



The Reason I Won't Invest in Netflix Right Now

Description

For over a year now, I've looked at **Netflix** ([NASDAQ: NFLX](#)) and its steep stock pullbacks multiple times, but I just haven't been able to bring myself to buy in.

It isn't the high valuation that's kept me away (even though the company sports a forward price-to-earnings ratio of 52), nor the torrid growth of expenses to stock up on and create content (a negative free cash flow of \$594 million in the second quarter of 2019 alone). What's kept me from buying the dip is the history of the "early mover" business model — and the inevitable shakeout that ensues when peers that were disrupted by the early mover strike back.

History books and other anecdotal evidence

Early movers and their shareholders often front the bill for new technology by testing and proving the efficacy of a new business model. I recently came across a rant from an early smart-home adopter furious that **Alphabet's** Google was unifying its device ecosystem, making support for some of its peers' smart-home devices a real headache. Frustrating? You bet! But it's unfortunately what happens to early adopters of new tech. Those quick to take up new ideas often get "guinea-pigged" and stuck with some of the bill for later mass adoption.

Investors in new technology and business models are familiar with this, too. Innovating companies need cash, and they often turn to selling stock and burning up the cash raised for a later payoff. Sometimes this plays out in grandiose style, as with Netflix and its massive returns since its initial public offering in 2002. **Amazon's** early entrance into cloud computing, in the early 2000s, has also yielded huge sums of wealth for shareholders. Other times, though, the payoff isn't quite the same: Later businesses enter and disrupt the disruptors with more refined offerings, once the initial concept has had the kinks worked out. Here are a few historical examples.

Early Mover

Jack in the Box pioneered the drive-thru in 1951.

McDon
[lead th](#)

Early Mover

In 1994, Yahoo! released its web directory — it added other search and web-related services over the years.

Fitbit helped get the [wearable fitness-tracker](#) movement started with its 2007 debut and was the market leader for several years.

Google
[business](#)

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Data sources: *Money* magazine; *Encyclopedia Britannica*; eLearners.com; IDC.

Other examples abound, including the smartphone market, the current [disruption in the cybersecurity space](#), and the responses of retailers like **Walmart** and **Target** to Amazon. These examples might not be perfect analogies to the world of streaming, but they still illustrate the cycle of new business models and innovation.

With Netflix pulling in millions of new subscribers — [mostly internationally](#) at this point — it's become clear that streaming TV is the future, and there's plenty of growth to be had. Early Netflix investors have been rewarded handsomely, but we are entering a period when the industry will go from essentially a few options to many, and the competitive landscape will be reshaped.



Image source: Getty Images.

Don't underestimate the field

It could be easy to write off the mounting competition and say Netflix will be fine, because it has enjoyed such a big head start in the world of streaming TV. But periods of industry transition like this can be bumpy, and the new entrants that Netflix is fending off aren't start-ups. **Disney** ([NYSE: DIS](#)) owns arguably some of the most recognizable and popular franchises ever, and while [Disney+](#) will only debut in three countries in November, it will roll out to other major markets over the next two years and will be bundled with Hulu and ESPN+. [Apple TV+](#) is debuting in 100 countries right out of the gate in November. And **Comcast's** (NASDAQ: CMCSA) NBCUniversal streaming service could be a serious contender next year, with Comcast controlling a significant presence in Europe thanks to its [Sky acquisition last year](#). It's not even the competitive price tags on these other competing services: There are only so many hours in a day for consumers to be entertained and so much money in their monthly budgets for streaming subscriptions.

Don't get me wrong, I'm not predicting the death of Netflix — or even that it will lose its leadership role in the streaming TV industry anytime soon. I'm just not ready to invest until the shakeout starts to take shape. At the very least, Netflix no longer seems to have a real competitive advantage (as it obviously did over cable).

The company is still priced as if it's a cutting-edge pioneer and innovator — the only game in town. The business model is starting to mature, and I'm not seeing enough innovation at Netflix (creating original content is something everyone is pursuing) for me to get really excited right now. And the current valuation seems based on an assumption that Netflix will continue as the only game in town for quite some time.

That's why I'm staying away from this stock and plan to do so until some of the heavy-hitting competing services come out and have some operating history under their belts. It's been an incredible run for Netflix, but a breather — at least a couple of years' worth — is certainly in the cards.

CATEGORY

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5. NASDAQ:GOOGL (Alphabet Inc.)
6. NASDAQ:NFLX (Netflix, Inc.)
7. NYSE:DIS (The Walt Disney Company)

8. NYSE:MCD (McDonald's Corporation)
9. NYSE:TGT (Target Corporation)
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Date

2025/08/16

Date Created

2019/09/19

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