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Video Streaming

February 9, 2024

Communication Services Sector

Industry Rating **Market Weight**

Investment Thesis

Streaming services have experienced continued subscriber growth during the past year, but Netflix remains the only streaming service to ever earn a profit[15]. The industry is headed toward consolidation and a "rebundling" of offerings, akin to the cable bundle. Smaller companies ditching or merging their streaming services with other content providers will ease the burden on consumers and make the industry more functional. For that reason, we recommend a **Market Weight** rating for the Video Streaming industry over the next year.

Drivers of Thesis

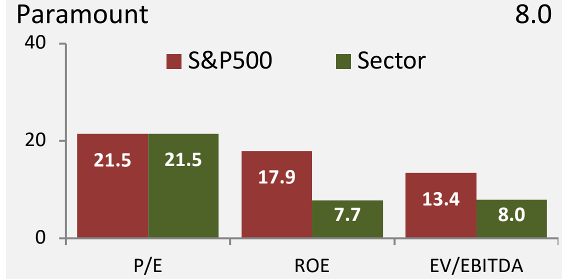
- The video streaming industry is maturing and likely headed towards a more stable business model through M&A and rebundling.
- Streaming video advertising revenue is projected to grow by 77% from 2023 levels by 2029[4], after a shift in industry philosophy back towards embracing ads.
- Gaming and experiences present a promising revenue stream for companies who plan to implement them as a support to their streaming services.

Risks to Thesis

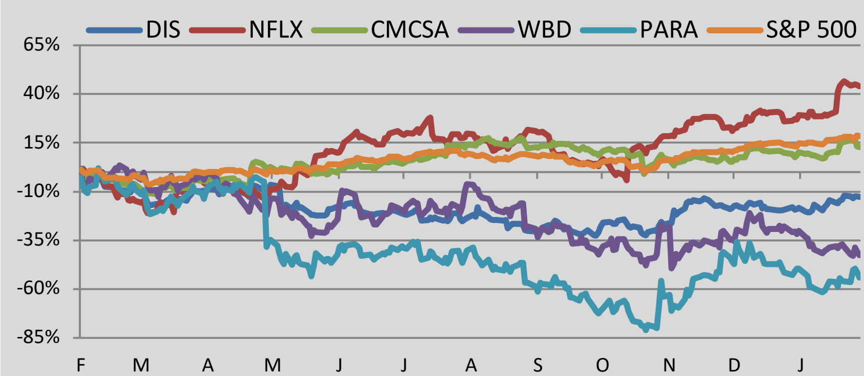
- A potential recession would take consumer spending away from non-essential goods such as streaming services, causing a much harder environment for growth.
- Companies continue to muddle through with individual services and do not work towards a more consumer friendly solution.
- The costs of live sports rights and original content continue to rise, causing firms with traditional linear assets and studios to slow the growth of their streaming services.

Industry Statistics (via FactSet)

Market Cap	(In $ Billions)
Apple	2,873.6
Google	1,776.8
Amazon	1,775.5
Netflix	244.4
Comcast	179.1
Walt Disney Company	178.2
Warner Bros Discovery	24.5
Paramount	9.1
P/E (TTM)	
Apple	27.9
Google	24.1
Amazon	52.4
Netflix	40.5
Walt Disney Company	63.1
Comcast	11.8
Warner Bros Discovery	-
Paramount	10.5
EV/EBITDA	
Apple	21.7
Google	16.9
Amazon	19.1
Netflix	10.3
Comcast	7.2
Walt Disney Company	14.1
Warner Bros Discovery	15.1
Paramount	8.0



12 Month Performance[1]



Industry Description

Video Streaming is a sub-industry of the communications sector and is rapidly changing how costumers consume media and entertainment. There are a handful of companies that make up the industry, including traditional broadcasters, legacy Hollywood studios, and major tech companies. The streaming industry is currently at a crossroads after initial developments created a clear hierarchy.

INDUSTRY OVERVIEW

As streaming has cannibalized linear TV and cable the past decade and a half, the way media companies operate has shifted rapidly to adjust to the new technology. The business model for content companies shifted from the cable bundle to paying a la carte for streaming services, such as Netflix. The cable bundle was a great source of income for companies with linear TV assets such as Disney and Paramount. These companies were able to dine off affiliate fees for years. They would air live sports, a hit show or two, and then air reruns and inexpensive content. Because there were no other platforms to turn to, if you wanted to watch ESPN or Nickelodeon, you had to have the cable bundle. If you had no interest in sports, you still had to pay for ESPN because it was part of the cable bundle. This created an incredibly profitable business for traditional media companies.

In 2007, Netflix pivoted from physical media and disrupted the entire entertainment and media business by becoming the first video-on-demand streaming company. This disruption set off 17 years of deteriorating cable, and companies responded by creating streaming services of their own.

Today, the market has around eight to ten major players. They vary from legacy Hollywood studios that have crumbling linear assets such as Disney and Warner Bros. Discovery, to tech companies such as Apple and Amazon that entered the industry as an advertising front for their core businesses.

Firm	Market Cap ($B)	FY23 Revenue ($B)	FY23 Net Income ($B)
Apple	2,873.6	383.3	97.0
Google	1,776.8	307.2	73.8
Amazon	1,775.5	574.8	30.4
Netflix	244.4	33.7	5.4
Comcast	179.1	121.6	15.4
Disney	178.2	88.5	2.4
Warner Bros.	24.5	41.3	-3.1
Paramount	9.1	29.7	-1.3

Source: FactSet

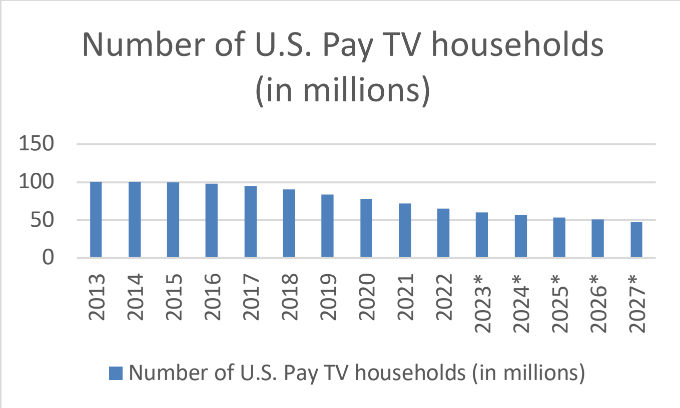
As the streaming model has matured, there have been multiple developments in the past year or two that have shifted progress. Prices of services have gotten more expensive, making it less appealing to pay for many individual platforms. The largest issue plaguing the industry is an over-saturated market with too many services and no centralized tech for consumers to use. Momentum in the industry is headed back toward a model like cable, where you can get all your options in one stop.

As of now, the industry is flawed and needs M&A activity and strategic partnerships to become fully functional. Profit margins in streaming are much lower than linear TV's were in its peak. The main issues are high costs of content and customer acquisition. New streamers in the space have faced high levels of customer churn which hurts their bottom line and ability to build customer loyalty. We are bullish on the potential of large tech companies who have dipped into streaming (Apple, Amazon, Google) to serve the entire industry as a shop for streaming content and services. 17 years after Netflix disrupted the media and entertainment business, they remain the only company to earn a profit on its streaming service. This makes the sector ripe for change.

PRODUCT LINES

Streaming Services

Due to the vast difference in company size and core business, there are varying motivations to operating a streaming service. Companies like Apple and Amazon support their main business of selling devices and consumer goods by utilizing content production to promote their brands. Historic studios such as Warner Brothers and Paramount use streaming to earn money on their vast content libraries. Those with declining linear assets such as Disney, Comcast, and Paramount pivoted to streaming to regain customers that were cutting the cord on cable. The chart below shows the number of households paying for traditional linear TV, which is projected to decline at a CAGR of -6% through 2027.



Source: Statista

The massive rush to create a streaming service for every company that owns a piece of content generated an inefficient market. For purely streaming-focused subscriptions, Netflix leads the industry in total subscribers, followed by Disney+ and Max (WBD).

Streaming Service	Total Subscribers (M)
Netflix	**260**
Prime Video (Amazon)	230*
Disney+	150
Max	98
Paramount+	67.5
Hulu (Disney)	48.5
Peacock (Comcast)	31
Apple TV+	25*
YouTube TV	8

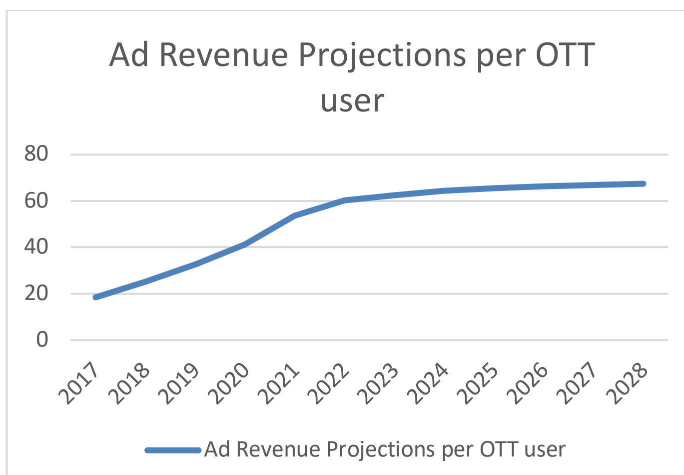
Source: Company Financial Statements; estimation*

Subscription Revenue

The fundamental aspect of the streaming model is subscriber revenue. Consumers choose which services they want and pay for them individually. Across the industry, subscribers are growing as more customers transition away from cable to digital streaming. However, due to economic factors, high production costs, password sharing, and customer churn rates, subscription revenue alone has not been enough to turn services profitable. We believe that a shift to more expensive premium subscriptions with lower priced ad-tiers will be the model that is sustainable for streamers. Some services at the bottom of the totem pole who have already implemented this such as Paramount+ and Peacock (Comcast), but have failed to earn a profit[11], which is a sign they need M&A activity or to shutter their services and offer their content as part of a larger bundle.

Advertising Revenue

In recent years, companies such as Netflix have added in cheaper ad-supported subscription tiers as the industry cracks down on password sharing. Their 180 on how to handle shared accounts contributed to a successful fiscal year 2023 and is becoming a model for other companies to adopt[17]. For example, Amazon Prime switched all subscriptions to ad-based and made their premium tier three dollars more per month. I do not think this move will work as well for Amazon, as it is a "cherry on top" service for Prime customers who have a membership for cheap shipping. However, this is a step in the right direction for making the streaming market more efficient. Free-ad-supported-TV (FAST) is also a new source of income for streamers. FAST offers viewers access to a variety of content with commercials throughout, just like regular cable. It is a smaller play for most streamers but can be a solid way to monetize content that would not be watched on their regular service. Advertising makes up a small percentage of the pie for most streamers but will grow into focus in the coming years. Advertising revenue per Over-The-Top user (streaming video customers) is expected to grow by a CAGR of 1.5% through the next five years, which bodes well for Netflix and Prime who are leaders in the ad space. Our team believes these estimates may be a bit conservative, as Netflix and others have seen early success in their advertising tiers, and we expect this trend to continue.



Source: Statista

Experiences

The traditional Hollywood studios who own famous brands and franchises utilize parks and experiences as another way to monetize their content. After the Covid-19 shock to in-person experiences, attendance has been on the rise at these parks. Netflix has also tested the waters with in-person experiences such as Stranger Things and Bridgerton pop-ups and is expanding on that by opening "Netflix Houses", which plan to offer merchandising, food, and show related activities[18]. We believe that taking advantage of strong content brands through experiences is a step more video streamers should take. Parks and experiences offer a consistent flow of revenue that serves as a hedge against subscriber churn.

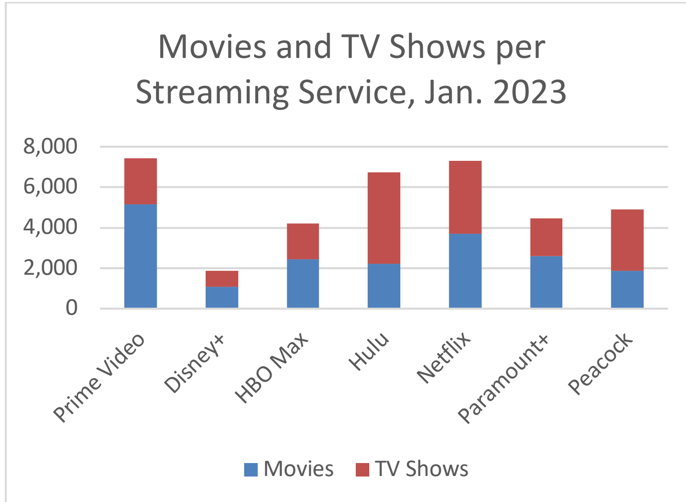
Licensing Fees

Another method for streaming services to make money is through licensing their content to other streaming services. This is what originally built Netflix as the top streamer, as companies with large content catalogs licensed their content to Netflix for some extra cash. Once these companies such as Disney and NBC realized that their flagship programs were building a giant in Netflix, they stopped licensing so they can air their original content on their own streaming services. In the past year, we have seen a shift back to licensing, as struggling streamers look for extra cash. Many firms went all-in on original content for streaming but high production costs and low revenues per subscriber has contributed to unprofitable services. Licensing provides a cheaper alternative to original content as the industry retracts the amount of TV and movies being made. In 2023 the amount of scripted TV series dropped 24%, to a total of 481 shows. This number was down from 2021 and 2022 highs of 633 shows[20]. We expect this trend to continue, and we anticipate licensing to grow as a result.

FIRM DIFFERENTIATORS

Content Catalog

Many of the firms in the streaming business have long backgrounds of content production. Firms such as Disney have been producing films for around 100 years and have a very deep catalog of beloved brands and franchises. Other tech-oriented companies, such as Apple and Netflix just started producing content in the past five to fifteen years. Netflix's massive spending in original content has given the company worldwide phenomena such as *Stranger Things* and *Squid Game*. Arguably the biggest issue in streaming is subscriber churn, where customers can cancel at any moment. Companies with large content libraries are positioned well for the future. If companies with large libraries and middling services such as Comcast, Warner Brothers Discovery and Paramount do not have the strength to support their own streaming services, we believe that folding their own service and licensing their content to a larger streaming bundle would be a good business decision.



Source: Statista

Declining Linear Assets

Some video streaming companies still own traditional TV assets, such as cable channels. The decline of linear television forced the hand of many companies to create their own services. Although the business is dying and moving to a streaming model, companies that still own linear television have a couple potential ways to make money off cable. Milking as much cash out of linear TV assets will benefit organizations who are still dealing with unprofitable streaming services. We believe live sports rights and airing the first few episodes of a TV season with a call to action to subscribe to a streaming service to finish the season are beneficial business decisions. Live sports are the only thing keeping cable intact, and we believe it will take a while for US consumers to fully adopt a streaming-only sports environment.

Motivation of Firm

Companies in the streaming industry have wildly different interests. Traditional media companies pivoted to streaming because their linear television model is slowly falling apart, while tech giants utilize their streaming services to promote their core businesses. This creates an interesting environment where large tech companies have a blank check to pay massive sums of money for live sports rights, films, and television shows. However, they do not have the large content libraries that others do, which is a key driver for preventing subscriber churn. Aside from Netflix, each company in the streaming industry has other businesses that they pair with their service. Disney has parks, Comcast sells high-speed internet, Apple sells devices, etc. Media conglomerates leverage their service to air their content, while tech companies use streaming to integrate into their broader ecosystems. Because there are a multitude of reasons companies are in the streaming industry, it gives concern as to whether these competitors will be able to work together to generate a more efficient market. This may look like the iTunes of streaming, where one app serves as a one-stop shop to buy streaming a la carte. We believe that one of the tech giants in the space will need to drop their own content production and serve as a hub to all streaming options.

Service Maturity

The age of a streaming service plays a large role in customer churn. Netflix secured a massive first-mover advantage by being ahead of the curve with streaming. Because they were the first, they have become synonymous with streaming as a technology. Newer services have less consumer loyalty and are much more susceptible to customers leaving. Netflix is set up very well for the future given how they have navigated new entrants into the market and remained the top service.

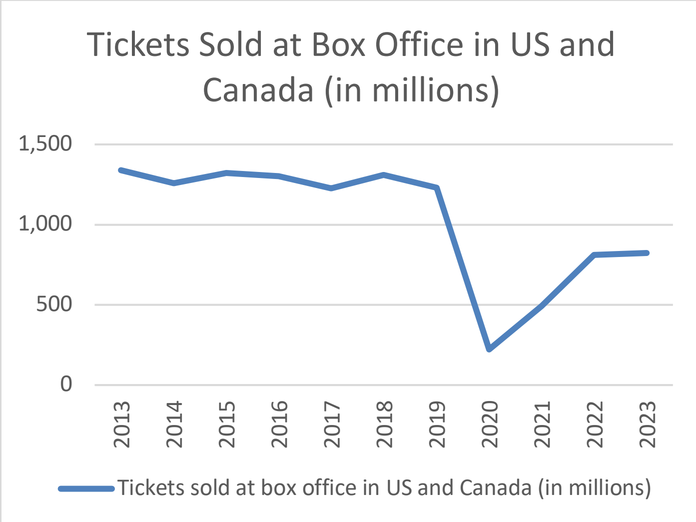
RECENT DEVELOPMENTS

Hollywood Strikes

In 2023, multiple Hollywood unions went on strike simultaneously for the first time since 1960[15]. Tensions about compensation through streaming boiled over and ignited months of strikes. The Writers Guild of America (WGA) and Screen Actors Guild (SAG-AFTRA) protested the streaming model, arguing they had a lack of residuals and from the advent streaming services. The two unions also had a major dispute with the Alliance of Motion Picture and Television Producers (AMPTP) over the use of Artificial Intelligence and its potential to wipe out jobs for screenwriters. Ultimately both unions came to an agreement with the AMPTP and received rule changes regarding production rules, residual compensation, and Artificial Intelligence. SAG-AFTRA signed a deal where actors will receive a 7% increase to pay minimums, while the WGA got a 3-5% increase. Both unions got a residual bonus that kicks in if 20% or more of a streaming service's domestic subscribers watch a TV series or movie in the first 90 days of its release. The streaming model was bound to cause some issues with residual compensation since platforms were built off airing popular old programs, and these agreements will create a better system for talent and production. We anticipate that these agreements will not hurt large streamers such as Netflix and Disney but may help contribute to the downfall of smaller streamers such as Paramount. We believe this may be the tip of the iceberg for the Artificial Intelligence debate within Hollywood. As AI grows rapidly, it is unclear how soon AI productions will be in motion and affecting the business of streamers. The strike also delayed some projects from releasing, but the financial repercussions should only be short term.

COVID-19 & Movie Theaters

The Covid-19 pandemic had a profound impact on the entertainment business, and streaming services are still dealing with the fallout to this day. The lockdowns led to a substantial increase in streaming subscriptions, which led some stocks to all-time highs. The growth was so rapid that Disney beat their five-year growth goal in a matter of a couple months. Disney and Warner Brothers Discovery also started to implement straight-to-streaming movie releases. Although this was convenient for consumers, it was highly costly to the studios. In the past year or so, there has been a shift back to theatrical releases, with all streamers besides Netflix utilizing them. Despite theaters growing out of favor with consumers and becoming increasingly tough to run, they are beneficial to streamers on multiple fronts. They allow the initial rush of fans to pay for the individual title and serve as an advertising and marketing play for when the titles drop on streaming. It will be important for streamers to decipher which movies are theater plays versus straight to streaming. The recent "Barbenheimer" and "Gentleminions" phenomena display that there is still a desire for theatrical events. Theaters may never fully recover from the pandemic, but still play an important role in entertainment distribution.



Source: Statista

M&A Activity

M&A is one of the key areas to monitor in the streaming space. The industry is ripe for movement, and we anticipate there to be many moves towards a consolidated There has been major M&A activity to start 2024. Three major developments include:

1. *Paramount up for sale*[16]

Paramount Global, the home to Paramount Pictures and CBS is up for sale, marking the first time that executive leader Sheri Redstone has publicly weighed a sale. The company has faced challenges as the Hollywood business model shifts toward streaming, making it rely on network TV and theatrical releases. The potential sale has attracted interest from multiple media companies, including Skydance Media, Warner Bros. Discovery, and Byron Allen's Allen Media Group. Selling off Paramount for parts makes sense, as the company has not had success in streaming and likely does not have enough brand power to operate its own streaming service. We believe the best move for Paramount is to sell itself to another media company or shutter its streaming service and become purely a content producer and licenser.

2. *Disney, Warner Brothers Discovery, and Fox to create sports streaming service*[5]

Disney, Warner Bros. Discovery, and Fox are joining forces to create a comprehensive sports streaming service, which is a significant shift in the sports media landscape. The yet-to-be-named service will be launched in the fall and offer content from all major leagues. Each company will have one-third ownership of the new service, a model like the original Hulu. The new service is expected to encompass 55% of US sports rights and will be available as a standalone app or as part of bundles for Max, Hulu, and Disney+ subscribers. The new service will not include content from Comcast's NBCUniversal or Paramount, who both hold major sports rights. Consumers will likely win from this deal, but there are still question marks for the companies. Despite the new service being targeted towards people who are cord-nevers (young people who have never subscribed to a traditional TV bundle), if the platform is successful, it will accelerate the decline of linear television. As these companies are still earning profit from traditional pay-TV, they may contribute to the downfall of that business segment. The companies have also been fierce competitors in the market for live-sports rights and their own streaming services. It remains to be seen if they will be able to set their individual motivations aside to work together on this project. Our team would like to see information on pricing and how the service will be bundled, but this exemplifies the shift back to a cable-like model where you can get all your channels in one place.

3. *Disney to buy a $1.5 billion stake in Epic Games*[1]

On February 7, Disney announced a deal to buy a $1.5 billion equity stake in Epic Games, the gaming company behind Fortnite. The two companies have collaborated in the past, bringing Disney characters to the Fortnite Universe. The deal exemplifies a growing relationship between media and gaming. Disney will be able integrate and advertise its content through Fortnite and other Epic Games properties. There is also potential for Disney to produce Fortnite movies, TV shows, and parks experiences. Video game adaptations are growing in popularity, as *The Last of Us* was a hit HBO show in 2023 and *The Super Mario Bros. Movie* was the second highest earner at the box office[19]. Gaming offers streaming companies a different source of revenue while providing vertical integration to promote their brand. All the details have not released yet, but moves like this will keep media brands competitive in the long-term.

The M&A Activity in streaming is important to track as the next iteration of companies takes place. The industry is at an inflection point, and firms with declining linear assets are at risk of being left behind by competitors. We believe Netflix and Disney are suited well to survive M&A Activity in their current states. Comcast, Warner Bros. Discovery, and Paramount are all ripe for mergers and acquisitions.

The primary reason is that these firms do not have the content library or tech they need to turn their streaming services into profitable standalone ventures.

INDUSTRY TRENDS

The *Suits* Phenomenon

While original content slowed during the strikes over the past year, *Suits* dominated streaming as the number one television show. The power of Netflix was on full display, as an old show (originally aired in 2011) from the USA network became the number one hit in America in 2023. Because Netflix has such a large user base, their platform is a machine for creating hits[6]. The success of *Suits* on Netflix has led other streamers to license their old hits to Netflix, such as *Ballers* and *Six Feet Under* from Warner Bros. Discovery. This establishes Netflix as a clear leader in the streaming space. After the rush to compete with Netflix, traditional media companies are crawling back asking for help. Netflix is positioned extremely well given the viral nature of their platform. Despite other competitors having older TV content, Netflix is uniquely positioned to utilize old content. The firm's top ten lists, and algorithmic recommendations serve as a hit-making machine that other firms do not have. Many consumers log on to Netflix without an idea of they watch, while they go to other platforms for specific titles only.

Global Growth

The global expansion of streaming services, exemplified by the success of shows like "Squid Game," shows a shift in consumer preference and allows US services to grow worldwide. By 2028, the worldwide penetration rate of over-the-top video is projected to grow to approximately 55%, which is about 10% higher than current levels. With most growth for streaming subscriptions coming internationally, there is a huge opportunity to make diverse content that will garner foreign customers. According to analyst forecasts, Netflix is projected to spend more on international content than domestic content in 2024[20]. Services with global audiences and brands such as Netflix and Disney are positioned best to distribute streaming globally.

Gaming

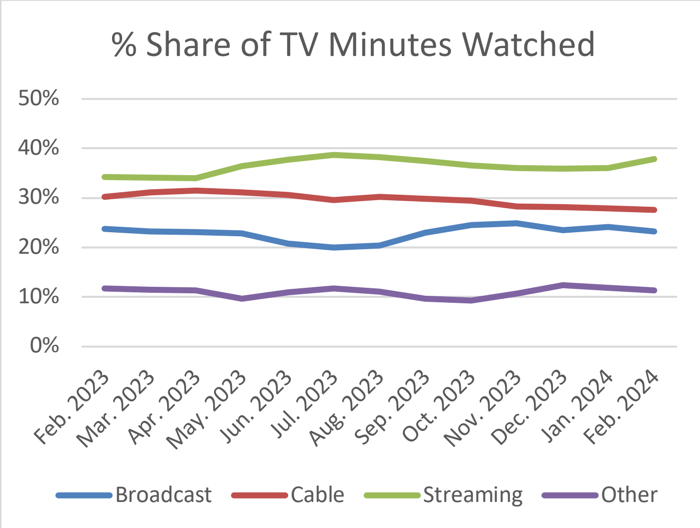
Netflix and Disney are at the forefront of incorporating video games into their streaming offerings. Netflix has added many popular games to their mobile app, indicating that they are serious about making their platform a hub for all-things entertainment. Disney has also pursued gaming with their recent equity purchase in Epic Games. Both developments are positive outcomes for each company as they diversify their offerings and add new sources of income with high growth potential. Netflix's gaming efforts are not enough to change its financial outlook yet, but we believe their initiative shows strong forward outlook from management[21].

Short-Form Video

Eyeballs may be taken away from highly produced content on streaming services as younger generations flock to social media to spend their time. In particular, the growth of Tik Tok and Instagram Reels is concerning for media companies who are competing for attention. In 2019, Tik Tok had approximately 650 million subscribers, which has grown to around two billion in five years. Given the addictive nature of short-form video, consumers may be quicker to ditch streaming services in favor of social media if disposable income levels lower. We hold the opinion that short-form video can play well with streaming services, however. Apps like Tik Tok can generate buzz for titles coming from streamers and be used as a promotional tool.

Minutes Watched

In an industry driven by attention, minutes watched play a crucial role in subscriber retention. The longer a service can hold a subscriber's attention, the less likely that customer is to churn. According to Nielsen, streaming takes up approximately 37.7% of TV viewing. Cable and broadcast TV take up a little over 50% of minutes watched, showing they still have some economic value despite being in decline. The larger trends at hand are streaming's share increasing while linear declines, but the chart below shows there is some seasonality to TV viewing. Cable and broadcast took a dip in the summer months, when there are less live sports, while streaming hit its peak for 2023 in July. Netflix pursuing live sports will help round out the edges to its programming schedule.



Source: Nielsen

MARKETS AND COMPETITION

Streaming Subscriptions

Netflix is a leader in this category. It displays the company's dominance. Not only are they the largest streaming service, but they are also the only company to see a dime of profit on one. This gives them massive scale and the ability to dictate market outcomes. Netflix's ad tier generated one of their best quarters of growth ever in 4Q, 2023, and Paramount+ and Peacock both appear to lack the growth prospects to catch up to the pack.

Streaming Service	Total Subscribers (M)
Netflix	**260**
Prime Video (Amazon)	230*
Disney+	150
Max	98
Paramount+	67.5
Hulu (Disney)	48.5
Peacock (Comcast)	31
Apple TV+	25*
YouTube TV	8

Source: Company Financial Statements; estimation*

Major Players

To examine the companies that make up the streaming industry, they easily divide into three major categories: large tech firms who are in streaming as a side hustle, leading streamers, and lagging streamers. Each firm has varying pricing plans and motivations to be in the industry.

Streaming Service	U.S. Standard Plan Monthly Cost (ex-ads)
Netflix	**$15.49**
Prime Video (Amazon)	$12
Disney+	$13.99
Max	$15.99
Paramount+	$11.99
Hulu (Disney)	$17.99
Peacock (Comcast)	$11.99
Apple TV+	$9.99
YouTube TV	$72.99

Source: Company Websites

Large Tech Firms:

Free Cash Flow (in $ billions)	
Apple	106.87
Google	69.50
Amazon	32.22

Source: FactSet

All three of the major tech firms that are involved in streaming are positioned well to be leaders in the consolidation of the streaming industry. The future of each company is not reliant on streaming which adds an interesting element to the industry since they are the most equipped with cash.

Apple (AAPL):

Apple, one of the largest companies in the world, introduced their streaming service in late 2019, and it has mostly been for high-end content and promoting the Apple brand. In an ideal world, Apple's goal would likely be to replicate the business they had with the iTunes store with streaming. Given their penetration of the US smartphone and device market, they are a very strong candidate to seamlessly integrate a hub for streaming.

Google (GOOGL):

Google is a unique case given their business with YouTube. They created the most popular streaming broadcast TV platform in YouTube TV[1] and have a constant pipeline of advertisable content on YouTube. In the past year, they acquired the rights to Sunday Ticket, which proved to be a boon for the company. Google, like Apple, has a large user base and would be able to host a central streaming bundle under the YouTube umbrella. Google's streaming ventures are set up well through YouTube alone, as its customers generate its monetized content.

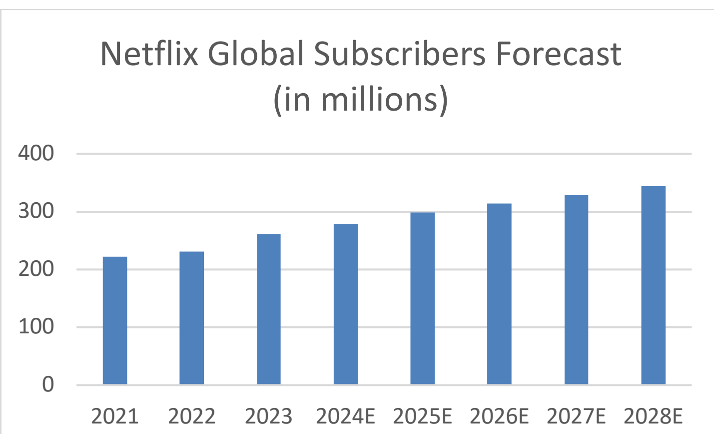
Amazon (AMZN):

Prime Video has a large subscription base through Amazon Prime subscribers. Most subscribers to Prime Video are focused on free shipping and buying household goods. Amazon pivoted to have all subscribers receive ads and made a premium tier worth an extra three dollars. We anticipate the ad revenue to generate more cash for Amazon since a low percentage of customers are projected to pay up for the more expensive tier[1]. Amazon has also dipped into live sports with Thursday Night Football and is a strong contender to be the originator of a future streaming bundle. They already offer some other services such as Max and Paramount+ as add-ons to Prime Video, which is a sign that they hope to bundle streaming subscriptions.

Leading Streamers

Netflix (NFLX):

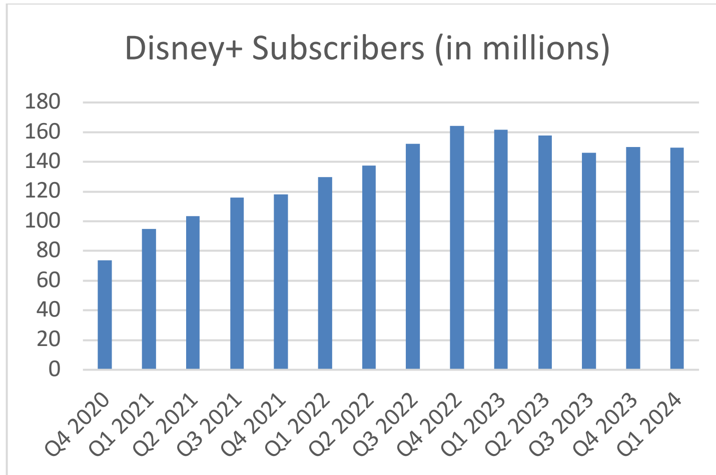
Netflix is the most dominant streaming service. They have the most subscribers and are the only streamer to turn a profit. Their data driven approach has turned old, licensed content into new hits, and they also have created original shows that have become worldwide brands. In the future, their growth prospects revolve around ad revenue, gaming, and adding live sports rights. Netflix's next step in increasing shareholder value is adding live sports. If they choose to do so, hosting recurring games and events will contribute to lower subscriber churn.



Source: Netflix 10k & HF Estimates

Disney (DIS):

Disney is the most notorious and well-known media company. Their entertainment, sports, and experiences create a well-rounded brand that is hard for consumers to avoid. After mismanagement under Bob Chapek, Bob Iger returned as CEO to get things in order. We are just now seeing developments of his second tenure as CEO come through. We expect subscriber growth to stop stagnating and to increase due to new projects spearheaded from Iger. Disney's strong brand and large streaming footprint through Disney+ and Hulu set the firm up better than other competitors who also have declining linear assets.

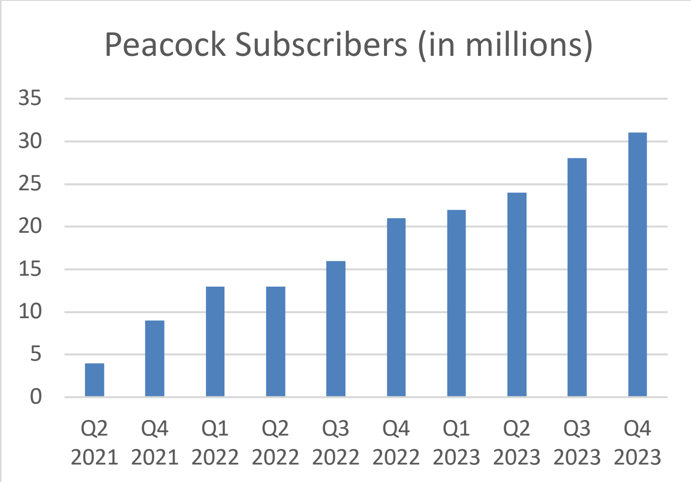


Source: Statista

Lagging Streamers

Comcast (CMCSA):

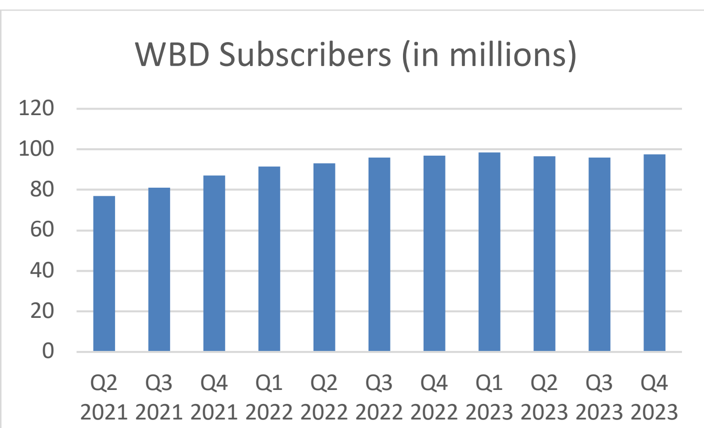
Comcast has utilized Peacock to stream its content library but has not been able to turn a profit on it yet despite subscriber growth. The company recently aired the first ever exclusively streamed NFL playoff game, which set streaming records but still lagged linear TV the prior year in the same window[7]. Peacock struggles with churn, as consumers come in for sports and then leave when seasons end. Their content library leaves a little to be desired, and they seem to typically be a step behind. For example, they licensed out *Suits* to Netflix last year which was a huge success for their competitor. Comcast has spent large amounts on Peacock, and despite growth in subscribers, they lost more money in 2023 than 2022. It appears unlikely they will be able to garner they scale they need to make the service profitable. For Comcast to become an appealing investment, the Peacock experiment would need to end.



Source: Statista

Warner Bros. Discovery (WBD):

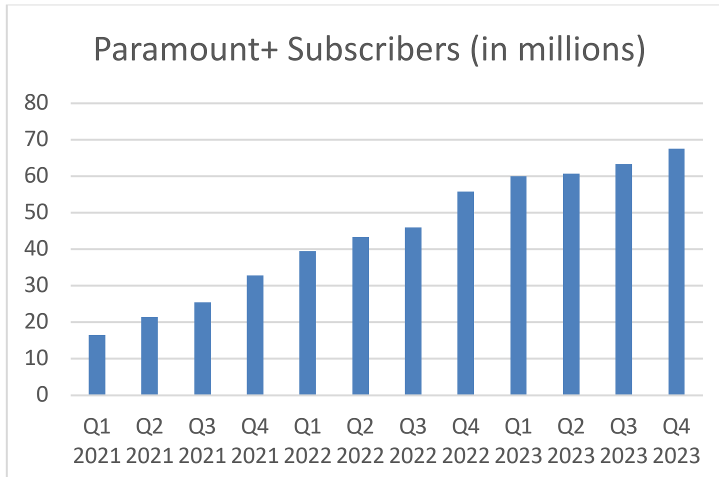
Warner Bros. Discovery has undergone major change in the past year. They rebranded their streaming service from HBO Max to Max and have taken aggressive tactics to get rid of their large debt amount. These include cutting already finished new movies for tax rebates and licensing content to Netflix[1]. The company seemingly will struggle to pay for expensive NBA rights coming out in the next year, but their new sports streaming service with Fox and Disney has the potential to remedy that. In upcoming months, WBD will be allowed to merge or acquire again, which is where we anticipate the company is headed. It is hard to envision an outcome where they become the destination streaming service for general content. Netflix beat them to the punch there.



Source: Statista

Paramount (PARA):

Paramount has lost a considerable amount of market cap over the past year. With the company up for sale, it may be the first domino in several M&A moves to reconstruct the streaming industry. They are skating by on the NFL and college football and are too weak to support their own streaming service. The firm has struggled to adapt to the streaming landscape and has taken large losses on its streaming service. The combination of personal dynamics with the Redstone family, a shift away from legacy media, and a risk of bankruptcy has put a major dent into the prospects of Paramount as a standalone company. What happens with the sale and how many parties are involved will be something to watch over the coming months. We believe the deal with David Ellison and Skydance Media is the odds-on favorite, however, we would not be surprised if shareholders make a push for a large private equity firm.



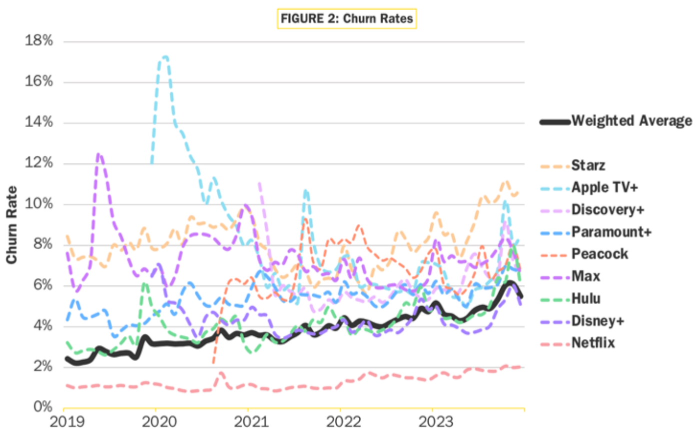
Source: Statista

Structure and Stability

The streaming industry is hyper-competitive and shaped by consumer preferences and the evolving maturity of media companies shifting from traditional TV to streaming. The firms are nowhere near an equilibrium state, as they are all adapting to the marketplace and figuring out whether they will be able to compete or not. A main issue is many services try to be a one-stop-shop and general content hub but do not have the audience to compete with Netflix and Disney. In the next couple of years, it is highly likely that there will be movement to create a more sustainable sector and traditional media companies are likely to lose out and sell their parts to Disney, a tech company, or merge together. Firms that are a most likely to see M&A activity are Warner Bros. Discovery and Paramount.

Risk of Substitution

The risk of substitution in the streaming industry revolves around the potential for customers to switch services or to shift to alternative forms of entertainment such as short-form video or gaming. Because the market is too saturated with streaming services, subscriber churn is high. This heightens the competition between competitors and ultimately has created a clear hierarchy of who the best companies are moving forward. Netflix is at the top of that list, who has a 2% monthly churn rate, which is much lower than competitors. We believe the primary reason for this is due to its first-mover advantage.



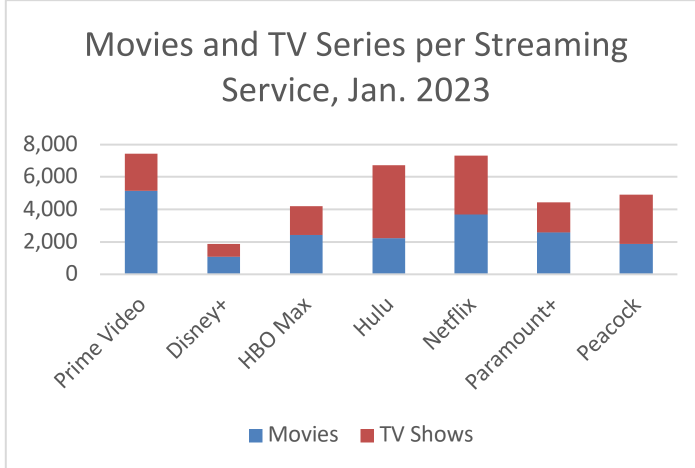
Source: Antenna

Threat of New Entrants

There are significant barriers to entry to get into the streaming industry. You either need a ton of cash and a high amount of consumers (see tech companies) or have massive amounts of content. All the potential players in the streaming industry have entered the arena, and now we are approaching the point where only the top companies will survive.

Peer Comparisons

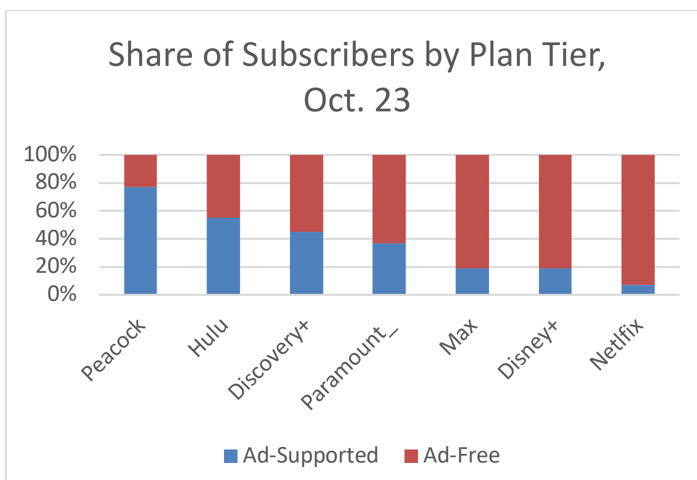
Titles per Streamer



Source: Statista

Each streaming service has a unique makeup of movies and TV series on its platform. Netflix has an almost even split, with 51% of their content in movies. Amazon Prime Video has the highest percentage of movies with 69% invested, compared to 31% in TV series on their platform. The only two services with more television than movies are Hulu and Peacock. Hulu was built up as a television service, and Peacock has a stable of content from NBC. We believe Netflix's near even split contributes to its generalist nature. Consumers utilize Netflix for all things entertainment.

Advertising Share of Subscribers

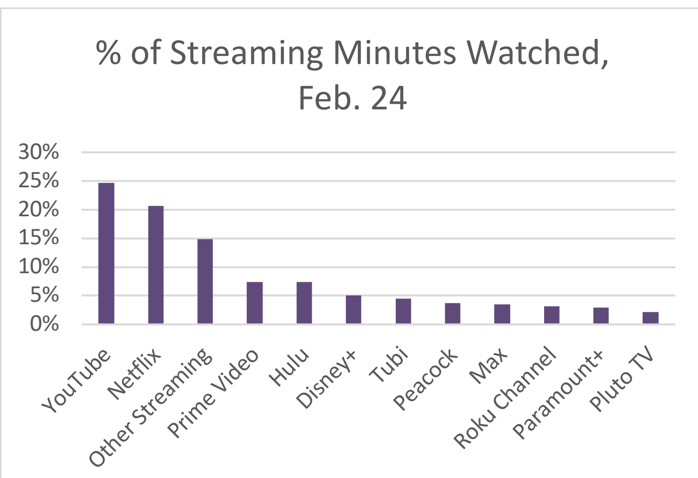


Source: Antenna

Netflix's ad-supported tier takes up a much lower percentage of its subscriber base than its competitors. The main reason for that is because its ad-supported tier is relatively new. We believe that the share of subscribers purchasing Netflix's ad-supported tier will rise but remain below most competitors. This is due to consumer preference, and subscribers being trained to the idea of having Netflix without ads. Netflix's share of advertising subscribers should rise to a level between where it is now and where Max and Disney+ currently stand. On the other end of the spectrum, Peacock and Hulu have more ad-supported subscribers than ad-free. We believe Hulu will shift to have more ad-free than not once it is merged on to Disney+, but Peacock's ad-supported rate should remain high due to many subscribers buying the cheaper tier as it is a secondary service to most consumers.

Minutes Spent Watching

The power of Netflix is on full display in the chart below. It was easily the best performing streaming service in 2023. Netflix's domination of streaming bodes well for its future, as it has captured mainstream notoriety, while historic Hollywood studios are fighting at the bottom for attention. In the chart below, the market share of each streaming service is on display. Streaming makes up 37.7% of TV market share.

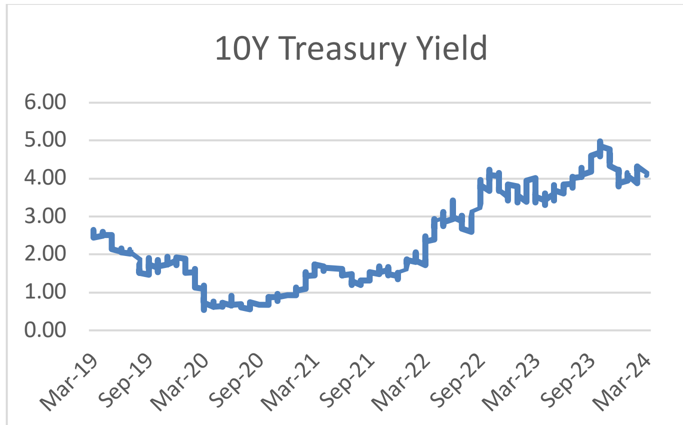


Source: Nielsen

ECONOMIC OUTLOOK

Interest Rates

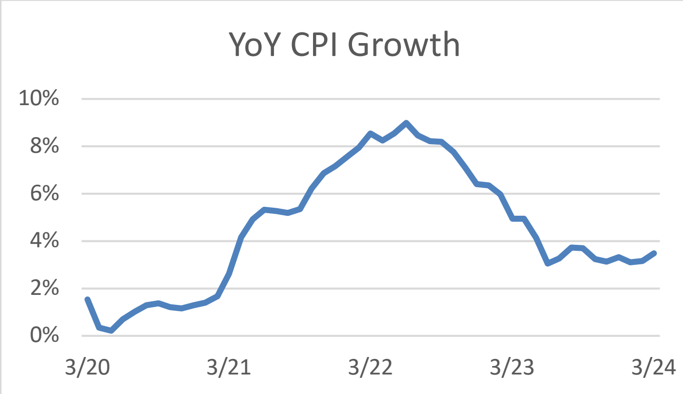
Interest rates are a significant factor for streaming services, particularly in terms of content production. In previous years, zero-interest-rate policy allowed for a boom in original programming. As streaming services were building out, it was easier for companies to get projects off the ground while cash was cheap. With the recent rise in interest rates, and Fed Chairman Jerome Powell saying he expects rates to stay higher for longer[13], original content is bound to slow down in the short-term. We believe this will expand upon the trend of licensing content between streamers. This gets fresh content onto platforms while not having the high costs of producing new content. This is beneficial to Netflix in particular, who has seen licensed old content from other studios become viral on its platform. In the long-term however, we expect the yield curve to normalize and for content to become cheaper to produce.



Source: Federal Reserve Economic Data (FRED)

CPI Inflation

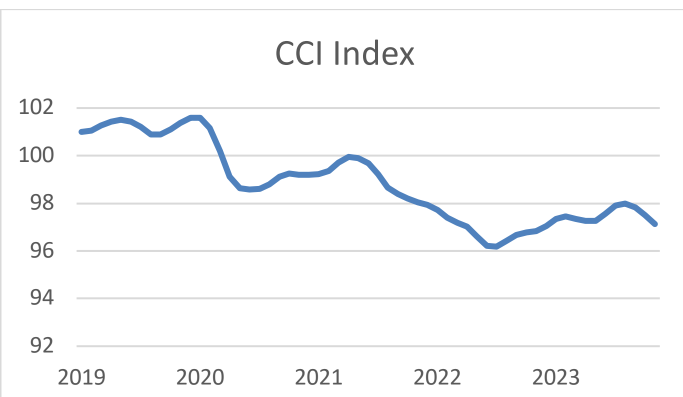
Inflation impacts streamers from multiple perspectives. As living expenses rise, streamers face increased costs of production and licensing content, and may have to hike the subscription price of their service. That in turn affects consumers, who may be quicker to cancel their subscriptions with higher costs. Inflation may lower discretionary spending as consumers pivot to spend more on important goods than luxury media and entertainment. The firm has seen the cost of original content production rise through inflation, so it has leaned on old content. We believe inflation will slow, which should create a better environment for producing content and retaining subscribers.



Source: Federal Reserve Economic Data (FRED)

Consumer Confidence

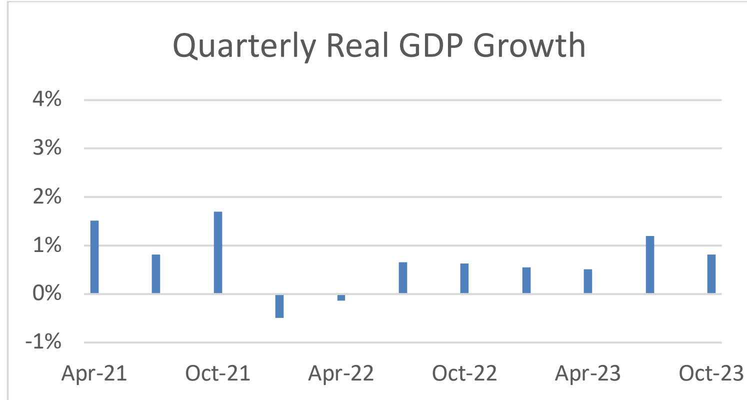
Consumer Confidence plays a crucial role in shaping the landscape for firms with streaming services. High levels of consumer confidence correlate with high levels of disposable income. As a non-essential good, streaming services rely on a consumer-friendly economy to perform well. Consumer confidence is still attempting to reach pre-pandemic highs but has grown 17% over the past year. If the Fed pulls off a soft-landing, it is our belief that streaming services will be set up well to continue subscriber growth with consumer confidence on the rise.



Source: OECD

Real GDP

Real GDP is an important economic component for streaming services. As a key indicator of economic health, changes in real GDP can influence consumer spending habits. When Real GDP continues to grow, consumers are more likely to spend disposable income on experiences and entertainment, including streaming services. Aside from a dip due to Covid-19 in the spring of 2020, Real GDP has grown consistently over the past five years. Our team expects this level of growth to continue, which would be a beneficial development for the industry as the industry heads towards consolidation and competition heats up.



Source: Federal Reserve Economic Data (FRED)

CATALYSTS AND KEYS TO MONITOR

Overall, the streaming industry is at an important crossroads. New entrants rapidly joining the market in the past five to compete with Netflix and compensate for declining linear TV created a flawed market. In the future, expect M&A activity and companies to reevaluate whether they have the capacity to operate a streaming service.

As this trend develops, it is clear which companies are positive long-term investment opportunities and which are too questionable to touch. In the short-term, stock prices may vary due to the Fed's ability to complete a soft landing, but the streaming industry should see positive momentum from its reorganization.

Tech giants Amazon, Apple, and Google are all positioned to perform well and serve the industry as a consolidating platform. Each has a motivation to come in off the top rope and become the key figure of the industry.

Netflix also has a positive outlook. Netflix's dominance in 2023 solidified it as the leading streaming service, and their potential growth in gaming and live events is a key factor to unlocking more shareholder value.

Of the traditional Hollywood studios with declining traditional TV assets, Disney is positioned best. They have diversified sources of income through experiences, sports, and entertainment. Their strategic initiatives, such as the sports streaming service and investment in Epic Games show the company has a plan long-term. We anticipate more changes to Disney over the next year as Bob Iger rights the ship with more moves, as he once did in his first tenure as CEO.

Comcast, Warner Bros. Discovery, and Paramount are similar due to their declining linear TV assets and their failure to grasp a solid market share of over-the-top video consumers. They are set up poorly, as their money-maker is falling apart, and they still have not been able to make progress in streaming. An important variable to monitor is M&A and bundling their content with other streamers. These companies do not have what it takes to survive as standalone services and need to stop wasting precious resources on losing money in streaming.

The video streaming industry is maturing, signaling a shift towards a more stable business model driven by M&A and rebundling strategies. Growth in advertising revenue is promising for the sector as many companies have pivoted to earn advertising revenue and not just subscription income. The potential of gaming and experiences also serves as a promising source of income for streamers as they try to capture elusive consumer attention.

Despite a positive outlook, the industry still has multiple risks that could derail momentum. The looming threat of a recession poses a significant challenge to streamers, as consumer spending would be diverted away from non-essential goods like entertainment. Additionally, the wildly different motivations of competitors within the industry may contribute to a lack of collaboration in making the sector more efficient. On top of this, the escalated costs of live sports and original content continue to rise rapidly, which could cause issues with keeping streaming profitable. We believe that these issues are manageable in the long-term and that companies will realize it is in their best interest to recreate a cable-like system.

Our overall industry recommendation is a market weight, given the vastly different stages competitors are in. We are most bullish on Netflix and Disney's positioning for the future. This is due to Netflix's lead ahead of the market on many fronts, including international growth and advertising, and Disney's diversified revenue streams and strong brand. We believe Paramount and Warner Bros. Discovery are two firms to avoid as their streaming services struggle and M&A activity looms.

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