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The Video-Streaming Wars in 2019: Can Disney Catch Netflix?

After Bob Iger, chief executive officer of The Walt Disney Company (hereafter 'Disney'), one of the world's leading entertainment companies, thrilled investors with details about Disney's upcoming foray into video streaming during its annual Investor Day on April 11, 2019, he saw his firm's stock price soar to an all-time high of over $130 per share. Meanwhile Netflix, the dominant incumbent in the video-streaming-subscription space, led by chief executive officer Reed Hastings, ended the next day with its share price down nearly 5% (see **Exhibit 1** for key financial information for the two companies).[1]

Disney's move was only the latest in a series of actions taken by new and established entertainment companies in a fight for dominance in video streaming. Netflix had established an early foothold in that market after entering in early 2007. En route to amassing 140 million subscribers worldwide by early 2019 and spending $10 billion on content annually, it had evolved from a company that relied on content licensing deals to one that also had significant success with its own original programming and that had signed some of the television's world most high-profile creators to long-term deals.[2]

Now, Disney was joining the fray with its signature service, after first collaborating with other broadcasters in establishing Hulu, later buying up a majority stake in that service, and launching sports-content subscription service ESPN+ in 2018. Disney planned to launch its subscription service, Disney+, in November 2019 at price of $6.99 per month—just a little over half of Netflix's standard $13-a-month plan—and was planning to spend $1 billion on original programming for the service in its first year alone. Disney executives projected Disney+ to reach 60 to 90 million subscribers by 2024 and reach its break-even point in that same year. "Disney is approaching streaming offerings with guns blazing, looking to take share and quickly ramp up subscriber growth," said one director at a credit-rating firm, pointing out that "Disney+ will be loaded on day one with attractive [intellectual property] and franchises."[3]

The battle for what many industry observers regarded as the future of the television business was truly on. Had Iger and his team of executives found the right formula to unseat Netflix as the leader in video streaming? Was there room for both players in the marketplace? Or would Hastings and his team at Netflix need to respond in some way to the looming threat posed by Disney?

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Netflix

Netflix's Early Days

Founded in August 1997 by Reed Hastings and Marc Randolph, Netflix started as a distributor of DVDs by mail.[4] Initially, Netflix perhaps most stood out from traditional movie-rental companies like Blockbuster for not imposing due dates by which consumers needed to return the DVDs and for not charging late fees. While the company first charged customers a few dollars per DVD borrowed, it later switched to a monthly subscription fee that came with unlimited rentals.

Hastings had a vision for an online streaming service from the very beginning. Ted Sarandos, who became Netflix's chief content officer in 2000, recalled, "Back then, [Hastings] said that postage rates were going to keep going up and the internet was going to get twice as fast at half the price every eighteen months. At some point those lines would cross, and it would become more cost-efficient to stream a movie rather than to mail a video. And that's when we get in."[5]

In fact, Hastings brought that idea to Blockbuster, offering to build a streaming service under the brand name of the video rental giant (Blockbuster.com) and sell a 49% stake in Netflix for $50 million. At the time, Blockbuster had 7,700 stores, millions of customers, and a gross profit of $3 billion, while Netflix's proposed technology was still a couple of years away from being market ready, had 300,000 subscribers, and was losing money (see **Exhibit 2a** for trends in Netflix subscribers and **Exhibit 2b** for revenues). Blockbuster declined the offer. (It would file for bankruptcy in 2010).[6]

Continuing without a partner, Netflix filed for its IPO in 2002 (see **Exhibit 2c** for trends in its stock price). Around the time the company delivered its one billionth DVD in early 2007, Netflix launched its streaming service. While it had 70,000 DVD titles in its catalog, its streaming offering started with around 1,000 movies and television shows.[7] The assortment it could offer was severely limited by the long-term rights agreements that the studios that produced the content had negotiated with the television networks that aired it—in some cases, broadcast and cable networks had tied up rights for as long as nine years after a piece of content made its debut.

Pursuing Content Licensing Deals with Television Companies

To expand Netflix's catalog, its executives soon turned to negotiating licensing deals with television companies. As its first major deal, Netflix in 2008 signed a $30-million-a-year contract with premium cable network Starz for 2,500 movies and television shows as well as first-run rights to films from Disney and Sony Pictures.[8] Under the deal, Netflix could offer the content on its online service as soon as Starz did on television. Although Sarandos protested at the time that the deal was "about three times [his] budget," Netflix was only just beginning its spending spree (see **Exhibit 3** for early content deals).[9]

The 'big four' major broadcast networks, ABC, NBC, FOX, and CBS, and their production studios all began licensing content to Netflix. CBS sold rights to older content that was no longer airing on CBS network.[10] NBC offered Netflix 200 movies and older seasons of its television shows.[11] Fox also licensed past seasons of current shows airing on FOX network. ABC allowed Netflix to offer past seasons of its television shows, along with episodes from current seasons, sometimes as soon as two weeks after their original broadcast date.[12] Netflix cut big checks for hit shows on cable networks, too: it paid an estimated $1 million per episode for 91 episodes of AMC's *Mad Men*, and purchased three previous and three upcoming seasons of *Breaking Bad*.[13] To get fresher film content for the library, Netflix also made deals with Epix, Lionsgate, MGM, Paramount, and Relativity Media, among other firms. By 2010, Netflix had secured streaming rights to films that collectively brought in nearly half of the domestic box office for that year.[14]