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Netflix Q1 growth outshines Q4 despite struggles and increased dependence on global audiences

Article

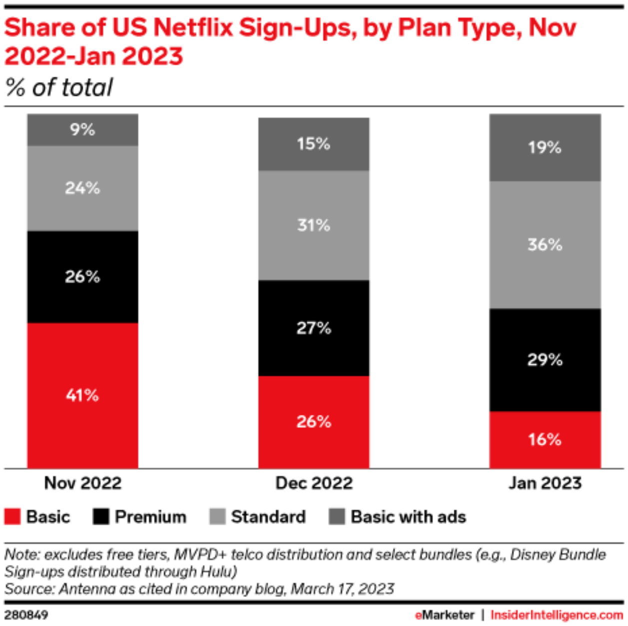
The news: Netflix reported Q1 results on Tuesday that failed to meet its revenue guidance and analyst estimates. Subscriber additions also fell below market expectations.

- The company achieved 3.7% year-over-year (YoY) growth. For context, that's better than last quarter's 1.9% revenue growth—but trails the three quarters preceding it.
- Global streaming paid memberships rose 4.9%—higher than Q4's 4.0% growth.
- 1.75 million new global streaming paid memberships was far lower than 7.66 million in Q4, but outperformed the three preceding quarters. The first two quarters of 2022 resulted in negative net additions.
- The company forecast revenues of $8.24 billion for the second quarter, which would represent 3% YoY growth but just barely edging up from Q1's $8.16 billion.

Analyst insight: "Revenue outlook for Q2 is below what investors were expecting," said principal analyst **Paul Verna**. "It's a worrying sign for a business that, despite still being a market leader, is struggling to get its mojo back."

Dropping viewers: Netflix is expected to lose viewers for the second consecutive year in 2023 according to our forecast update, with the number of viewers decreasing by 0.5% to 170.6 million.

- The decline is attributed to the implementation of paid account sharing, which will likely cause casual viewers to drop off and subscribers to downgrade or cancel their plans.
- In announcing Q1 earnings, the company said that in Canada, its paid membership base rose with the launch of paid sharing—and the market's revenue growth is at a faster pace than the US. Despite that, the company declined to announce a firm date for the feature's US debut but did point to sometime in Q2.
- The focus on generating revenues over customer satisfaction may hurt long-term loyalty, particularly among Gen Z users, college students who may not be able to afford their own subscriptions.
- Interestingly, the decline persists despite Netflix's new lower-priced ad-supported option, which has underperformed market expectations to date.

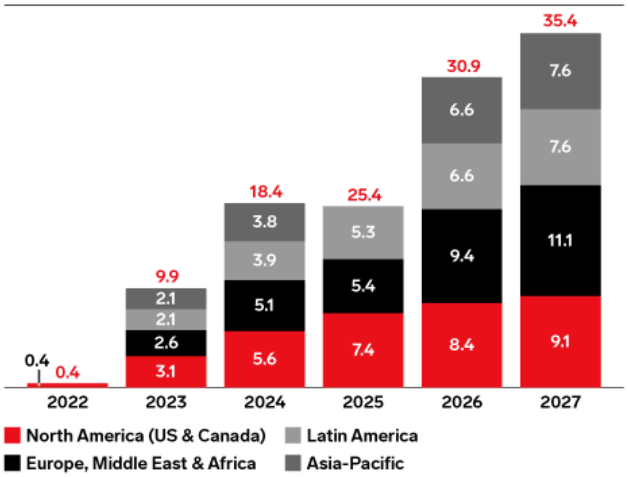


Growth where you can get it: Given stagnating growth in key markets including North America, Netflix is looking to emerging markets to take up the slack.

- The service has lowered subscription costs in over 30 countries, including Eastern Europe, sub-Saharan Africa, the Middle East, Southeast Asia, and Latin America, as it aims to retain users who have a choice of various streaming options. In some countries, subscription costs were cut by up to 50%.
- Yesterday's shareholder letter acknowledged that these regions represented below 5% of the company's 2022 revenue, but "increasing adoption in these markets will help to maximize our revenue longer term."
- Another reason to invest in these markets: Average Revenue per Membership (ARM) increased in Q1 versus the previous quarter in Netflix's EMEA, LATAM, and APAC regions, but dropped in US and Canada.
- This focus on EMEA should pay dividends: According to some estimates, by 2027, the region will have **22% more ad-supported subscribers** than the next-closest region (North America). That's important, since that region monetizes significantly better than Latin America or Asia-Pacific.

Netflix Ad-Supported Subscribers Worldwide, by Region, 2022-2027

millions



Source: SVB MoffettNathanson estimates as cited in MediaPost, March 14, 2023

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