

NETFLIX

Situation Analysis

By Melissa Pilkey

INTRODUCTION

Netflix, Inc. is a subscription service that provides digital streaming of movies and TV shows as well as a DVD-by-mail option for customers.

Over the years, the company has gone from a small start-up in Scotts Valley, California, to an international powerhouse, with services available in 50 countries.

Today, Netflix controls over 36 percent of the digital streaming market, with more than 57 million subscribers around the world.

Netflix is clearly a force to be reckoned with. Although other competitors are entering the field, the company is positioned in the market to be around for many more years to come.

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HISTORY

Netflix was founded in 1997 by Marc Randolph and Reed Hastings as an online DVD rental service. The two men had worked together at a company called Pure Software, which Hastings had launched in 1991, and came to be known as Pure Atria, after a series of acquisitions. The company was founded around a computer program called Purify that Hastings had created to identify bugs in software programs. Just five years after the company's launch, it had taken off. However, Hastings was not prepared to manage such a large company that had grown to 600 employees. So, in 1997, Pure Atria merged with a company called Rational Software for \$585 million and both Hastings and Randolph left the company.

A popular story surrounds the birth of Netflix. The story being that after returning the movie "Apollo 13" to his local video store and incurring a \$40

late fee, as the movie was well overdue, this was when Hastings got the idea for Netflix. However, that is just a story, and not the truth. Apparently Hastings liked to tell that story because it led to everything Netflix was created for: The simple return of a movie with little to no late fees.

The true story is that Hastings and Randolph would often commute together to Pure Atria, and before the big merger happened and they knew they'd be leaving the company, Randolph would bounce ideas off Hastings for a new business. Randolph knew he wanted to have a business over the Internet, something dealing with e-commerce. He would spend most of

their commute laying out a plan he had to Hastings who would begin to shoot holes in his ideas.

They had both originally shot down the idea of an online video rental services, as the cost of VHS tapes was expensive, as was the cost to ship them. However, Randolph soon became aware of a new video format, the DVD, which were soon to be released and were the same size as a compact disc. They placed a disc in an envelope and mailed it to Hastings and it arrived a day or two later in perfect condition. That was when they thought they might have something worth investing in.

Hastings put up \$2 million to back Randolph's new e-commerce start-up,

After returning the movie "Apollo 13" to his local video store and incurring a \$40 late fee, as the movie was well overdue, this was when Hastings got the idea for Netflix. However, that is just a story, and not the truth.

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which was headquartered in Scotts Valley, California at the beginning. Their selling point would be their large selection of DVD movies, as the brick-and-mortar stores, such as Blockbuster and Hollywood Video, weren't carrying any, or a very limited amount at the time.

When it came to choosing a name, Randolph, Hastings, and several others they had recruited to help start their new company decided that it should only be two syllables. One syllable relating to the Internet, and one syllable relating to movies. Using a whiteboard, they created two side-by-side columns of Internet slang and movie terms and matched them up to see what worked best. From this exercise, Netflix was born.

Their initial business plan with Netflix was to rent DVDs a la carte, meaning they would charge the video store going rate for each rental: \$4 plus \$2 shipping for a single disc and \$3 for



Netflix website back in 1999. (http://www.hackingnetflix.com/2005/06/netflix_in_1999.html)

each additional one. They also wanted to make their DVDs for sale to their customers. They could keep the rental for seven days and return it in the postage-paid mailer, or they could choose to keep the DVD and purchase it

for 30 percent below retail value.

OFFICIAL LAUNCH

The Netflix website officially launched on April 14, 1998, just six months after the project began. Their servers reached

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Netflix headquarters, Los Gatos, California. (<https://pr.netflix.com/WebClient/loginPageSalesNetWorksAction.do?contentGroupId=10531&contentGroup=Headquarters>)

capacity in 90 minutes and crashed. As they worked to continue bringing the site back online, their laser printer jammed from the amount of orders they were receiving and orders were half

completed and in piles on the floor. By nighttime, they had received more than 100 orders to ship out over 500 discs.

When the company first began, the Netflix “vault” contained about 925

titles, which was just about every movie title available on DVD at that time. By August 1998, their vault climbed to about 1,500 titles as more movie studios were beginning to accept the new format and release more titles on DVD. In the company’s first four months, they shipped out and got back 20,000 rented DVDs and Netflix hit \$100,000 in monthly revenue.

The strongest source of revenue for Netflix at this time was from their DVD sales. Hastings knew, however, that the DVD sales market was a dangerous one to stay in because high-volume retailers such as Amazon and Walmart would crush them as soon as they began selling more and more DVDs on their own sites and in their stores. So it was decided that they stop selling DVDs and focus solely on their DVD rental service, as it would be better for the company in the long run.

By 1999, Netflix had outgrown the small office in Scotts Valley. They found a new

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building in Los Gatos, California that was large enough for the company at the time and would allow them to continue to grow. It is also where the company is still headquartered today.

In July 1999, they decided to run tests on new concepts for rental service in order to capture customers for several “rental

turns,” or to make sure they kept coming back to rent more movies. They came up with two subscription programs; one called the Home Rental Library and another called Serialized Delivery. The Home Rental Library allowed customers to rent up to six movies at a time for \$20 per month with no late fees. As soon as they returned those

By April 2000, they had reached a subscriber base of 120,000 and their warehouse in San Jose was shipping 800,000 DVDs per month.

six movies, they could then receive six more. The Serialized Delivery featured the a la carte prices but allowed each customer to have an account with Netflix where they could store a list of desired DVDs, using a new feature that Netflix

was also testing called the Queue.

Focus groups loved each program, so Netflix decided to combine them into one offering. In September 1999, they unveiled the Marquee Plan to all customers as an alternative to the a la carte rentals, which they still offered with no subscription. The Marquee Plan allowed customers to choose and receive four movies for \$15.95 per month. This plan pushed up the website’s volume by 300 percent in just three months to 100,000 discs shipped per week.

By April 2000, they had reached a subscriber base of 120,000 and their warehouse in San Jose was shipping 800,000 DVDs per month. Prior to this, on February 14, 2000, they decided to drop the a la carte rental service altogether, as it was proving too costly in manpower and resources. They then renamed the Marquee Program the Unlimited Movie Rental service and raised the price to \$19.95 per month. Customers were allowed one free month to test the program, which included all the movies they would watch in a month, four at a time.

In early 2001, Netflix had 300,000 subscribers and they decided it was time for an IPO. The IPO went live May 23, 2001 at \$15 per share. The initial offering raised \$82.5 million. In 2004, the company was sitting at \$40 per share on the NASDAQ. However, to stay competitive with other heavy-

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By 2005, Netflix was shipping 1 million DVDs per day by mail and now had over 35,000 titles for customers to choose from.

weight contenders coming into the market (Blockbuster Online launched in August 2004 and Amazon was a potential threat to come into the DVD rental market) they had to make sure their prices were very reasonable and decided to reduce the cost of their subscription plan to \$17.99 for the three-out-at-a-time plan.

By 2005, Netflix was shipping 1 million DVDs per day by mail and now had over 35,000 titles for customers to choose from. By the end of the year, the company had 4.2 million subscribers and no debt. Netflix was now worth about \$1.5 billion.

In 2007, the company launched their digital streaming feature to instantly

watch movies on a computer. When this feature debuted, it was simply offered as another service to those that already held a Netflix subscription at no extra charge. The initial selection of titles available for the streaming service was only about 1,000 movies. However, it was extremely simple for customers to use, as it only took one click of the mouse to load the movie and less than 30 seconds for the movie to begin playing, with DVD-quality resolution.



Netflix wanted to incorporate its streaming software into some type of set-top box in order for its customers' to be able to get the streaming signal from their Internet onto their big-screen TVs. In 2008, Roku, a streaming technology company, unveiled the Netflix-powered set-top box. This company was started at Netflix by Anthony Wood and Hastings as a way to get the streaming service available on customers' TV sets. Netflix also partnered with Microsoft to offer its streaming service on the company's Xbox 360.

After the success Netflix had with Roku and Microsoft, this opened up a number of deals from other companies.

Over the next three years, the company had implanted the streaming software in more than 200 types of Internet- and video-enabled devices. By the end of 2008 and early

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2009, people were signing up for Netflix at a rate of 10,000 per day, and in spring of 2009, the company surpassed 10 million subscribers.

In 2010 and 2011, Netflix expanded its streaming-only service in Canada. Within a year the company gained over 1 million subscribers in Canada. Not long after the launch in Canada, Netflix unveiled a Portuguese and Spanish-language streaming-only service in 43 countries in Latin America and the Caribbean. The company was now up to 25 million subscribers.

Netflix became the top U.S. online seller of movies and TV shows in 2011, replacing Apple's iTunes store. The company's subscription service claimed 44 percent of online movie business.

In October 2011, Netflix decided to split its subscription services, offering a standalone streaming subscription service separate from its DVD rental service. Although Netflix lost about

800,000 subscribers because they were so angered by this decision, the company bounced back quickly, and continued to gain new members.

By 2014, Netflix had expanded its services to the United Kingdom, Ireland and Nordic countries, the Netherlands, Austria, Belgium, France, Germany, Luxembourg and Switzerland. At the end of 2014, the company had garnered 57.4 million subscribers around the world.

GROWTH

Just by reading through the history of Netflix, from their small start-up in 1997 to where they were at in 2014, it's easy to see their growth has been nothing short of astronomical. The company went from having \$100,000 in monthly revenue in 1998, to \$1.48 billion for just the fourth quarter of 2014, with revenue for the entire year at \$5.5 billion.

After Netflix unveiled its first

subscription plan in September of 1999, they were able to garner 120,000 subscribers by April 2000. As the company continues to expand into more and more countries their subscriber base keeps climbing. At the end of the fourth quarter of 2014, the company gained 4.33 million more subscribers to their service, bringing their total to 57.4 million worldwide.

As the company looks to the future, they see international expansion as a large part of their strategy. Netflix received 2.43 million new foreign subscribers in the fourth quarter of 2014. The company's streaming service is currently available in 50 countries and is expected to be available everywhere in the world in the next two years. Expansion into Australia and New Zealand are next on the list and are expected to be added by the end of the first quarter of 2015.

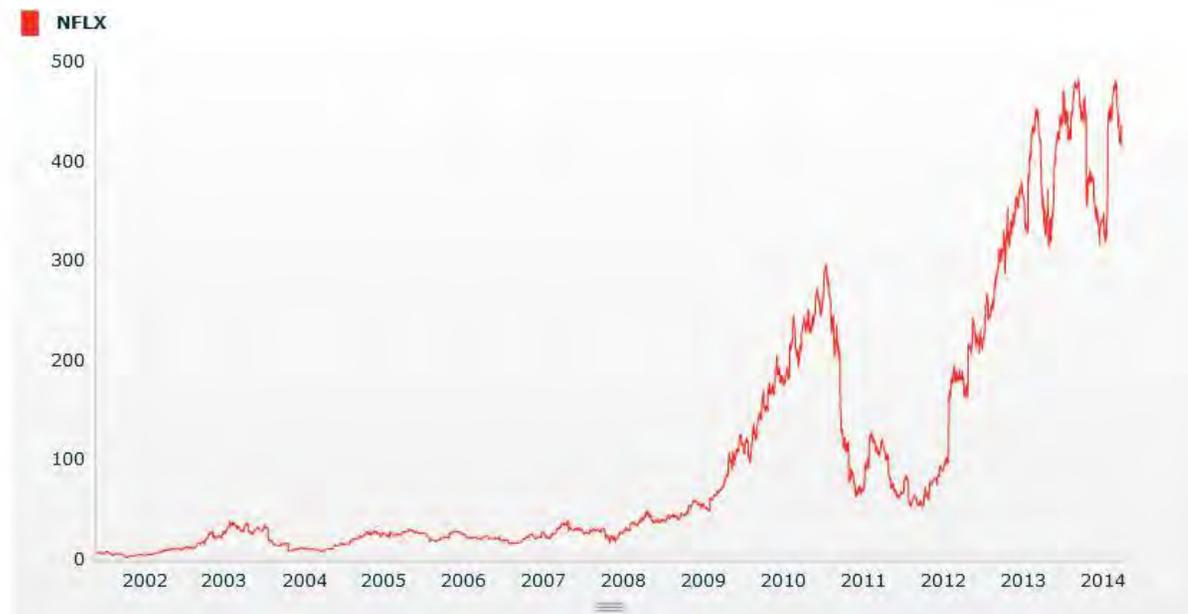
Netflix has come a long way since their IPO back in 2001 when they launched

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Netflix (NASDAQ: NFLX)

4:00 PM ET on Mar 30, 2015

Last Price	Change	Open	Day High	52-Week High
422.57	7.80 ↑ (1.881%)	418.01	423.95	489.29
	Volume	Previous Close	Day Low	52-Week Low
	1,893,600	414.77	415.55	299.50



Netflix stock on the NASDAQ as of March 30, 2015. The company's stock price history since 2002 is also shown on the graph. (<http://ir.netflix.com/stockquote.cfm>)

at just \$15 per share. As of March 30, 2015, Netflix is sitting at a little over \$422 per share, with some fluctuations each day. In looking at a chart of the company's stock prices since they went public, there has been several periods of extreme

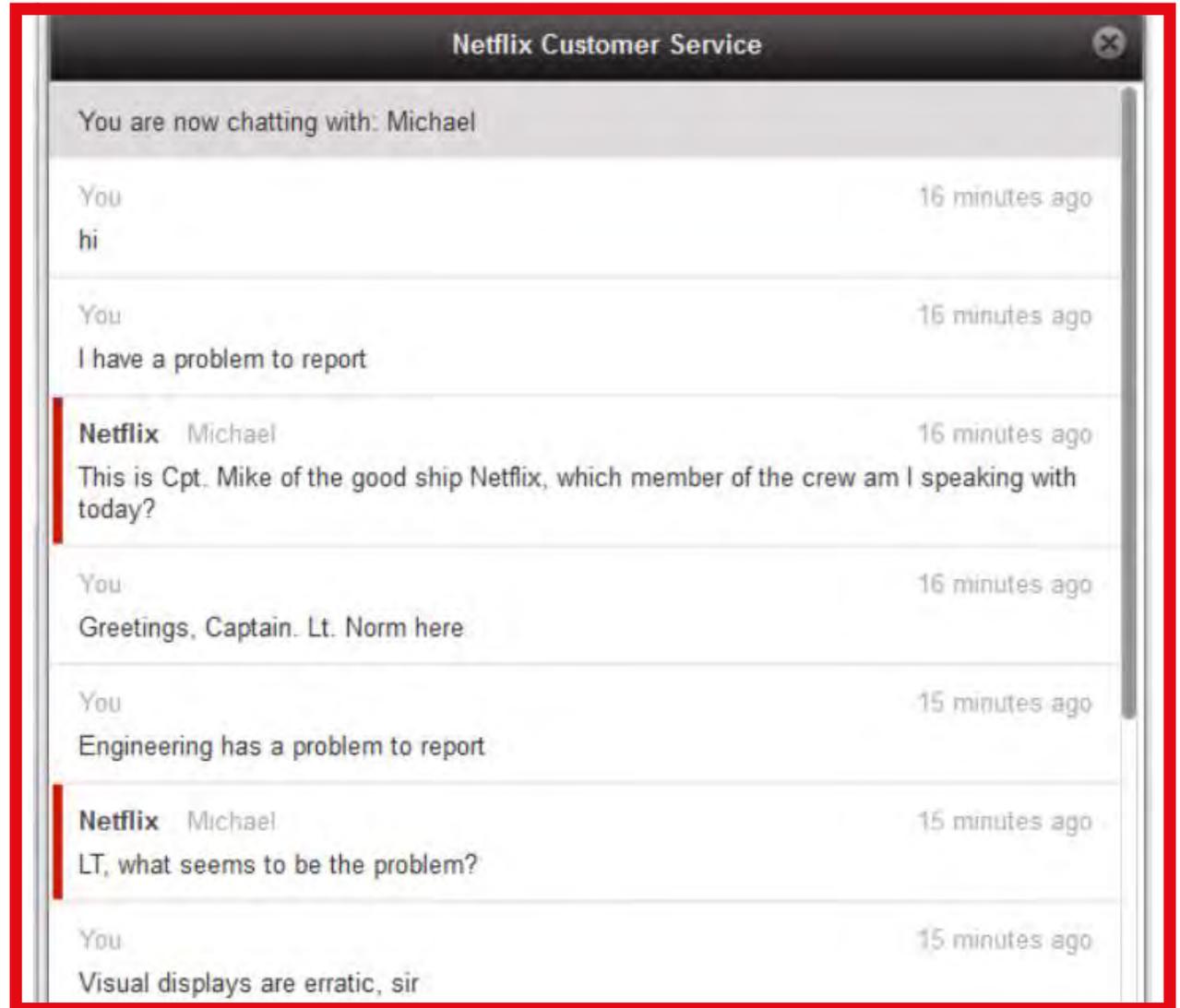
growth in the company's stock, the largest appears to be within the last three years, most likely due to their expansion into other countries and the release of more content on their streaming service.

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REPUTATION

From the very beginning, Netflix has prided itself on having a great reputation for getting deliveries out on time, providing a quality streaming service when it became available, and having very helpful customer service. However, there were a few hiccups along the way, one of those being the Qwikster fiasco.

In 2011, Netflix was losing money on their DVD-by-mail service due to the rising costs of postage and shipping. Hastings decided that he wanted to split the company's streaming service from the DVD-by-mail service into two separate subscription areas. He also wanted the DVD-by-mail service to be run entirely by a company called Qwikster. This company had its own website and checkout and would handle all the DVD-by-mail subscribers and payments. This outraged Netflix customers,



Part of a customer service chat where the agent acted like a captain from Star Trek and the customer played along. (http://www.huffingtonpost.com/2013/10/11/netflix-customer-service_n_4086365.html)

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as they loved the combined services, and split services would raise the cost if they wished to still have both. Plus, customers didn't like the fact that some other company would be handling their DVD subscriptions, as they had grown to trust Netflix, but they knew nothing about Qwikster.

Upon hearing all the opposition to this plan from customers, Hastings apologized publicly and decided to reverse his decision and keep the plans under Netflix and not deal with Qwikster at all. Even after he reversed the decision, Netflix stock took a major hit, going from \$305 per share to \$65, and the company lost about 800,000 subscribers in the third quarter of 2011 due to this disaster.

But it didn't take long for Netflix to get

back on track. The company continued to provide great service and people began flooding back. In 2014 and 2015 Netflix received the award of Harris Poll EquiTrend Video Streaming Subscription Brand of the Year. According to the Harris Poll site, "Using an academically vetted brand equity model with elements like familiarity, quality, and purchase consideration, brands create powerful connections with consumers. The stronger the brand, the greater the bond. The Harris Poll EquiTrend study benchmarks how deep those bonds go and honors the highest ranked brands in each award category."

Not only is Netflix winning awards for its brand, but they have also received recognition in the press for the excellent, non-conventional customer service. Customer service agents at

Netflix aren't required to follow many rules. They can say just about anything they would like when dealing with a customer (aside from being rude) and are only really required to ask the customer if they'd like to take a quick, one-question survey at the end of the call or chat. The survey simply asks the customer if they were satisfied with their Netflix experience. Agents aren't told to get customers to add a service to their subscription, and if a customer would like to cancel, they simply help the person cancel, not force the service upon them. Netflix encourages its customer service agents to joke around with customers, connect with them on some level, and even pretend to be a fictional character from a movie, TV show, etc. if they want to. One customer service agent acted like a captain from Star Trek during an online chat with a customer, and the customer played along and loved it. The entire transcript of that chat can be read [here](#) and shows how interesting a customer service call or chat to Netflix can be.

Netflix encourages its customer service agents to joke around with customers, connect with them on some level.

THE SERVICE

HISTORY

When Netflix first launched to the public in 1998, they offered an a la carte DVD rental plan and offered DVDs for purchase as well. Since they didn't have a huge amount of customers, the cost wasn't really a concern, and the \$2 shipping charge (plus \$4 rental fee for a single disc and \$3 for each additional) were enough to cover it. They were able to fit three discs in one mailer a time, if customers ordered that many, so they would only have one shipment. If customers chose to purchase a DVD, they were able to do so through Netflix for 30 percent below the retail value.

The company's customer base was growing but they began to lose money on each transaction by the end of 1998, partially due to the labor-intensive mailing operation. Although the company's strongest revenue growth was coming from the sale of DVDs, they decided to do away with sales and focus solely on DVD rentals.

Netflix soon rolled out a new program in September 1999 called the Marquee Program. This was a new subscription plan that offered customers an alternative to the a la carte rentals. The cost of the program was \$15.95 per month for four movies. This plan allowed Netflix to ensure customers kept coming back for more rentals; something the a la carte plan had been failing to do.

In early 2000, Netflix dropped the a la carte rental service altogether, as it was costing too much in resources to continue. They changed their Marquee Program to the Unlimited Movie Rental Service and raised the price to \$19.95 per month, which included all the movies a customer could watch in one month, with four movies out at a time. Although the service was more expensive, customers were now able to try the service free, for one month to see if they liked it before having to pay for it. In late 2004, Netflix decided to drop the cost of its subscription plan

to \$17.99 per month, which by this time had changed to having three movies out at a time. The cost reduction came when Blockbuster Online was about to launch its online rental service, and there was a threat that Amazon may come on the market with the service as well. Netflix wanted to make sure they were priced competitively.

When 2007 rolled around, Netflix launched their digital streaming feature. At that time it was offered as a free additional service to those that already held a subscription. Though there weren't too many titles available at first – about 1,000 – it was very simple to use and customers enjoyed the option.

By 2012, Netflix decided to split their digital streaming and DVD rental subscription services. Their streaming service was growing very rapidly, yet they didn't want to do away with the DVD rentals, as that service still remained popular with many. The company has plans to keep the service

THE SERVICE

DVD.NETFLIX.COM Browse New Releases Top 100 Movies, TV shows, actors, directors Sign In

Unlimited rentals. First month free!

Plans from \$7.99 a month.

Start Your Free Month

- New Releases
- Netflix Top 100
- Popular Television
- Action & Adventure
- Anime & Animation
- Blu-ray
- Children & Family

SHERLOCK HOLMES IRON MAN RED INGLORIOUS BASTERDS

Netflix's DVD-by-mail subscription website, dvd.netflix.com.

until DVDs basically become obsolete, or the service is completely losing money.

To this day, Netflix has kept both of these subscription services separate. Customers who subscribe to either

the streaming or the DVD service only see the catalog of titles available for that specific service, while people who subscribe to both services see the entire Netflix catalog of titles. If someone wishes to sign up for the DVD only rental service, they must go to [dvd](http://dvd.netflix.com).

netflix.com while those who wish to sign up for the streaming service can simply go to netflix.com.

It seems that by doing this Netflix is primarily promoting their digital streaming service, as there is not even a

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link on the Netflix.com site to get to the DVD site. But, if someone is a current subscriber to the digital streaming service and they wish to add the DVD rental service as well, it is easy to add the plan under one's account settings, with all plan options listed. The original pricing options for these plans were \$7.99 per month for either plan, or \$15.98 for both.

On May 9, 2014 Netflix announced that they would be increasing the price of their streaming plan by \$1 for new members to \$8.99. Existing customers will retain their current price for two years. However, the company still offers a \$7.99 streaming plan, but all titles are SD-quality, whereas the \$8.99 plan allows customers to enjoy HD-quality movies and TV shows.

DEVICE SUPPORT

When Netflix first introduced its digital streaming plan in 2007, it was only available on a computer. They knew



Netflix is available to use on a plethora of devices today. (<https://pr.netflix.com/WebClient/loginPage-SalesNetWorksAction.do?contentGroupId=10523&contentGroup=Streaming+Devices>)

most people wanted to watch content on their big-screen TVs, so the company had to find a way to get the Internet software to their customers' TVs. That

is when Roku unveiled the Netflix-powered set-top box in 2008. This small box, which connected to a customers' TV, enabled subscribers to stream content from Netflix to their TV sets.

THE SERVICE

Netflix eventually began to partner with different companies to make its streaming service easier than ever for people to use. It began with a partnership with Microsoft, which offered the service on the Xbox 360. From there, the number of partnerships Netflix made with different companies multiplied. In just a few short years, from the first Roku box in 2008, the

company's streaming software was available in more than 200 types of devices.

CONTENT

Netflix began with a library of 925 DVD titles in 1998 and expanded that to 1,500 by August of that year. By 1999,

the company had 3,000 DVD titles in its library, but it was extremely expensive to build such a large library due to the costs they had to pay movie studios for copies of the DVDs. However, by 2000 the major film studios finally decided to embrace the DVD format and the profit margin that it promised for them. These studios felt that Netflix was the best way for people to test this

Music & Musicals
Romance
Sci-Fi & Fantasy
Special Interest
Sports & Fitness
Thrillers



Over 93,000 movies & TV shows available to rent

[Start Your Free Month](#)

Netflix's DVD-by-mail subscription website, dvd.netflix.com, stating they currently have over 93,000 movies and TV shows to rent.

THE SERVICE

new format, without having to commit to a full-blown purchase of a DVD. More movie studios began doing business with Netflix. By the end of 2000, Warner Home Video and Columbia Tristar Home Video both agreed to a DVD revenue-sharing agreement with Netflix. With this deal, Netflix was able to acquire DVDs for \$3 to \$8 each, where before they were paying about twice that amount. This allowed the company to increase the amount of titles they carried in their warehouse.

Netflix had an agreement with Starz, however, in September of 2011, the company did not wish to renew its contract with Netflix. The reason was mainly due to the fact that Starz no longer saw it to

be profitable to have their content available on Netflix and instead wished to retain as many of their own paying customers as possible. All of the Starz films and series were pulled from the Netflix streaming service in February of 2012, however DVD titles were not affected.

Netflix holds rights, on its streaming service, to back-catalog titles of films from several companies. These include Warner Bros., Universal Pictures, Sony Pictures Entertainment, 20th Century Fox and Walt Disney Studios Motion Pictures. The company also holds current and back-catalog rights to television shows from a multitude of companies. These companies include Disney-ABC Television Group, DreamWorks Classics, Warner

Bros. Television, Hasbro Studios, CBS Television Distribution and many more.

Netflix currently boasts a digital streaming library of over 9,500 titles. However, it is important to note that for the streaming service, Netflix counts each TV show episode as one title, so the actual amount of different TV show series and movies are less. As for their current DVD library, Netflix has over 93,000 movies and TV shows available to rent.

Over the past few years, Netflix also began creating original content, available on its streaming service. With its own content, the company doesn't have to worry about paying for rights or licensing. In 2013, Netflix earned 31 primetime Emmy

nominations for "House of Cards," "Orange is The New Black," and "The Square," making the company the first-ever Internet TV network nominated. "House of Cards," won three Emmy awards that year. In 2014, Netflix won seven Emmy awards for "House of Cards," and "Orange is The New Black." The company has also earned 10 Golden Globe and two Academy Award nominations

The company's Chief Content Officer Ted Sarandos recently announced that Netflix could successfully launch around 20 original, high-quality series per year. However, not all of those would be available in the United States, as Netflix offers some varied content in different countries to appeal to the numerous tastes around the world.

DISTRIBUTION

DISTRIBUTION CENTERS

In 1999, Netflix hired a man named Tom Dillon to run the company's fulfillment operations. It had been discovered by the company's marketing team that there was a positive relationship between one-day delivery and the rate of new customers signing up for the service. Dillon designed a software program that allowed him to discover the best locations for distribution "hubs" around the country that would allow Netflix to give one-day delivery to the majority of their customers.

As of 2011, Netflix had 58 distribution centers. The location of the centers seem to be kept a secret by the company for a couple reasons. First of all, each location houses several million DVDs and expensive mail sorters, and second, Netflix has found that when customers learn the exact location of a warehouse, they begin to drop DVDs off at the door, as they think this will hasten the delivery of their next movie.

Netflix accounts for 34.9 percent of all downstream traffic during peak hours.

The buildings are intentionally kept bare of all signage and tend to appear very drab. Even the trucks used for deliveries and drop offs are unmarked. At the end of 2014, the company's DVD-by-mail service had 5.8 million subscribers.

INTERNET

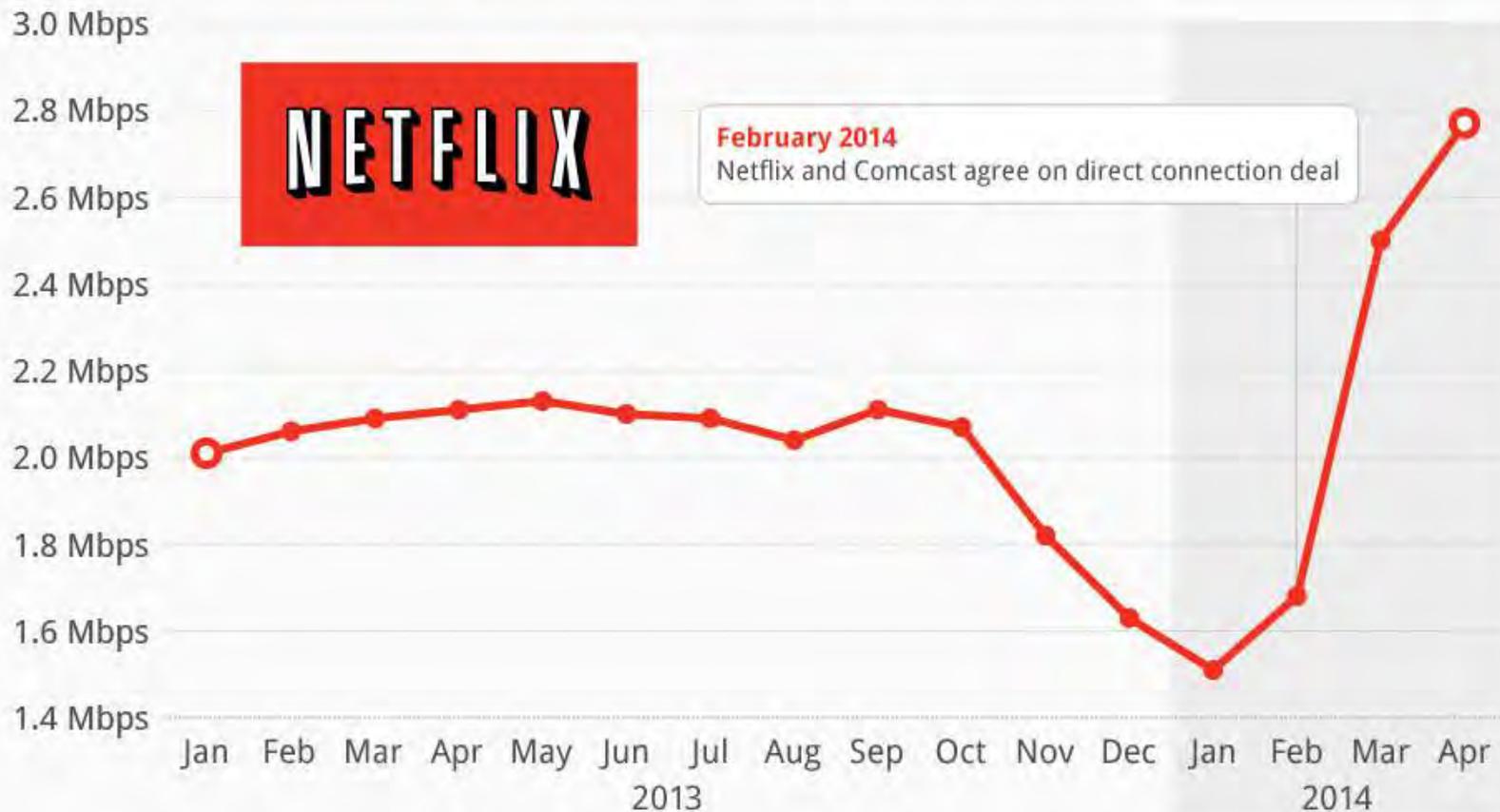
Netflix has a total of 57.4 million subscribers around the world for the digital streaming service. About 39 million of those are from the United States. That is a lot of people using the Internet to watch movies and TV shows. The company's digital streaming service is the largest consumer of bandwidth on the Internet in North America. As of November 2014, it accounts for 34.9 percent of all downstream traffic during peak hours. To put that amount in

perspective, YouTube only accounted for 14 percent of downstream traffic and Amazon's Instant Video accounted for just 2.6 percent. Obviously Netflix is a very popular service.

Many Internet service providers (ISPs), mainly Comcast, had started to meter traffic requested by Netflix subscribers, as it was congesting their network, leading to poor performance for both Netflix customers and Comcast customers, whether they used Netflix or not. Those who were viewing Netflix using Comcast's broadband network saw viewing quality drop to near-VHS quality levels. The two companies eventually reached an agreement in which Netflix would pay Comcast for the use of so much of its bandwidth. Viewing quality for Netflix streaming subscribers on the Comcast network went back to HD-quality. To keep the streaming service the best it could be for the customers, Netflix also entered into similar agreements with Time Warner Cable, AT&T and Verizon.

Netflix-Comcast Deal Marks The End Of Net Neutrality

Average Netflix connection speeds on Comcast's broadband network



NETFLIX - COMCAST DEAL

Those who were viewing Netflix using Comcast's broadband network saw viewing quality drop to near-VHS quality levels. The two companies eventually reached an agreement in which Netflix would pay Comcast for the use of so much of its bandwidth. Viewing quality for Netflix streaming subscribers on the Comcast network went back to HD-quality.

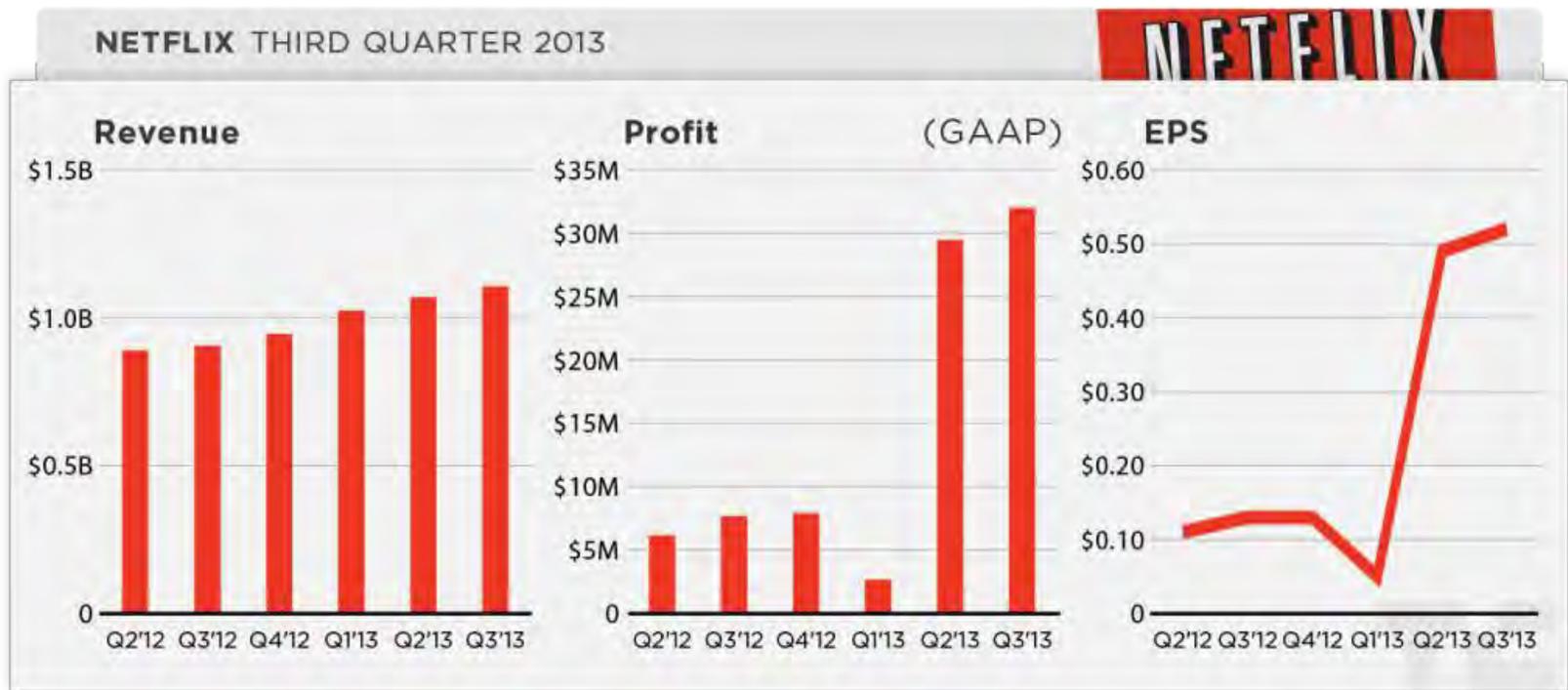
SALE & PROFIT HISTORY

In 1998, the only real source of profit was coming from the company's sale of DVDs, though the rental service was growing. They were earning about \$100,000 in monthly revenue at the time. However, they decided to do away with selling the DVDs, knowing they would take a hit in revenue, and posted an \$11 million loss at the end of 1998.

Hastings sought money from various venture capitalists, as he knew the company was soon to be on the rise. In early 1999, he garnered more than \$100 million from venture capitalists over 18 months to keep the company going. By the end of 1999, the company showed a \$29.8 million loss but was soon

to bounce back from that.

In the fourth quarter of 2002 Netflix reported revenue of \$45.2 million and a net income of \$463,000. The company kept climbing the revenue ladder each year as it diversified its content, subscription prices and offerings, both DVD and digital. By the fourth quarter of 2014, Netflix reported revenue of over \$5.5 billion with a net income of over \$266 million.



Netflix revenue, profit and EPS (earnings per share), from 2012 to 2013. (<http://techcrunch.com/2013/10/21/netflix-q3-2013/>)

MARKETING

Throughout the years, Netflix has spent an enormous amount of money on marketing efforts. At the end of 2014, Netflix spent over \$607 million on marketing for their streaming service. This includes over \$293 million for the domestic market and over \$313 million in the company's international markets.

The company's marketing efforts for their DVD-by-mail service have dropped dramatically over the years. While this service was Netflix's main focus at one point in the company's history, it is now a very distant second to the digital streaming service. In the fourth quarter of 2012, Netflix spent just \$559,000 on marketing for this service. In 2013 that number dropped to \$292,000 and in 2014 Netflix shows no expenditures for the year on marketing for their DVD rental service. While the company has no plans to do away with the DVD rental service anytime soon, it is clear that Netflix wishes to focus their efforts on digital streaming, which they feel will net them more profit in the long run.



The original logo for Netflix when the company launched in 1998.

But, whether the goal was to achieve new subscribers for their DVD-by-mail service, the digital streaming service or make themselves more known in the company's ever-expanding international markets, Netflix has used a variety of different marketing techniques over the years.

LOGO/MAILER

When Netflix began, the company's logo and mailers weren't in the popular red and white we know today. Rather, it was a purple and white logo that bared the Netflix name along with an unspooling reel of film. The original



The original mailer for Netflix with the purple, white and black logo.

mailer that held DVDs for shipment featured the purple and white logo on an all-white background. This didn't exactly stand out and wasn't instantly recognizable.

In early 2000, a woman named Leslie Kilgore was hired to take over the company's marketing department. She soon realized how valuable the mailer was, as it served as a piece of advertising in itself. She sought out to make it as eye-catching as possible. Working with an outside advertising

MARKETING

agency, Kilgore redesigned the logo and color scheme. The result was the ever-popular, instantly recognizable arched black and white rendering of Netflix placed on a “cinematic red” background.

TV ADVERTISING

In early 2004, Netflix decided to add television commercials to the company’s marketing plan for the first time. When they did so, they saw their subscriber sign-ups increase rapidly. By the end of the first quarter in 2004, the company’s revenue was up 24 percent from the previous quarter and they acquired 760,000 new trial subscribers (as all new subscribers were given a free one-month trial). In the first quarter of 2004, they spent roughly \$26.7 million on marketing efforts, whereas in the fourth quarter of 2003, Netflix spent \$14.6 million. By the fourth quarter of 2004, Netflix spent \$98.7 million on marketing efforts, compared to just

\$49.9 million the year prior. There seems to be a direct link here with the massive increase in marketing expenditures to the company’s television advertisements.

While Netflix still runs television advertisements to this day, it is unclear what their exact expenditures on this form of marketing are. What is clear is that the company is spending large sums of money on all its marketing efforts, spending over \$607 million in 2014, as was stated above.

SOCIAL MEDIA

Social media has become a prominent part of the Netflix marketing plan. Whether it’s through a blog, Facebook, Twitter or YouTube, Netflix seeks to connect with individuals through their preferred social media source. In doing so, they hope to not only keep their current subscriber base interested in what the company has to offer, but entice newcomers to join the service as

well.

THE NETFLIX BLOG

The company maintains a *blog* to share information about Netflix with subscribers and interested parties. The Netflix Blog is broken into eight different regional blogs, so that different content can be presented for the different regions. These regions are: US & Canada; UK & Ireland; Nordics; Latin America; Brasil; Benelux; France, and DACH. Each region’s blog caters to that area’s main language as well, and contains content pertinent to the region. For example, Netflix gives monthly updates on which ISPs are currently providing that regions best streaming experience for prime-time hours.

THE NETFLIX TECH BLOG

The Netflix Tech Blog is different than the company’s blog in that it focuses on technology and the issues that surround

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technology. The company uses this blog to share their “perspectives, decisions and challenges regarding the software (they) build and use to create the Netflix service.” Since this blog deals with more general topics on technology, it may not only appeal to current subscribers of Netflix, but those simply interested in learning more about technology issues or what Netflix is working on software-wise. This could be a way for the company to interest tech-savvy individuals to enjoy the back-end of their company enough to where they want to sign up for a subscription service.

FACEBOOK & TWITTER

Netflix maintains various **Facebook** pages and **Twitter** feeds. Just as with the company’s blog, they have Facebook and Twitter accounts to accommodate customers from different regions. Since Netflix does not carry the same content in all countries, these social media sites give information about movies, TV



The Netflix Facebook page with nearly 13 million “Likes” as of March 30, 2015. (https://www.facebook.com/netflixus?brand_redir=1)

shows and original content for each region.

On Twitter, each region’s feed shows the amount of followers for that

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particular Netflix feed. The Netflix US feed boasts 1.28 million followers and nearly 11,000 tweets. While this Twitter feed has the most followers for the company, the Netflix UK & Ireland feed has only 215,000 followers but well over 23,000 tweets and even Netflix Brasil has nearly 19,000 tweets with only 178,000 followers. It seems that in those countries, Twitter is much more popular than it is in the United States, meaning that Netflix should perhaps focus more on those feeds, as the international subscribers seem to like this social media format.

As for Facebook, the company uses the social media site for similar efforts as it does Twitter. Listing information about new or upcoming movie or TV show releases and original content. While Netflix does have multiple pages for different regions to, again, cater to the variances in content, each page does not have its own set amount of "Likes." It seems that if you "Like" one Netflix page, you simply like the whole

company. Because of this, Netflix has a total of over 12.8 million "Likes" on Facebook. While that may not seem like a lot when you consider the company has over 57 million members throughout the world, people that are on Facebook tend to share a lot of content and talk about things that they enjoy. So even if every subscriber that's on Facebook doesn't "Like" the company's page, that doesn't mean they won't see, or hear about, new content from all of their friends who may "Like" it. This is also true for non-subscribers on Facebook as well. The fact that users can easily share content from the Netflix Facebook page with their friends means the company is getting excellent word-of-mouth-type free advertising.

YOUTUBE

Just as with the previous social media sites, Netflix maintains multiple channels on **YouTube** for the various regions they represent. The YouTube

channel for the United States currently has over 290,000 subscribers, with the Brasil channel next in line with 31,000, and the other channels at 16,000 or less.

YouTube offers Netflix a great way to show subscribers trailers for new and upcoming TV shows and movies, as the ability to watch a trailer for a show or movie is not available through the company's actual streaming service. This, then, allows customers, or potential customers, to view content available on Netflix to see if they would like to watch a particular program or perhaps sign up for the company's service.

CROSS PROMOTION

When Netflix did away with the sale of DVDs, as they knew they couldn't compete with big-hitters such as Amazon in this area, they decided to make a deal with the company. In 1999, the two companies agreed to do cross promotion. Netflix would direct their

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customers wishing to purchase a DVD to Amazon's website, while Amazon would place ads on their website for Netflix's rental service.

In 2005, Walmart ended their online rental service. Walmart made an arrangement with Netflix that they would direct their customers to the Netflix service. Walmart's small subscriber base were given the opportunity to continue their service with Netflix, at their current discounted rate from Walmart, for one year. Walmart also agreed to promote Netflix on the company's main website, and Netflix would now direct customers to Walmart if they wished to purchase DVDs.

OTHER

In 1998, Netflix pitched an idea to DVD player manufacturers to include a coupon for free DVD rentals inside the box of the DVD player. This gave people more of an incentive to purchase the

DVD player, since at the time, there really wasn't anywhere to rent DVDs, so Netflix gave them that option, leading to the sale of more DVD players. Netflix's thinking behind this was that people would get hooked on their service after their free rentals were up and begin to pay for DVD rentals. Toshiba was the first manufacturer to take this deal, and a few others soon followed. Netflix continued these coupons after starting their digital streaming service subscription plans and instead of free rentals, it offered customers a free one-month trial for the service.

AROUND THE WORLD

In 2015, Netflix intends to spend over \$600 million on marketing efforts to

The digital posters can change ... content to match ... their surroundings.

attract people to their service around the world. If they do in fact spend this amount, it would be close to twice the amount they spent on international marketing in 2014, showing just how strongly the company is trying to break into every international market they can.

OUTDOOR ADVERTISING

To promote the company's launch in France, Netflix wanted to create a unique advertising campaign. They hired Ogilvy Paris and had the agency install digital posters that could "change their content to match the context of their surroundings." The digital poster campaign, which was to run through Christmas of 2014, utilized animated GIFs from the Netflix content library for France. They include snippets from shows such as "Orange is the New Black," "Breaking Bad," and "Fargo." The posters could be changed to "convey a range of emotions based on major current events, such as a sporting victory or the weather."

When
NETFLIX
makes outdoor



NETFLIX DIGITAL POSTER CAMPAIGN - FRANCE

Click on the play button above to watch the YouTube video about this very interesting and unique campaign that ran in France in 2014.

THE MARKET

Back in 2001, 80 percent of Netflix's subscriber base was high-earning young males with above average computer skills. At the time, Netflix still wasn't connecting with average Americans like they were hoping they would, since the majority of these people were still renting movies from the brick-and-mortar stores. But, as more and more people began adopting the DVD format, Netflix was typically the better option because they offered a much larger variety of titles than the stores. Gradually people began to move to Netflix and away from renting in the store and the company's subscriber base grew rapidly.

WHO

Today, Netflix's market is one that is very diverse and continually changing due to advances in technology and consumer behavior trends. As of 2013, the age range of Netflix subscribers was 18 to 68+. Although the majority of adults

in America over age 49 subscribe to cable, more and more are subscribing to Netflix. It appears that 18 to 36 year olds are rapidly moving away from cable and turning to Netflix, which means the company's future is very promising.

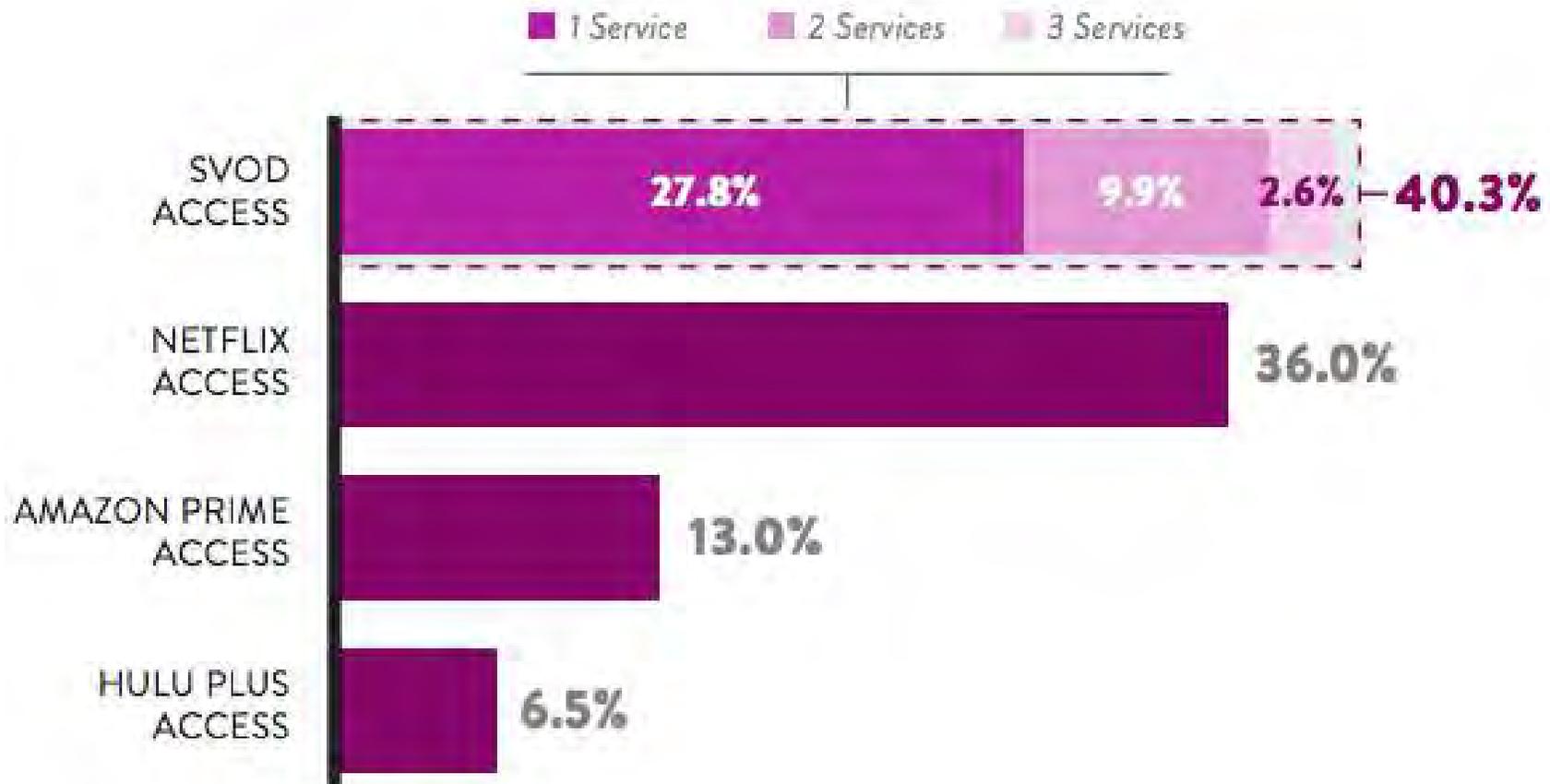
It is clear that the company's market varies widely in age, but they also vary in just about every other way as well. The company's customers, and potential customers, are diversified in their income, geographic areas, education, and preferences on what to watch. Depending on how you look at it, these facts can either help or hinder Netflix. Although it seems like a great thing that pretty much everyone who enjoys watching TV and/or movies is the target for Netflix, giving them a very large potential subscriber base, this can also be difficult for the company. Because so many people have a wide variety of tastes in TV and movies, it could be extremely costly for Netflix to attempt to cater fully to everyone's tastes.

However, Netflix appears to be doing a good job at continually adding new content, so that even though one new show that was just added may not appeal to some of their customers, or potential customers, perhaps they will add something in a month or so that will appeal to them. It's all about balance and Netflix has been doing this well.

WHERE

Netflix began expanding into international markets in 2011. As has been previously stated, at the end of 2014, the company had 57.4 million subscribers to the streaming service in 50 countries around the world. Although growth in the domestic market slowed down over the year, 2.4 million international subscribers were added in the fourth quarter of 2014. By the end of the first quarter of 2015, Netflix expects to have over 61 million subscribers as they keep expanding into new international markets.

SHARE OF MARKET



Netflix's share of the digital streaming market compared to Amazon Prime Instant Video and Hulu Plus. (<http://www.geekwire.com/2015/netflix-still-king-of-streaming-video-but-amazon-gaining-market-share/>)

DVD RENTALS

It's no secret that DVD rentals are on

the decline in America. However, many people still enjoy renting and watching DVDs as opposed (or even in addition

to) streaming services, as the viewing quality is often better, especially if one rents a Blu-ray disc instead of a plain

SHARE OF MARKET

HD DVD. There is also a much broader range of content available on DVDs than through a streaming service, as licensing requirements are simpler.

As of 2011, Netflix held about 30 percent of the DVD rental market, holding steady from the year prior. Physical rental stores held a little more than 15 percent, which was down by 7 percent from 2010. However, Redbox seems to be on the rise in this market, as the company accounted for 25 percent of all rentals in 2010 and shot up to 37 percent in 2011 and 43.5 percent at the end of 2012.

In mid-2014, Netflix had 6.26 million subscribers to the DVD rental service, which is about 400,000 less than the

company had in the previous quarter. Although it is unclear how much of the market Netflix currently holds, from the numbers stated above, it would appear that their shares are slowly declining in this area.

DIGITAL STREAMING

As of the fourth quarter of 2014, Netflix was the top streaming service in the United States with 36 percent of the market. Amazon's Instant Video was second in the market at 13 percent. While this is only about one-third the share of the market that Netflix holds, Amazon Instant Video has been rapidly increasing its market share year after year as it had 6 percent in 2013 and

a mere .6 percent in 2012. Obviously Amazon's service should not be ignored, and will be looked at further in the Competition section of this analysis.

Hulu Plus comes in third in this area for market share. The company held 6.5 percent of the market in the fourth quarter of 2014. Again, although this seems like a small amount, Hulu Plus has been increasing its market share year after year as well.

Demand for the online streaming services are constantly growing. Over 40 percent of American households subscribe to a streaming service of some kind. While more than 27 percent of households only subscribe to one service, those that hold subscriptions to multiples services are on the rise. Roughly 10 percent hold subscriptions to two streaming services and nearly 3 percent subscribe to three services. It is clear this is a popular market to be in and Netflix is still dominant. For now.

In mid-2014, Netflix had 6.26 million subscribers to the DVD rental service, which is about 400,000 less than the company had in the previous quarter.

SWOT ANALYSIS

STRENGTHS

- Strong brand recognition
- Large number of subscribers worldwide
- Great, unique customer service
- Expanding list of original content
- Strong device support for streaming service
- Various subscription options
- Numerous distribution hubs for fast DVD delivery

OPPORTUNITIES

- Completing international expansion, worldwide recognition
- Expanding original content even further
- Could expand to rent video game discs or stream games

WEAKNESSES

- Purchasing content rights and licensing is costly
- International expansion is expensive
- Cost to package and ship DVDs
- DVD-by-mail subscribers getting smaller
- Subscription prices often rising

THREATS

- Competition is increasing
- Film/TV studios could go elsewhere as more companies come into market; prices for content could go higher
- International content laws hinder expansion
- Having to pay more and more ISPs for increased use of bandwidth

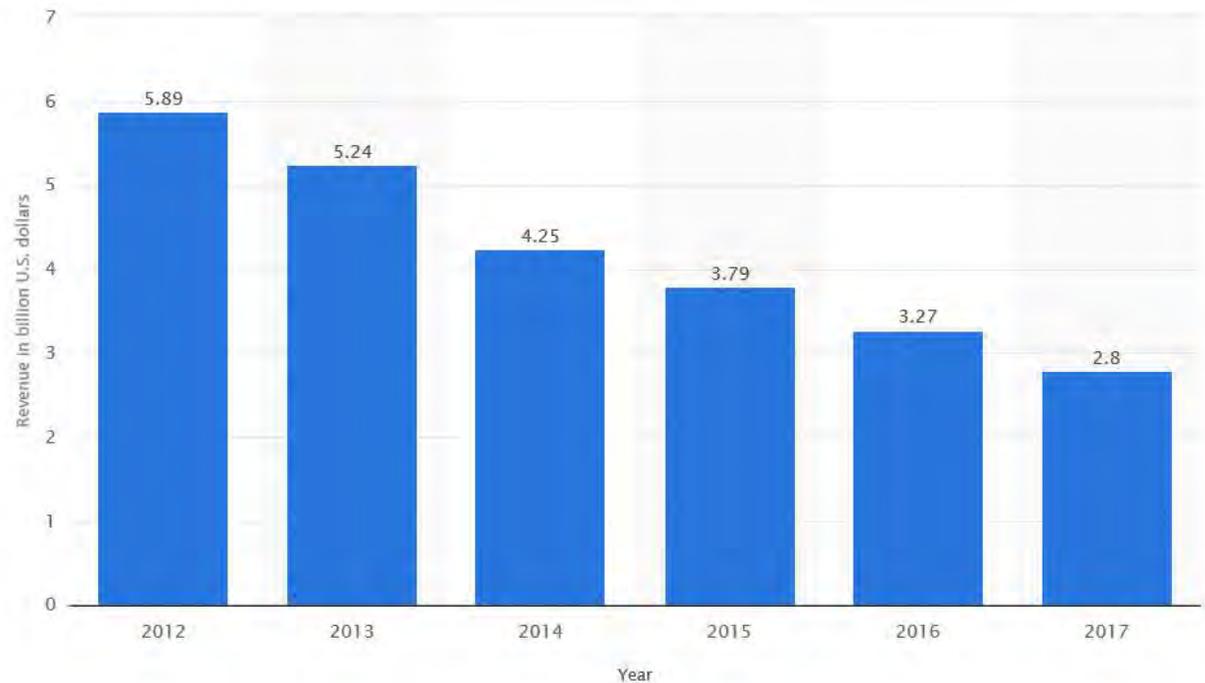
THE INDUSTRY

Netflix is a part of not only the video rental industry, but also the increasingly popular subscription video on demand (SVOD) industry as well. While at one time the video rental industry was thriving, today it is on the decline, and the SVOD industry is on the rise.

VIDEO RENTAL

Before movies and TV shows were streamed directly to our TVs, computers, phones, tablets and other devices, individuals and families had to go to the brick-and-mortar stores to find something they wished to watch and bring it back home for a night of entertainment. The first video rental store appeared in 1977 in Los Angeles. It was based on purchasing either an annual membership for \$50 or a lifetime membership for \$100. The membership allowed customers to then rent videos for \$10 per day. The store was a huge success and quickly grew to 42 other stores in less than two years.

Revenue of the DVD, game and video rental industry in the United States from 2012 to 2017 (in billion U.S. dollars)



In the 1970s and 1980s, both Betamax and VHS formats were offered, but most stores eventually went with the VHS format only, which caused Betamax to be completely phased out. A rental chain called Rogers Video, based out of Canada, was the first to offer DVD rentals. Many other chains and

independent stores eventually began to carry this format as well, and for those that are left in the industry, they now carry Blu-ray disc formats too.

During the 1980s and 1990s, video rental chain stores were popping up everywhere. By the middle of 1985 there

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were 15,000 video rental stores in the United States. Blockbuster owned 4,500 stores by 1995, clearing \$785 million in profits on \$2.4 billion in revenue. They garnered a lot of their profit off of late fees from overdue rentals, as it required minimal labor and no additional product sales.

Today in the United States, the video (and game) rental industry is declining. In 2012, the industry had revenue of nearly \$5.9 billion. Revenue has gone down each year since then, with 2014 revenue of \$4.25 billion. The estimated revenue for this industry in 2015 is about \$3.8 billion, and is projected to be about \$3.27 billion in 2016 and \$2.8 billion in 2017.

SUBSCRIPTION VIDEO ON DEMAND

SVOD services seek to provide customers video content anytime they wish, on any device from just about anywhere. Companies that offer SVOD services are continually striving to offer

more exclusive content and original programming to subscribers, typically for a monthly flat rate. Customers can easily pause, fast forward, rewind and stop the content they are watching, which is frequently updated by the various service providers.

SVOD service providers are not limited by the typical FCC broadcast regulations, and can therefore show whatever content they wish to carry, making these services very popular with the public. In 2010, revenue from SVOD services was only about \$4.3 million. However, in 2011, as technology began to advance and more subscription services came into the market, revenue jumped drastically to \$454 million, making SVOD services the largest segment in the online movie industry in the United States.

North America has the most developed market to offer SVOD services. As of 2013, there were over 25 SVOD service providers. Netflix, Amazon Instant Video

and Hulu Plus are currently the three most popular service providers.

In other parts of the world, Western Europe held 11 percent of this market as of 2012 with 7 million subscriptions and revenue for the year of \$575 million. In the same year, Eastern Europe held about 7 percent of the total SVOD market with over 4 million subscribers and revenue of \$253 million.

Asia had nearly 5 million SVOD subscribers in 2012 with revenue of \$255 million. This region of the world has very dense populations and holds a lot of potential for growth. In fact, as of 2012, it was predicted that over the next five years, markets in Latin America, Asia and Eastern Europe, which collectively comprised 20 percent of the market, would show immense growth and increase their market share significantly.

By 2017, the SVOD market is expected to reach close to \$8 billion and have more than 120 million global subscribers.

COMPETITION

SUBSCRIPTION VIDEO ON DEMAND

There are two main companies that appear to be Netflix's top competitors when it comes to subscribers and content. These companies are Amazon Instant Video and Hulu Plus.

AMAZON INSTANT VIDEO

As previously stated, *Amazon Instant Video* holds about 13 percent of the SVOD market as of the fourth quarter of 2014. Amazon's service can be utilized on practically any Internet-enabled device, just as Netflix can.

In April of 2014, Amazon unveiled their Fire TV streaming device, which, when compared to Roku, has three times the performance. The Fire TV also helped



Amazon reduce and even eliminate online video stream buffering that often occurs before a movie or TV episode begins. This device even offers a voice search feature, saving users from having to waste time scrolling through pages of content or typing in a search, which is much slower.

Amazon Instant Video is tied into the company's Prime service, which currently costs \$99 for a one-year

membership. The membership not only offers access to unlimited movies and TV shows that are available with the service (which was over 40,000 movies and TV episodes as of January 2014), but also free two-day shipping with purchases from Amazon.com, unlimited access to over a million songs, free unlimited photo storage with Amazon's Cloud Drive and access to over 500,000 free eBooks.

Even if a member was only interested in the Instant Video service and none of the other features that Prime offers, the \$99 price tag equates to only \$8.25 per month, which is slightly less than Netflix's \$8.99 HD streaming option.

Amazon Instant Video is tied into the company's Prime service, which currently costs \$99 for a one-year membership.

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However, the downside to this service is that a member must pay for a full year upfront, whereas with Netflix there is no obligation to stay a set amount of time, as it is a month-to-month service.

It's also important to note that not all streaming titles on Amazon Instant Video are included as part of the Prime membership. Instead, customers have to pay extra for these titles, which is typically \$1.99 per SD episode and \$2.99 per HD episode. This could anger some customers as they just paid \$99 for a service expecting to have access to all of the Instant Videos that they can search for, only to find that many of them they still have to pay extra for.

Amazon is a huge company with massive amounts of profit from their business. So it wouldn't be difficult for them to shell out a significant amount of money to market their Instant Video service. However, as of January 2014, Amazon hadn't really done any major marketing of the service, which could explain why its market share is far behind Netflix. They have since rolled out commercials for the service, but it is unclear as to how much they spent on their marketing efforts.

The service's movie selection is rather poor, however, TV shows are often aired on Hulu Plus the day after they appear on TV.

HULU PLUS

As of 2014, *Hulu Plus* held about 6.5 percent of the SVOD market, and a subscriber base of 6 million, which was up from 5 million in December 2013. As with Amazon Instant Video and Netflix, Hulu Plus subscribers can use the service on just about any Internet-enabled device.

Hulu Plus is oriented more toward television shows, as it has close relationships with all of the major networks. The service's movie selection is rather poor, however, TV shows are often aired on Hulu Plus the day after they appear on TV. The company has also begun featuring its own original series, as with Netflix and even Amazon Instant Video, to offer more content to

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their subscribers.

In the summer of 2014, Hulu began streaming a select amount of ad-supported TV episodes on mobile devices for free. Before this, Hulu's free service was only available on a computer and mobile remained a part of the company's premium service. The offering of free content is a great way to get people using Hulu's service and if they like it, they can sign-up for the paid subscription service.

While Hulu Plus offers customers unlimited streaming of all its content for \$7.99 per month (which is priced well for the service), it does feature a "modest amount" of advertisements during a show's normal commercial break. While this "modest amount" is usually around two to three short commercials, it can still be a downside to the service. One reason people enjoy streaming services is because they don't have to sit through commercials. But, perhaps because shows are instantly



available the day after they air on network TV, people are willing to sign up for the service to watch it with the very limited commercials as opposed to the large commercial breaks that often accompany a show on a cable network.

Advertisements on Hulu Plus are often interactive, in that users can click a button stating whether or not the ad was relevant to them. This allows an algorithm to predict which audiences will be appropriate for a particular brand's advertisements. Messages can also be tailored to subscribers based

on where that person is accessing the content. Since 2008, the Hulu Plus service has had more than 1,000 advertisers leverage their service.

DVD RENTAL

In the DVD rental market Netflix appears to have one main company as their top competitor: Redbox.

REDBOX

Redbox has been the clear market share winner in the video rental market the

COMPETITION

past few years. The company held 43.5 percent of the market heading into 2013, while Netflix was falling farther behind.

The company offers new-release DVDs and Blu-ray discs as well as video game rentals through their fully-automated, self-service rental kiosks. Redbox is stationed at about 35,000 locations nationwide which includes placement in grocery, drug and convenience stores and some Walgreens, Walmart and McDonald's locations.

The Redbox kiosks are equipped to hold over 600 DVDs at a time with anywhere from 70 to 200 different titles that are updated each week. The price per rental was recently increased at the end of 2014. The cost to rent a DVD is now \$1.50 per day (up from \$1.20), a Blu-ray disc is now \$2 per day (up from \$1.50) and video game rentals are now \$3 per day (up from \$2).

Though this may not seem like a lot of

Kiosks are equipped to hold over 600 DVDs at a time with anywhere from 70 to 200 different titles.

money, each disc must be returned to the Redbox kiosk within 24 hours of rental, otherwise the customer will be charged for another day, as one must use a credit card to pay for the rentals. If a customer is going to be out and about the next day and nearby the Redbox kiosk, perhaps it's not that big of a deal. However, for others, a special trip has to be made the next day to return the disc, which isn't as convenient as using Netflix's DVD-by-mail service where customers can keep them for as long as they wish.

But, Redbox is a service based around spur-of-the-moment convenience. Customers don't always want to wait a day or two to watch a movie. Redbox offers a way for customers to enjoy a

movie the very same night they choose to rent it.

In 2014, Redbox launched a point-based loyalty program called Redbox Play Pass that allows customers to earn free movie rentals. Members earn 10 points for each movie or game rental and after accumulating 100 points, the customer earns a credit for a one-day rental. The Play Pass program also gives members free movie nights on their birthdays and on the anniversaries of the program itself. This is a great marketing effort on Redbox's part to get more people interested in their service. Just for signing up with the Play Pass program, members receive a free one-night DVD rental as well.

Since the company began in 2002, they have rented more than 3.7 billion discs. Redbox has digital-marketing channels that "span 36 million email subscribers, 26 million app downloads and 5.4 million SMS subscribers" as of the end of the third quarter of 2014.

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