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Final Project: Netflix

Introduction

This paper will focus on Netflix as a company in the streaming video on demand services industry and provide strategic recommendations to key issues. Netflix is an American subscription video on-demand streaming service that was founded in 1997 by Reed Hastings and Marc Randolph. Their initial idea was to rent DVDs by mail, which transformed into a successful subscription model in 1999. After going public in 2002, Netflix issued a patent to cover subscription rental services. In 2007, they introduced streaming to allow viewers to instantly watch content without having to wait for a rental DVD. They began creating original content in 2013 and won three Primetime Emmy awards that year for House of Cards. By 2016, they had reached 190 countries and provided content in 21 languages. In 2022, they launched an in person festival and created a lower-priced ad-supported plan in 12 countries.

The key problem that we are focusing on is Netflix's narrow revenue channel. We recommend that Netflix diversify its offerings on its platform and make changes to its pricing structure to alleviate the issue.

Industry Analysis

Netflix is a player in the entertainment industry, specifically focusing on streaming video on demand services. Other major companies in this segment are Disney+, Paramount+, Amazon Prime Video, HBO, Apple TV+, and Hulu. In order to better understand the dynamics driving competition in the industry, one can employ Porter's Five Forces Model.

Barriers of entry strongly indicate fierce competition. Maintaining a streaming video on demand service platform requires high operational costs in order to ensure each user's experience is as streamlined as possible. It is also essential to maintain user privacy on these sites. Technology is constantly changing which requires the platforms to adapt to the current trends. Advertising requires data analysts who can examine viewer trends and suggest the most effective ads. Although these companies have been advertising since their initiation, it is finally projected that in 2023 advertising spending is expected to surpass revenue in the United States. A decrease in customer spending has caused the growth rate to decline. From 2021 to 2022, the percentage of new viewers decreased from 10.6% to 5.4% and is projected to continue decreasing to 2.8% in 2026. The high costs coupled with a chance at lower revenue is perhaps the largest barrier for a new company to enter the streaming video service industry.

There is strong competition between rivals in the field. Most, if not all, of the companies mentioned previously are closely affiliated with a production studio. When it comes time for

these companies' movies to be brought to a home audience, they only release it on their platform. Disney+ was released in November 2019 yet they had already terminated their contract at the beginning of that year. Through future acquisitions, it is possible for market positions to consolidate and strengthen a few key players rather than have a wider range of smaller companies.

The threat of substitutes also increases competition in the industry. Substitutes for streaming video on demand services fall under two categories: social media user generated video content or cable and broadcast television. In 2022, streaming video on demand services surpassed cable and broadcast television revenue. Streamers also started to offer ad-supported live television for cheaper rates than traditional cable. Hulu with Live TV costs users $70 monthly whereas cable averages to $140 monthly. This encourages users to turn to streaming video on demand platforms as it will help them reduce costs while also getting to select channels that are best suited to their preferences. The other extreme lies with social media user generated video content, which allows viewers the utmost personalized viewing experience. This content comes from videos, images, and blog posts and can be posted on platforms such as YouTube, TikTok, and Instagram. This segment is a larger threat since it is more accessible and cheaper than subscribing to a streaming platform. A final threat of substitute comes from live entertainment. Revenues from concerts, sporting events, and other in-person entertainment experiences increased from $66.6 billion in 2019 to $68.7 billion in 2024 and is expected to increase another 9.6% through 2027.

Supplier power has a mild effect on industry competition. As mentioned previously, companies tend to only supply their content to one platform, usually the one it is most closely affiliated with. Another set of key suppliers are advertisers. They must be convinced to collaborate with the streaming company so that ad revenues can offset subscription prices and amount spent on content. This would hopefully reflect onto viewers by decreasing their monthly fees. The declining production and distribution costs would also help alleviate this issue.

Buyers have strong power in the industry. Audiences are not loyal to only one service, and many subscribe to more than one platform since switching between them is no harder than clicking a different app icon. This is indicative of low switching costs. It is also incredibly easy for users to cancel a subscription. The companies must put their users first when implementing new features. The newest trend points towards more interactive experiences, similar to gaming platforms.

An interesting complement to streaming video on demand services is the use of artificial intelligence. From a supplier perspective, it can be used to deliver highly specialized advertisements based on a buyer's internet history. From a buyer perspective, it can be used as a more efficient search engine that can suggest accurate recommendations based on time of day, tastes in previous movies, and other factors.

Through Porter's Five Forces Model, it is evident that the streaming video services segment of the entertainment industry is a highly competitive space that is not conducive for new

entrants and favors established companies that can quickly adapt to dynamic changes in technology.

Internal Company Analysis

Netflix's business strategy is focused on providing a diverse range of high-quality entertainment to a global audience through its user-friendly platform. As an industry giant, Netflix competes with various strategies to prevent the loss of market share within its industry.

Using Porter's Five Forces Model allows for the understanding of key forces that influence industry profitability, such as rivalry and buyer power in the streaming video-on-demand industry (SVOD). Netflix strategically competes in the SVOD industry by using vertical integration in content production as a primary cost driver, aimed at enhancing profitability and gaining a competitive advantage.

In Netflix's value chain (Figure 2), its in-house content production and content acquisition activities are categorized as integral activities of the company's procurement processes. Netflix's procurements come in two forms; partnerships with different production houses as media suppliers and original in-house content. Both sources of media content contribute to delivering superior value to customers. Third-party licensing agreements are critical to Netflix's diversified library and increased customer satisfaction. However, specific content-licensing partnerships within the SVOD industry often demand substantial costs. For example, in 2019, Netflix outbid competing firms to secure five-year contracting rights to 'Seinfield', with a deal exceeding $500 million. These content licensing agreements act as short-term competitive advantages (Figure 3).

As part of its vertical integration efforts, Netflix utilizes its own production house to supply its original media. Since 2012, Netflix has released over 3,750 original titles. Over time, Netflix invested heavily in partnerships with top producers, actors, and writers that users would value. Examples of deals included the $300-million five-year contract with Ryan Murph and the exclusive partnership with Shonda Rhimes, Grey for exclusive content. to have her own series. This commitment to original content has resulted in a competitive advantage for Netflix, as seen in the industry's demand trends. In 2022, seven of the top 100 most in-demand TV series were Netflix originals. In Q4 of the same year, Netflix achieved an industry-leading 40.9% in U.S. demand share for all steaming originals. Fans of Netflix's unique content extend globally, with Netflix originals having a stronger demand globally than in the U.S. in 2022. However, competitors such as NBCUniversal, Disney+, and Paramount possess a competitive advantage due to their ability to rerun content with their established networks to create a willingness to pay (WTP) while decreasing costs, or selling licensing contracts. Even newcomers to the industry, such as AppleTV and Amazon Video, are investing in original content. Despite joining the content production game later than rivals with historical advantage, Netflix maintains its lead in demand share for original content. This success could be attributed to strategic decisions within Netflix's value chain, benefitting from its status as a first-player, or its independent approach compared to partnered media companies.

The procurement activities of Netflix's production house widen the wedge between customer WTP and the company's operating costs. Despite substantial upfront costs associated with in-house production, investments contribute to creating a long lifespan for content, benefitting the company in the long run. This strategy proves to be a sustainable competitive advantage (Figure 4).

Continuing the assessment of its value chain, activities within Netflix's marketing processes build a competitive advantage. A distinctive activity involves integrating various activities together to cultivate a strong brand image, establishing a competitive advantage for Netflix. The company has hosted various immersive experiences tied to its original content, such as the Bridgerton-themed ball, fostering a deeper connection between users and the value Netflix offers. These events offer a linkage between different activities within the company's value chain and present an opportunity to enhance customer WTP. As the synergy among activities strengthens, the potential for replication decreases, positioning this strategy as a competitive advantage for Netflix. This strategy fits into the VRIO framework, offering a unique experience for watchers. However, with the likelihood of costs rising as WTP increases, Netflix must strategize to widen the gap between the two. However, because costs will likely rise with WTP, Netflix must ensure an effective strategy to widen the gap between the two.

Netflix's strategic positioning revolves around innovation and user-friendly experiences. The company's mission emphasizes continuous personalization and content recommendation through a seamless subscription model, adding value to the technological development activities within its value chain. Rather than a streaming-video-on-demand service, Netflix positions itself as an entertainment service company that offers movies, TV series, and games – distinguishing itself from competitors.While this contributes to Netflix's differentiation, these activities are not strong enough to prove a sustainable competitive advantage outside of an imitable operational advantage that might erode any advantages accrued. In a Netflix Investor article, the company states,

"Netflix is a focused passion brand, not a do-everything brand: Starbucks, not 7-Eleven; Southwest, not United; HBO, not Dish. We are not a generic "video" company that streams all types of video such as news, user-generated, live sports, and music videos. We are a movie, TV series, and games entertainment service."

Netflix utilizes a needs-based positioning strategy, tailoring activities to meet the varied preferences of its customer segments globally. Recognizing the diverse preferences of its customer base, Netflix adopts a customer-centric approach, acknowledging varying levels of price sensitivity, media preferences, and information needs among its global target audience. When thinking about tradeoffs, Netflix opted against partnerships with other SVOD industry leaders to delve into live sports streaming, a move like Hulu's Live TV partnership. Though this decision could have been a profitable opportunity, Netflix's choice of saying "no" helped the company differentiate itself and increase WTP for their very first sports event in November 2023, "The Netflix Cup. The new edition of Netflix's original live content within its procurement activities has enabled the company to add more value to its production house, establishing a

competitive advantage. While there will be an increase in costs for production, Netflix must strategize and plan how to prove great value and competitive advantage with the increased WTP. This strategic move highlights Netflix's ability to innovate.

Key Strategic Problems

As one of the leading streaming services, Netflix has the burden of facing and solving multiple problems in order to remain a top player. One such issue that companies within the streaming industry face is a stagnant revenue model. Streaming services differentiate themselves by supplying various on-demand video content for a cheaper-than-cable monthly payment. However, their dependency on user subscriptions confines the industry to only a few revenue channels that won't disrupt the qualities that made the service unique in the first place. Therefore, it is only a matter of time before Netflix depletes all or majority of its possible income streams from paid user subscriptions.

Netflix currently operates with a total of four different subscription plans. The lowest cost plan, titled "Standard with Ads," is $6.99 per month and is the newest addition. There is also the Standard Plan at $15.49 per month which features no ads and full HD content. The Premium Plan is $22.99 per month and includes ultra HD content and the ability to watch on 4 devices at a time as one of many additional benefits. The last one is their Basic Plan which does not include ads for a lower HD quality than the Standard Plan. It should be noted that the Basic Plan has been discontinued for new members but remains available for customers who previously used it. These existing customers pay $11.99 per month for the plan while new or rejoining customers must decide between the cheaper ad-supported plan and the two higher-cost plans. The pricing for the Basic and Premium plans is relatively new and marks another price hike of around $2 to $3 since the last hike in 2022.

As mentioned, the rollout of an ad-supported plan this year was Netflix's attempt to introduce another revenue source. With the new plan introduction, ads and paid subscriptions have become the two revenue channels for the company. The opportunities within these channels are extremely limited. On the subscription side, their options are to segment new plans for specific target markets or to increase prices. However, differentiating plans becomes harder as the number available increases, leading to redundancy. Additionally, raising prices too often without a unique factor to compensate will push customers away.

Currently, Netflix has not experienced the full limitations of its small revenue channels. The company reported an estimated $8.54 billion in revenue for Quarter 3 of 2023, which is its highest quarterly earnings to date. This has been attributed to their ad-supported plan and around 17 million new subscribers since 2022. Despite a sluggish start, Netflix now reports that their ad-tier subscriptions are growing around 70% each quarter. Around 30% of new subscribers are purchasing the ad-tier plan. Furthermore, part of these new subscribers come from Netflix's new "password sharing" rule. Netflix accounts must be shared only by members of the same household in the same location. Customers on the Standard plan are able to add an extra member outside the household for an additional $7.99 per month while the Premium plan allows for 2

extra members at the same price option per extra person. This year's successful results in new subscribers and revenue follow the timing of the ad-supported plan's introduction and password-sharing rule, making Netflix believe they made the right decisions to increase profits.

Unfortunately, there are various factors that suggest these numbers could easily plateau. With lingering inflation in the economy, consumers are undoubtedly not excited about the increase in prices. A survey of 2000 adults by Vorhaus Advisors states that of the Americans who canceled a streaming service recently, 37% had chosen to cancel Netflix. This suggests that Netflix is the first streaming service to be cut, ironically due to the fact that it is the largest player. Money is typically the strongest factor in making this decision, which would ultimately bring Netflix into a tough position of raising prices for profit while risking the loss of customers. Additionally, there is a general slowing of customer attraction. Only 1.75 Million new customers were added in the first quarter of 2023. The uptick in subscribers in the following quarters is enough to make up for this moment of slow growth, but it can also be due to the end of password sharing. Therefore, it is hard to tell if Netflix is attracting customers or simply bringing out "hidden" users who were encompassed into another household. Nevertheless, the service has a theoretical number of maximum possible consumers. There are 77.32 Million Netflix subscribers in the U.S. and Canada. There are roughly 135 Million households in both countries combined. Not taking into account age and access to technology, Netflix has already garnered a decent amount of consumers from the two countries. They may increase the number of paid users but will eventually be confined to asking for certain prices from all of them that can't be easily increased for more profit.

Another emerging problem for Netflix is the increase in competition. Following the lifecycle of a product, it can be said that the streaming industry is reaching or has already reached the maturity stage. The market is highly saturated at the moment and many of Netflix's competitors have high brand recognition. At this stage, companies must work on differentiating themselves and increasing a buyer's willingness to pay by creating value. It is at the point where major players are already merging with each other to bring new value and lower costs. For instance, HBO Max and Discovery Plus merged earlier this year into Max. Meanwhile, there are also plans for Disney+ to merge with Hulu. This is able to be done because Disney+ and Hulu fall under the same parent company, similar to HBO Max and Discovery Plus. These mergers then reduce the attraction of Netflix. Since Netflix is its own parent company, they are unable to perform this kind of merger that would combine resources and reduce costs, giving them less of a competitive edge.

Netflix must then battle its competitors on content and price. With saturation in the market, many consumers are feeling streaming fatigue and generally believe that there are too many services available. Therefore, companies need to differentiate themselves even more to not be seen as just another streaming service. Netflix is not the cheapest option available, but it can be considered within the range of its competitors. However, they should be wary of their competitors attracting customers with lower prices. Furthermore, Netflix is dependent on its original content to draw in viewers. Their competitor, Disney+, benefited from their huge catalog

of previous, original content when they launched their services. However, Netflix faces the challenge of creating brand-new shows that will retain customers.

There are many difficulties in creating content that will resonate with the greatest number of people, but pre-made content comes with its own challenges that Netflix must balance. Original content is expensive. Netflix as a studio must put forth large amounts to pay for the development, filming equipment, cast, etc. of each show or movie. The Co-CEO of Netflix, Ted Sarandos, stated that Netflix will spend around $17 Billion on content for next year, similar to the spending in 2023. Meanwhile, Disney will spend around $30 Billion on all content it produces, not just for streaming. These costs eat up Netflix's revenue. Netflix has had great success with some of its originals, such as Stranger Things, Bridgerton, and Squid Game. However, there are lots of other original Netflix content that either fail or receive only moderate success. Pairing this with the fact that the content faces depreciation as assets means that multiple failed shows could be damaging to Netflix's financials. Netflix has to weigh the risk with each show it invests in. Additionally, there is a risk with successful original content when consumers subscribe to watch only that specific content and cancel afterward. Meanwhile, pre-made content is safer but includes licensing contracts and does little to differentiate the service. Netflix manages to succeed as its own studio but suffers from a lack of network. As mentioned previously, Disney owns its entire catalog which means it doesn't have to deal with contracts. Disney+ is also able to use the resources of its parent company when producing new content. Therefore, Netflix must engage in contracts with other distributors, which can also become expensive. Overall, Netflix has to find a balance between these two content types and find the pairing that attracts the most customers.

Among the challenges that Netflix faces, the company should prioritize finding new channels for revenue. From a short-term perspective, Netflix needs to be profitable in order to continue business and find ways to differentiate itself from competitors. If Netflix chooses to focus on creating original content, then there needs to be a steady supply of income to produce quality shows and movies. New means of revenue would also mean flexibility in pricing, which they could use to their advantage against their competitors. If Netflix captures all or the majority of its market segment, it would eventually be constricted in terms of profitability as users could gain power with their price elasticity. Therefore, it is in Netflix's best interest to find new ways to increase its profit margin besides just increasing consumer subscriptions.

Strategic Recommendation

As stated, the most pertinent strategic problem facing Netflix is the need to expand revenue streams beyond the simple user subscription and ad-supported plans. To this, there are plenty of strategic recommendations that Netflix can implement to remain competitive and alleviate their main strategic problem. Our recommendations will focus on sustainable and competitive advantages to allow Netflix to adapt in the rapidly changing industry.

Currently, Netflix's revenue model relies heavily on subscription fees and an ad-supported plan. While these models have provided substantial revenue, there are limitations

when it comes to market saturation and growth potential. Therefore, for Netflix to alleviate their problem, a pressing need for diversification is necessary. This diversification can serve to mitigate risks associated with Netflix's over-reliance on stream based revenue. It also allows for Netflix to capitalize on emerging marketing opportunities.

To diversify its revenue, Netflix should explore alternative models. First, they should explore premium content offerings for select plans. For example, Netflix can offer a new subscription tier that gets exclusive early access to select new releases. Additionally, they can release titles with alternative viewing options such as virtual reality or continue with their interactive series. HBO Max has already done something similar by allowing access to blockbuster movies early to higher paying customers. Netflix should diversify itself from this by releasing their own originals (instead of movies) earlier for their customers.

Another opportunity for diversifying revenue streams is by capitalizing on the popularity of original series by launching merchandise related to shows like "You" or "Stranger Things" or the newly released Squid Games remake. Netflix can release a variety of merchandise that can vary from mass produced, to limited edition items. History has shown that this strategy has worked well for Netflix's competitors. For example, Disney has amassed over 5 billion dollars in revenue for merchandise sales year after year. Therefore, Netflix should explore the opportunities of releasing officially licensed merchandise for fans. Additionally, Netflix should be acquiring additional partnerships with cable platforms, smart TVs, or phone carrier brands. By allowing a consumer to receive our product for free through a complimentary product, Netflix can capture a new audience and profit off the additional partnerships they acquire.

Netflix can continue its strategic improvements by experimenting with its pricing strategies in an attempt to boost customer retention. Dynamic pricing models offer an innovative way to generate revenue while catering to different customer segments. For example, Netflix could introduce variable pricing based on viewing hours. They should add a new ad-supported variable pricing subscription to appeal to price sensitive consumers and also boost revenue through advertising. They can offer discounts to those who only stream up to a certain average amount of time a month. This would let them provide discounted rates for those who do not record high screen time and who would normally be turned away by another static subscription. This approach aligns pricing with customer usage patterns and helps create a fair pricing point for consumers. It also opens the door to attracting more price-sensitive customers who might otherwise be deterred by a single flat-rate model.

Moreover, the introduction of a loyalty program could be a significant step towards improving customer retention. By rewarding long-term subscribers with exclusive content previews, discounts on Netflix-branded merchandise, or invitations to special events and screenings, Netflix can foster a stronger connection with its audience. Moreover, they can market through curated original content such as allowing loyalty members to compete for a large prize. This not only boosts customer retention, but also revenue as consumers will respond well to these marketing tactics (using YouTube videos with the same idea). Looking at competitors, this strategy of creating a loyalty program has been effectively employed by Amazon Prime, where

their program extends beyond streaming to encompass various shopping benefits. Consumers not only know Prime Video as a streaming service, but also somewhere to shop at non-watching times. Therefore, a cost based loyalty program can effectively provide a new stream of income if paired with the right benefits.

It is important to measure the feasibility of these recommendations given Netflix's resource constraints through a thorough risk assessment for each new recommendation. For instance, before a full-scale implementation, Netflix could test these concepts in select markets to gauge consumer response. By diversifying revenue streams through content offerings, merchandise sales, dynamic pricing models and a loyalty program, Netflix can effectively address its main strategic challenge. These recommendations are designed to enhance and ensure Netflix's position and adaptability in the rapidly evolving streaming industry.

Appendix

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B. Figures

Figure 1. Porter's Five Forces for the Streaming Video On Demand Services industry. Red indicates strong competition. Yellow indicates mild competition.

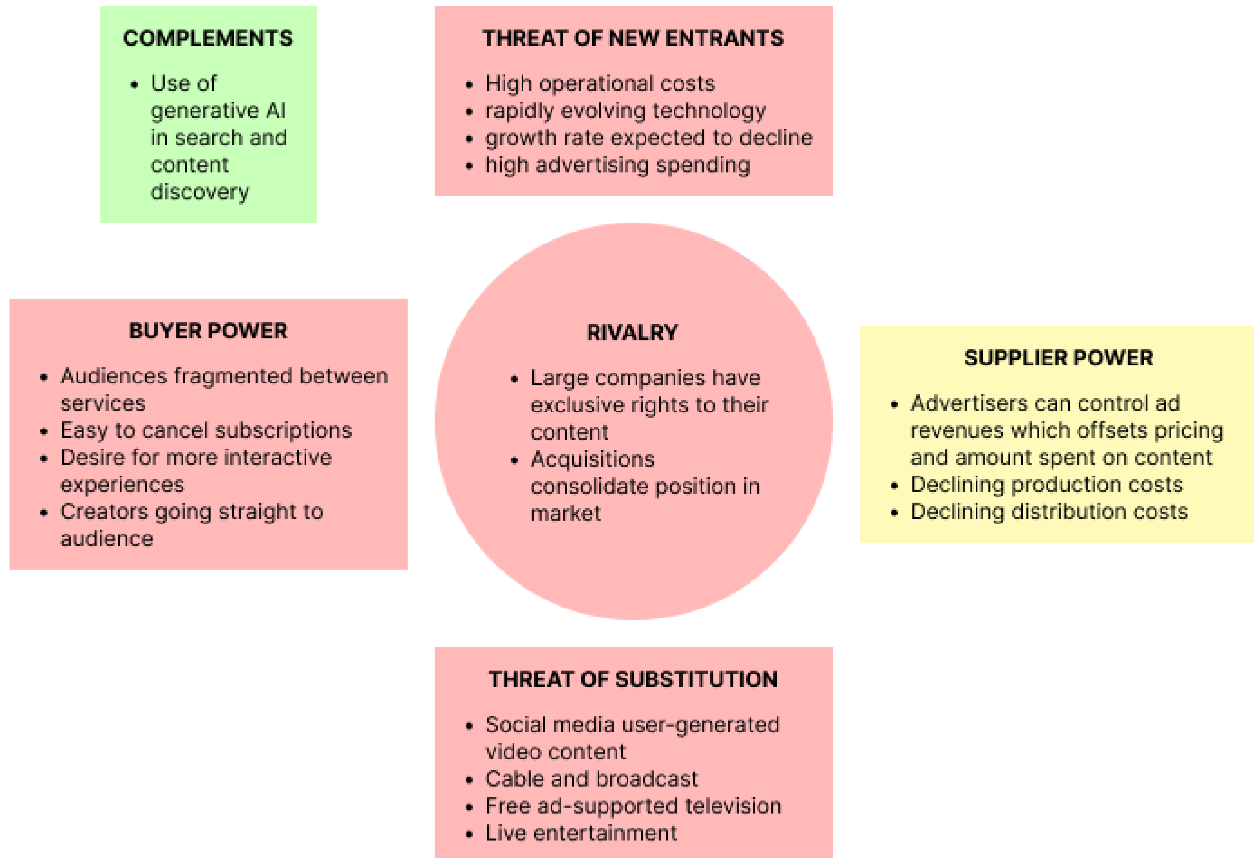

Figure 2. Value Chain Analysis of Netflix
The Value Chain (Porter 1991)

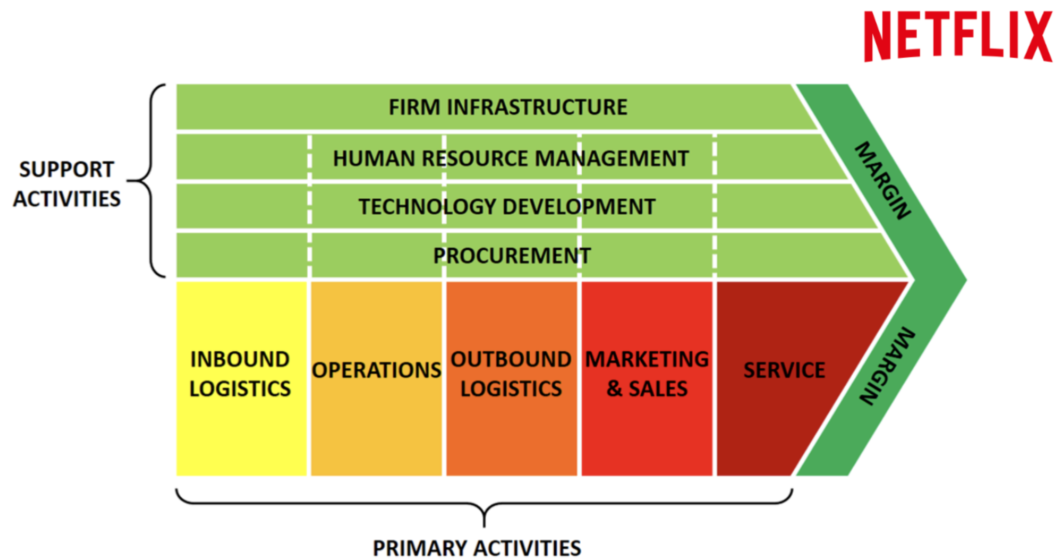

Figure 3. Activities of Acquiring Short-Term Content Rights from Production Houses are Operationally Effective
Though acquiring rights to certain movies and TV series increases WTP, Netflix must balance investment between licensing content and producing original content. Acquiring the media brings a temporary advantage because the strategy is not within the VRIO framework. Though operational effectiveness is often necessary for the company, it is not sufficient. Operational effectiveness can be imitable. Competitors of Netflix are able to perform the same activity once they acquire licensing rights to the same media. Activities must be performed differently or consist of different activities to prove their sustainability.

Figure 4. Sustainable Competitive Advantage of Netflix's Original Production – Evaluation of VRIO Framework

Netflix proves a competitive strategy to have a sustainable competitive advantage with its in-house production activities. This strategy follows the VRIO Framework

- VRIO
- **V**aluable
- **R**are
- **I**nimitable (Costly to imitate)
- ***O****rganized to capture value*

Valuable:
Netflix's original content brings a refreshing, valuable experience for its customers. Netflix makes great investments in high-quality movies, documentaries, TV series, and interactive content. This process keeps users engaged, brings value to their experience, and attracts new customers.

Rare:
Netflix fosters a sense of exclusivity with its original content production. Given Netflix operates in 190 countries, providing content in over 30 languages, Netflix has a unique advantage.

Inimitable:
When Netflix releases various original content that act as spin-offs for its last, activities are built to be even more fit, increasing the sustainability due to the low probability of copying. Original series create a sense of community within its fanbase, which cannot be replaced.

Organized to Capture Value:
Netflix honors innovation and constantly aims to connect with its customers. With its immersive experiences, interactive media, and recent livestreaming events, Netflix captures value due to the fit between its processes, structure, and culture.

Figure 5. Chart of Netflix's different subscription plans.

Standard w/ Ads	Standard*	Premium**	Basic***
Cost: $6.99 Ad-supported Some content unavailable Watch and download on 2 supported devices at a time Full HD	Cost: $15.49 Unlimited and ad-free content Watch and download on 2 supported devices at a time Full HD Add 1 extra member *Extra member can be added for $7.99 each/ month	Cost: $22.99 Unlimited and ad-free content Watch on 4 supported devices as a time Download on 6 supported devices at a time Ultra HD Add up to 2 extra members **Extra member can be added for $7.99 each/ month	Cost: $11.99 Unlimited and ad-free content HD (720p) ***Plan is not available to new or rejoining users

Figure 6. Table of Recommendations for Secondary Problem

Problem: Password Sharing
Strategy: Netflix can implement a stricter authentication process that is programmed to spot password sharers
Strategy: Higher price subscription tiers that allow for multiple password sharing
Strategy: Enhance user content with personalization to make the sharing of a password undesirable and inconvenient for the user.