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Complete Analysis of Netflix, Inc.

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COMPLETE ANALYSIS OF NETFLIX, INC.

By

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DEDICATION

This thesis is dedicated to everyone who has encouraged and motivated me throughout this process. To my parents, Bert and Angel Gregory, thank you for pushing me and believing in me. To my fiancé, Trevor Buse, thank you for believing in me and supporting through the hard times. I could not have made it through this process without all of the love and support that you each provide!

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ABSTRACT

ANNA KATHRYN GREGORY: Complete Analysis of Netflix, INC (Under the direction of Bonnie Van Ness)

This thesis focuses on the company, Netflix, INC and the projected value of this company. This study provides valuable information regarding the projected value of Netflix, INC and future stock price predictions. I derived my findings through several procedures. The most important procedure in analyzing the future value of Netflix was the use of a Discounted Cash Flow Analysis. This analysis provided me with a projected value and share price for Netflix, INC in five years and again in ten years. The second method used to evaluate Netflix was the multiples valuation. This method provided information on whether or not Netflix is overvalued or undervalued. I also analyzed the industry in general and provided information regarding Netflix's strengths and weaknesses. To summarize my findings, I believe that Netflix is, for the most part, on the overvalued spectrum. This is proven through my multiples valuation. This statement is supported by my DCF valuation as well. Netflix's value and share price are projected to increase over the next five years, but then will face a down turn be year ten (2030). This will cause Netflix's value to decline as well as its share price. In conclusion, I would recommend holding NFLX stocks until 2025, then selling to receive maximum prophetization. If you do not currently own Netflix stock, I would recommend buying now and also selling around 2025 to make a profit.

TABLE OF CONTENTS

LIST OF TABLES

Introduction

For years, Netflix has been known for its innovation and early-entry into different segments of the entertainment and media industry. Netflix began as the first DVD-by-mail service, but soon became the first in other categories as well including a DVD subscription plan and then a streaming service. Over 50 percent of adults living in the United States currently have a Netflix subscription (Steveliesman). Netflix has been a front runner in the streaming industry for years, but their success has attracted new competitors to join the streaming industry. Disney+ is a new entrant that has taken the streaming industry by storm. Although Netflix is still very popular and successful, without strategic planning and the addition of new features and content, Netflix could lose its hold of the streaming industry. Throughout my thesis, I will elaborate on the history of Netflix, evaluate the entertainment and media industry, and conduct both an internal and financial analysis of Netflix. After my complete valuation of Netflix, Inc, I will provide my conclusion and recommendation in regards to Netflix stock.

Chapter I: A Timeline and the History of Netflix, INC.

Netflix was formed in California in 1997 by Reed Hastings and Marc Randolph. Hastings and Randolph came up with the idea of a starting a DVD rental service via mail. Netflix.com was launched in 1998 as the first DVD rental site. A year later, Netflix debuted its subscription service that offered its members unlimited DVD rentals on a monthly basis. In 2002, Netflix made its IPO at a selling price of one dollar per share under the NASDAQ ticker, NFLX. A milestone of one million accounts was reached by 2003, and the amount of subscribers doubled over the next few years. In 2007, Netflix introduced its streaming service. Their introduction of the streaming service became a turning point for Netflix. They became a sensation in the entertainment and media industry. Netflix thrived through its mail system and then grew exponentially with its streaming service. Netflix was innovative; they offered a totally new approach to watch movies and television series. They eventually became so popular that traditional DVD rental leaders, like Blockbuster, simply could not compete and were forced to file for bankruptcy. A few years later, Netflix expanded into the international market by offering their service in Canada. In 2013, Netflix expanded operations and began producing original content, like 'House of Cards' and 'Orange Is the New Black.' That same year, Netflix received 31 primetime Emmy nominations. They were the first ever internet TV network to be nominated for a Primetime Emmy (McFadden). Netflix continued to expand into many new territories over the next few years, while offering content in 62 different languages. Netflix is currently available in 190 different countries (Where is Netflix available?). It also has 193 million subscribers as of July 2020 (Moody). Netflix has grown into a multibillion dollar company, but can they remain relevant in this evolving industry?

Chapter II: Media and Entertainment Industry Analysis

The media and entertainment industry (M&E) in the United States is a sizable market with a value of 703 billion dollars. It accounts for one-third of the global media and entertainment industry, which makes the United States the largest M&E market in the world (Nate Nead). The media and entertainment industry is made up of several different components. The five main components are film, television, video games, music and publishing. Netflix falls into the film and television sectors of this industry. Film and television alone account for 74 percent of the entire media and entertainment industry in the United States. While Netflix can be considered a technology, media or entertainment company, CEO Reed Hastings says that he prefers the entertainment classification (Sherman). Hastings continues by saying that “media” tends to involve advertising, and Netflix does not stream advertising on its viewing platform. According to CNBC, Netflix’s valuation is significantly higher than traditional entertainment companies. This ties into their innovation and unique approach to watching film and television. For years, Netflix has been the epitome of success in the streaming industry. In my opinion, success in both the entertainment and streaming industry is dependent on several key factors including creativity, technology and consumer demands.

II.I: Creativity

The first factor that the M&E industry is dependent on is the element of creativity. The entertainment industry is all about creating new and exciting content, while also incorporating unique elements. This industry relies heavily on fresh ideas and new innovation in order to thrive. Creativity is what distinguishes one company from another in this industry. Netflix has been able to create a unique experience for customers for years. From the first DVD-by-mail rental business to the first streaming service, Netflix has embodied innovation and creativity. To further their innovation, in 2012, Netflix took its creative ideas to production and began producing original movies and television series. Netflix's original content became a huge success among customers, even winning prime television awards (Scott).

II.II: Technology

The second factor that I find vital for streaming platform success is technology. All of the M&E industry sectors require extraordinary, technological features. Therefore as technology develops, companies in the media and entertainment industry must learn to use new technology to their advantage and incorporate it to create a new experience for their customers. Netflix has used technology to its advantage for several years now. Before Netflix was even a streaming service, they used the internet to ship DVDs to renters via postal service. They also incorporated several unique features and programs to make the customer's experience more personalized. The first technological element would be Netflix's unique algorithm for content suggestion ("How Netflix's Recommendations System Works"). This algorithm takes data of the movies that a customer has rented in the past to make suggestions of new films that the customer might also enjoy. Netflix also incorporated profiles to their online site so different members in a family could all have a personalized experience with DVD recommendations. The next phase of innovation began when Netflix launched its streaming service. Within the streaming service, Netflix has incorporated several key features that really tailor the user's experience. For example, Netflix added the same profile system to their streaming service. This allows the users to continue to have the customized, personal experience with streaming. Netflix also partnered with companies such as XBOX and several television manufacturers to include a Netflix button on remotes and devices to allow customers convenient access to their Netflix accounts (Humphries).

II.III: Consumer Demands

When considering consumer demands, satisfying customers becomes more difficult in the media and entertainment industry. While all industries rely on the demands of their consumers, the media and entertainment industry is much more unique and complex. The M&E industry has many different factors that affect a consumer's wants and demands. Culture and language expectations vary worldwide. Customers are also unique in what type of genre satisfies their psychological, emotional and aspirational desires ("Media & Entertainment Industry: An Overview"). Netflix has done well over the years satisfying the needs and wants of its customers. Unfortunately, new entrants into the streaming industry has made it a bit more difficult to maintain their content collection. Netflix signs contracts for a given period of time in which they can stream certain movies and television series that other companies have produced. Over the past two years, several producers have decided to launch their own streaming service, leaving Netflix to lose big-name titles such as the hit sitcom, *Friends*, and a large variety of Disney movies ("How does Netflix license TV shows and movies?"). A smaller and more concentrated collection might not continue to satisfy the need of some customers, causing subscription rates to fall. For example, since the launch of competitor Disney+, analysts estimated that Netflix lost over one million subscribers (Murphy). One way Netflix can try to meet consumer demands is by continuing to produce more original content. Personally, I feel that Netflix's best opportunity at staying relevant and strong in the streaming industry is to continue to produce original content, even if it is more expensive.

Chapter III: Corporate Governance

Corporate governance is a system of direction and control that dictates how a board of directors governs and oversees a company ("Corporate Governance - Overview, Principles, Importance"). Netflix has a unique corporate governance. Its Board of Directors is composed mostly of independent board members. According to Netflix's approach to governance, "the hallmark of good corporate governance is an independent-minded board of directors to oversee management and represent the interest of shareholder" (Larcker and Tayan). Netflix's board of directors consists mostly of members independent from Netflix, Inc, making it diverse and unique. Netflix also takes a different approach to sharing information among the CEO, executive team and board of directors (Larcker and Tayan). Their goal is to significantly increase transparency among these three parties. Netflix's approach incorporates two unique practices. First of all, board members periodically attend senior management meetings to observe how management interacts and works together. Second, board communications are written narratives (usually around 30 pages) including links to supporting data. This narrative also includes open access to all data and information that Netflix possesses. Netflix's process of sharing information contributes to the efforts of trying to be efficient and transparent. The "Netflix culture" is also reflected in the board. According to Netflix, their culture emphasizes individual initiative, the sharing of information and a focus on results rather than processes (Larcker and Tayan). Overall, Netflix's corporate governance adds value to the company as a whole. Its unique approach to sharing information across all parties is very inclusive and strategic. Netflix's board of directors is also very diverse. The majority of its members are not from inside the corporation, therefore I think it makes them stronger and more receptive. Netflix's innovative approach to handling corporate governance is unlike most companies and should ultimately increase the value of Netflix, Inc.

III.I: Overview of the Board of Directors

Netflix currently has ten members on its board of directors. The members are as follows: Reed Hastings, Richard Barton, Rodolphe Belmer, Mathias Dopfner, Timothy Haley, Jay Hoag, Leslie Kilgore, Ann Mather, Brad Smith and Anne Sweeney. Out of the eleven listed board members, only one is dependent. The only dependent board members is Reed Hastings. Reed Hastings is a co-founder and co-CEO of Netflix. Hastings is an educational philanthropist and served on the California State School Board of Education in the early 2000's. He is currently on the board of multiple education organizations. Susan Rice is listed on Netflix's website as a board member, but she recently stepped down to join the Biden Administration. The remaining board members are independent. Netflix's board members have a unique variety of specialties and serve in many industries. I believe that Netflix's Board of Directors is diverse and well-rounded. Netflix does not appear to have a staggered board or a limit on years they can serve. The board of directors, aside from Reed Hastings, is broken into three main committees. The committees are audit, compensation and nominating and governance. All of the information on the members of the board of directors for Netflix can be found on Netflix.net ("Leadership & Directors").

III.I: Audit Committee Members

The first of the audit committee members is Richard Barton. Barton serves as Chief Executive Officer of Zillow Group. He was also a venture partner at Benchmark for 13 years. He is a board director for Netflix, but also Quarte, Artsy and Zillow Group. Leslie Kilgore also serves on the audit committee. Kilgore previously served as Netflix's Chief Marketing Officer from 2000 to 2012. She has worked for several large corporations including Amazon and Procter & Gamble. Kilgore also serves on the boards of Nextdoor, Pinterest and Medallia. The last member of the audit committee is Ann Mather. She has been on the board of directors for Netflix since 2010. She also has been on the board of directors for Bumble, AirBnB, Glu Mobile, Google and Arista Networks. Mather has also been an independent trustee to the Dodge & Cox Funds board of trustees. She has serves as Executive Vice President and Chief Financial Officer earlier in her career.

III.III: Compensation Committee Members

Rodolphe Belmer is a member of the compensation committee. Belmer has been on the board of directors since 2018. He has served as CEO for both Eutelsat and Canal + Group. Belmer is also a board member of Brut. Mathia Dopfner is another member of the compensation committee. Dopfner is chairman and CEO of Axel Springer SE. He is also a member of the Board of Directors for Warner Music Group. Timothy Haley is also on the compensation committee. He has been on the board of directors since 1998. Haley is a co-found of the venture capital firm Redpoint Ventures. He also serves on the board of directors for several private companies. Anne Sweeney is the fourth and final member of the compensation committee. Sweeney has been on the Board of Directors since 2015. She is an expert in the entertainment industry, serving in senior positions at Walt Disney Co., 21st Century Fox and Viacom.

III.IV: Nominating and Governance Committee Members

Jay Hoag is a member of the nominating and governance committee. Hoag has been on the Board of Directors for Netflix since 1999. Hoag also served as a founding General Partner of Technology Crossover Ventures. He currently serves on the Board for Electronic Arts, Zillow Group, TripAdvisor and several private companies, including Peloton. Brad Smith is also on the nominating and governance committee. Smith has been on the board of directors since 2015. He also works for Microsoft.

Chapter IV: PESTEL Analysis

A PESTEL analysis is a strategic analysis used to monitor and evaluate external factors that can have serious effects on a business ("PESTEL Analysis"). The PESTEL analysis is also useful when evaluating a business for expansion into foreign markets. The external factors that are evaluated by the PESTEL analysis are divided into six different categories. The categories are as follows: political, economic, social, technological, environmental and legal ("PESTEL Analysis"). Each category is important, but importance may vary depending on the company and industry in which it operates. For example, an international media and technology company, like Netflix, probably has less environmental concerns and more concern for the social and technological aspects of the PESTEL analysis.

IV.I: Political Factors

Political factors are all about how and to what extent a government intervenes in the economy or within a certain industry ("PESTEL Analysis (PEST Analysis) EXPLAINED with EXAMPLES"). Taxes and laws are two of the most influential political factors for a business. Political factors have evolved for Netflix over the past decade. Netflix serves a large number of countries, all of which have their own political stance. Every country has their own set of regulations and guidelines that Netflix must follow. Laws and regulations are also constantly changing. For example, in the European Union the government is considering new tax laws for international tech companies, which could heavily increase Netflix's tax liability in Europe (Amaro). Tax increases can be detrimental if the impact is not evaluated properly. In some cases, it might be better for Netflix to refrain from offering their services in some countries due to different laws and more strict government regulations. Another political factor to consider is that some content is not allowed to be viewed in certain countries. Therefore, Netflix must be aware of the content that is banned in certain countries and make sure that it is not available for users within that specific region.

IV.II: Economic Factors

Economic factors are not only based on consumer's purchasing power or the price of a product/service, but also on exchange rates, economic growth and disposable income. Netflix's monthly price is not the same worldwide. Netflix must use economic factors to determine what the appropriate price is for each country in which their services are offered. This price is determined by the country's economic stance and the content that Netflix finds culturally appropriate for that region. Netflix has also taken into consideration that customers in different countries want different features out of their stream service. For example, Netflix launched a mobile only plan in India as any additional option to their existing three plans. This mobile only option is more budget friendly and appeals to a great part of the Indian population ("Netflix launches Mobile Plan for India at INR 199/month"). One of the most important economic factors is the economic/business cycle. The 2nd and 3rd quarter periods of 2020 for the United States fell into the contraction period of the economic cycle which could be explained by the pandemic and COVID-19. The 4th quarter of 2020 and the 1st quarter of 2021 were reported to be in the recovery stage (Management®). This could be explain by our country opening back up and the COVID-19 vaccinations. While this is important to see where our country is currently at, Netflix seemed to operate a bit in reverse. Netflix had extremely high ratings in 2020 which can be explained by everyone staying home and not having many entertainment options. I believe that Netflix is nearing the end of its expansion period and will hit its peak within the next decade.

IV.III: Social Factors

Social factors can be thought of as a representation of demographic characteristics and values of a population ("PESTEL Analysis (PEST Analysis) EXPLAINED with EXAMPLES"). Some demographic characteristics that affect social factors are age, gender, socioeconomic status, etc. Values can be represented by culture and/or religion. Personally, I think social factors play a bigger role for Netflix than they ever have before. As Netflix has grown and expanded into new territories, so have their social forces and factors. As previously mentioned, Netflix is available in 190 countries. Several social factors that Netflix must take into consideration are culture, religion and language. Movie and series genres and demands vary based on individual customers and regions. Although each customer is unique, society and culture tend to play a significant role in what most consumers want to see. Netflix must be cautious of cultural and religious factors in order to maintain their popularity and social platform. Language is a very obvious social factor. Most consumers prefer content in the language(s) that they speak and understand. Although subtitles are an option, I assume most consumers would prefer to watch a series in their preferred language. Netflix provides content in 62 different languages to best suit the majority of their customers (Moore). This is important for Netflix as a company. If language poses as a barrier, Netflix will lose customers. Therefore, it is extremely important for Netflix to continue to produce content in a variety of languages to reach its full potential. Other social factors that I believe are relevant, but are not as intense, can include age and gender. Age and gender play a significant role in diversifying the type of content that Netflix provides. Netflix must maintain content that appeals to every age group and gender.

IV.IV: Technological Factors

Technological factors refer to innovations in technology that have the potential to change operations in the industry (“PESTEL Analysis (PEST Analysis) EXPLAINED with EXAMPLES”). Technological factors are becoming increasingly important as technology evolves. I believe Netflix is advanced when it comes to its technology and online features. For example, Netflix uses a software to minimize the data it takes to watch a movies and shows without distorting any quality. This software helps reduce the amount of data that Netflix consumers are using on their personal devices. This data reduction also reduces the amount of energy that is being used. Along with the data reduction, Netflix added a feature that allows viewers to download content to watch at a later date (“Downloads Make It Even Easier to Watch Netflix on the Go”). This gives customers the ability to watch Netflix content when service is not adequate or even when offline. Netflix also has software through their website and applications that allow customers to rate the movies and television series they have watched. Netflix uses complex algorithms to suggest new content to its users based on the ratings of their previous shows and movies (“How Netflix's Recommendations System Works”). This technology along with the personal profile features through Netflix allow customers to have a more customized and unique experience while using Netflix.

IV.V: Environmental Factors

The concern for the environment has become increasingly popular over the past decade with the increasing awareness of issues like climate change and global warming. Environment factors include a variety of ecological and environmental aspects such as weather, climate and climate change ("PESTEL Analysis (PEST Analysis) EXPLAINED with EXAMPLES"). Netflix is not as demanding on the environment as some companies considering they do not produce any products. Therefore, natural resources are not wasted on behalf of Netflix (Tapalaga). With that being said, Netflix still has a negative effect on our environment through pollution in the form of carbon dioxide emissions. While most online sources differ in the actual impact of Netflix and video streaming on the environment, it can be agreed upon that Netflix must make efforts to minimize their carbon footprint. Netflix's last report on environmental impact was in 2017. They released their goals around sustainability and clean energy were as follows: "use as little electricity as possible, use renewables for the electricity we directly consumer in our owned facilities, and encourage renewables or offset non-renewable energy in facilities we do not control" ("Renewable Energy at Netflix: An Update"). Netflix's goals around sustainability are appreciated, but it is uncertain if they are following through or not considering their last environmental report was three years ago. There has yet to be an update by Netflix on the progress they have made towards these efforts. As of 2020, Netflix effectively sources all of its electric power from renewable sources (Bylund). Bylund's article also states that "where no direct source of green power is available, the company purchases renewable energy certificates to make up the difference."

IV.VI: Legal Factors

Legal factors are similar to political factors, but they tend to be more specific when referring to laws ("PESTEL Analysis (PEST Analysis) EXPLAINED with EXAMPLES"). Like political factors, Legal factors can differ depending on the country in which a business is operating. Therefore, a business that operates internationally might need to put more consideration into legal factors. One of the biggest legal concerns that Netflix faces is copyright laws (Mora). Netflix has had trouble in the past with international customers hacking streaming content that is available in other countries. Hackers are concerning for Netflix because it breaks copyright agreements and can ultimately lead to copyright lawsuits from the owners of the content. Because of this, Netflix had to implement new technology to ensure laws are not broken in regards to copyright. Another legal concern is protecting the data of customers and keeping their information private (McClellan and McClellan).

Chapter V: SWOT Analysis

A SWOT analysis is a business analysis that monitors four factors of the business. The first two factors are strengths and weaknesses within the business. Strengths and weaknesses are internal factors that can benefit or hinder a company's growth. On the other hand, the other two factors in the SWOT analysis are opportunities and threats. These two factors analyze the company from an external point of view. A SWOT analysis can be used for the following: "make the most of what you've got, reduce chances of failure, understand what a company is lacking and eliminate hazards" ("SWOT Analysis: – How to Develop a Strategy For Success"). A SWOT analysis can indicate what an organization should continue to focus on, what they should improve and how other businesses within the industry might pose a threat.

V.II: Strengths

Personally, I think Netflix is a strong competitor in the media and entertainment (video streaming) industry. With that being said, Netflix has many strengths. Netflix's biggest strength lies in the size of the company. In general, I believe that size (market share) directly coordinates with revenue. Over the past two decades, Netflix has grown exponentially. As of today, Netflix is an international company serving 190 countries. With over 193 million customers, Netflix holds a large portion of the market share (Where is Netflix available?). Another strength of

Netflix is its popularity or brand recognition. Most everyone has heard of Netflix. I believe that Netflix is a trust-worthy streaming service that has proven its worth to customers. They have also been very competitive with their pricing. An affordable monthly fee is one of the top priorities of customers and Netflix provides just that. Netflix's rise of new, original content is also a vital strength. The production of original content is especially important for Netflix as it provides content that cannot be lost. Anything on Netflix that is not produced by Netflix has the potential to be removed at the end of any given contract. Netflix also has strength in their dedication to customer service. Netflix provides algorithms to better suggest new films and shows to its customers. They also provide a way to download content to watch at a later time. The ability to download content is extremely unique and beneficial for their consumers. A major strength that Netflix has is its lack of advertisements on its platform. Ad-free streaming is a major strength that makes Netflix unique among its competitors. In regards to why Netflix has remained ad-free, CEO, Reed Hastings, states that "there's much more growth in the consumer market than there is in advertising" (Siegal).

V.II: Weaknesses

In my opinion, the biggest weakness for Netflix is the loss of content from producers entering into the streaming industry. These new competitors used to provide Netflix with content to stream. Netflix used to pay companies like Disney and WarnerMedia for streaming rights to select shows and films, but with the increasing popularity of streaming, these companies and many others have decided to enter into the industry. With these producers and many others allowing their contracts with Netflix to expire, Netflix has lost some popular content like the television sitcom, "Friends". The loss of this content weakens Netflix's hold on the industry and could potentially threaten their long term success. Netflix also has a large amount of long-term debt which is a major weakness for the company. As they continue to raise more debt to fund the purchase of new content, it does not appear that Netflix will begin paying off debt any time soon (The financial details will be discussed later in the financial analysis). This could also lead to a rise in subscription prices, which could be considered a weakness. A major weakness that Netflix needs to consider is their dependence on the North American market. Netflix is a global company but they began in North America and still rely heavily on the North American market for revenue. Fifty percent of Netflix's revenue comes from the North American market, with is nearing saturation (Carolina et al.).

V.III: Opportunities

With the rise of new competitors, it is important for Netflix to find new opportunities to stand out. Netflix has the opportunity to remain competitive with its pricing. Netflix's pricing is average in comparison to other streaming services, therefore it is just as appealing as other platforms. One opportunity that Netflix has is to reward existing customers with a discounted yearly rate. Netflix could potentially offer an annual subscription versus the typical monthly subscription. An annual subscription plan would offer customers a small discount for committing to Netflix for a year while also guaranteeing Netflix that business for a year at a time. Another opportunity that Netflix possesses is the capacity to produce original content for specific regions. Netflix has started producing its own movies and series, this gives them the ability to create content for specific target audiences to better suit the wants of its customers. Producing its own content also gives Netflix an opportunity to expand its content collection without the risk of losing contracts. Any content creating by Netflix can remain on Netflix indefinitely. Netflix has proven successful with its originally produced content, therefore its opportunities are endless in regards to producing.

V.IV: Threats

Personally, I believe the biggest threat that Netflix has encountered thus far is the entrance of new competitors. Netflix was the first streaming service in the media and entertainment industry, creating the streaming industry. After launching their streaming service, Netflix proved that there was a demand for streaming in the M&E industry. Even though many new competitors have entered the industry, Netflix still holds the seat for top streaming service. But with these competitors growing in market share, Netflix may not stay at the top. For example, Disney launched their own streaming service, Disney+, in 2019. Disney+ alone is a major threat to Netflix, not even considering all of the other streaming platforms like HBO Max and Hulu. Another threat is the chance of another increase in subscription costs. With the rise of expenses, Netflix may not have a choice but to raise their subscription prices. In return, this could cause Netflix to lose customers to its competitors, who are even cheaper. Like previously mentioned as a weakness, market saturation proves to be a big threat to Netflix in regards of North America. American and Canadian subscriber growth has nearly leveled out. This saturation puts heavy pressure on Netflix's impact in other countries. The pressure of succeeding and moving into new foreign countries is even more difficult in regards to government regulations. For example, Netflix does not appear to be available in China any time soon due to China's restriction on foreign content (Carolina et al.). Environmental factors such as carbon emission is also a threat to Netflix as environmental issues are becoming a front runner in today's society.

Chapter VI: Porter's Five Forces Analysis

Porter's five forces analysis was created by Harvard professor Michael Porter to analyze an industry's attractiveness and potential profitability ("Porter's Five Forces: - Understanding Competitive Forces to Maximize Profitability"). Porter's analysis is used to identify forces of the industry's competitive environment. It is broken into five different factors. The factors are as follows: competitive rivalry, supplier power, buyer power, threat of substitution and threat of new entry.

VI.I: Competitive Rivalry

Competitive rivalry has been very intense for the media and entertainment industry for quite some time, but it has evolved over the past few years for the streaming industry. The streaming industry began with a single company, Netflix. Then as their success became prevalent, other companies have decided to join the streaming industry. Competitive rivalry for Netflix is extremely high. Each streaming service has its own benefits and special features. One of Netflix's biggest competitors is Disney+. The Disney fan base is very strong, ranging from children to adults alike. Disney+ also offers exclusive Disney content only available with a subscription. They also offer a bundle package for the whole family including ESPN+ and Hulu. Another major competitor in this industry is Amazon Prime. Not only does Amazon Prime offer its streaming services, they offer other exclusive benefits like 1-2 day shipping, free online books, etc. With competitors like Disney+ and Amazon Prime, Netflix is in a constant battle to not only gain new subscribers, but to maintain their current customers as well. In addition to competing with the nice perks offered by various competitors, Netflix is also losing content to the owner's new streaming services. This is one of Netflix's biggest disadvantages. To remain relevant in the streaming industry, Netflix must find a way to produce quality content and experiences to compete with their rivals.

VI.II: Supplier Power

The power of suppliers has dramatically increased over the past few years for Netflix. Netflix was the only streaming service available for several years. This gave them huge power over their suppliers. For the most part, Netflix had their pick at the content the wanted to stream. This is how Netflix was able to score big name titles like the sitcom, Friends and a large variety of Disney films including newer films, like Moana. But as new entrants came into the streaming industry, Netflix's suppliers gained bargaining power. Several of the companies that supplied Netflix with content decided to join the streaming industry as well. This caused Netflix to lose a significant amount of content, therefore losing most bargaining power to the suppliers. As more content suppliers join the industry with their own streaming services, Netflix's suppliers become more powerful. A lot has changed over the years with content suppliers. Within the streaming industry, the majority of bargaining power is primarily held by the supplier.

VI.III: Buyer Power

With an increase of competitors entering into the streaming industry, buyers (viewers) have more bargaining power than ever before. When there are more options for streaming services available, the power ultimately shifts to the viewers. Viewers can choose between a variety of providers depending on the features and content that the customer desires. The power of the buyer is also extremely high considering the ease of switching providers. Most streaming services are paid for monthly and can be cancelled at any point, this volatility makes the power of the viewer even more intense. The industry is not extremely price-sensitive as most subscriptions around priced around $10 a month. Therefore the deciding factor for customers mostly lies within the content that is offered. With that being said, some customers may follow the content that they prefer to watch instead of trying to make do with the service they have. In this case, if Netflix continues to lose content without creating their own valuable content, they could potentially lose their customers as well.

VI.IV: Threat of Substitution

The threat of substitution as of right now is pretty low for the streaming industry. Streaming has taken over the media and entertainment industry, almost wiping out television programming entirely for teens and young adults. The younger generation is more keen to streaming than traditional television, therefore TV programming isn't much of an option for a substitute. Another substitute for streaming services could be YouTube, where users can watch free content posted by other users. While YouTube is extremely successful, it does not appear to be a substitute for streaming in general due to the lack of professional content. YouTube also offers its own streaming service, therefore I do not think the free site alone is enough to substitute any streaming services. As far as substitutes are concerned, streaming is not threatened by the current substitutes that exist in the M&E industry.

VI.V: Threat of New Entry

Threat of new entry has been an issue for several years, but is now on the downfall. Entry into the streaming industry at this point is very demanding. The biggest barrier consists of content. If a company does not already produce its own content, it could be virtually impossible to successfully enter into the streaming industry this late into the game. Netflix was the pioneer company in the streaming industry. After their success proved steady, other companies joined in as well. At this point, there are several large streaming services that did not start out as producers but have evolved into producers and all of the big-name producers have already joined into this industry. After the entrance of Disney, Hulu, HBO and countless television producers have joined this industry, there is not much room for anyone who is not already a large producer. When you take into consideration the amount of talent that is already in this industry, it proves that the threat of new entrants is almost nonexistent.

Chapter VII: Business and Corporate Level Strategies

When analyzing business-level strategies, Netflix best fits into the differentiation strategy. A differentiation strategy is based around the idea of providing a product/service that has unique features compared with its competition. A company that uses the differentiation strategy does not necessarily mean they are more expensive, they just tend to focus more on what the can provide rather than what to charge. Netflix differentiates itself very well. One of Netflix's biggest means of diversification is the lack of advertisements that Netflix implements. Netflix does not include advertisements in its streaming platform; this gives users an ad-free experience for as long as they watch. This is a huge advantage among other streaming services like Hulu who use advertisements. Another feature that really makes Netflix stand out amongst its competitors is there recommendation software and algorithms. Netflix is known for their profiles and ability to recommend content based on what its users are watching and how they are ranking content. This is a huge advantage for Netflix as it personalizes the user's experience. Netflix has also become a producer and has added original content to the Netflix platform. This helps differentiate Netflix from other competitors through offering content that can only be viewed on Netflix. The basis of corporate level strategies is how a company differentiates itself. Netflix's diversification strategy is best defined as a single business strategy. Netflix has two sources of revenue. Those two sources are DVD rental service and a streaming platform. Although Netflix technically has two businesses and streams of revenue, they fall into the single business strategy based on the dominance of their streaming platform. A single business level strategy is best defined as a business where 95 percent of a company's total revenue comes from a single business. Netflix fits this description. Netflix's DVD rentals account for a mere 1.5 percent of total revenue. The remainder (about 98.5 percent) of their revenue comes from their online streaming platform. As a whole, Netflix's DVD rentals are not very significant to their total revenue. It is rumored that Netflix might attempt to diversify into new sectors of the media and entertainment industry, like music, but that has not been confirmed by Netflix. With growing competitors in the streaming industry, it might not be a bad idea for Netflix to attempt to expand into new areas of business.

Chapter VIII: Financial Statement Analysis

The financial statements provide important financial data on every aspect of a business (Kenton). Companies use their financial statements to manage the operations of their business and also to provide transparency to shareholders. To begin the financial analysis process, We will compare the income statements and balance sheets over the past 5 years (2016-2020) for Netflix, INC. I will start by analyzing the income statements and balance sheets using a horizontal analysis. The financial statements can be used to evaluate the performance of a firm and to compare percent changes over the years. All of the data used for the financial analysis of Netflix, INC can be found in the consolidated income statement and balance sheet found below. All of the data was found on Netflix.com.

Netflix, Inc.
Income Statements from the past five years
(in thousands)
All data in this spreadsheet was found on Netflix.com and was derived directly from their financial statements.

	Income Statements from the past five years				
	2016	**2017**	**2018**	**2019**	**2020**
Revenues	**$ 8,830,669**	**$ 11,692,713**	**$15,794,341**	**$20,156,447**	**$24,996,056**
Cost of revenues	(6,029,901)	(7,659,666)	(9,967,538)	(12,440,213)	(15,276,319)
Marketing	(991,078)	(1,278,022)	(2,369,469)	(2,652,462)	(2,228,362)
Technology and development	(852,098)	(1,052,778)	(1,221,814)	(1,545,149)	(1,829,600)
General and administrative	(577,799)	(863,568)	(630,294)	(914,369)	(1,076,486)
Operating Income	**379,793**	**838,679**	**1,605,226**	**2,604,254**	**4,585,289**
Other income (expense)					
Interest expense	(150,114)	(238,204)	(420,493)	(626,023)	(767,499)
Interest and other income (expense)	30,828	(115,154)	41,725	84,000	(618,441)
Income before income taxes	**260,507**	**485,321**	**1,226,458**	**2,062,231**	**3,199,349**
Benefit from (provision for) income taxes	(73,829)	(73,608)	(15,216)	(195,315)	(437,954)
Net income	**$ 186,678**	**$ 411,713**	**$ 1,211,242**	**$ 1,866,916**	**$ 2,761,395**

Table 1

Netflix, Inc.
Consolidated Balance Sheets from the past five years
(in thousands)
All data in this spreadsheet was found on Netflix.com and was derived directly from their financial statements.

	Consolidated Balance Sheets from the past five years				
	2016	**2017**	**2018**	**2019**	**2020**
Assets					
Current assets:					
Cash and cash equivalents	$1,467,576	$2,822,795	$3,794,483	$5,018,437	$8,205,550
Short-term investments	266,206	0	0	0	0
Current content assets, net	3,726,307	4,310,934	5,151,186	0	0
Other current assets	260,202	536,245	748,466	1,160,067	1,556,030
Total current assets	**5,720,291**	**7,669,974**	**9,694,135**	**6,178,504**	**9,761,580**
Non-current content assets, net	7,274,501	10,371,055	14,951,141	24,504,567	25,383,950
Property and equipment, net	250,395	319,404	418,281	565,221	960,183
Other non-current assets	341,423	652,309	910,843	2,727,420	3,174,646
Total assets	**$13,586,610**	**$19,012,742**	**$25,974,400**	**$33,975,712**	**$39,280,359**
Liabilities and Stockholders' Equity					
Current liabilities:					
Current content liabilities	$3,632,711	$4,173,041	$4,681,562	$4,413,561	$4,429,536
Accounts payable	312,842	359,555	562,985	674,347	656,183
Accrued expenses	197,632	315,094	481,874	843,043	1,102,196
Deferred revenue	443,472	618,622	760,899	924,745	1,117,992
Short term debt	0	0	0	0	499,878
Total current liabilities	**4,586,657**	**5,466,312**	**6,487,320**	**6,855,696**	**7,805,785**
Non-current content liabilities	2,894,654	3,329,796	3,759,026	3,334,323	2,618,084
Long-term debt	3,364,311	6,499,432	10,360,058	14,759,260	15,809,095
Other non-current liabilities	61,188	135,246	129,231	1,444,276	1,982,155
Total liabilities	**10,906,810**	**15,430,786**	**20,735,635**	**26,393,555**	**28,215,119**
Stockholders' equity:					
Common stock	1,599,762	1,871,396	2,315,988	2,793,929	3,447,698
Accumulated other comprehensive loss	(48,565)	(20,557)	(19,582)	(23,521)	44,398
Retained earnings	1,128,603	1,731,117	2,942,359	4,811,749	7,573,144
Total stockholders' equity	**2,679,800**	**3,581,956**	**5,238,765**	**7,582,157**	**11,065,240**
Total liabilities and stockholders' equity	**$13,586,610**	**$19,012,742**	**$25,974,400**	**$33,975,712**	**$39,280,359**

Table 2

VIII.I Income Statement Comparisons

The income statement breaks down the revenue a company earns against the expenses involved in its business to provide a net income profit (or loss) over a period of time (typically on a quarterly and annual basis). CFI states that the income statement is a great place to begin a financial model given that it requires the least amount of information out of the three main financial statements (“Income Statement - Definition, Explanation and Examples”). Like the balance sheet, the income statement also plays a significant role in the financial analysis process. The income statement can provide useful information that can provide clarity on the performance of a company over previous years and if they have effectively making changes to make its company more profitable. The income statement analysis can determine whether Netflix's revenues and costs are increasing and at what percentage. One of the most important figures on the income statement is revenue. Over the past five years, Netflix had an average increase in revenue of 22.86 percent per year. Netflix's 2020 end of year revenue was 2.83x more than it was in 2016. Overall, Netflix's revenue has increased each year. This can be explained by the increased demand in streaming services and the goal of users to save money on cable subscriptions. Netflix had an average cost of revenue percentage of 20.72 percent. The cost of revenue for 2020 was 2.53x higher than the 2016 cost of revenue. Netflix also had an average growth of 47.05 percent in net income. From 2016 to 2017, its net income increased a significant 54.66 percent. Then in 2017 to 2018, Netflix had a record net income growth of 66.01 percent. This is significant growth percentages, but they did not hold out for the long run. From 2018 to 2020, the growth percentages were around 33.50 percent. While it did decline toward the end of the five year period, Netflix's net income growth percentages are still good. Overall, Netflix's net income in 2020 was 14.79x higher than its 2016 net income. This dramatic increase in net income can be explained by Netflix's growth and popularity. The demand for streaming subscriptions has also increased dramatically over the past five years. Netflix has also raised prices several times, which might contribute to the net income growth. The chart below represents the change between years in terms of the income statement.

Horizontal Analysis of the Income Statement from 2016-2020

	2016	2017	2018	2019	2020
Revenue	1.00	1.32	1.79	2.28	2.83
Cost of Revenue	1.00	1.27	1.65	2.06	2.53
Other Costs	1.00	1.32	1.74	2.11	2.12
Operating Income	1.00	2.21	4.23	6.86	12.07
Other income/expenses	1.00	2.96	3.18	4.54	11.62
EBIT	1.00	1.86	4.71	7.92	12.28
Net Income	1.00	2.21	6.49	10.00	14.79

Table 3

VIII.II Balance Sheet Comparisons

The balance sheet is a report of a company's financial worth in terms of book value. It is comprised of three parts: assets, liabilities and shareholder's equity (Kenton). The balance sheet is a basic overview of what the company owns, owes and the amount invested by shareholders. The balance sheet plays a significant role in the financial analysis process. According to CFI, the balance sheet is based on the following fundamental equation: Assets = Liabilities + Equity ("Balance Sheet - Definition & Examples (Assets = Liabilities + Equity)"). The balance sheet is interesting to evaluate because the percentage increases for assets is the same as the percentage increases in liabilities and stockholders' equity. For total assets, Netflix had an average annual increase of 23.10 percent. Netflix's total assets in 2020 was 2.89x higher than its total assets in 2016. Netflix's cash and cash equivalents had an average growth rate of 34.21 percent. Cash and cash equivalents for 2020 was 5.59x higher than 2016. Property and equipment have also steadily increased its growth percentage, with an average of 28.09 percent increase per year. The growth in property and equipment might be justified by Netflix's increase in content (therefore more cloud storage is needed) and its increase in original content, which Netflix has to have space to film. For total liabilities and stockholders' equity, Netflix also had an average annual increase of 23.10 percent. Just like the total assets, the liabilities and stockholders' equity in 2020 was 2.89x higher than it was in 2016. Netflix's current content liabilities growth percentage has dropped consistently over the five year period, averaging only 4.52 percent. This could be due to the large amount of content that Netflix is losing to new streaming services. Accounts payable had an annual growth rate of 15.72 percent. Accrued expenses also had a relatively consistent annual growth rate of 34.56 percent per year. Netflix's deferred revenue growth percentage has been decreasing over the five year period, averaging at 20.50 percent. Deferred revenue growth percentage began at 28.31 percent for the years 2016-2017 and ended at 17.29 percent for 2019-2020. Netflix did not have any short-term debt until the year 2020. Netflix's total liabilities growth rate over the five year period averaged 20.70 percent. Total liabilities in 2020 was 2.59x greater than the liabilities in 2016. Common stock has had an average growth percentage of 17.45 percent over the past five years. The 2020 common stock was 2.16x higher than 2016. Retained earnings has also had a relatively steady growth rate. The average growth rate has been 37.82 percent over the five year period ranging from 34.8 percent to 41.17 percent. By 2020, retained earnings increased by 6.71x the 2016 value. Total stockholders' equity has increased at an average rate of 29.80 percent per year. The chart below represents all of data used to analyze the balance sheet.

Vertical Analysis of the Consolidated Balance Sheet from 2016-2020

	2016	2017	2018	2019	2020
Assets					
Current Assets:					
Cash and cash equivalents	1.00	1.92	2.59	3.42	5.59
Total Current Assets	1.00	1.34	1.69	1.08	1.71
Non-current content assets	1.00	1.43	2.06	3.37	3.49
Property and equipment	1.00	1.28	1.67	2.26	3.83
Other non-current assets	1.00	1.91	2.67	7.99	9.30
Total assets	1.00	1.40	1.91	2.50	2.89
Liabilities and Stockholders' Equity					
Current liabilities:					
Current content liabilities	1.00	1.15	1.29	1.21	1.22
Accounts payable	1.00	1.15	1.80	2.16	2.10
Accrued expenses	1.00	1.59	2.44	4.27	5.58
Deferred revenue	1.00	1.39	1.72	2.09	2.52
Total current liabilities	1.00	1.19	1.41	1.49	1.70
Non-current content liabilities	1.00	1.15	1.30	1.15	0.90
Long-term debt	1.00	1.93	3.08	4.39	4.70
Other non-current liabilities	1.00	2.21	2.11	23.60	32.39
Total liabilities	1.00	1.41	1.90	2.42	2.59
Stockholders' equity:					
Common stock	1.00	1.17	1.45	1.75	2.16
Retained earnings	1.00	1.53	2.61	4.26	6.71
Total stockholders' equity	1.00	1.34	1.95	2.83	4.13
otal liabilities and stockholders' equity	1.00	1.40	1.91	2.50	2.89

Table 4

Chapter IX: Valuation Using the Discounted Cash Flow

To predict the future value of Netflix, INC, I conducted a discounted cash flow analysis. I found the net present value (NPV) and the predicted share value at both the five year and ten year range. To begin the DCF valuation, I started with basic data and calculations needed to start analyzing the company. The beginning information for my analysis is inserted below.

DCF valuation information for NFLX

revenue in thousands (beginning in 2021)	24,996,056
short term growth (2021-2024)	21.00%
long term growth (2025+)	4.00%
costs (% of revenue)	52.00%
tax rate	30.00%
initial assets in thousands (2020)	39,280,359
investment in thousands (Y1)	4,500,000
investment in thousands (Y2)	5,625,000
investment in thousands (Y3)	7,031,250
depreciation (% of assets)	20.00%
net working capital (% of revenue)	35.11%
debt in thousands	$15,809,095
WACC	6.73%
shares outstanding	441,800,000

Table 5

Our 2021 beginning revenue was simply taken from the 2020 end of year (EOY) revenue. Short term growth is used to predict the revenues for the years 2021 through 2024. The average growth rate of the previous four years was around 23 percent, but was steadily declining. The decline in growth rate could possibly be related to the new intrants into the streaming market as well as an increase in buyer power due to the availability of many new streaming platforms. I settled at a short-term growth rate of 21 percent. In regards to long term growth rate, the average is around 1 to 3 percent per year for United States companies. Regardless of new competitors (including Disney) entering into the streaming industry, I feel as if there is still a lot of potential left for growth within the streaming industry. I predicted Netflix's long term growth rate would be around 4 percent. I do not believe this is a perpetual rate, and it will not last throughout the extent of Netflix's lifespan. I chose 4 percent to represent a decline in the short term growth rate, but I do not believe it will reach perpetuity within the next ten years. Overall, a much more effective actual long term rate would be around 1-3 percent, like the US GDP growth rate, but for the purpose of only analyzing Netflix until 2030, I believe 4 percent is an acceptable rate. I believe they will continue to see constant growth, but not at the rate of the short-term growth that has steadily been decreasing. Netflix has a very high cost percentage in regards to revenue. I believe this could be explained by the content that Netflix provides for its customers. Highly-demanded content is only available from one producer, making Netflix's bargaining power almost inexistent. Therefore, Netflix is required to pay high costs to lease and stream content. Netflix's costs over the past four years have been around 60 percent of revenue, but they have been decreasing. I chose to set their cost percentage at 52 percent in hopes that Netflix's costs will continue to decline over the next ten years. A small decrease in cost percentage can be explained by Netflix's efforts to produce more original content. In this case, there are costs associated with producing original films and series, but it is not ongoing and therefore more profitable. For the tax rate, I averaged the average annual effective tax rate (around 27 percent) and the maximum tax rate that can be imposed (35 percent). My tax rate was 30 percent. Initial assets for my DCF valuation were simply taken from the 2020 EOY assets. For my short term investments, I used some data found in Netflix's financial statements to make my forecast. Netflix has increased their investments averaging around 20-25 percent over the past few years. Therefore, I predicted that Netflix would continue to increase their investments at this rate for the short term years (2021-2023). I only estimated 3 of the years for short term, because investment percentages varied. I started with an investment of 4.5 billion in 2021. Depreciation is calculated as a percentage of assets. The majority of Netflix's content is leased from other producers, most contracts being on a four year basis. This would make depreciation around 25 percent per year for their leased content. When you take into consideration that Netflix also has content online that is Netflix produced, this lowers the depreciation rate in terms of assets. Buildings and other forms of assets claimed by Netflix also have a much longer life span than four years. Therefore, I estimated the depreciation in terms of assets to be around 20 percent. This covers the content that we know has a four-year life span as well as content and assets that have a much longer lifespan. Net working capital was estimated using information in Netflix's financial statements. First, I subtracted liabilities from assets to give me the working capital. I then divided my working capital by revenues to come up with a net working capital (NWC). I calculated the NWC over the past 4 years and configured an average percentage of 35.11 percent. Debt was found in Netflix's 2020 EOY financial statement. For my weighted average cost of capital (WACC), I calculated a WACC of 6.73 percent. The WACC is an equation made up of equity, debt, cost of equity, cost of debt and tax rate. For my cost of equity, I used the Capital Asset Pricing Model (CAPM). Within the CAPM equation, I used a risk free rate of 1.53 percent. This risk free rate is the 10 year treasury maturity rate (U.S. Department of the Treasury). The beta is Netflix's beta of .83. For my expected return on the market, I used an estimate of 8 percent based on Gurufocus.com and other online sources (Netflix WACC %). My cost of equity averaged out to be 6.9 percent. For cost of debt, I used a simple formula of dividing interest expenses by long term debt. My cost of debt is 4.85 percent. The number of shares outstanding as of December 31, 2020 were 441.8 million. All of this information has been used in terms of calculating Netflix INC's free cash flow (FCF) for the next ten years as pictured in two parts below.

DCF valuation for NF
(in thousands)

Year	2020 (Y0)	2021 (Y1)	2022 (Y2)	2023 (Y3)	2024 (Y4)
Revenue		24,996,056.00	30,245,227.76	36,596,725.59	44,282,037.96
Costs		12,997,949.12	15,727,518.44	19,030,297.31	23,026,659.74
EBITDA		11,998,106.88	14,517,709.32	17,566,428.28	21,255,378.22
Depreciation		7,856,071.80	7,184,857.44	6,872,885.95	6,904,558.76
Assets (EOY)	39,280,359.00	35,924,287.20	34,364,429.76	34,522,793.81	35,903,705.56
NWC (EOY)	8,776,115.26	10,619,099.47	12,849,110.35	15,547,423.53	16,169,320.47
Rev / Assets (check)		**63.6%**	**84.2%**	**106.5%**	**128.3%**
EBITDA*(1-t)		8,398,674.82	10,162,396.53	12,296,499.80	14,878,764.76
Deprec*t		2,356,821.54	2,155,457.23	2,061,865.79	2,071,367.63
Invest (FA)		4,500,000.00	5,625,000.00	7,031,250.00	8,285,470.51
Chng in NWC		1,842,984.20	2,230,010.89	2,698,313.17	621,896.94
FCF		**4,412,512.15**	**4,462,842.87**	**4,628,802.41**	**8,042,764.93**
					306,391,045

'LX

2025 (Y5)	2026 (Y6)	2027 (Y7)	2028 (Y8)	2029 (Y9)	2030 (Y10)
46,053,319.48	47,895,452.26	49,811,270.35	51,803,721.17	53,875,870.01	56,030,904.81
23,947,726.13	24,905,635.18	25,901,860.58	26,937,935.01	28,015,452.41	29,136,070.50
22,105,593.35	22,989,817.09	23,909,409.77	24,865,786.16	25,860,417.61	26,894,834.31
7,180,741.11	7,467,970.76	7,766,689.59	8,077,357.17	8,400,451.46	8,736,469.52
37,339,853.78	38,833,447.93	40,386,785.85	42,002,257.29	43,682,347.58	45,429,641.48
16,816,093.29	17,488,737.02	18,188,286.50	18,915,817.96	19,672,450.68	20,459,348.71
128.3%	**128.3%**	**128.3%**	**128.3%**	**128.3%**	**128.3%**
15,473,915.35	16,092,871.96	16,736,586.84	17,406,050.31	18,102,292.32	18,826,384.02
2,154,222.33	2,240,391.23	2,330,006.88	2,423,207.15	2,520,135.44	2,620,940.85
8,616,889.33	8,961,564.91	9,320,027.50	9,692,828.60	10,080,541.75	10,483,763.42
646,772.82	672,643.73	699,549.48	727,531.46	756,632.72	786,898.03
8,364,475.53	**8,699,054.55**	**9,047,016.73**	**9,408,897.40**	**9,785,253.29**	**10,176,663.43**
				372,771,554	

Tables 6.1 and 6.2

By calculating the free cash flows and the terminal values for years five and ten, I was able to find my forecasted net present value (NPV) for Netflix, INC. The NPV projected five years from now (2025) is 266.68 billion, with a share price of $567.83 per share. That is $55.78 higher than the current price per share for NFLX. The NPV projected for ten years from now (2030) is not as good as the five year projection. The projected value of the firm in 2030 is 266.2 billion, with a share price of $539.54 per share. This analysis forecast that for the next five years, the stock price will increase almost $56, but then it will drop $28.29 by the end of the ten year forecast. The value of the firm is also predicted to drop around $12.5 billion. I believe that the decline in share price and overall value can partially be explained by the emerging competition within the streaming industry. It also ties into the loss of content available for leasing and Netflix not producing as quickly as need be. The net present value calculations can be found below.

NPV in 5 years	
Value (firm) in thousands	266,676,569.30
Value (equity) in thousands	250,867,474.30
Price per share	$567.83

NPV in 10 years	
Value (firm) in thousands	254,175,890.87
Value (equity) in thousands	238,366,795.87
Price per share	$539.54

Table 7

Based solely on the calculations of the net present value of Netflix, INC., I would suggest purchasing shares now and selling them in 2025 to receive maximum prophetization. Between years 2025 and 2030, the net present value and the share price is predicted to fall. This suggestion does not take into consideration drastic changes within the industry or company and is not a guarantee. The suggestion to buy and hold until 2025 and then sell is partially based on qualitive information in the first few chapters.

Chapter X: Sensitivity Analysis

A sensitivity analysis is used to analyze how the different values of a set of independent variables affect a specific total dependent variable ("Overview of Sensitivity Analysis - What is Sensitivity Analysis"). A sensitivity analysis is especially useful in Finance do see how changes in variables, such as growth rate and WACC, change the overall forecasted net present value or price of the stock. Cost of revenue is an important factor for Netflix, INC. Netflix has a very high costs percentage, but has been expected to go down. In our DCF valuation, the costs percentage is set at 52 percent, which is lower than the 60 percent they have produced in the past, but still significantly higher than average. For the sensitivity analysis of cost or revenue, I used 5 percent increments to test the value of the firm and share price over the two time periods of 5 years and 10 years. cost of revenue is the least sensitive variable in our analysis, therefore it is tested on a 5 percent basis. When cost of revenue decreases by 5 percent (going from 52 percent to 47 percent), our value in five years will be about $52 billion higher. Our five year share price will also increase by $116.77. The value of the firm in ten years, with a 5 percent decrease in costs, will result in a $49.5 billion dollar increase. The share price at ten years will also rise by $112. When you increase costs by five percent, the opposite happens: our value declines. The five year value of the company decreased by $51.6 billion. The five year share price also declined by $116.76. The ten year value also decreases from $254.18 billion to just $204.68 billion. Similarly the ten year share price falls by $112. With either a decrease or increase in costs, Netflix is still more attractive to year five and then appears to decrease significantly by year ten.

Sensitivity Analysis of Netflix's Cost of Revenue

	Original 52%	Decrease 5% 47%	Increase 5% 57%
Value of the firm in billions (5 years)	$266.68	$318.26	$215.09
Netflix share price (5 years)	$567.83	$684.60	$451.07
Value of the firm in billions (10 years)	$254.18	$303.67	$204.68
Netflix share price (10 years)	$539.54	$651.57	$427.50

Table 8

Long term growth rate is the second variable in Netflix's sensitivity analysis. It is much more sensitive than the costs of revenue, therefore it is only evaluated on a one percent basis. The five year value of the firm is $266.68 billion at our original growth rate of four percent. When the growth rate decreases to three percent (one percent decrease), our five year value declines by $57.56 billion. There is also a decline in the five year share price when the growth rate decreases by one percent. The five year share prices decreases from $567.83 to $437.56, resulting in a decrease of $130.27. Both the ten year value of the firm and the ten year share price decrease as well. The value of the firm in ten years decreases from $254.18 billion to $200.25 billion. That is a decrease of $54 billion. The share price in ten years also decreased by $122 to settle at $417.48. One the other hand, a one percent increase in long term growth rate would result in major increases for Netflix, INC. The value of the firm in five years with a five percent long term growth rate would be $390.76. That is a $124.08 billion increase in value. There is also an increase in the value of the firm on a ten year basis. The five percent increase in growth rate results in an increase of $116.26 in value over the ten years. The forecasted stock prices also increase significantly when growth rate increase to five percent. The stock price in five years will increase from $567.88 to $848.70, that is a $280.87 difference. The ten year stock price will also increase by $263.15. Overall, the growth rate is very sensitive and has a high impact on value.

Sensitivity Analysis of Netflix's Long Term Growth Rate

	Original 4%	Decrease 1% 3%	Increase 1% 5%
Value of the firm in billions (5 years)	$266.68	$209.12	$390.76
Netflix share price (5 years)	$567.83	$437.56	$848.70
Value of the firm in billions (10 years)	$254.18	$200.25	$370.44
Netflix share price (10 years)	$539.54	$417.48	$802.69

Table 9

The WACC is one of the most sensitive variables within our data, therefore it is analyzed last. To analyze the sensitivity in WACC, I used a .5 percent change. WACC, similar to the cost of revenue, has a reverse effect on the value: as WACC decreases, value increases. The value of the firm in five years at the original WACC of 6.73 percent is $266.68 billion. When WACC decreases by .5 percent to 6.23 percent, the value increases by $61.03billion ($327.71 billion). On the other hand, when WACC increases by .5 percent to 7.23 percent, the value of the firm in five years decreases to $224.55 billion, resulting in a loss of $42.13 billion. Netflix’s five year share price also reflects the same trend. When WACC decreases to 6.23 percent, the share price increases by $138.14, going from $567.83 to $705.97. When WACC increases to 7.23 percent, there is a decline in the five year stock price of $95.35. The value of the firm in ten years also increases when the WACC decreases .5 percent. The value of the firm in ten years increases by $58.65 billion. When the WACC increases by .5 percent, the value of the firm in ten years decreases by $40.47 billion. The stock price in ten years also follows the same pattern. When the

WACC decreases to 6.23 percent, the stock price increases by $132.75. On the other hand, the stock price decreases from $539.54to $447.93 (-$91.61) when the WACC increases by half a percent. Overall, WACC is proven to be one of the most sensitive variables and must be taken into serious consideration when valuing a company.

Sensitivity Analysis of Netflix's WACC

	Original 6.73%	Decrease .5% 6.23%	Increase .5% 7.23%
Value of the firm in billions (5 years)	$266.68	$327.71	$224.55
Netflix share price (5 years)	$567.83	$705.97	$472.48
Value of the firm in billions (10 years)	$254.18	$312.83	$213.71
Netflix share price (10 years)	$539.54	$672.29	$447.93

Table 10

Chapter XI: Liquidity Ratios

Liquidity ratios are financial ratios that are used to determine a company's ability to pay short-term debt obligations ("Liquidity Ratio - Overview, Types, Importance, Example"). It helps measure if a company has enough current and liquid assets on hand to pay for its current liabilities. Two of the most common liquidity ratios are the current ratio and the quick ratio, both of which will be discussed later in the chapter. According to CFI, the structure of the liquidity ratios provides vital information. Considering that "current liabilities" is in the denominator of both ratios, results are easy to interpret. A ratio above 1.0 is ideal. Any ratio at 1.0 or above means that the company has the means to pay off its current liabilities using current assets. On the other hand, a ratio of less than 1.0 means that a company is not able to pay for its current liabilities on current assets alone. There are several reasons why liquidity ratios are important. The first and main reason has already been mentioned: It helps measure if a company has enough assets to handle its current liabilities. The liquidity ratios can also be used for the following: determine a company's credit worthiness and investment worthiness. Creditors use liquidity ratios to determine if they should extend credit to a company ("Liquidity Ratio - Overview, Types, Importance, Example"). Financial instability would more than likely disqualify a company from obtaining loans. Investors also use liquidity ratios to determine if a company is "worthy" of their investment. Similar to creditors, investors would turn away from a company that demonstrates financial instability.

XI.I Current Ratio

The current ratio can simply be defined as current assets divided by current liabilities. This ratio is the easiest liquidity ratio to calculate. Although it is easy to use, the current ratio is not the best liquidity ratio to get an accurate depiction of the company's ability to pay short-term debts. For example, current assets includes accounts receivables and inventory, both of which are not very liquid. This can cause results to seem better than they might actually be. Considering the current ratio includes all current assets, it is extremely important for a company to have a ratio well over 1.0. The overall current ratio average of all companies within the United States is 1.55. At the end of 2020, Netflix, INC had a current ratio of 1.251. While it meets the criteria of being above 1.0, Netflix is below US average. It is not ideal to be below average, but Netflix has a reliable current average, therefore I do not think it completely deters their creditors or investors.

Current Ratio

Current Assets ($B)	9.762
Current Liabilities ($B)	7.806
Current Ratio	1.251

Table 11

XI.II Quick Ratio

The quick ratio is defined as inventory subtracted from current assets and then divided by current liabilities. This ratio is a little more strict than the current ratio. The purpose of the quick ratio is to only take into consideration the most liquid assets. Liquid assets include cash, accounts receivables and marketable securities. The quick ratio does not take inventory into consideration because it is not as liquid of an asset. The quick ratio is more reliable and effective in assessing a company's ability to satisfy current liabilities. Since the quick ratio takes into consideration that inventory is not as liquid, the quick ratio will be lower than your current ratio. As long as a company's quick ratio is above 1.0, they should be deemed as financially stable by creditors and investors. Netflix, INC has a reliable quick ratio of 1.051. The average quick ratio for all companies within the United States was 1.0. Netflix is above average and above the recommended threshold of 1.0, therefore Netflix can be deemed as financially stable. It is worth noting that the difference in Netflix's current ratio and quick ratio is not all that different. This is due to the lack of inventory Netflix has as a streaming service. Most of their "inventory" is digital content that is either self-produced or leased on a multiyear basis. This means that Netflix has a pretty small and consistent inventory, making Netflix financially reliable.

Quick Ratio

Current Assets ($B)	9.762
Inventory ($B)	1.556
Current Liabilities ($B)	7.806
Quick Ratio	1.051

Table 12

Chapter XII: Solvency Ratios

Solvency ratios are used to analyze a company's financial position. Solvency ratios are similar to liquidity ratios in the aspect that they analyze a company's ability to meet financial obligations, such as debt. One of the biggest differences is that solvency ratios are on a more long term basis. Solvency ratios are useful from a variety of users including lenders, potential investors, suppliers and others considering doing business with that specific company ("Solvency Ratio - Overview, How To Compute, Limitations").

XII.I Debt to Equity Ratio

The Debt to Equity ratio can simply be defined as total debt divided by the total equity of a firm. Total debt included short term debt, long term debt and other fixed payments. The Total equity of the firm refers to Stockholders' equity. The debt to equity ratio is used to calculate the weight of debt and financial liabilities against stockholders' equity. On average, most companies, both public and private, have a debt to equity ratio of 1.0 to 2.0. Netflix fits into this range with a debt to equity ratio of 1.429. This is an acceptable debt to equity ratio because it shows that Netflix can meet its financial obligations, but it is also taking advantage of using leverage to increase equity returns.

Debt to Equity Ratio

Total Debt ($B)	15.809
Total Equity ($B)	11.065
Debt to Equity Ratio	1.429

Table 13

XII.II Debt to Total Assets Ratio

The debt to total assets is a solvency ratio that can be used to figure a company's amount of leverage and compare it among other company's leverages within the same industry. The debt to total assets ratio can easily configured by dividing total debt by total assets. A firm's debt to total assets ratio can ultimately depict how financially stable a company is. The higher the debt to total assets, the higher the risk of investing into that firm (Hayes 2). On average, a healthy debt to total assets ratio is around 40 percent. While there isn't a "perfect" number, this target number shows that companies are utilizing the tax benefits of acquiring debt, but they are not overwhelmed with debt. An average above 60 percent indicates that a firm is risky and may not be able to afford to pay its debt. Netflix, INC has a debt to total assets ratio of 28.2 percent, this is good in comparison to the average ratio. It shows that Netflix is utilizing its debt for tax benefits, but it is not overwhelmed with debt. The debt to total assets ratio for Netflix indicates that the company is financially stable and is able to meet its financial obligations.

Debt to Total Assets Ratio

Total Debt ($B)	11.065
Total Assets ($B)	39.280
Debt to Total Assets Ratio	0.282

Table 14

Chapter XIII: Profitability Ratios

Profitability ratios are used to assess a company's ability to generate earnings in regard to revenues, operating costs, assets and shareholder equity (Hayes 1). Profitability ratios can also indicate how efficiently a company generates profit and value for stockholders.

XIII.I Return on Assets (ROA)

The return on assets (ROA) is used to indicate how profitable a company is in relation to its total assets ("Return on Assets - ROA Formula, Calculation, and Examples"). ROA can be found by dividing net income by total assets. Ultimately, the higher the return, the more productive management is in using its resources. In general, an ROA over 5 percent is considered good, while an ROA over 20 percent is excellent. It is important to take into consideration that industries vary within the number of assets needed. Therefore, it is best to compare a company's ROA with other firms in the same industry. Netflix, INC has an ROA of 7 percent. According to the general scale, Netflix has a good ROA. It is difficult to compare Netflix's ROA with other firms in the streaming industry considering most other streaming services (like Disney+ and Amazon Prime) are involved in much more than just streaming and production.

Return on Assets	
Net Income ($B)	2.761
Total Assets ($B)	39.280
Return on Assets	0.070

Table 15

XIII.II Return on Equity (ROE)

Return on equity (ROE) is used to evaluate investment returns. ROE can be calculated by dividing net income by shareholders' equity. ROE is a unique ratio, considering it incorporates values from the balance sheet and the income statement. ROE should increase over time, proving that a company is good at creating shareholder value by reinvesting its earnings wisely ("Return on Equity (ROE) - Formula, Examples and Guide to ROE"). If the ROE is declining over a long term period, it can be said that management is making poor reinvesting decisions. The average ROE for companies in the S&P 500 is around 14 percent (Fernando, 1). Netflix has an ROE of 25 percent, which is higher than the S&P 500 average. The five year trend for Netflix's ROE also proves efficient considering it has increased since 2015, with some variation. At the beginning of 2015, Netflix had an ROE of 15 percent, therefore it has increase roughly 2 percent per year ("Netflix ROE 2006-2020: NFLX"). Therefore, it can be stated that Netflix is capable of wisely reinvesting its earnings to generate more shareholder value.

Return on Equity	
Net Income ($B)	2.761
Shareholders' Equity ($B)	11.065
Return on Equity	0.250

Table 16

Chapter XIV: Multiples Valuation

Valuation of multiples are defined as “financial measurement tools that evaluate one financial metric as a ratio of another” (“Types of Valuation Multiples – Equity & Enterprise Value Multiples”). Multiples are a great source in comparing companies with one another. They can also be used to compare a company to the industry as a whole. Multiple valuation is both favorable and unfavorable in its simplicity. Its simplicity makes it easy and efficient for most analysts to use. In contrast, its simplicity is also a downfall in the fact that it simplifies very complex information into just one, simple value. It should also be noted that the multiples are configured for a single instance, not an extensive period of time (“Types of Valuation Multiples – Equity & Enterprise Value Multiples”). This factor makes it useful in the moment and for comparing current companies, but it offers almost no insight into the future predictions of the company. The ratios that are calculated for Netflix will be compared to the entertainment industry as a whole, rather than individual streaming competitors. This is due to the fact that most other streaming services are derived from companies that are much more broad than Netflix. For example, Disney owns Disney+, their streaming service, and Hulu, but they also have extensive lines of products and even theme parks to consider in their financial data. The variety of services offered by Disney makes it difficult to compare directly to Netflix as a company. This same condition applies to Amazon and its streaming service, Amazon Prime. Amazon is much more than just a streaming service, therefore its financial ratios are difficult to compare to Netflix. Although multiples valuation is still common and useful, it has become overshadowed by the DCF valuation. With that being said, I will take into consideration the multiples analysis, but forecasting relies primarily on the DCF valuation. Throughout the multiples valuation, three of the four ratios provided information regarding that Netflix might be overpriced. The EV to EBIT ratio is the only ratio suggesting that Netflix might be undervalued. Netflix might be considered overpriced due to the entrant of new competitors and losing some of its hold in the streaming and entertainment industries. Overall, the multiples valuation as a whole seems to agree with the verdict of the DCF valuation: Netflix is overvalued and its price will drop within the next ten years. For the multiples valuations that I will conduct in sections 13.1 through 13.4, I will used the data that is in the chart below. The data is divided into two different categories: Market and Financial. The market data used in the valuation is derived from Google Finance and Yahoo! Finance.

Multiples Valuation of NFLX (EOY 2020)		
Market Data	Price ($/share)	540.73
	Market Cap ($B)	239.49
	EV ($B)	247.59
Financial Data	Revenue ($B)	25.00
	EBITDA ($B)	4.70
	EBIT ($B)	3.76
	Earnings ($B)	7.57

Table 17

XIV.I: EV/Sales Ratio

The EV to sales ratio compares the company's enterprise value to its annual sales. This metric bases a company's value on sales, in consideration of its equity and debt as well. The EV to sales ratio can often indicate if a company is overvalued or undervalued. A higher EV/Sales ratio suggests that the company might be overvalued. The reverse applies to a company with a lower EV/Sales ratio ("Enterprise Value-to-Sales (EV/Sales) - Overview, Calculation, & Example"). A lower value also might indicate a good investment opportunity if the company is undervalued. I chose to incorporate the EV to Sales ratio in my analysis because it is much more efficient than the Price to Sales ratio. This is due to the fact that enterprise value is much more in-depth, and therefore, more accurate than market capitalization. EV to Sales is not perfect, but can be useful when analyzing a company. Netflix has a EV/sales ratio of 9.91x. According to a study conducted at NYU, the average EV/sales ratio for the entertainment industry is 6.81x ("Revenue Multiples by Sector (US)"). Looking at EV to sales alone, Netflix appears to be overvalued within the entertainment industry, thus suggesting that now might not be the best time to invest withing Netflix, INC. The chart below shows the values and basic calculations of finding the EV to sales ratio.

EV to Sales ratio

EV ($B)	247.59
Sales/Revenue ($B)	25.00
EV / Sales Ratio	9.91

Table 18

XIV.II: EV/EBITDA Ratio

The EV to EBITDA ratio (EV/EBITDA) is the most common enterprise value multiple. EBITDA is frequently used as a substitute of free cash flows ("Types of Valuation Multiples – Equity & Enterprise Value Multiples"). It is computed as a proportion of the Enterprise value to earnings before interest, tax, depreciation and amortization. EBITDA measures a firm's overall financial performance. Enterprise value determines the firm's total value (Maverick). The EV to EBITDA ratio is another way to measure if the company is over or under valued. I chose to incorporate the EV to EBITDA ratio into my analysis because it holds valuable information in regards to the firm's overall value. The EV to EBITDA ratio is typically higher in high-growth industries. This explains why Netflix, and the streaming industry as a whole, is significantly higher than average. The average for the entertainment industry in 2020 was 36.3x ("United States: EV/EBITDA media and advertising 2021"). In comparison, Netflix had an enterprise value to EBITDA ratio of 52.68x. This comparison also emphasizes that Netflix, INC. might be overvalued for its industry. Based on the EV to EBITDA ratio alone, we might reconsider if it is the right time to invest in Netflix, INC.

EV to EBITDA ratio

EV ($B)	247.59
EBITDA ($B)	4.70
EV / EBITDA Ratio	52.68

Table 19

XIV.III: EV/EBIT

Similar to the other ratios we have looked at, the enterprise value to earnings before interest and taxes (EBIT) ratio is used to determine if a stock is overvalued or undervalued ("EV/EBIT Ratio - Overview, Formula, Interpretation and Example"). The EV/EBIT ratio is similar to the EV/EBITDA, but it takes into consideration depreciation and amortization. I incorporated EV to

EBIT into my analysis because it is an improved, and more accurate version of the P/E ratio ("EV to EBIT (Meaning, Formula): Step by Step Calculation Examples"). The EV to EBIT ratio is used to decide how a firm's shares are priced in regard to other firms within the industry. Similar to the EV to EBITDA ratio, the smaller the ratio, the better a company is. With that being said, Netflix is actually doing better than the entertainment industry in regards to EV to EBIT. The average enterprise value to EBIT ratio for the entertainment industry is 89.24x ("Revenue Multiples by Sector (US)"). That is significantly higher than Netflix's EV to EBIT ratio of 65.85x. In contrast to the previous ratios, this ratio is below industry average. Therefore suggesting that Netflix, INC. might actually be undervalued. This suggestion differs from what we have seen so far, which proves why it can be valuable to evaluate a company on many different scales.

EV to EBIT ratio

EV ($B)	247.59
EBIT ($B)	3.76
EV / EBIT Ratio	65.85

Table 20

XIV.IV P/E Ratio

The price to earnings ratio (P/E ratio) is an equity multiple used to compare the proportion of share price to earnings per share (EPS). The P/E ratio can be used to determine the relative value of a company's shares in comparison to its own historical records or to other firms in a similar industry (Fernando, 2). I incorporated the Price to Earnings ratio into my analysis due to popularity of this ratio. The P/E ratio is very common and well-known. It is one of the only ratios that is directly displayed on the main page for any given stock on Yahoo! Finance. Due to its commonality, I found it necessary to include in my valuation. The average price to earnings ratio in the Media and Entertainment industry is 41.22x ("Overview of Market Industries: Valuation and Profitability"). Netflix has a P/E ratio nearly double that of the industry. Netflix's price to earnings ratio is 71.40x. While this might seem like shareholders are getting more for the shares, it also can allude to the fact that Netflix, INC, like previously stated, might be overvalued.

Price to Earnings ratio

Price ($/Share)	540.73
Earnings ($B)	7.57
P / E Ratio	71.40

Table 21

Chapter XV: Catalysts: COVID, Competitors and Consolidation

XV.I: COVID-19

Overall, I believe that COVID-19 was a major catalyst for 2020 and beginning of 2021 growth, but I do not think it will completely diminish once we have moved past the pandemic. Streaming has shortened attention span, and has created a disliking to commercial breaks and weekly airing of episodes. This has strengthened due to the increase in screen time caused by the pandemic. Netflix users have become very acquainted with the commercial-free content and ability to binge-watch. Therefore, I believe that consumers will have a difficult time reverting back to commercial programming or even commercial sponsored streaming services, like Hulu. Netflix has also been successfully producing new, exclusive content that will encourage customers to keep their subscriptions. As the United States and other countries begin to open up, resuming college and professional sports, as well as reducing travel bans, I believe Netflix will see decline in streaming but not necessarily subscriptions. Users will be busier and spend less time watching films and television series, yet I do not think it will be serious enough to lose a large amount of subscriptions.

XV.II: New Competitor

It is important to take into consideration the new entrants that have entered into the streaming industry. Overall, more competition makes Netflix's growth possibilities more difficult. This is evident with the introduction of Disney+. I believe the high growth volume that is explained by COVID-19, really offset the negative impact of the growing popularity of Disney+. With that being said, it does not change the negative impact that new competitors, like Disney+, have on Netflix. Therefore, I believe that increased competition will have an impact on Netflix's growth, but it should not be as detrimental considering Netflix has first mover advantage.

XV.III: Consolidation

Consolidation has really taken over in the streaming industry. For years Netflix was a clear front-runner with very little competition. Now that the streaming industry has proven profitable, many new competitors have entered into the market. The streaming industry is not that demanding, therefore, many producers and networks have consolidated their resources into a single streaming platform. Others have individual platforms, yet offer discounted "bundle" rates. For example, Disney+ can be purchased on its own, or can be bundled with ESPN and Hulu as a package deal. This is very common and Netflix is one of the only streaming platforms to remain solo. As of right now, I do not believe consolidation is within Netflix's benefit, but it could be a possibility in the future. Although Netflix has no intentions of consolidating any time soon, the consolidation within the streaming industry definitely impacts Netflix. Consolidation makes Netflix's competitors more attractive, therefore, it could threaten Netflix's value and hold of the industry.

Conclusion

To sum up the analysis of Netflix, INC, I would first like to point to the evidence that Netflix is more than likely overvalued, therefore the price will eventually decline. Based on my DCF valuation, Netflix's stock price should rise over the next five years and reach its peak price point. Three of the four ratios in my multiples valuation suggest that Netflix is overvalued, but this is not definite. Overall, I believe that Netflix, Inc. is a profitable company and is still growing and trying to maintain its market share. Therefore, to conclude my thesis analysis and research, I personally would recommend purchasing Netflix stock. I believe that the price will increase, therefore, a profit is achievable in this investment.

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