NETFLIX

Netflix Inc.

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Recommendation

We recommend that the fund purchase 52 shares of NFLX and sell a mix of 15 ADBE and 30 DIS shares. There are two reasons that we are recommending selling Adobe and Disney in addition to purchasing Netflix. The first being that both ADBE and DIS are highly correlated to NFLX with correlation coefficients of 0.56 and 0.44 respectively. The second reason being that Disney is also in the SVOD market with Disney +, Hulu, and ESPN +, we believe that selling off some shares would reduce the risk exposure to that industry.

Stock Performance (1 Year)

Business Model

Netflix currently has two sources of revenue: Primarily subscription membership fees, and a small portion coming from DVD rentals. An example of the 3-tiered subscription plan for United States consumers is seen on the next page. Subscription costs vary across global regions, but all follow this structure. Potential future revenue streams include revenue from advertising and gaming opportunities, however, gaming has yet to be profitable and an ad-based subscription plan is not guaranteed, only speculated.

	Basic	Standard	Premium
Monthly cost* (United States Dollar)	**$9.99**	**$15.49**	**$19.99**
Number of screens you can watch on at the same time	1	2	4
Number of phones or tablets you can have downloads on	1	2	4
Unlimited movies, TV shows and mobile games	✓	✓	✓
Watch on your laptop, TV, phone and tablet	✓	✓	✓
HD available		✓	✓
Ultra HD available			✓

Growth Opportunities

- US & Canada Growth
  - Competition is catching up; growth will come from subscription price increases and crackdown on account sharing.
- International Markets
  - Far ahead of the competition, region-specific original content, and significant room to grow in these markets.

Board Summary

Netflix currently has 12 members on their Board of Directors, 9 of whom are independent directors. They currently have Co – Ceo's Reed Hastings and Ted Sarandos, who joined in 1997 and 2000 respectively. The board has decades of diverse experience in the entertainment industry and the ability to push Netflix in the optimal direction.

SWOT Analysis

Strengths: • Large market share • Original content development • Brand recognition	Weaknesses: • High priced subscription • Limited copyrights • Small backlog of original content
Opportunities: • International expansion • Gaming industry • Partnerships	Threats: • Growing competition • Inflation / Recession • Cybersecurity

Company Background

In April of 1998 a company that had only been founded less than a year earlier started allowing DVDs to be rented through the mail (Oomen, 2020). Fast forward two decades and that same company is one of the most prominent companies in the media industry. It goes by the name of Netflix, Inc. and it truly revolutionized the way entertainment is consumed today. Back when the company was first founded the only way to watch a movie or TV show was to either catch it on TV, own the disc or VHS tape, or rent the disc or VHS from your local video store. One of Netflix's founders and current CEO Reed Hastings saw rising popularity of DVD players over VHS players and decided to create a more consumer-friendly and extremely convenient way to allow people to rent and watch DVDs (Oomen, 2020). Hastings' gamble on DVDs becoming the main form of at home entertainment paid off.

Just allowing people to get DVDs sent to their door caused a large shift within the industry, and then Netflix created a subscription rental service which allowed subscribers to get a fixed amount of DVDs for a monthly fee. The new subscription service took the industry by storm and by 2007 Netflix had delivered a billion DVDs to customers (Peters, 2007). It was at this point that Netflix started allowing subscribers to stream movies and TV shows via the internet. Three years later in 2010 when Netflix offered a streaming only subscription is when streaming really took off (Hosch, 2009). Since then, Netflix has produced many of its own movies and TV shows, some of which have gained massive popularity (Bird Box, Squid Game, and Don't Look Up). It has maintained its status as the most popular streaming service to date with 222 million current subscribers (Silberling, 2022).

Netflix has two main sources of revenue. The first and more significant source is through their streaming subscription fees. The prices of these range from $8.99 to $17.00 per month. The other source of revenue is through their DVD rental service that many people do not realize still exists. There are two subscriptions for this service, one for $7.99 and the other for $11.99 (Martel, 2022). Out of the $29.7 billion in revenue from 2021 that Netflix had listed in their income statement only $200 million of that came from their DVD rental service (Gruenwedel, 2022). However, few streams of revenue are common when it comes to SVoD (Subscription Video on Demand) service providers.

Key Strengths & Weaknesses

Netflix, despite being the largest streaming company in the world, has some weaknesses. Firstly, Netflix added 8.3 million subscribers during the last quarter of 2021, about 200,000 fewer than management had forecasted. Netflix also projected an increase of 2.5 million subscribers during the first three months of this year, well below analysts' expectations of 4 million (Q4 earnings…). This could be largely because new streaming services are becoming more popular such as Disney+, HBO Max, and Hulu. Now Netflix has more subscribers at 222 million (Silberling, 2022), and many people are subscribed to multiple services, but the increasing popularity and content are potentially dangerous for Netflix moving forward. Disney specifically creates some of the most popular films which are exclusively available on Disney+ as the picture below shows. Netflix may also have to deal with price elasticity issues in the future as they are already the most expensive streaming service with plans to increase subscription prices in the future. Disney + offers a single plan of $7.99 monthly with the option to package with Hulu and ESPN + for $13.99 monthly. With competitors undercutting their prices, it will be important for Netflix to produce attractive original content to retain their subscriber base.

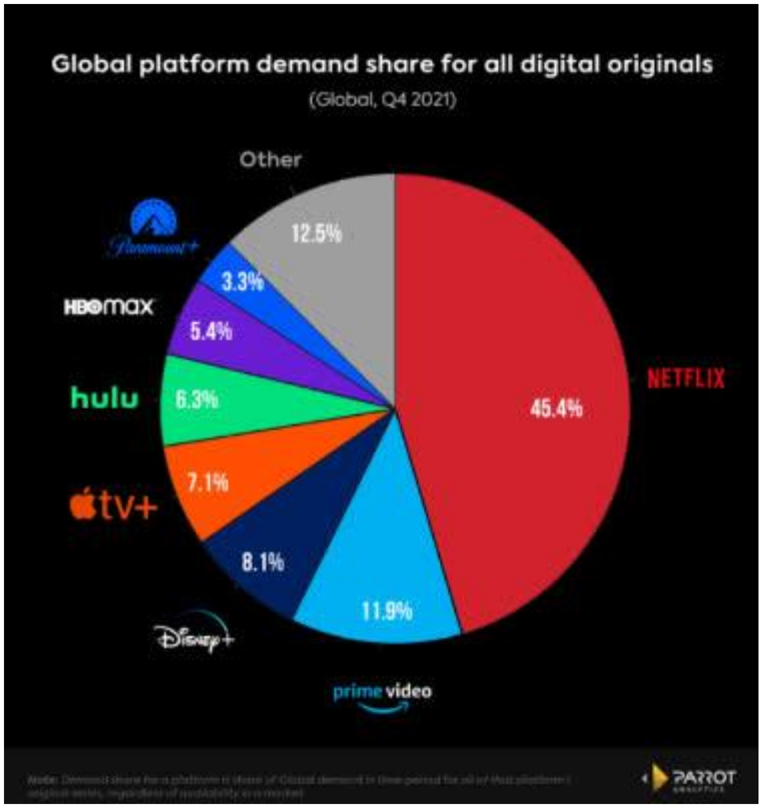
2021 Top 15 Streaming Movies

	Program name	Originator	Persons 2+
1	LUCA (2021)	Disney+	10,592
2	MOANA	Disney+	8,896
3	RAYA AND THE LAST DRAGON	Disney+	8,343
4	FROZEN II	Disney+	5,746
5	RED NOTICE	Netflix	5,528
6	FROZEN	Disney+	5,416
7	SOUL (2020)	Disney+	5,282
8	CRUELLA	Disney+	5,174
9	MITCHELLS VS THE MACHINES	Netflix	4,517
10	JUNGLE CRUISE	Disney+	4,425
11	BLACK WIDOW	Disney+	4,410
12	THE TOMORROW WAR	Amazon	4,049
13	COCO	Disney+	4,009
14	WE CAN BE HEROES	Netflix	3,770
15	AVENGERS: ENDGAME	Disney+	3,679

12/28/2020 - 12/26/2021 | Persons 2+ Minutes Viewed In Millions
Source: Nielsen Streaming Content Ratings (Netflix, Amazon Prime, Disney+, Apple TV+ and Hulu), Nielsen National TV Panel, US Viewing through Television

Nielsen

Despite these weaknesses, Netflix has some pretty solid strengths. The first key strength Netflix has right now is they are becoming free cash flow positive and are considering share buybacks because of it (Q4 Results…). This is a great sign for investors. Netflix currently has an advantage over other streaming services as it is an integral part of popular culture in today's day and age. This is due to their "first-mover advantage" as the first major streaming company, they have captured a substantial portion of the market. Even though competitors have been capturing large portions of the market in the US, Netflix and their original content is still in high demand. The picture below shows the global demand share for all digital originals. Netflix has nearly four times more demand for their original content than their next closest competitor Amazon Prime Video.



The next one of Netflix's strengths is one of their largest sources of revenue, as well as expenses, their original content. Out of all the streaming services, Netflix's originals do much better than their competitors. According to Nielson TV ratings, Netflix had 11 of the top 15 most streamed original content in 2021. As you can see in the tables below, the vast majority of content on Netflix is from acquisitions. The company has an excellent track record of acquiring some of the most popular shows available. In 2021 Netflix had 12 of the top 15 in this category.

2021 Top 15 Streaming Programs (Originals)

	Program name	Originator	# of Episodes	Persons 2+
1	LUCIFER*	Netflix	93	18,342
2	SQUID GAME	Netflix	9	16,432
3	GREAT BRITISH BAKING SHOW	Netflix	75	13,636
4	VIRGIN RIVER	Netflix	30	12,908
5	BRIDGERTON	Netflix	8	12,356
6	YOU*	Netflix	30	11,124
7	COBRA KAI*	Netflix	30	10,915
8	THE CROWN	Netflix	40	9,651
9	LONGMIRE*	Netflix	63	8,892
10	THE HANDMAIDS TALE	Hulu	46	8,564
11	OUTER BANKS	Netflix	20	8,301
12	TED LASSO	Apple TV+	22	8,161
13	MAID (2021 SERIES)	Netflix	10	8,103
14	WANDAVISION	Disney+	9	7,284
15	THE WITCHER	Netflix	16	7,067

12/28/2020 - 12/26/2021 | Person's 2+ Minutes Viewed In Millions
* Program originally aired on another network/distributor Squid Game includes viewing to both English and Korean versions
Source: Nielsen Streaming Content Ratings (Netflix, Amazon Prime, Disney+, Apple TV+ and Hulu), Nielsen National TV Panel, US Viewing through Television

Nielsen

2021 Top 15 Streaming Programs (Acquired)

	Program name	Originator	# of Episodes	Persons 2+
1	CRIMINAL MINDS	Netflix	322	33,865
2	COCOMELON	Netflix	15	33,278
3	GREYS ANATOMY	Netflix	382	32,625
4	NCIS	Netflix	354	29,529
5	HEARTLAND	Netflix	215	20,410
6	MANIFEST	Netflix	42	19,923
7	SUPERNATURAL	Netflix	329	18,912
8	SCHITTS CREEK	Netflix	80	18,062
9	GILMORE GIRLS	Netflix	153	14,704
10	NEW GIRL	Netflix	146	14,680
11	SHAMELESS	Netflix	134	14,406
12	THE BLACKLIST	Netflix	169	12,137
13	BONES	Amazon/Hulu	246	11,012
14	SEINFELD	Hulu/Netflix	166	10,447
15	THE WALKING DEAD	Netflix	153	10,377

12/28/2020 - 12/26/2021 | Person's 2+ Minutes Viewed In Millions
Source: Nielsen Streaming Content Ratings (Netflix, Amazon Prime, Disney+, Apple TV+ and Hulu), Nielsen National TV Panel, US Viewing through Television

Nielsen

One of Netflix's largest strengths and arguably largest advantages over their competitors now is their massive amount of advanced user data and analytics. Netflix started collecting data from its users way back when DVD rental was the only form of Netflix, but since Netflix started their streaming service in 2007 their collection and use of user data has grown exponentially. Netflix's advanced data is used to do things such as predict the popularity of their original content before they even decide to make it, optimize production planning, personalize marketing content, and provide users with personalized recommendations for movies and tv shows. This is important to Netflix because approximately 80% of the content that is streamed on Netflix is from their recommendation system. They collect extremely specific data from their users to be able to recommend the right shows to them and create original content in the future that will please their customers. Not only does Netflix remember what shows and movies you have watched, they remember the day, time, location, and device that it was watched on, whether it was paused, fast forwarded, rewound, or rewatched, they know if you stopped watching something and at what time and rate you stopped, they know what you search for, and they also know your browsing and scrolling behavior (Mixson, 2021). They have been collecting that kind of data before some of the other popular streaming services were even ideas in their creators' heads. This allows Netflix to understand their user base better than any other service out there.

Industry Summary

The industry that Netflix falls into is entertainment. More specifically SVoD (Subscription Video on Demand) market. Other popular SVoD services include Amazon Prime Video, Hulu, HBO Max, and Disney +. Netflix's market share in the SVoD market is the highest at 25%, but its competitors have been steadily growing while Netflix itself is seeing drops in subscriber numbers every quarter. Netflix's top competitors are Amazon Prime with a market share of 19%, Hulu and Disney both with 13%, and HBO Max with 12% (5% gained throughout 2021). Disney could potentially be Netflix's largest threat since they own Disney +, Hulu, and ESPN + bringing their total market share slightly above Netflix's 25% (Espósito, 2022). So, while it is currently true that Netflix is the top leader in their market, it may not remain that way for much longer.

The outlook for the SVoD market looks promising, but not on track to keep up with the insane growth it has experienced in the past decade. According to the statistics published by Statista, revenue, average revenue per user, and number of users are all expected to significantly increase in the next few years. The statistics show that revenue is expected to reach $36.5 billion in 2022 while continuing to grow at an annual growth rate of 7.22% which will create a market volume of $48.25 billion by 2026. The average revenue per user is expected to grow to $231.38 from the current level of $211.04 while it is estimated that the number of users will also increase to 166.2 million from 152 million (Statista, 2022). These numbers show that the market isn't growing as fast as it has in recent years, but it is still growing at a rate that will continue to provide profits to the current companies operating in the market while also enticing new companies to enter.

Growth Story

Netflix is currently the largest streaming service in the world with approximately 75 million subscribers in the United States and Canadian market, and a total of 221.8 million worldwide, as reported in their 2021 Q4 earnings report. Netflix struggled with new subscriber growth early in 2021, adding just 1.5 million new subscribers in Q2 2021, but saw that number rise to 4.38 million in Q4. This number beat Wall Street expectations and was a sign that Netflix can continue gaining new subscriber growth as they expand into foreign markets. This expansion will be a major factor in future revenues and earnings for the company as they attempt to tap high population markets like India, Japan, and South Korea. As of Q4 2021, Netflix had 32.63 million paying subscribers in the Asia Pacific market, an increase of 28% YoY mainly due to the success of original content

Netflix has been producing in South Korea. In 2021, Squid Games became Netflix's most successful original show yet, gathering 1.65 billion viewing hours in the first 28 days after its premier and topping Netflix charts worldwide for 10 weeks until it was ousted by another Korean produced show, Hellbound. Netflix plans to release another season of Squid Games in 2022 along with several other shows and movies from their Korean studio.

They invested nearly $500 million in their South Korean expansion in 2021, which has affected their cash flow numbers, but the success they are seeing should lead to long-term steady growth in subscribers and revenue throughout the APAC region. From Statista, the South Korean SVoD market is projected to reach $731 million in 2022, of which Netflix controls roughly 40%, and is expected to have a CAGR of 5.3% into 2026 and reach $900 million. The company also expects to see stronger growth numbers in Japan, where they have made another large investment in a studio and plan to release 50 new titles in the country in 2022. Netflix also has an opportunity to reach underserved markets in India and Malaysia, although at a lower subscription price point, and we expect them to take advantage of these markets to offset weak subscriber growth in the US & Canada. The continued expansion will be a key driver for Netflix's growth as the untapped market is much larger than in the United States, Canada, or Europe.

US & Canada Market

Another major growth opportunity for Netflix comes through price increases on subscription plans. In January, the company announced it would increase prices on all US subscriptions, the standard plan, which is the most popular, from $13.99 to $15.49 starting in February of 2022.It would also increase the price of their basic plan from $8.99 to $9.99 and their premium plan from $17.99 to $19.99 each month. According to Morning Star, Average Revenue per User was $14.78 in Q4 2021, this number plus the $1.50 average price increase, equals $16.28

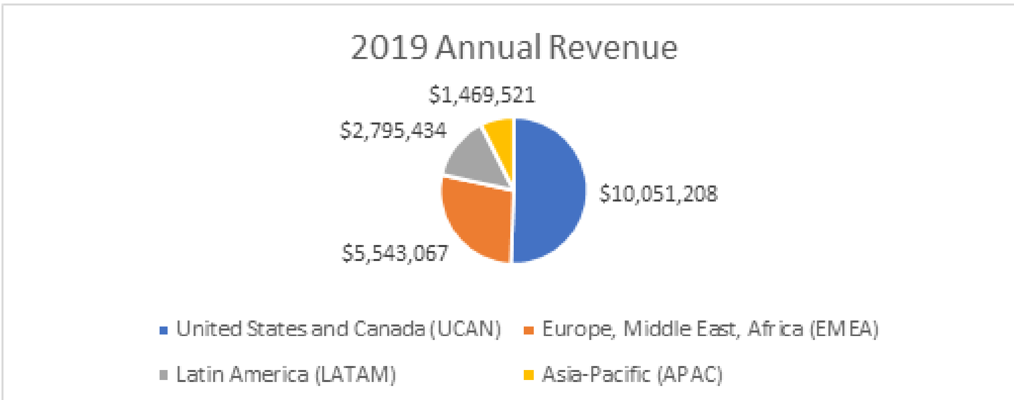
per user. This number combined with a boost in subscribers to 76 million, would put Netflix's monthly revenue at roughly $1.25 Billion in the US & Canada. Netflix plans to raise prices in all markets incrementally and expects to see increases in revenue to follow. It will be important for Netflix to monitor the effect of these price increases on new subscriber growth and retention rate of current subscribers. The company raised prices in 2015 and most recently in 2017 and observed lower growth numbers immediately after the increase, but relatively no impact on their retention rate. If Netflix can retain their current base and avoid a severe decrease in subscriber growth, they should be able to generate higher returns in the coming years.

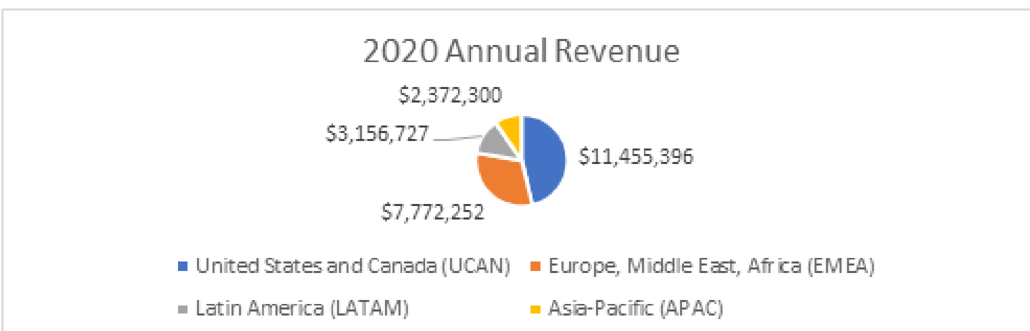
It seems that Netflix will continue to profit from increasing their subscription costs over the next few years. However, they are losing subscribers to their competitors due to the increase in rival streaming services within the past few years and even with the subscription price increases, their decreasing subscriber growth will eventually lead them to fall behind their top competitors. A better way for them to stay ahead in the game would be to try to increase their international subscribers since they are already much further ahead than their competitors in that category, and with all the information that they have in their cloud database they will be able to make improvements on areas that they see struggling and continue to make content that they see rising popularity in.

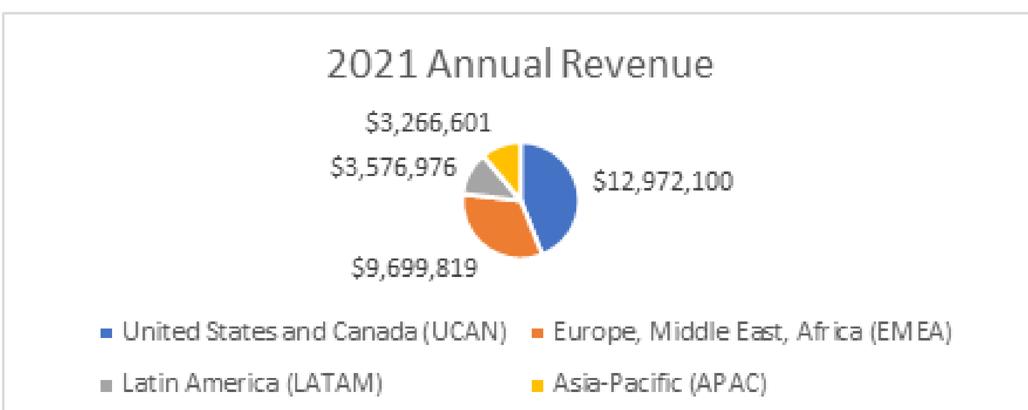
International Market

The projected growth for average number of subscribers and yearly revenue per membership is calculated based on the historical trends from 2019-2021 seen above. As you can see in the first table, international markets are poised for much more growth in subscribers compared to the US & Canadian market. The Asia-Pacific (APAC) market specifically has a major growth opportunity as membership growth increased over 90% from 2019-2021. We expect these membership growth numbers to increase throughout 2026 as Netflix continues to release new shows and focus more on international activities and thus generate more revenue. The majority of Netflix's revenue currently comes from the US & Canada market, but with increased competition in the region we believe Netflix will have more success focusing on their international markets.

Revenue History







Revenue Breakdown by Region

Region	% of Total Revenue		
	2019	**2020**	**2021**
United States and Canada (UCAN)	50.61%	46.27%	43.95%
Europe, Middle East, Africa (EMEA)	27.91%	31.39%	32.86%
Latin America (LATAM)	14.08%	12.75%	12.12%
Asia-Pacific (APAC)	7.40%	9.58%	11.07%

The charts above give visual to how Netflix's revenue has been distributed in their 4 markets over the past 3 years. The pie chart of 2019 compared to 2021 shows a big story in growth. Although the revenue numbers continue to increase in each region, revenue coming from international regions (EMEA, LATAM, APAC) have become a higher percentages of Netflix's total revenue. In 2019, the UCAN region accounted for 50.61% of total revenue. By 2021, the region accounted for 43.95%. This proves that Netflix's efforts to increase presence in international markets is increasing their revenue at a greater rate than we are seeing domestically. Regardless of optimism, we expect this trend to continue as Netflix grows more into these international regions.

Scenario Analysis

Our pessimistic and optimistic scenarios for Netflix were mostly based on international subscriber growth. Of course, we included US subscriber growth in the calculations, but they were not the main driver of the results since the international subscriber base has a lot more room for growth. Another thing that was included in our calculations was the introduction of the password sharing add-on fee of ~$3 that Netflix has been testing out in a few countries in recent months. One of our growth opportunities that we see for Netflix is its entry and future growth in the video game development market. However, we decided not to include this into both of our scenarios because this is something that Netflix has only recently started and calculating its potential profits and effect on Netflix seem nearly impossible since Netflix has not released any detailed plans about what the future of company looks like regarding video games.

Our baseline scenario consists of Netflix growing its subscriber base at a rate that was calculated by taking the projected growth of the SVOD market multiplied by one plus the decrease in Netflix's market share of each year. We assumed that Netflix would continue to lose market share at an increasing rate of the previous year's percentage change in market share plus 0.98 percent. That 0.98 percent came from the change in loss of market share from 2020 to 2021. The scenario also factors in the 200,000-subscriber loss reported in the Q1 earnings call and the 2,000,000 projected loss for Q2. Since Netflix did announce in their earnings call that they will be cracking down on password sharing soon, that has also been included. They stated that there are currently 100 million people who are using their services and not paying (leeches). They are planning to give those people the choice to either pay $3 to become part of the person's plan that they are using or get their Netflix privileges revoked. We assume in our baseline scenario that 20% of those leeches will start to pay. The revenue generated from that kicks in halfway through 2023 because that is when we are predicting that Netflix will roll out that additional fee since they said in their Q1 earnings call that it will take a little over a year from them to get it rolled out. That revenue is also added in every year after that since it is a recurring monthly fee for those users. The average price of subscriptions grows at different rates depending on the region. Those rates were calculated by taking the average yearly growth of their subscription prices over the past two years. You can see our projections for our baseline scenario below broken down by region.

US & Canada (UCAN)					
	2021	**2022**	**2023**	**2024**	**2025**
Number of Subscribers (Millions)	74.23	73.59	75.48	77.04	78.28
% Change in Subscribers	-	-0.87%	2.58%	2.06%	1.60%
Avg. Cost of Subscription	$14.56	$15.57	$16.65	$17.81	$19.05
% Change in Subscription Price	-	6.95%	6.95%	6.95%	6.95%
Avg. Yearly Rev./User	$174.72	$186.87	$199.86	$213.75	$228.61
Yearly Rev. From Account Sharing Fee (Millions)	-	-	$149.40	$298.80	$298.80
Yearly Revenue (Millions)	$12,972.10	$13,751.36	$15,235.55	$16,766.07	$18,193.39

Europe, Middle East, Africa (EMEA)					
	2021	**2022**	**2023**	**2024**	**2025**
Number of Subscribers (Millions)	69.52	72.10	78.88	84.43	88.84
% Change in Subscribers	-	3.72%	9.39%	7.04%	5.23%
Avg. Cost of Subscription	$11.63	$12.28	$12.96	$13.69	$14.45
% Change in Subscription Price	-	5.58%	5.58%	5.58%	5.58%
Avg. Yearly Rev./User	$139.56	$147.34	$155.56	$164.24	$173.40
Yearly Rev. From Account Sharing Fee (Millions)	-	-	$95.68	$191.36	$191.36
Yearly Revenue(Millions)	$9,699.82	$10,624.17	$12,365.58	$14,057.72	$15,596.50

Latin America (LATAM)					
	2021	2022	2023	2024	2025
Number of Subscribers (Millions)	38.57	38.42	40.86	42.86	44.45
% Change in Subscribers	-	-0.40%	6.35%	4.90%	3.71%
Avg. Cost of Subscription	$7.73	$7.88	$8.04	$8.20	$8.36
% Change in Subscription Price	-	1.99%	1.99%	1.99%	1.99%
Avg. Yearly Rev./User	$92.76	$94.60	$96.48	$98.40	$100.36
Yearly Rev. From Account Sharing Fee (Millions)	-	-	$45.06	$90.12	$90.12
Yearly Revenue (Millions)	$3,576.98	$3,634.67	$3,987.39	$4,307.77	$4,551.26

Asia-Pacific (APAC)					
	2021	2022	2023	2024	2025
Number of Subscribers (Millions)	28.46	34.35	39.41	43.55	46.85
% Change in Subscribers	-	20.71%	14.71%	10.52%	7.57%
Avg. Cost of Subscription	$9.56	$9.70	$9.85	$10.00	$10.15
% Change in Subscription Price	-	1.51%	1.51%	1.51%	1.51%
Avg. Yearly Rev./User	$114.72	$116.45	$118.21	$120.00	$121.81
Yearly Rev. From Account Sharing Fee (Millions)	-	-	$43.46	$86.92	$86.92
Yearly Revenue (Millions)	$3,266.60	$4,000.61	$4,701.97	$5,313.32	$5,793.68

Our pessimistic and optimistic scenarios involve nearly all the same information, but the numbers are just slightly different. For example, in our pessimistic scenario we assume that the SVOD market grows 3% slower than expected, Netflix's market share shrinks at a rate twice as fast as the normal scenario (-1.86%), they lose more subscribers in 2022 than they projected, and only 10% of leeches choose to pay the additional $3 add-on charge. In our optimistic scenario we assume that the SVOD market grows 3% faster than expected, Netflix doesn't lose market share after 2023, they lose less subscribers in 2022 than they projected, and 30% of leeches choose to pay the additional $3 add-on charge. These small changes have a large effect on subscriber numbers and revenue projections. Underneath are the projected subscriber numbers for each scenario.

Netflix Projected Subscriber Numbers (2021 Data from NFLX Financial Statements) (Pessimistic Scenario)

YEAR	**2021**	**2022**	**2023**	**2024**	**2025**
UCAN	74,234,000.00	72,431,686.86	73,569,247.36	74,309,901.19	74,709,041.92
EMEA	69,518,000.00	70,683,100.69	74,746,509.48	77,392,152.74	78,817,898.41
LATAM	38,573,000.00	37,720,128.31	39,184,507.14	40,137,948.98	40,651,761.86
APAC	28,461,000.00	32,581,839.37	35,615,334.05	37,590,410.93	38,654,786.21
TOTAL	**210,786,000.00**	**213,416,755.22**	**223,115,598.03**	**229,430,413.84**	**232,833,488.39**

Netflix Projected Subscriber Numbers (2021 Data from NFLX Financial Statements) (Normal Scenario)

YEAR	**2021**	**2022**	**2023**	**2024**	**2025**
UCAN	74,234,000.00	73,589,276.38	75,484,706.30	77,039,580.93	78,275,460.52
EMEA	69,518,000.00	72,104,912.23	78,875,459.01	84,429,529.50	88,844,137.77
LATAM	38,573,000.00	38,419,968.59	40,859,950.84	42,861,537.11	44,452,481.85
APAC	28,461,000.00	34,354,016.08	39,408,495.88	43,554,828.22	46,850,507.13
TOTAL	**210,786,000.00**	**218,468,173.28**	**234,628,612.03**	**247,885,475.77**	**258,422,587.28**

Netflix Projected Subscriber Numbers (2021 Data from NFLX Financial Statements) (Optimistic Scenario)

YEAR	**2021**	**2022**	**2023**	**2024**	**2025**
UCAN	74,234,000.00	74,746,865.90	77,422,791.82	80,194,316.52	82,736,939.45
EMEA	69,518,000.00	73,526,723.77	83,085,231.52	92,985,221.72	102,067,566.19
LATAM	38,573,000.00	39,119,808.87	42,564,521.69	46,132,298.59	49,405,410.79
APAC	28,461,000.00	36,126,192.80	43,261,995.24	50,652,727.79	57,433,055.59
TOTAL	**210,786,000.00**	**223,519,591.34**	**246,334,540.27**	**269,964,564.62**	**291,642,972.02**

EPS Projections

		EPS				
Scenario:	TTM	2021	*2022*	*2023*	*2024*	*2025*
Baseline	11.24	11.47	11.83	13.15	13.96	15.33
Low growth/pessimistic	11.24	11.47	11.74	12.54	12.96	13.9
High growth/optimistic	11.24	11.47	12.22	14.13	15.62	17.79

The major assumptions made in calculating EPS, besides what is stated in the previous sections, are the following: Netflix is not buying back any shares but increasing at the 4-year average rate of .29%, Netflix's net profit margin remains unchanged from 2021, and the DVD sales keep declining at the same rate as 2021. Although, the company approved of a 5 billion share buyback program with no expiration date, the projections were left growing at the .29% rate to be conservative with shares outstanding and therefore the EPS. The company's net profit margin has been increasing quarter over quarter for years, however leaving it at the most recent year's average of ~17% allows for a conservative estimate of future earnings. Finally, the DVD/other revenue business has been declining year after year with the sharpest decline from 2020 to 2021, and since it is not a major part of the business (less than 1% of revenues) the rate of decline was left at 25% year over year.

The third and possibly most intriguing opportunity for Netflix is their newly developed gaming service. In November 2021, the company announced they would be developing a mobile game service available to Android and iOS customers with games based on their original series like Stranger Things and other casual games. In their most recent earnings call, co-CEO Reed Hastings said “"We have to be differentially great at it, there's no point of just being in it,". Netflix is strongly committed to developing its gaming service and plans to rival larger platforms like Microsoft and Sony. Netflix plans to develop and release more games on to the platform throughout 2022. The gaming industry is projected to be one of the fastest growing industries over the next few years with some projections predicting the industry to be worth $300 billion in 2025. All Netflix subscribers are granted access to this service, which could help stimulate new subscriber growth and retain customers through price increases. The expansion from being strictly a streaming service to a multi-entertainment platform gives Netflix an opportunity to develop revenue streams in two of the largest and fastest growing markets today.

Key Financial Information

Industry Averages:

P/E - 58.17

P/B - 4.3

ROE TTM – 7.46%

ROA – 3.33%

NPM TTM – 8.62%

3 Year EPS – 22.57

Netflix (NFLX)

	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	TTM
P/E	26.05	32.90	30.63	73.46	33.33	31.02
P/B	12.37	11.95	11.54	11.06	10.49	9.77
ROE	13.25%	9.76%	9.46%	3.83%		38.02%
ROA	4.25%	3.30%	3.39%	1.36%		9.23%
NPM	23.82%	18.43%	19.36%	7.87%	17.23	17.23%
P/S	5.99	5.98	5.98	5.99	5.74	5.35
EPS	3.75	2.97	3.19	1.33	3.53	11.24
PEG	2.38	1.63	1.50	1.48	1.76	1.6

	Year of 2019	Year of 2020	Year of 2021
P/E	103.71	87.36	54.32
P/B	18.40	22.51	17.77
ROE	24.62%	24.95%	32.28%
ROA	5.49%	7.03%	11.47%
NPM	9.26%	11.04%	17.22%
P/S	7.37	9.83	9.23
EPS	4.13	6.08	11.24
PEG	2.23	2.29	1.48

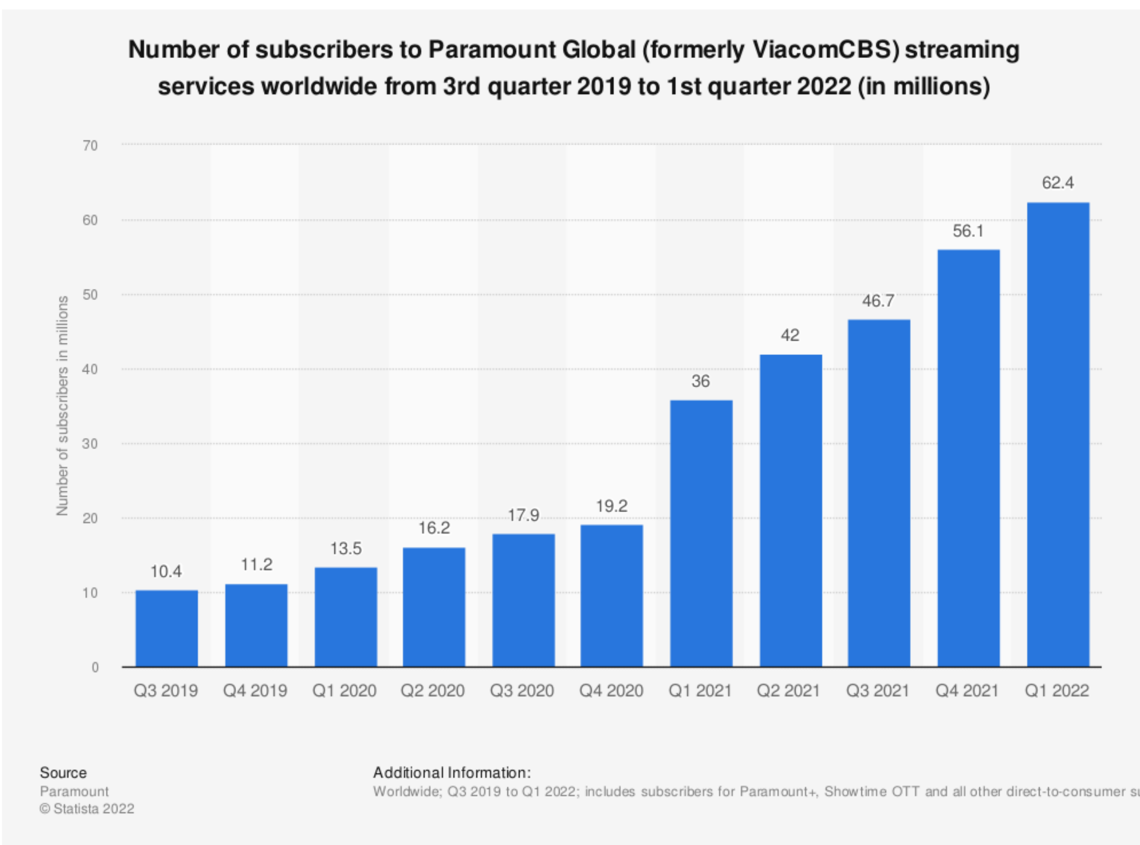
One takeaway from these ratios is the decreasing P/E ratio that can been seen over the past 3 years. When looking at a stock that is undervalued to a strong buy, low P/E is an important factor. Netflix's stock price has decreased by a great amount in the last year and a half, and its P/E ratio has been reflected by that performance. Although both the P/E and P/B ratios aren't as low as they could be, Netflix's future growth opportunities highlighted earlier are strong enough to generate profits and increase the future stock price. Going along with this, another important piece to note is Netflix's net profit margin. We have seen an increase in this margin from 9.26% to 17.22% from 2019 to 2021 and a TTM margin of 17.37%. Compared to the industry average of 8.62%, Netflix is still generating more profit than their competitors even though their stock price has declined over the past year. This can be attributed to unique platform factors such as "Netflix Originals" shows that are exclusive to Netflix's platform. As Netflix does not pay dividends, we expect the company to continue to reinvest profits into areas that are poised to grow in the future and generate return for shareholders via increasing overall value and NFLX stock price.

Key Competitor Financial Information

2021 Financial Ratios	Paramount Global (PARA)	Roku (ROKU)	Netflix (NFLX)
P/E	5.55	74.26	54.32
PEG	.76	N/A	1.48
P/B	1.92	6.133	17.77
ROE	20.27%	8.76%	32.28%
ROA	7.74%	5.94%	11.47%
NPM	15.89%	8.77%	17.22%

D/E	1.59	.475	1.81

The biggest competitors of Netflix are other streaming services such as Hulu, Disney+, and HBO Max. It would however be redundant to analyze and compare the financial ratios of Disney, for example, to Netflix because of the multiple streams of revenue that Disney has. They are much more than a streaming service. Paramount Global and Roku are both companies in the entertainment industry that still pose a threat to the success of Netflix. The high D/E ratio is driven by NFLX's large amount of liabilities. By taking out these liabilities, Netflix can pump out wide varieties of content for their viewers in hopes of gaining more subscribers. It is clear these efforts are successful in terms of profitability, as they report a higher net profit margin of 17.22% than these two competitors and the rest of the entertainment industry.



The graph on the previous page shows Paramount's increasing presence in the streaming industry. In just the 4th quarter of 2021, their total number of subscribers increased by 9.4 million. Although Netflix reported a larger increase of subscribers for this period, Paramount's presence still cuts into these numbers. This is key because subscription costs are the only source of revenue for Netflix.

Valuation

Using the free cash flow method to estimate the stock price of Netflix yielded results that were nearly three times the price that it is currently trading at in the NASDAQ market. Our result from the FCFF method was a stock price of $668.98 while our result from the FCFE method was $698.68. That makes the average of the FCF method a stock price of $683.83, which is 218.06% higher than the current stock price of $215.00.

It seems that the high profits and high amount of depreciation are what is causing the FCFE method to yield results that are so much larger than the current stock price. Those same things combined with low interest expenses and low capital spending are what cause FCFF to rise to a similar level. However, Netflix plans to continue investing heavily in production studios and original content creation which may affect capital expenditures in the future.

The P/E method estimated the stock price to be $228.48, which is closer to the current price of Netflix but still an upside of 25.53%. The target price that we determined for Netflix was $270.11 which has a 48.41% upside. The weights that we decided to use when determining our target price were 0.9 for the P/E method and 0.1 for the FCF method. We decided to weigh our target price like this since the P/E method price was significantly closer to the current price of Netflix and we wanted to be conservative with our results so that our recommendation to buy, sell, or hold would be more reliable. With that being said, we believe that Netflix appears to be a buy given the current assumptions and projections. We recommend buying 52 shares which would be $9,464 and about 2.4% of the fund. Our price estimates are included underneath along with our estimates for both our pessimistic and optimistic scenarios.

NFLX Price Estimates

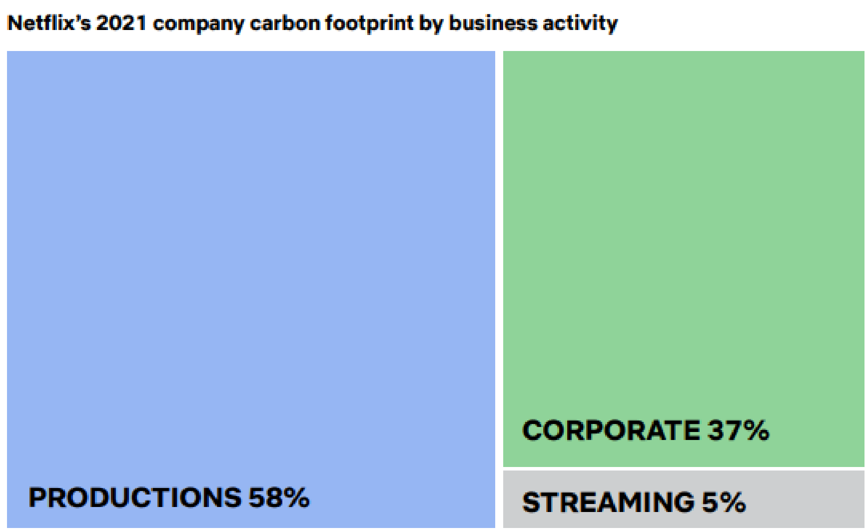
FCFF	**FCFE**	**FCF (Avg.)**	**P/E**	**Target**	**Current**
$629.08	**$660.46**	**$644.77**	**$228.48**	**$270.11**	**$182**

Scenario:	**FCFF Valuation**	**FCFE Valuation**	**FCF Valuation (0.5FCFF +0.5FCFE)**	**1-year ahead P/E Estimate**	**P/E Method Valuation**	**Combined Target Price**
Baseline	629.08	660.46	664.77	21	228.48	$270.11
Low growth/pessimistic	558.85	585.84	572.35	15	125.10	$169.82
High growth/optimistic	708.15	743.41	725.78	30	365.70	$401.71

ESG

Environmental

In their most recent 2022 Q1 earnings report, Netflix reported that they have made "good progress" in their climate commitments announced last year. This goal allowed Netflix to reduce more than 14,000 metric tons of emissions in 2021 which reduces their carbon footprint by more than 10%. They are on track to eliminate 45% of emissions by 2030. As an entertainment company, over half of Netflix's carbon footprint comes from the physical product of content. The rest of their carbon footprint is seen in the figure below.



Social

Netflix has made the most positive impact in their social ESG aspect through inclusion and diversity among employees. They have put emphasis on this aspect by publishing their first inclusion report in January 2021 and showing progress in their updated report February 2022.

- Women make up 51.7% of global workforce, up from 48.7% in 2020
    - Includes 6.9% growth of women directors and above

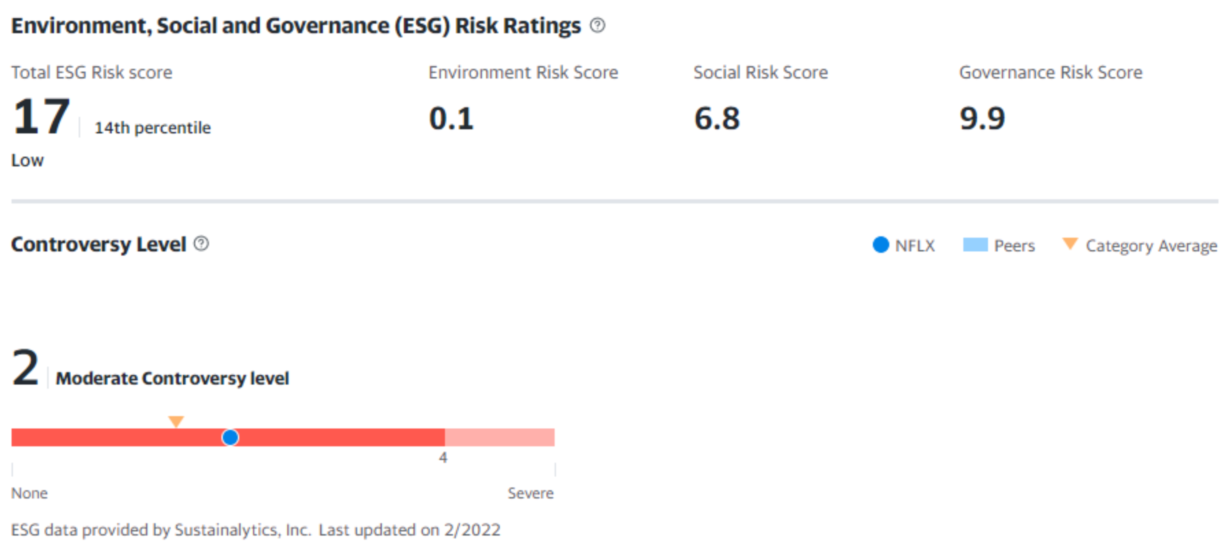
- 50.5% of US workforce is made up of people from racial backgrounds, up from 46.8% in 2020
- Number of Black US employees increased from 8.6% - 10.7% and Black leadership (directors and above) increased from 10.9% - 13.3%
- Number of Hispanic/ Latino employees increased slightly from 7.9% - 8.6% and leadership grew from 4.3% - 4.4%
- Of 22 leaders on senior leadership team, ten (45%) are women and five (22.7%) have historically excluded/ racial backgrounds

Netflix has also improved their overall culture around inclusion by expanding their inclusion strategy team to international markets such as Latin America, Asia-Pacific, Europe, the Middle East, and Asia. This diversification should help Netflix grow into these markets even more in the future as they are expected to contribute more towards overall revenue each year as the United States and Canada market slows down.

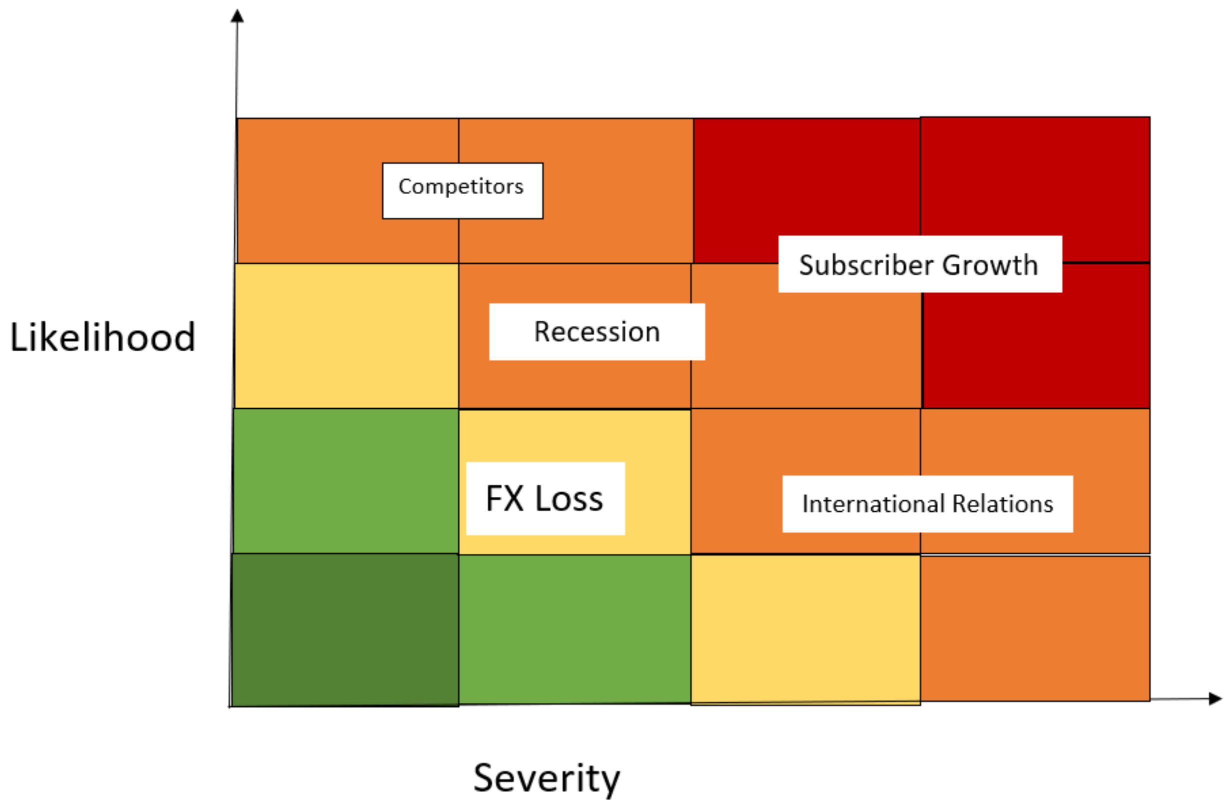
<u>Governance</u>

Netflix has eight board members and ensures that the proper checks and balances are in place between the board, shareholders, and management. Over half of the board members are also independent directors, which means they don't have an official relationship with Netflix. This helps eliminate bias within the company, so the most appropriate decisions are made. There are three board members who have been added since 2010. This is important as there isn't a high turnover rate in this area, so all members work well together and share the same vision for Netflix. The 2021 ESG report details that with the scaled revenues, operating profit, and margins, the Board decided to evolve to a more standard large-cap governance structure. They will be recommending several changes at the 2022 ESG meeting. This all proves Netflix is constantly adapting to the changing industry as they look to continue growth and dominate the entertainment industry. One potentially risky factor within Netflix's governance is CEO Reed Hastings. He has an outspoken history and can create some negative attention with vulgar statements. However, as he has been the CEO since 1998, we don't see this substantially risky.

Our overall ESG rating for Netflix is **favorable.** Netflix has stayed relatively quiet from negative buzz since they were founded in 1997. There is always a risk of controversy within content as they look to expand into foreign markets – but their increased focus on inclusivity specifically helps reduce this risk. We look forward to the expansion of Netflix as a company both revenue and ESG wise. Yahoo! Finance ESG ranks for comparison are listed below.



Risk Matrix



Netflix faces 5 major risks:

- Subscriber Growth- Netflix posted its first loss in total global subscribers in over a decade in their Q1 earnings report. They also projected a loss of 2 million for Q2 and a net loss for 2022. While already being the highest priced SVOD service, facing increasing competition, and projecting more price increases in the future, Netflix will need to find ways to justify their higher prices beyond original content or face continued losses in subscribers.
- Recession- With high inflation and interest rates expected to rise, the economy could face recessionary conditions in the coming months and Netflix may be vulnerable to subscriber loss if consumers must cut back on expenditures.

- Foreign Exchange Loss- Netflix does large amounts of business outside of the US and estimated they lost roughly 3% of annual revenue in 2021 due to FX. They plan to recover those losses over 2022 but will need to monitor exchange rates and its effects in the future.
- Competition- As mentioned above the streaming industry is becoming more and more saturated, and Netflix is likely to lose some of its market share to other companies. However, Netflix has such strong brand recognition and company structure that with proper management they should be fine.
- International Relations - Expansion into international markets is the major growth opportunity for Netflix in the next few years and with foreign governments looking to promote their own companies, Netflix may have to operate under stricter regulations in order to provide service to these audiences. As seen in Q1, Netflix lost 700,000 Russian subscribers after temporarily removing the service following the invasion of Ukraine and should be able to recover a sizeable amount of these subscribers when the conflict resolves.

Portfolio Fit

Partial Correlation Matrix for Netflix

SAP	.14	GOOGL	.25	INTC	.34
PG	.17	JNJ	.26	BKNG	.34
UNP	.20	HEAR	.26	AAPL	.40
CVS	.20	NEE	.27	AMT	.40
PFE	.21	SBUX	.27	MA	.40
NXST	.21	PRU	.27	AMAT	.422
KO	.22	QCOM	.28	DIS	.44
BA	.23	UNH	.29	GM	.48
JPM	.23	EMR	.30	RIO	.53
FB	.24	PYPL	.32	ADBE	.55

We conducted a correlation analysis using the monthly returns of Netflix compared to the rest of the stocks in the Gordon Spellman Portfolio dating back to 4/28/2017. Netflix is part of the entertainment industry in the communication services sector. Netflix's monthly returns are most highly correlated with the technology, financial services, and communication services companies listed above. That includes Adobe, Disney, Meta Platforms, SAP, and Mastercard. This high correlation in returns over the past 5 years may be because of the heavy reliance in advancements of technology and change in consumer tastes, especially since the initial Covid outbreak in March 2020. Netflix is least correlated with healthcare, consumer defensive, and consumer cyclical companies. Specific companies in the Spellman Fund are seen in the table above which includes CVS Health, Coca-Cola, Starbucks, Pfizer, and Johnson & Johnson.

Final Recommendation

After extensive research, we believe that Netflix's opportunities both domestically and internationally in the streaming industry will provide long term growth for the company. The recent decline in stock price following the Q1 earnings report on April 19th, 2022 provides the fund with a great opportunity to capitalize on Netflix's historically low stock price that is trading at a lower P/E ratio than the company has seen since its initial listing. We recommend purchasing 52 shares of Netflix at approximately the current market price of $180. We also recommend selling 15 shares of Adobe in accordance with the presenting group and high correlation, as well as selling 30 shares of Disney due to the high correlation and increasing competitiveness in the streaming industry. Calculations and thorough analysis reveal a baseline target price of $270 which would provide a return of 48% for the Gordon Spellman Fund.

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