Executive Summary

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- **Shorting** Netflix (NFLX) is recommended due to the company's high valuation - according to our analysis it is overvalued by **32-47% and** the stock's price could decline significantly in the next 3-6 months

- **Investment Thesis:** Netflix is unlikely to sustain the immense growth it has been subject to over the past 2 years due to severe competition in its main markets UCAN & EMEA; penetration in emerging markets is also taking place at a slow pace; Netflix does not have enough pricing power and the degree of competition of the industry alongside with decline in playing time and user amount after COVID-19 pandemic are catalysts for future decline in revenue growth

- **Valuation:** The intrinsic value of the company lies around $200-$220 / share for the base case and around $260 / share in the optimistic case

- **Catalysts -** the company is unlikely to sustain the immense competition in India (one of its main presumed drivers of growth) from local content providers that fiercely compete based on price and different forms of content which prevents a successful subscriber acquisition strategy within the region

- **Risks –** the main diversifier of Netflix as SVOD – its original content is perceived by users as truly unique and fails to promotes future subscriber growth that outperforms the guidance of net user added of ~9m

- We can mitigate these risks by purchasing call options at current levels of $370-$380 exercise prices and exercise at the announcement of Q2 2022 numbers.

Company Overview and Market Outlook

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- **Industry – Entertainment;**

- **LTM Financials:** $29.54 B (Revenue), $6.23 B (EBITDA)
- **Market cap -** $168.71 B, **Enterprise Value -** $185.43 B
- **LTM Multiples: 6.2x EV/Revenue; 29x EV/EBITDA**

- **Product** – SVOD; pioneer in the industry; biggest cash content spent globally
- **Global Subscribers** – 222 mm worldwide, biggest market – UCAN & EMEA

- **Expected CAGR –** 8.9% – 12%
- **Biggest competitors –** AppleTV+, Disney+, HBOMax, Amazon Prime

Investment Thesis

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	Our View	Valuation Implications
Market environment	▪ Slower pace of growth due to higher prices and difference in content ▪ Newly emerging companies are penetrating the market engaging in the so-classed “streaming wars” ▪ The SVOD market becomes more diversified	▪ This resulted in significant decrease by 30% in 2021 in the USA ▪ Netflix’ valuation is highly dependent on its and only business unit.
Peak in Popularity	▪ Netflix looks to have reached a plateau in terms of acquiring new users to the platform ▪ The COVID-19 boost has ended	▪ Harder revenue generation ▪ Higher costs for the generation of new content that prompts more people to subscribe to the platform, ultimately influencing free cash flows
Substitution	▪ Social Videos raise (Tik-Tok saw a 70% YoY increase in revenue) ▪ Netflix is not well-positioned for the provision of short-form content ▪ The Metaverse hype	▪ All new forms of substitution are influencing the decrease in the growth of Netflix due to users switching to other entertainment opportunities

2021 FCF Margin vs Revenue Growth

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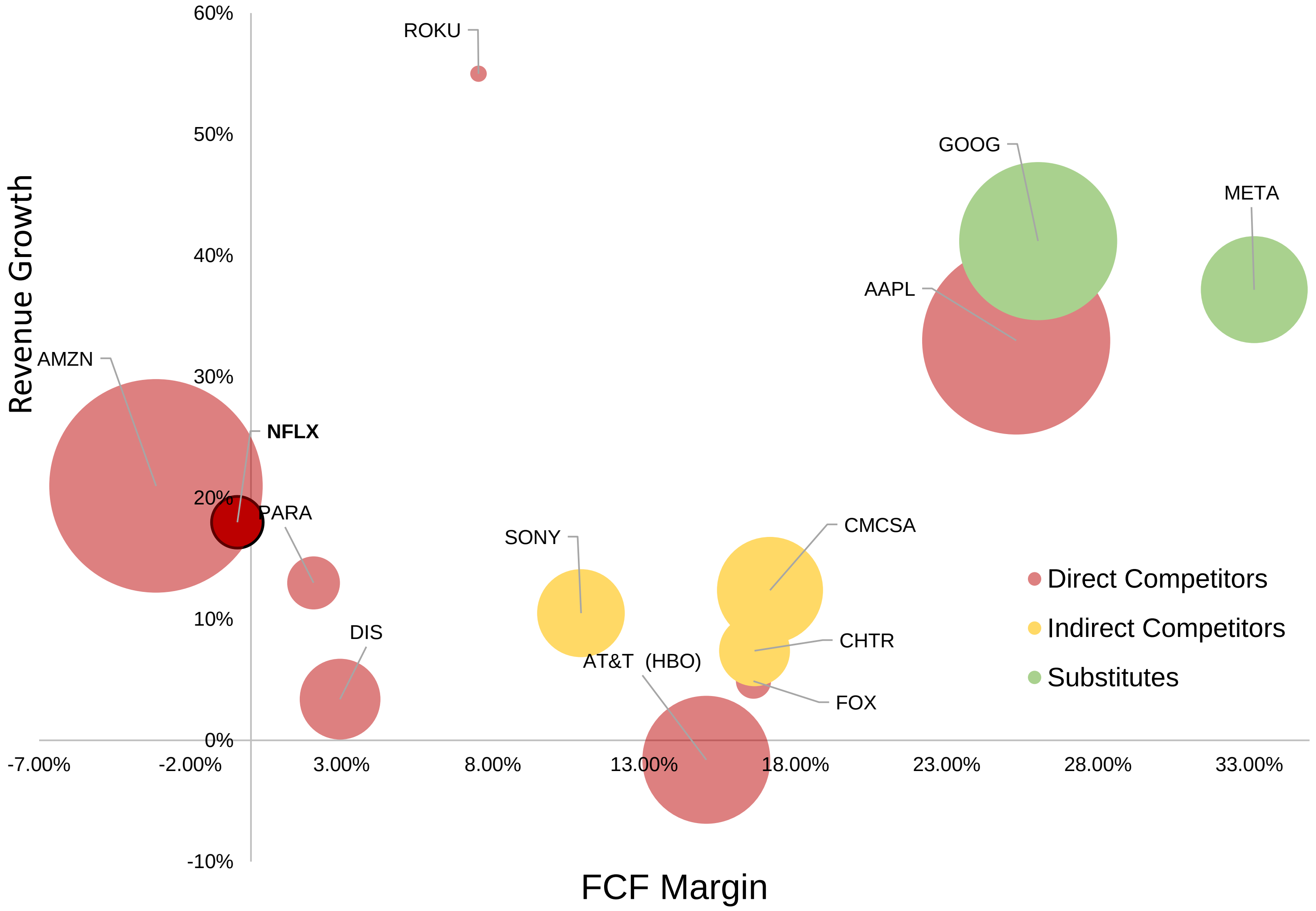

Low Growth, Low Free Cash Flow

NFLX FY ’21 Revenue / Growth Y-o-Y
$29 698M / 18%

FY ‘21 FCFM / Margin
-$131M / -0.44% Y-o-Y

There are presumably other more lucrative opportunities for the entertainment industry

Catalysts

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#1	Weakening of the COVID-19 restrictions	Weakening the restrictions will make people start travelling, exploring and socializing again which would mean less screen time at home. Preferred option might be theaters and cinemas.
#2	Q2 2022 Subscriber Guidance Miss	The Q1 Reports will influence the decisions of the investors and might decrease the price if Netflix continues to perform worse than its competitors and not meeting its targets
#3	Netflix fails to produce hit content over time	If Netflix is not capable of replicating its success with series such as “House of Cards”, “Squid Game”, etc. this will make it harder for the company to continue to grow its user base and retain existing subscribers.

Valuation Summary

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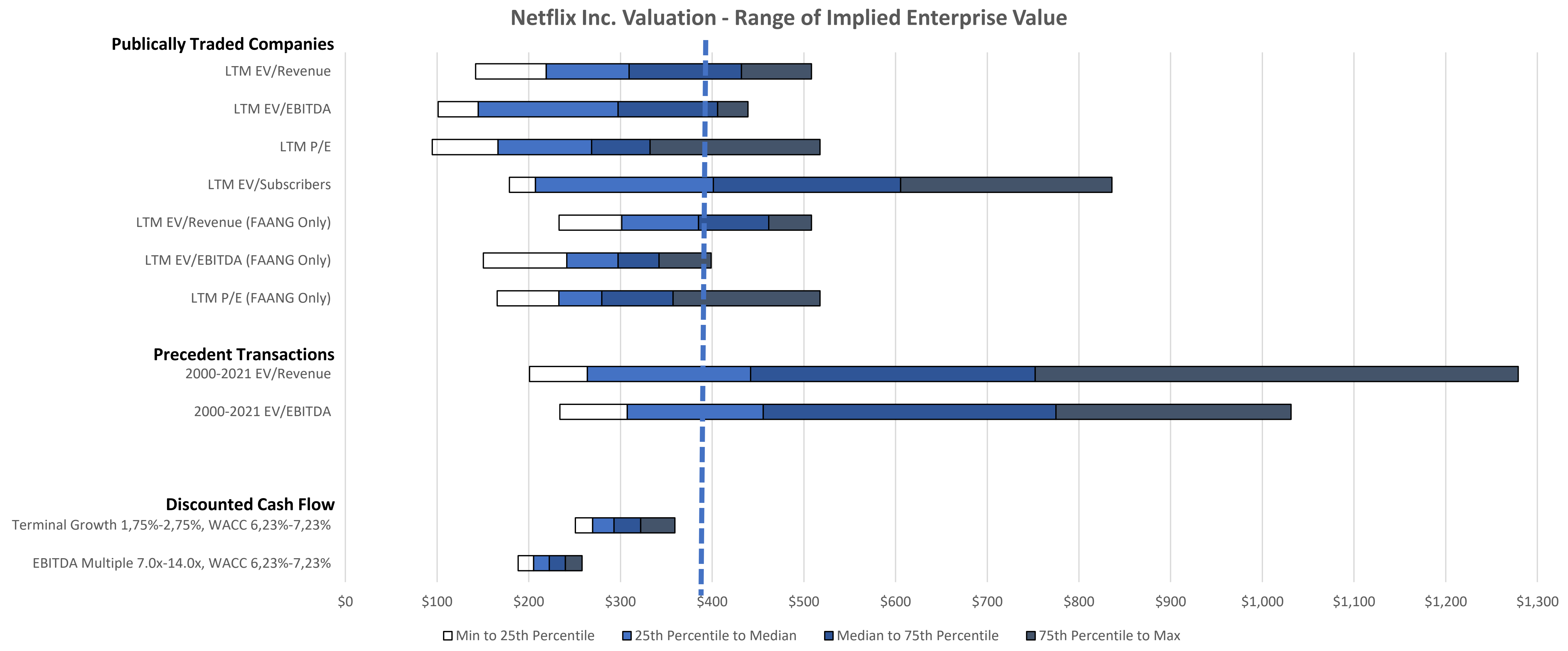

- Netflix stock trades in line with the higher end of the multiples of public companies and is slightly below those of the Precedent transactions
- The DCF, with our long-term views produces an implied EV at a significant discount to current share price to **30%-47%**
- In terms of LTM EV/Subscribers, the current valuation of the company is approaching the median value

Summary of DCF Assumptions

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	Downside	Base	Upside
UCAN Region Peak Sales	▪ $15.1B in FY 26	▪ $16.2B in FY 26	▪ $17.7B in FY 26
EMEA Region Peak Sales	▪ $13.9B in FY 26	▪ $17.1B in FY 26	▪ $18.4B in FY 26
LATAM Region Peak Sales	▪ $4.4B in FY 26	▪ $5.3B total in FY 26	▪ $5.8B in FY 26
APAC Region Peak Sales	▪ $5.3B total in FY 26	▪ ~$7B total in FY 26	▪ $8.2B total in FY 26
Operating Margins	▪ Falling down to 15%	▪ Remaining at 20%	▪ Climbing up to 25%
WACC	▪ 6.71%	▪ 6.71%	▪ 6.71%
Terminal Value	▪ 2.25% Terminal Growth	▪ 2.25% Terminal Growth	▪ 2.25% Terminal Growth
Implied Share Price	▪ ~$157	▪ ~$210	▪ ~$257

DCF Analysis - Sensitivities

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- In the Base Case, it seems unlikely that the company is undervalued

Sensitivity - Terminal FCF Growth Rate vs. Discount Rate and Implied Share Price from DCF Analysis

		WACC						
		5,98%	6,23%	6,48%	6,73%	6,98%	7,23%	7,48%
DCF Share Price Perpetuity Approach (WACC & Pereptuity Growth Rate) (steps up & down by 0,25% per year over 5 years)	1,50%	$ 278,45	$ 267,10	$ 256,89	$ 247,65	$ 239,26	$ 231,59	$ 224,57
	1,75%	$ 291,71	$ 278,98	$ 267,60	$ 257,36	$ 248,10	$ 239,69	$ 232,01
	2,00%	$ 306,63	$ 292,27	$ 279,51	$ 268,10	$ 257,84	$ 248,56	$ 240,12
	2,25%	$ 323,55	$ 307,22	$ 292,83	$ 280,04	$ 268,61	$ 258,32	$ 249,01
	2,50%	$ 342,90	$ 324,18	$ 307,82	$ 293,39	$ 280,57	$ 269,11	$ 258,79
	2,75%	$ 365,24	$ 343,58	$ 324,82	$ 308,42	$ 293,95	$ 281,10	$ 269,61
	3,00%	$ 391,33	$ 365,97	$ 344,26	$ 325,45	$ 309,01	$ 294,51	$ 281,63
	3,25%	$ 422,19	$ 392,12	$ 366,71	$ 344,94	$ 326,09	$ 309,61	$ 295,07

The only share prices that exceed the current share price

There is no share price that exceeds the current one for the EBITDA Multiple Approach

Sensitivity - EBITDA Multiple vs. Discount Rate and Implied Share Price from DCF Analysis

		WACC						
		5,98%	6,23%	6,48%	6,73%	6,98%	7,23%	7,48%
DCF Share Price EBITDA Multiple Approach (WACC) (steps up & down by 0,25% per year over 5 years)	7,00	$ 170,39	$ 169,14	$ 167,90	$ 166,69	$ 165,49	$ 164,31	$ 163,14
	8,00	$ 185,64	$ 184,21	$ 182,80	$ 181,41	$ 180,04	$ 178,69	$ 177,36
	9,00	$ 200,90	$ 199,29	$ 197,70	$ 196,14	$ 194,60	$ 193,08	$ 191,58
	10,00	$ 216,15	$ 214,37	$ 212,60	$ 210,87	$ 209,16	$ 207,47	$ 205,80
	11,00	$ 231,41	$ 229,44	$ 227,51	$ 225,60	$ 223,71	$ 221,85	$ 220,02
	12,00	$ 246,66	$ 244,52	$ 242,41	$ 240,32	$ 238,27	$ 236,24	$ 234,24
	13,00	$ 261,92	$ 259,60	$ 257,31	$ 255,05	$ 252,82	$ 250,63	$ 248,46
	14,00	$ 277,18	$ 274,67	$ 272,21	$ 269,78	$ 267,38	$ 265,01	$ 262,68

DCF Analysis – Sensitivities | Continued

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- A relatively higher amount of share prices for the perpetuity approach is above the current price, however, mostly at levels of WACC and Terminal FCF Growth that are too optimistic

Sensitivity - Terminal FCF Growth Rate vs. Discount Rate and Implied Share Price from DCF Analysis

DCF Share Price Perpetuity Approach (WACC & Pereptuity Growth Rate) (steps up & down by 0,25% per year over 5 years)	WACC						
	6,00%	6,25%	6,50%	6,75%	7,00%	7,25%	7,50%
1,50%	$ 371,75	$ 356,57	$ 342,91	$ 330,55	$ 319,31	$ 309,05	$ 299,64
1,75%	$ 389,47	$ 372,46	$ 357,24	$ 343,55	$ 331,16	$ 319,89	$ 309,60
2,00%	$ 409,40	$ 390,22	$ 373,17	$ 357,92	$ 344,19	$ 331,76	$ 320,47
2,25%	$ 431,98	$ 410,20	$ 390,97	$ 373,88	$ 358,59	$ 344,83	$ 332,37
2,50%	$ 457,79	$ 432,84	$ 411,00	$ 391,73	$ 374,59	$ 359,26	$ 345,47
2,75%	$ 487,57	$ 458,71	$ 433,69	$ 411,80	$ 392,48	$ 375,30	$ 359,94
3,00%	$ 522,31	$ 488,56	$ 459,62	$ 434,54	$ 412,60	$ 393,23	$ 376,01
3,25%	$ 563,36	$ 523,38	$ 489,54	$ 460,54	$ 435,40	$ 413,40	$ 393,98

The only share prices that exceed the current share price

- Even in the upside case for the EBITDA Multiple approach with higher sales growth rates and operating margins, there are still no share prices above the current one

Sensitivity - EBITDA Multiple vs. Discount Rate and Implied Share Price from DCF Analysis

DCF Share Price EBITDA Multiple Approach (WACC) (steps up & down by 0,25% per year over 5 years)	WACC						
	6,00%	6,25%	6,50%	6,75%	7,00%	7,25%	7,50%
7,00	$ 228,04	$ 226,34	$ 224,67	$ 223,02	$ 221,40	$ 219,79	$ 218,21
8,00	$ 248,73	$ 246,80	$ 244,88	$ 243,00	$ 241,14	$ 239,31	$ 237,50
9,00	$ 269,43	$ 267,25	$ 265,10	$ 262,98	$ 260,89	$ 258,82	$ 256,79
10,00	$ 290,12	$ 287,70	$ 285,31	$ 282,95	$ 280,63	$ 278,34	$ 276,08
11,00	$ 310,81	$ 308,15	$ 305,52	$ 302,93	$ 300,37	$ 297,85	$ 295,37
12,00	$ 331,51	$ 328,60	$ 325,73	$ 322,91	$ 320,12	$ 317,37	$ 314,66
13,00	$ 352,20	$ 349,05	$ 345,95	$ 342,88	$ 339,86	$ 336,89	$ 333,95
14,00	$ 372,89	$ 369,50	$ 366,16	$ 362,86	$ 359,61	$ 356,40	$ 353,24

Key Risk Factors

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- **Risk #1: The SVOD industry's lifecycle is extended:** Users might relocate from craving short-form to longer form of content
- **Risk #2: Competition does no continue to aggressively penetrate the market:** Netflix retains its leadership market share position as its original content serves as a profound differentiator compared to the licensing model of other providers such as Apple+, Amazon Prime and the likes
- **Risk #3:** Netflix is able to create new content that attracts more users to the platform and surpass guidance for net added subscriptions of ~9m for 2022, implying higher long-term sales potential
- **Risk #4:** Netflix announces the initiation of a new project revolving around different forms of content and digital identity of users to diversify its revenue streams
- **Worst-Case Scenario:** If everything above came true and the company contuse to trade at the P/E and P/S multiple levels, share price might increase to ~$450-500
- **Recommended Hedges:** We can also buy call options at $370-380 exercise price levels

Conclusions and Recommendations

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#1	We recommend SHORTING Netflix	At its current share price the company is fundamentally overvalued by 30%-47% .
#2	Q2 2022 Subscriber Guidance Miss	The Q1 Reports will influence the decisions of the investors and might decrease the price if Netflix continues to perform worse than its competitors and not meeting its targets
#3	Netflix fails to produce hit content over time	If Netflix is not capable of replicating its success with series such as “House of Cards”, “Squid Game”, etc. this will make it harder for the company to not just grow its user base, but also to retain existing subscribers.
#4	Risk can be hedged quite easily	We can buy call options at $370-380 exercise price levels which mitigates the risks of any increases in price provided that the company outperforms and raises future guidance for subscribers’ growth.