How Netflix Became a Value Stock

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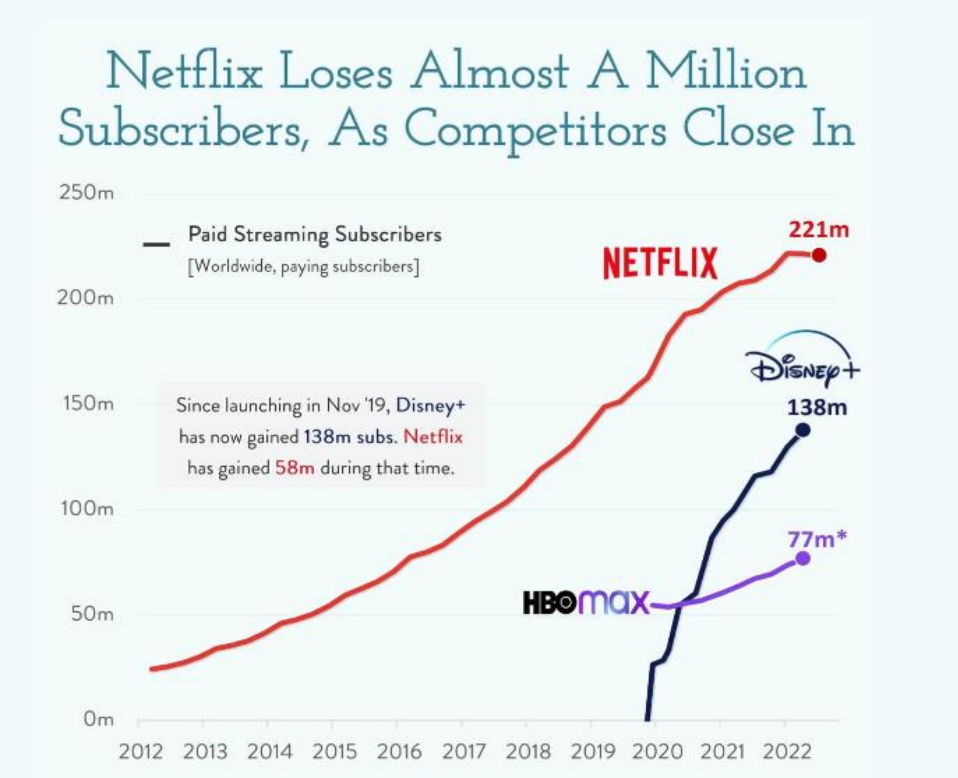
Case Study—Netflix (NFLX)

ENTERTAINMENT

Netflix shares crater 20% after company reports it lost subscribers for the first time in more than 10 years



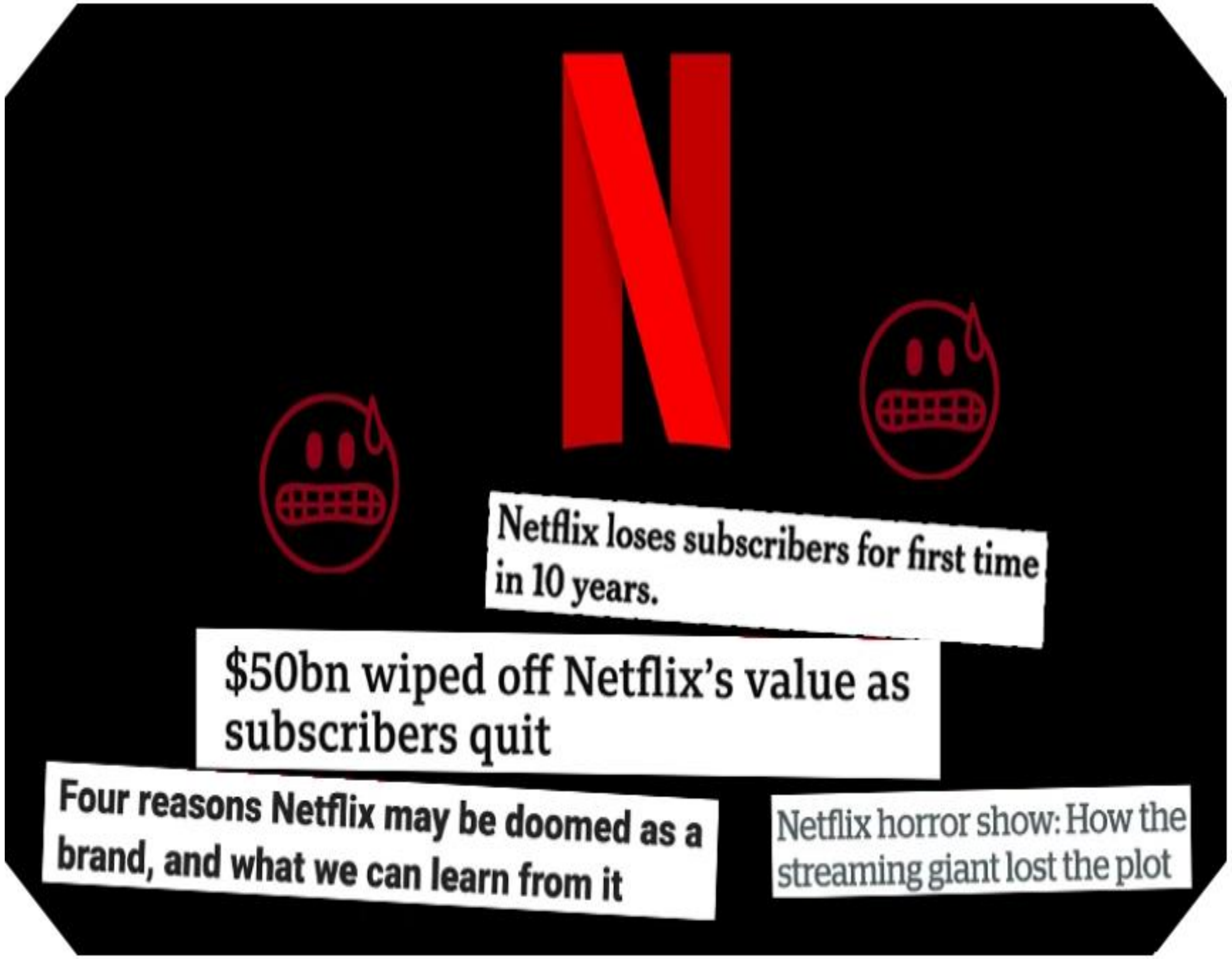


Image: Tina Tiller

Sources: honest-broker.com, thespinoff.co.nz, chartr.

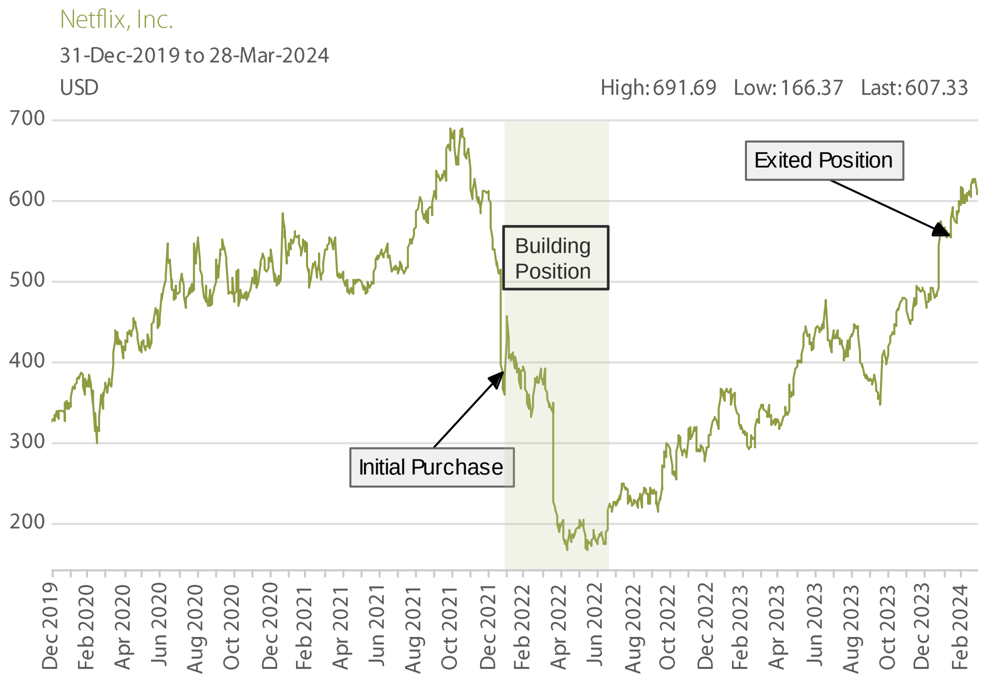
For illustrative purposes only.

STOCK EXAMPLE

Netflix (NFLX)

Company Description

A global leader in video streaming.



Attractive Business Economics

- Business scale creates competitive advantages: lower marketing costs per subscriber, more purchasing power for content, the broadest audience appeals to talent in the industry, the most data, and industry leading margins.
- Time tested business model: premium entertainment via compelling storytelling in a superior format (non-linear) vs. legacy competition.
- Bargain Cost: Netflix's streaming service is the best value in video media to consumers.
- Less economically sensitive: subscription-based revenue model is less economically sensitive.

Sound Financial Condition

- Transitioned from a company burning significant cash and having low operating margins to one that was positioned to generate significant free cash flow despite aggressive content investments.
- With $7 billion of cash and $15 billion of debt, Netflix has net debt to EBITDA of only 0.3x.
- 11X interest coverage.

Attractive Valuation

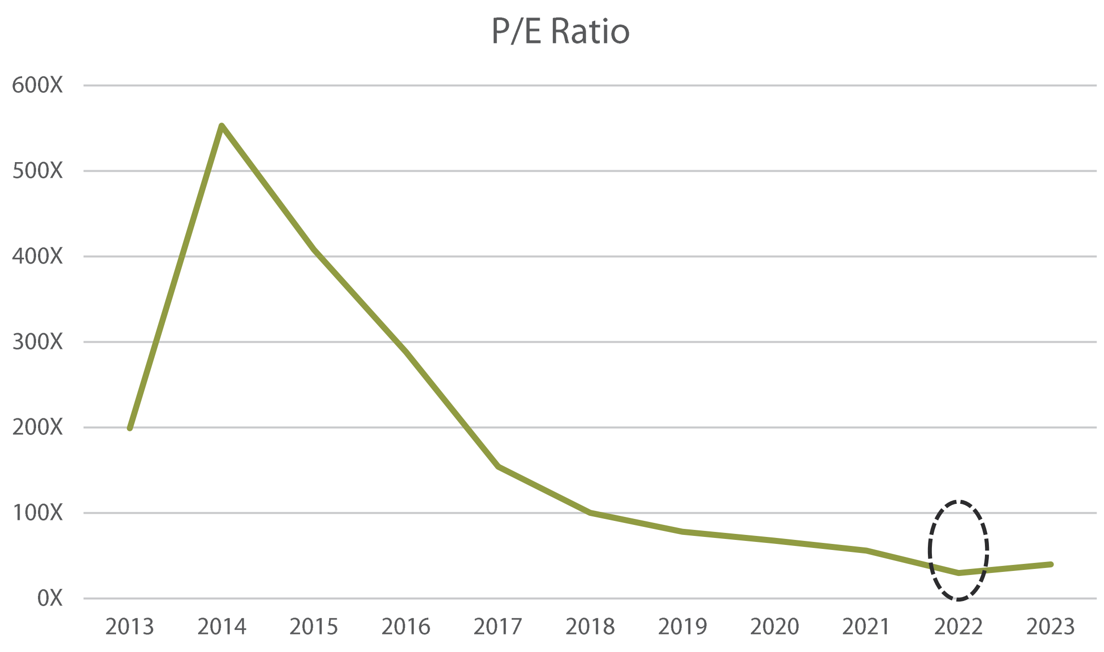
- At original purchase, the shares were 16X our view of 2-years forward earnings for a business growing double digits organically and a decade+ runway of subscriber expansion.
- Secondary purchase was under 10X our view of normal earnings.
- Rising revenues are significantly positive for operating margins because contribution margins of each incremental subscriber are 100%.

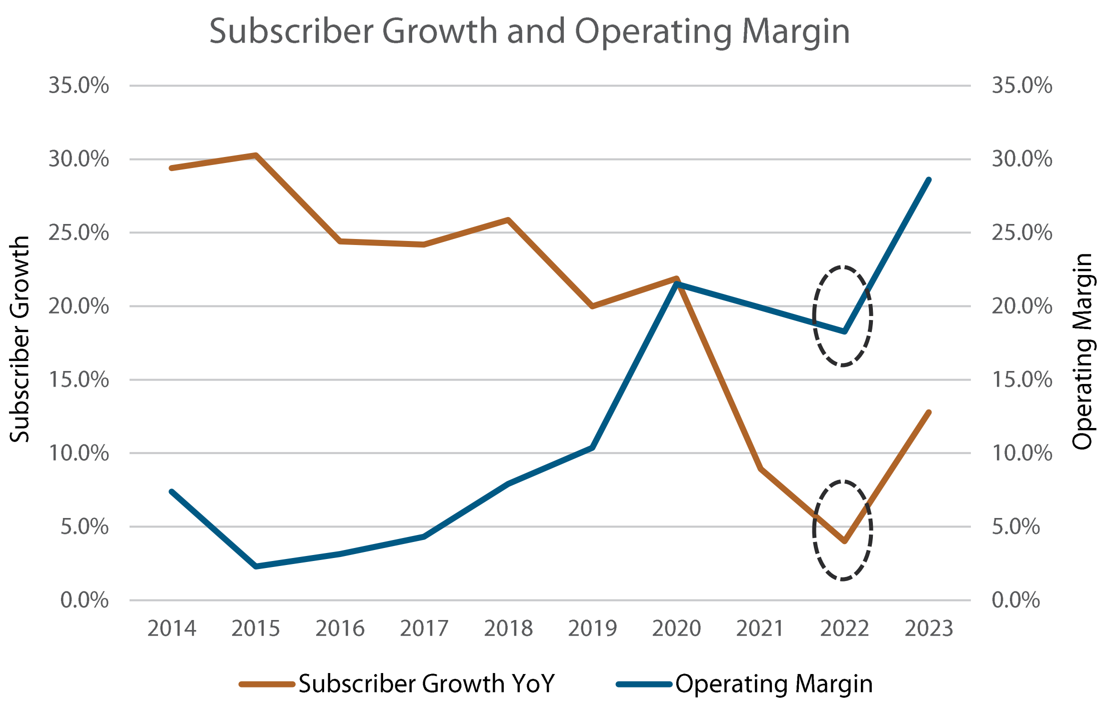
Source: Artisan Partners/FactSet. Previously held in Artisan Value Fund. **Past performance does not guarantee and is not a reliable indicator of future results.**

Variant Perception

- Streaming economics are proven at scale
- Growth is slowed due to unique COVID factors, but is structurally intact
- Advertising tier is a proven media/streaming model and will broaden the offering
- Password crackdown is fair and will be executed thoughtfully

From The Outhouse to The Penthouse





Source: Bloomberg.

Notes and Disclosures

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Artisan Value Fund

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Artisan Value Income Fund

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Definitions:

Financial Leverage is a factor that is calculated as a composite factor that includes degree of financial leverage, debt to equity, interest and cash flow coverage ratios. **Free cash flow** is a measure of financial performance calculated as operating cash flow minus capital expenditures.

EBITDA Earnings before interest, taxes, and amortization (EBITA) is a measure of company profitability used by investors. It is helpful for comparing one company to another in the same line of business. In some cases, it can also provide a more accurate view of a business's value.

Interest Coverage The interest coverage ratio is a debt and profitability ratio shows how easily a company can pay interest on its outstanding debt. It is calculated by dividing a company's earnings before interest and taxes (EBIT) by its interest expense during a given period.

Forward Earnings Forward earnings are predictions of a company's earnings for the next period, usually up to the end of the current fiscal year or sometimes into the following year.

P/E Ratio The price-to-earnings (P/E) ratio measures a company's share price relative to its earnings per share (EPS). Often called the price or earnings multiple, the P/E ratio helps assess the relative value of a company's stock. It's handy for comparing a company's valuation against its historical performance, against other firms within its industry, or the overall market.

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