THE WALL STREET JOURNAL.

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Netflix's Global Growth Faces New Threats

Rivals abroad band together, as competition at home intensifies, putting fresh pressure on the streaming giant

Eva Green as Vanessa Ives and Josh Hartnett as Ethan Chandler in the series 'Penny Dreadful.' *PHOTO: JONATHAN HESSION/SHOWTIME*

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Jan. 17, 2016 5:30 a.m. ET

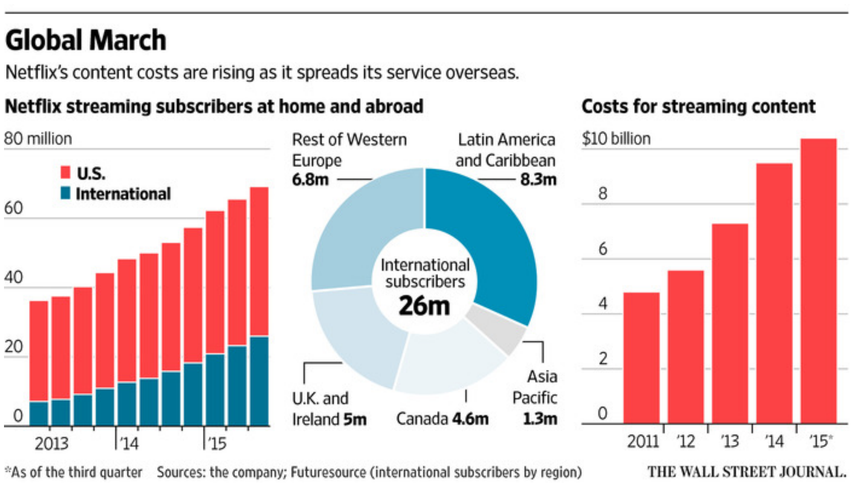
When Netflix Inc. won rights to premiere gothic TV drama "Penny Dreadful" in several European countries, local media companies that lost out were miffed.

They were growing increasingly frustrated that the streaming juggernaut has been scooping up exclusive rights to top shows as it pursues an aggressive global expansion, locking them out in their home markets. It was time to mount a response.

Shortly after the "Penny Dreadful" deal in late 2014, senior executives at French pay-television group Canal Plus and rival operator Sky PLC met to discuss jointly bidding for TV shows, a way to counter Netflix, people familiar with the discussions say.

" 'Penny Dreadful' was a big battle; we absolutely wanted it," a person familiar with Canal Plus's thinking said. "On our own, we couldn't do it anymore."

Similar discussions are taking place among Netflix's rivals elsewhere. Streaming service Viaplay in the Nordics has been talking with Australian streaming service Stan, Lightbox in New Zealand and Hulu in the U.S. with hopes of forming a bidding alliance in time for May's annual screenings of new shows for international buyers in Los Angeles, people close to the talks say.



Europe's Sky, which effectively is controlled by 21st Century Fox, has held similar conversations with Canada's Bell Media and Australia's Foxtel in recent months, other people involved say. Various providers, including Southeast Asian streaming services iflix and HOOQ, as well as Canada's Shomi, also are in the mix.

Executives say discussions are nascent and acknowledge hurdles toward getting multiple companies in different countries to agree on content. But taken together, the talks are a burgeoning rebellion against Netflix's growing global might. The companies hope banding together will allow them to make more appealing offers to TV studios that create and sell shows.

"The competition is bloody fierce," said Jakob Mejlhede, executive vice president at Sweden's Modern Times Group, which operates Viaplay. "If you enter into a straight up bidding war with Netflix, you are most likely going to lose."

With 69 million total customers, including 26 million outside the U.S., and a $5 billion content budget for this year, Netflix is willing to outbid most any local TV network or streaming service. The company this month announced it is now available in more than 190 countries, including 130 new markets such as Russia and India.

Still, Netflix has yet to turn its international investments into profits. It will need to keep up subscriber growth to offset ballooning content obligations, which could increase if rivals join forces and bid more aggressively.

Another potential challenge for Netflix: its well-funded U.S. streaming rivals that are ratcheting up global plans. Amazon.com Inc. has spoken with studios about taking options to buy world-wide rights to original series and reruns, people familiar with the talks say. Hulu is newly studying international expansion—whether to go it alone or partner.

Investors, who have sent Netflix shares up 121% during the past 12 months despite slowing U.S. subscriber growth, will get an update when the company reports earnings today.

Netflix benefits from simultaneously buying rights in many territories—traditionally studios have sold shows country by country. In the case of “Penny Dreadful,” Netflix bought rights across seven territories, paying more than what regional players offered in total. Sky’s German arm lost out, but it kept the rights in the U.K. because it helped co-produce the show. The prices the bidders offered weren’t disclosed, as is generally the case in content-licensing deals.

Netflix this month extended its deal to stream “Breaking Bad” to more than 150 countries world-wide, trumping interest from players such as HOOQ, people familiar with the deal said.

Netflix so far only can offer a slim library in many new markets compared with its U.S. service, so the company has prioritized acquiring global rights for content. It also wants a long exclusive window world-wide, seeking to keep shows for up to a decade after their last episodes go up.

“We’ve gotten enormous support from content owners for one reason—we’re outbidding local players,” Netflix Chief Executive Reed Hastings said in a recent interview. Prices are “significantly higher” than just four years ago due to Netflix.

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partnership discussions, some Netflix rivals such as Sky are more focused on co-financing expensive original series, while others are prioritizing bidding on global rights to Hollywood reruns. Sky is "very successful" in securing rights, across its territories, but has an "open mind" to striking global deals "if we thought it could add value," said Gary Davey, Sky's managing director of content.

Studio executives estimate that global streaming deals for reruns of the hottest serialized dramas are going for $3 million to $6 million an episode, though less-popular shows are less expensive.

For original series, Netflix offers to pay premiums equivalent to 120% to 150% of a show's cost for global rights. Studios typically recoup about 70% of their production costs by selling first-airing rights to a TV network and rely on uncertain revenue from reruns to generate a profit. Today, serialized dramas can cost about $4 million an episode to make, studio executives say.

Taking the rich global-rights fees Netflix offers can instantly make a show profitable and please the actors and producers who share in the returns. But there are trade-offs for studios. It is possible they could earn even more by selling a show to regional players. Ideally, studios would prefer to nurture competitors to Netflix.

They "have become very wary of what the future might look like if they enable much more of a global monopoly," said Mike Sneesby, chief executive of Australia's Stan.

Global consortia haven't materialized yet, but local players already are trying new ways of countering Netflix at home.

Media conglomerates such as Sky, Sweden's Modern Times Group and Australia's Foxtel increasingly are buying television and streaming on-demand rights to shows in a single bundled deal, effectively cutting out Netflix from their territories. In Sky's case, the merger in 2014 of its British, Italian and German units has given the company added heft for buying rights.

Foxtel won local rights to "Fear the Walking Dead" from studio Entertainment One—despite Netflix's global offer—by linking up with Presto, the streaming service it owns half of, and sister company 21st Century Fox's FX Network. (21st Century Fox, which also has a one-third stake in Hulu, was part of the same company as Wall Street Journal-owner News Corp until 2013. News Corp. owns 50% of Foxtel.)

Still, Peter Bithos, chief executive of Southeast Asian streaming service HOOQ, said bigger, pan-regional partnerships are necessary to really take on Netflix, and predicted they will form within six months. Going forward, "if you can't put global rights on the table, you're going to be at a disadvantage," he said.

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