Media industry update: battle of the streaming services and the emergence of Warner Bros Discovery

Introduction

In the rapidly evolving media landscape, the emergence of streaming as the primary battleground for viewer attention has ushered in a new era of competition and consolidation among media giants. As traditional broadcast and cable television give way to on-demand digital content, companies like Netflix[NASDAQ: NFLX], Disney[NYSE: DIS], and the newly formed Warner Bros Discovery[NASDAQ: WBD] are vying for dominance in the United States and across Europe. This shift towards streaming highlights a sector experiencing strong growth and transformation, where content is king, and the race to capture audiences' viewing time is fiercer than ever. Amidst this backdrop, the strategic moves of Warner Bros Discovery, especially its potential merger discussions with Paramount[NASDAQ: PARA] signal a critical movement in the industry's future. This article delves into Warner Bros Discovery's actions since its formation in 2021 and what a further consolidation could mean in a market already brimming with heavyweight contenders.

Media Industry Overview in the US and Europe

The United States: A Consolidated Powerhouse

In the United States, the media industry has long been characterized by its consolidation, with a few key players dominating the market. In the first six months of 2023, Amazon Prime Video, the streaming platform of Amazon [NASDAQ: AMZN] was the most popular subscription video-on-demand (SVOD) service in the United States, with a market share of 21%, based on the users' interest in adding content to their watchlists of specific streaming platforms. Netflix and relaunched service Max followed with 20% and 15% market shares, respectively. While subscription streaming platforms increased their subscriber bases in 2020 and 2021 due to the measures taken during the COVID-19 pandemic, 2022 and 2023 saw services such as Netflix and Disney+ lose a substantial number of customers. Furthermore, large media companies' direct-to-consumer businesses are struggling to profit, and Disney reported a loss of 4.5 billion U.S. dollars for its streaming services in 2022.

Streaming companies implemented several strategies to compensate for subscriber and income losses, such as launching more profitable ad-supported tiers, cracking down on credential sharing, laying off thousands of employees, and spending less on content. The Walt Disney Company was already able to increase DTC profits in the second and third fiscal quarter of 2023 and is predicted to achieve profitability by 2024. Its cost-cutting measures include layoffs and savings in content spending by reducing content produced and removing TV shows and movies from its streaming services. As a whole, the US's consolidated nature in this sector underpins the relentless push for growth and intense competition among established players to innovate and differentiate their offerings.

Europe: A Fragmented Landscape with Room for Growth

Contrastingly, the European market presents a more fragmented landscape, with a broader array of players and fewer exerting excessive control. This fragmentation is partly due to the diverse cultural and linguistic landscape across Europe, which necessitates a more localized content strategy and provides opportunities for niche and regional players to flourish. The less consolidated nature of Europe's media sector highlights the potential for significant growth, especially for players like Netflix, Disney and Warner Bros Discovery, capable of navigating its complexities with tailored content and distribution strategies. By 2024, the video streaming market in Europe is anticipated to generate a revenue of $20.89bn. It is expected to exhibit a compound annual growth rate (CAGR 2024-2027) of 8.33%, resulting in a projected market volume of $26.56bn by 2027 and 284.6mm users. When compared globally, the United States is projected to generate the highest revenue in the market, reaching $43.97bn in 2024.

The divergent paths of the US and European markets underline the strategic approach companies must make in their path for dominance. For Warner Bros Discovery, and potentially in collaboration with Paramount, the stakes involve expanding their content libraries and subscriber base and integrating their operations and strategies to leverage synergies. The prospect of merging these media titans holds the promise of creating a powerhouse capable of competing more effectively against Netflix and Disney, especially in markets where streaming is still flourishing, and the appetite for diverse, high-quality content is growing.

How Warner Bros Discovery plans to disrupt the streaming sector

Warner Brothers. Discovery Inc is an American entertaining company engaged in the production, creation, distribution, and licensing of all forms of entertainment. Initially founded in 1905 by the four Warner brothers (Albert, Sam, Harry, and Jack), the firm initially began as a movie theatre business, then growing to become a film distributor and producer. In 1923 the firm was incorporated as Warner Bros, Pictures. Incorporated. The firm is primarily known for its studio, which is one of the most successful of all time. It is involved in all areas of the entertainment industry ranging from film, television, and home entertainment, to animation, comic books and videogames. Moreover, because of its many years of existence, and its importance in the industry, the firm has one of the largest content libraries of all, consisting of over 145,000 hours of programming, 12,500 films and 2,400 television shows.

In 1989, Warner merged with publishing company Time, Inc. This led the firm into an era of significant growth and fame, producing the Harry Potter film series, the highest-grossing film series of all time (without adjusting for inflation). Moreover, in June 2018 Warner Bros parent company, Time Inc was acquired by AT&T[NYSE: T] for $105bn. At the time, this transaction enabled Warner to deliver their content to consumers to capitalized on the growing demand for video content, as well as to deliver it through a multiplatform basis. Over the next years, the firm went through a period of important growth, developing streaming platforms as HBO Max, as well as released box office leaders.

More recently, in April 2022, Discovery acquired Warner from AT&T for $79bn, forming Warner Bros Discovery. The transaction combined Warner's premium entertainment, news and sport divisions with Discovery's entertainment and sport businesses. For the transaction to be completed, AT&T spun off Warner into a new company which then merged with Discovery. Following tough negotiations, the two sides agreed to divide ownership, giving AT&T shareholders a 71% and Discovery a 29% share, respectively. Moreover, for AT&T, the transaction allows them to eliminate $43bn of debt, which stood at $169bn before the transaction. Furthermore, the consolidation will give rise to cost synergies, which are expected to bring savings of up to $3bn within the first two years after completion.

Together, the companies form the second-largest media group by revenue after Disney, with $41bn in revenue for 2023. Moreover, the group can grow to rival Netflix as they are one of the few global streaming services with +200m subscribers. Discovery operates in more than 80 networks across the world, with strong local language presence in several European countries. Moreover, the company is expected to never again enter into licensing deals that prevent them from broadcasting their services in some geographies, as the one they have with Comcast's

Sky which doesn't allow them to launch HBO Max in the UK, Germany and Italy until 2025. However, to continue its expansion the firm will have to decide whether to offer all its streaming services under one same platform, as Netflix does, or use a multiple brand approach, as Disney does with Star, Hulu, and ESPN on some markets.

In late 2023, it was revealed that Warner was in discussions with Paramount Global, the studio behind CBS News and the Top Gun and Mission Impossible films. The acquisition talks come at a time where US media groups are aiming to increase their profitability while they continue fighting, and trailing, on the streaming war with Netflix. This potential merger had the capacity to merge the Max streaming service, with about 95m subscribers, with Paramount Plus, with 63m subscribers (Q3 23' figures). However, analysts claimed that the deal was not great for Warner as it would mean increasing their presence in cable television, also known as linear TV, a sector currently facing pressure as tv networks are losing subscribers and the advertising market has slowed down. Hence, adding linear TV to an existing linear TV company would not necessarily have a major financial impact to the company, and they should rather focus on scaling down their linear TV presence. Moreover, Warner had limited ability to make a deal in the near term as a result of a provision in the deal structure from the merger between AT&T and Discovery, that created Warner Bros Discovery. This provision will expire in April 2024. Nonetheless, in February 2024, Warner Bros Discovery announced they were calling off their merger talks with Paramount. However, there are reports that the latter is actively seeking a deal, and there are rumours of ongoing negotiations with Apollo and Skydance.

Also, in February 2024, in the United States, ESPN, Fox[NASDAQ: FOX] and Warner Bros Discovery announced plans to launch a sports streaming platform that will bring together at least 15 different sport networks, including content from all the major US sports leagues and college sports. The three companies will share one-third ownership in the Joint Venture (JV) and service is expected to come live in the fall of 2024. This announcement comes at a time where two of the participants of the JV, ESPN and Warner Bros Discovery, are preparing to enter negotiations to renew their NBA rights. This is highly relevant as it is something that happens every 10 years. However, this will have no impact on the JV as it does not aim to acquire individual sports rights. Moreover, this JV comes at a time where sport leagues are charging higher fees for broadcasting rights, which are now being split between different media distributors.

This new offering will likely be appreciated by sport fans who over the past years have had to juggle between multiple networks and subscriptions to have access to the broadcasts of their favourite sports. The platform will include matches from the NFL, UFL, NBA, WNBA, MLB, NHL, WNDA, College Sports (NCAA, Big 10, SEC, etc.), Golf (PGA, PGA Championship, The Masters, TGL), Tennis (Wimbledon, US Open, Australian Open), Cycling (Giro d'Italia, UCI Mountain Bike Tour), Football (FIFA World Cup, MLS, La Liga, Bundesliga, UEFA, Concacaf), Combat Sports (UFC, Top Rank) and Auto (Formula 1, NASCAR, 24 Hours of Le Mans), among others. Overall, the service will aggregate about $16bn worth of sports rights according to estimates by Bernstein Research, one of Wall Street's main sell-side research companies. Moreover, subscribers will be able to bundle the product from this new JV with Disney+, Hulu and/or Max.

For Warner Bros Discovery, this JV will allow them to expand their viewers, among other positive impacts. By having the opportunity to connect their leading content with an unparalleled collection of sports channels and events, they will have exposure to an even larger user base than the one they had up until now. In the words of David Zalslav, Warner's CEO, "this new sports service exemplifies our ability as an industry to drive innovation and provide consumers with more choice, enjoyment and value and we're thrilled to deliver it to sports fans."

More recently, in March 2024, the company announced their expansion plans across Europe. Warner is going to launch its Max streaming service, which merge content from Discovery Plus and HBO Max, and is seen by the firm as one of the crucial business lines to grow and diversity their profits. Max will have more than double the amount of content that is currently available on HBO Max, plus it will also include some live linear network in European languages. Currently, about 80% of the company's profits come from the US, a highly competitive market. Hence, the expansion of Max to the Nordics, Iberia and CEE region starting May 2024 will likely yield positive results for the company. Later, the Max service is expected to expand to Poland, France, Netherlands and Belgium in the short term, but will have to wait to reach some other markets, such as the UK, because of past licensing deals with Sky that last until 2025. Moreover, this service is expected to have a significant increase in number of users as a result of several new shows that will be launched throughout the year, as well as because of their rights to broadcast all the live action from the 2024 Olympic Games. Furthermore, following Netflix's steps, Warner will also begin to crack down on password sharing among existing users.

How competitors are responding

While the streaming industry is very competitive, it has a clear frontrunner, Netflix. Moreover, the remaining big players, Disney, Amazon, Apple, Peacock, Paramount, Starz and Warner Media, face tough competition to grow market share, which has led to many mergers or alliances as portrayed earlier, as well as to try to distinguish themselves from their competitors, in order to gain an edge over them.

	Platform	Users (in Millions)
1	Netflix	247.2
2	Amazon Prime Video	200.0
3	Disney+	150.0
4	Max	95.1
5	Paramount+	63.4
6	Hulu	48.5
7	Peacock	28.0
8	ESPN+	26.0
9	AppleTV	25.0
10	Starz	15.8

Source: BSIC. Data from Forbes Home, February 2024.

Netflix is the clear frontrunner of the streaming industry. Beyond subscriber numbers, the streaming leader by users is also leader in terms of customer satisfaction. Forbes Home numbers show that 36% of streaming users claimed Netflix was their favourite platform, more than twice of the 2nd most preferred, which partially helps explain Netflix's undisputed leadership. Through a debt-fuelled expansion, followed by a cost-cutting and increased efficiency policies, Netflix expanded over the past years. Moreover, its ongoing crackdown on password sharing, as well as its more affordable subscription tier that comes with advertisement, and higher prices, have allowed them to increase their profitability margins over the last quarters.

Disney is also a strong contender in the streaming industry because of their large product offering. Not only do they own Disney+, but also Hulu and ESPN+. While being a relatively new service in comparison to Netflix, the firm has grown significantly over the past years, and aims to achieve a total of at least 230m subscribers by the end of 2024. However, to some extent Disney realized they cannot beat Netflix for the moment, and they recently decided to licence more of their proprietary TV shows to Netflix to cut down expenses, and losses, from its streaming service. Moreover, during 2023, Disney raised prices in an attempt to increase their profitability.

Amazon Prime is currently the 2nd streaming service with the largest subscriber base. However, much of its user base is said to come from the fact that when users subscribed to the Prime membership, they get access to the streaming service, along with some other of Amazon connected services. In 2023, Amazon increased the price of its annual membership after four years from $119 to $139.

Future outlook

As industries mature, a decline in profitability and several un-organic growth strategies, such as acquisitions, are expected. In the US, after a boom in 2022, the streaming industry's CAGR halved, to 10.1% in 2023, according to data from research firm Antenna. This underscores the end of the pandemic-induced boom in streaming services, which saw companies like Netflix and Disney reach unprecedented highs. Despite the relatively high CAGR, it is an inflated figure due to the high inflation reported across the globe in 2023. This, combined with the alarming downward trend in industry growth, signals a quite consolidated industry. Warner Bros Discovery is a player that has particularly made an effort to get ahead of its competitors, with the merger that created the company in April 2022, and several expected strategic moves, like the joint venture with ESPN and Fox and the rumoured merger with Paramount. Looking at the current league table in the US, the merger makes sense, as the new company would overtake Disney as the third largest player in the streaming market. Warner Bros Discovery has made its intensions of taking on Netflix and Amazon clear, therefore we expect the merger to happen in the coming years.

As for the European market, Warner Bros Discovery has an opportunity to disrupt the less consolidated, more culturally diverse market, through launching its Max platform across Europe. The potential merger with Paramount would further widen its product offering, thus making the potential service even more attractive for customers across Europe. Netflix and Disney are much better positioned across Europe however, with the former being the most popular streaming service across several European countries, including Germany, France and the UK. We expect Warner to find mixed success and have trouble dethroning Netflix, as customer switching costs are deceivingly high in the streaming market, with subscribers rarely switching from one platform to another. Data analytics firm Antenna found that the average monthly churn for streaming video services was 5.2% at the end 2021, up from 3.2% at the start of 2019. The increase has prompted firms to focus their strategy on customer retention. It is also important to note that most of the customers that cancel their subscription do so in order to lower their monthly expenses and rarely in favour of another streaming service. That being said, while we expected Warner Bros Discovery to grow in Europe, we see the league table staying stable in terms of ranking, both in the US and Europe.

Lastly, it is important to note the two key trends for the next year in the streaming industry. These are cost cutting and cracking down on password sharing. The former is a classic strategy in a maturing industry, where top-line growth is increasingly difficult to do. The latter has been a growing problem for streaming companies and is not easy to achieve. Netflix has been doing a particularly good job at achieving both cost-cutting and decreasing password sharing, underscoring their dominance in the industry, which we see as long-lasting. Furthermore, as a result of the tough competition and the ongoing economic environment, it is highly unlikely for growth to return to both the pandemic and early stages of mass streaming.

TAGS: streaming, Warner Bros Discovery, Netflix, Disney, consolidation, trends

