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Cloud Broadcasters Creating Barriers To Entry

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Summary

- Google, Netflix and Amazon have all emerged as threats to broadcasters.
- Google and Amazon do it with infrastructure, Netflix with rights.
- Of the three, Netflix is the most vulnerable.

When we think of broadcast networks we commonly think of **CBS** (CBS), **NBC** (CMCSA), **Fox** (FOX) and **ABC** (DIS).

They have two things that upstarts lack, rights and infrastructure. Their broadcast affiliates are able to deliver millions of simultaneous views on a set schedule, repeating it from a central store. And this mass creation of audience drives the industry.

In this decade a new "big three" of broadcasting is emerging, but none of these incumbents are invited to the party. We're talking here of **Google** (GOOG) (NASDAQ:GOOGL), **Amazon** (AMZN) and **Netflix** (NFLX). All three have rights and infrastructure. All three are creating barriers to entry for other players.

But for how long?

In the case of Google and Amazon, that barrier is infrastructure. Google's YouTube can deliver millions of streams of programming at the same time. So can Amazon Prime. What is new this week, with Amazon's $970 million purchase of Twitch, is to see that these streams could all be the same thing. Twitch, which has more of an audience than MTV, over 1 million individual "broadcasters," and pays them for their rights on a revenue share basis, just like many publisher web sites.

Netflix' barrier consists of cash for rights. The company paid about $100 million for "House of Cards," gaining 3 million new subscribers in the process. It followed that up with "Orange is the new Black." Hits, generating audience, generated subscription revenue.

The whole "controversy" over "net neutrality" is based on the need of the new "big three" to reach the last mile, where the bulk of subscribers are, using infrastructure mainly owned by Comcast (NASDAQ:CMCSA), the owner of NBC. Comcast will, once its purchase of Time Warner Cable (NYSE:TWC) is complete, control nearly 40% of the nation's broadband Internet subscribers, and essentially signed a peace treaty with Netflix earlier this year, taking payments for using its network which did not break Netflix' profitability.

In fact, Netflix' margins have been increasing and came in at over 5% for the quarter ending in June - 5 cents of every dollar went to the net income line. Combine that with year-over-year revenue growth of about 30% and the company's valuation of $28.4 billion starts to look rational.

In the end, however, Netflix may find itself less vulnerable in the last mile than in the first, since Netflix runs mainly on Amazon's AWS cloud. Right now Amazon is dropping prices on its cloud in order to maintain public cloud market share, but at some point that is going to change, once there is a cloud shake-out. At that point Netflix becomes vulnerable, and we may in the end be speaking about a "big two" - Google and Amazon.

At least that's the way my money is betting. In the end, history shows that rights follow infrastructure rather than leading it. Google and Amazon are each putting $1 billion each quarter into their infrastructure, and while some of Amazon's money is going into warehouses, and some of Google's is going into fiber optic lines, most of it is going into data centers, into public clouds that are slowly replacing broadcast networks as the way people watch TV. Those barriers exist, even if they're not yet being exploited.