhaps 4x worse), and short most of the rest of the market as well. The ability to drive viewership is distinct from the ability to produce long-term asset value. In addition, *Seinfeld*, like *Friends* and *The Office,* is a license. Being able to economically outspend competitors for the best licenses is an advantage, but such spending will forever be OpEx and never convert to library.

There are two common and important rejoiners here. First: Netflix's scale-related investment (or "break-even viewership") advantage is further bolstered by its international subscriber base. This is true, though international ARPU is also 28% lower. In addition, its competitors are also growing their foreign operations. HBO has been buying back its foreign networks for years, such as HBO Asia., and launching in those it hadn't already reached. Hulu plans to go mostly global in 2021, while Comcast now owns Sky (the leader in the UK and a dominant player in Italy and Germany). Showtime and CBS All Access are now available in select markets outside the US, while Starz is in 50+. In addition, Netflix's US-centric competitors still generate revenue/returns outside their operating markets by selling their content. HBO, for example, generates close to $1B per year in foreign sales (mostly to Sky). And these licenses are all pure profit.

Second: The aforementioned programming analysis is all US-centric. In most foreign markets, Netflix's content offering is *substantially* better than its American library because it includes many of the titles produced by its US competitors. *Better Call Saul*, *American Crime Story*, and *The Last Da*nce are all Netflix Originals in Europe, for example. This international argument is also true and important as it helps finance Netflix's domestic investments, too, and brings additional programming to American audiences (e.g. *Dark*, *Casa De Papel*). However, this pipeline is also winnowing as its US competitors move abroad. In addition, these are still licenses that never convert to library or produce asset value. Netflix must keep buying them each year or otherwise replace them.

The good news here is that Netflix is rapidly securing much of Hollywood's most talented writers, stars, and directors — from Ryan Murphy to Shonda Rhimes, Martin Scorsese, Kenya Baris, David Benioff, and D.B. Weiss. This means its hit rate should continue to grow. But if all it took was spending more on top talent, the video business would just be about who spends more. Hopefully, after the past 5,600 words, it's clear that it's not.

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