Proceedings of the 3rd International Conference on Business and Policy Studies
DOI: 10.54254/2754-1169/68/20241360

Financial Analysis of Netflix with a Strategic Approach

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Abstract: In the ever-evolving landscape of the entertainment industry, Netflix has emerged as a dominant force, fundamentally reshaping how audiences consume content. This paper delves into the financial intricacies of Netflix, a global streaming giant that has become synonymous with on-demand entertainment. This paper's objective is to conduct a comprehensive financial analysis, scrutinizing key performance metrics, and dissecting strategic choices that have promoted Netflix's meteoric rise. Using financial ratios, cash flow analysis, and assessments of profitability and leverage, I investigate Netflix's financial health and performance over the past five years, and the strategic maneuvers undertaken by the company, including content acquisition, international expansion, and original content production, to understand their implications on Netflix's financial outcomes. This paper unveils a nuanced understanding of Netflix's financial position, providing insights into the company's profitability, liquidity, and market impact. Beyond those, this analysis explores the strategic decisions underpinning Netflix's financial success and their broader implications on the media and entertainment industry. Furthermore, this research has relevance for investors and analysts navigating the evolving landscape of digital content delivery.

Keywords: Netflix, Financial Analysis, ratio, COVID-19, strategy

1. Introduction

The entertainment industry has experienced a profound shift in recent years, driven by technological advancements and evolving consumer preferences. At the forefront of this transformation stands Netflix, a company that has revolutionized how audiences access and engage with content. Netflix, founded in 1997, has since evolved into a global streaming powerhouse with a presence in over 190 countries, boasting millions of subscribers.

The temporary rise of Netflix is not solely attributed to its captivating content but is also intricately intertwined with its financial strategies and performance. This research paper embarks on a comprehensive financial analysis of Netflix, combining quantitative financial analysis with qualitative exploration of strategic decisions. For financial analysis, The author utilizes a conscientious examination of financial statements, cash flows, and an array of financial ratios. I endeavor to paint a detailed picture of Netflix's financial health. However, financial health does not exist in isolation; it is the result of strategic decisions and market dynamics. Therefore, this research extends beyond numbers to dissect the strategic choices Netflix has made over recent years. Content acquisition, international expansion, and original content production have been central to the company's journey. This knowledge has relevance not only for investors and industry analysts but also for media and entertainment professionals navigating the evolving landscape of digital content delivery.

2. Financial analysis

2.1. Ratio analysis

2.1.1. Profitability ratio: net profit margin & return on equity & current ratio

Net profit margin has increased in recent five years from 7% to 14%, which is a positive sign, indicating improved profitability. This suggests that Netflix has been able to manage its costs and generate higher profits relative to its revenue. In addition, the drop from 17% to 14% from 2021 to 2022 could be a concern [1]. It indicates increased costs or changes in the revenue mix that impacted profitability. ROE is trending upward between 2018 and 2021 but begins to decline in 2022 [2][3]. The upward trend suggests that Netflix has been effectively utilizing shareholder’s equity to generate returns. However, the downward trend in ROE in 2022 could be due to various factors, such as increased debt, and changes in net income. Under the covid-19, with people staying at home more, there was a surge in demand for streaming services, which led to an increase in subscriptions, which positively impacted Netflix's net profit margin. Furthermore, to meet the increased demand for content, Netflix had to invest more in acquiring and producing new shows and series. While this investment supported subscriber growth, it also resulted in higher content costs, which could put downward pressure on profitability ratios.

The current ratio has been trending downward in recent years compared to 2018, which indicates Netflix’s liquidity position has weakened over the years, and the company has a lower ability to cover the short-term liabilities within its current assets. From 2018 to 2021, the quick ratio is increasing, and decreasing after 2021 [2][3]. During the pandemic, Netflix experienced an increase in its viewership since consumers were put into quarantine at home [4]. While Netflix initially benefited from increased subscriptions during lockdowns, Netflix may have faced challenges in sustaining subscriber growth at the same rapid pace. A slowdown in subscription growth impacts Netflix’s revenue and consequently, its liquidity position.

2.1.2. Leverage ratio: debt-to-equity ratio

The debt-to-equity ratio is declining from 2018 to 2022, which shows a positive sign. Netflix is relying less on debt financing and is, instead, using more of its equity or cash flow to support its operations and investments. During the pandemic.

2.2. Financial statement Analysis

This part will introduce the performance of Netflix during recent years, and through the understanding of statements build more reliable financial information for Netflix [5].

In the income statement, the revenue is increasing from 2018 to 2022, which benefits from the COVID-19 pandemic because the housing economy brings more subscribers for Netflix, and Netflix’s income is decided by subscribers [5]. While the revenue is increasing, the cost of sales and expenses is also increasing. unfortunately, this is a decrease, 13% to 10%, in the percentage of cost of revenue from 2020 to 2022, and this is also decrease in the percentage of revenue growth from 18% to 6% [1][3]. In the post-pandemic. As the pandemic eased in subsequent years, the pace of subscriber growth may have slowed down, therefore, the revenue growth rate and cost of revenue rate decreased after the pandemic.

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2.2.1. Balance Sheet

In the balance sheet, there is a significant improvement in cash equivalent in 2020 and returns to a stable level after 2020 [3]. From 2020 to 2021, the long-term debt is decreasing, but the short-term debt is increasing. A decrease in long-term debt indicates a positive sign, which can contribute to lower interest expenses and improved financial stability. The pandemic may have accelerated the company's debt reduction strategy. On the other hand, Netflix chooses to use short-term debt for working capital needs.

2.2.2. Statement of Cash flow

In the statement of cash flow, the net cash provided by operating activities achieved positive cash flow from 2020 to 2022[1][3]. In addition, there is increased negative net cash provided by investing activities(from 2018 to 2022), and decreasing net cash provided by financing activities(from 2018 to 2022). An increase in negative net cash provided by investing activities suggests that Netflix is making significant investments, possibly in content creation and innovation.

For a streaming service like Netflix, content investments are a critical part of its business model. Without offering more products to customers Netflix will not be able to be the top streaming service forever. Innovation is necessary for Netflix to stay alive during and after the COVID-19 pandemic[6]. These investments can result in negative cash flows during the acquisition and production phases. I assume that Netflix gains substantial cash flow from revenue due to the increased subscription during a pandemic, which provides the company with a substantial pool of internal funds to finance its investments rather than relying more on external financing sources such as debt or equity issuances. As a result, the financing cash flow is decreasing from 2018 to 2022.

Thus, a reduction in external financing needs can reflect improved financial stability and the ability to fund operations and growth from internal cash flow.

2.3. Strategic

2.3.1. Investment

Content Acquisition: The investment and realization of original content has played an important part in the success of the company with Netflix identifying new streams of revenue from it, in addition to higher subscriptions [7]. Furthermore, Netflix has consistently invested heavily in content acquisition. This includes licensing content from major studios, securing exclusive rights to popular shows and movies, and producing original content. For example, Netflix had found a strategic advance on which they could rely, and they had decided to adapt the platform to a more specific range of viewers, the so-called Netflix for kids [7]. Impact on Financial Results: Content acquisition is a significant expense for Netflix, impacting its cost of revenue. However, it has been crucial in attracting and retaining subscribers, leading to revenue growth.

Market Position: Netflix's vast content library has helped it maintain a leading position in the streaming industry. Exclusive content has been a key differentiator, encouraging subscribers to stay with or subscribe to the platform.

2.3.2. International Expansion

Since Netflix is predominantly a subscription-based company, the expansion in international territory and thus the attraction of additional subscribers, enhanced a more considerable growth in its revenues [7]. Netflix embarked on a global expansion strategy, aggressively entering international markets to tap into a broader subscriber base. International expansion incurred initial costs related to market

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entry and localization. However, it has contributed to substantial revenue growth as Netflix gained subscribers worldwide. Netflix is now available in nearly every country, solidifying its position as a global streaming leader. International markets represent a significant portion of its subscriber base and revenue.

3. Discussion

Netflix's financial metrics have been influenced by these strategies. According to the annual financial report, the cost of revenue such as expenses directly related to content acquisition, production, streaming delivery costs, and other operating costs [8]. While the strategy of investing more content-related has increased due to the pandemic situation, Netflix has started to attract a larger customer base. revenue has grown substantially, resulting in improved profitability over many years. Thus, the higher subscriptions during the pandemic phase led to higher revenue growth and free cash flow, as evidenced above the net cash provided by operating activity increases, net growth margin increases.

Netflix is very close to sustainable free cash flow and it is expected that Netflix is not dependent on raising eternal financing to fund day-to-day operations [8]. The company's long-term debt may have decreased due to content investments, instead, Netflix utilizes its substantial cash pool of internal finance to finance its content investment, thus, Netflix is less likely to rely on external debt financing, as evidenced by a decreasing debt-to-equity ratio and increasing negative cash flow provided by investing activities and decreasing cash flow provided by financing activities shown on the Statement of Cash Flow.

The COVID-19 pandemic played a pivotal role in Netflix's financial performance, driving substantial subscriber growth and revenue expansion [6]. However, this surge has subsided, necessitating a shift in strategy to maintain growth in a maturing streaming market.

In conclusion, Netflix's financial analysis provides essential insights into its achievements and challenges. While the company has demonstrated profitability, reduced long-term debt, and strategic adaptability, limitations such as declining profitability in 2022, liquidity constraints, and the need for sustainable growth strategies should not be overlooked.

4. Conclusion

This research has provided valuable information about Netflix’s financial performance and its significant impact on the strategic approach on financial performance analysis. The results of this research demonstrate that Netflix’s strategic approach exerts a profound effect on its financial analysis and performance. Such as content acquisition because of the COVID-19 pandemic, the profit margin growth, and long-term debt decreased as mentioned above.

It is important to acknowledge the limitations of this research. This analysis is based on publicly available financial data up to 2022, it does not include encompass Netflix’s most recent financial data beyond that date, moreover, this paper only considers the relationship between the strategic approach and financial analysis, and does not consider other external factors, such as operational efficiency, currency exchange rates may also have impact on Netflix’s financial analysis. To improve this research, a more detailed examination of Netflix’s content strategy, regional market dynamics, and collection of long-term historical financial available data could provide a more concise understanding of its causality.

As the streaming industry continues to evolve and popularize, it is recommended that companies like Netflix remain adaptable and continue to invest in content diversification to stay competitive in the market because not only the broadcasts but also content producers face the greatest pressure for change [9]. Therefore, for safeguard the future revenue streams, Netflix will face many challenges if it does not invest more in content because the content is king in the entertainment market [9]. In addition, they should pay attention to regulatory development and market unstabilization that may affect their operation decision, and creativity in content acquisition is crucial to Netflix to remain the customer base to stay success.

As mentioned above, innovation and exploration are significant for Netflix to be competitive. Future researchers can explore how the innovation and exploration affect Netflix. Moreover, Future research can investigate deeply about Netflix's financial analysis from a macro perspective [10].

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