

MOVIEPASS: A NETFLIX FOR MOVIEGOERS?¹

Lorianne Dueck and Guoliang Frank Jiang wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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In December 2018, Mitch Lowe, the chief executive officer (CEO) of MoviePass, was facing some difficult decisions. A former senior executive at Netflix Inc. (Netflix), Lowe became MoviePass's CEO in 2016, and the company rose to stardom between 2016 and 2017 with its popular membership program for moviegoers in the United States. MoviePass's subscription-based service allowed its subscribers to watch movies in theatres at a low cost. However, the service saw its subscription base shrink sharply in 2018 and suffered crushing financial losses. Due to MoviePass's financial struggle, its parent firm—Helios and Matheson Analytics Inc. (H&M)—was under the threat of being delisted from the NASDAQ Composite Index (NASDAQ) at the end of 2018.²

The same subscription model that made Lowe's former employer successful seemed to be the downfall of MoviePass. However, MoviePass had subscribers, and the number of subscribers had increased from 20,000 to three million between 2016 and early 2018.³ Yet, the popularity of its service had not led to financial success. At the end of 2018, the company was contemplating changing its pricing menu. It was also exploring other revenue streams, including monetizing its user information, partnering with ancillary vendors, and creating its own content.⁴ MoviePass had to change. Lowe and his management team had to keep the company afloat while deciding how to help MoviePass regain its lost momentum and revitalize the once-promising upstart. The company had to stop bleeding cash and prevent H&M from being delisted.

MOVIEPASS

MoviePass was co-founded in 2011 by Stacy Spikes and Hamet Watts, both of whom had extensive experience in the entertainment industry and online advertising business. In 2011, MoviePass subscribers, who paid approximately US\$50⁵ a month, were entitled to receive one movie ticket per day.⁶ This was an attractive offer for moviegoers, especially movie aficionados. Customers could choose the movie they wanted to watch via a smartphone application (app) that provided movie locations and times. Admission to movie theatres required printed vouchers that customers took with them, but subscribers could attend only those theatres that had a partnership with MoviePass.

The service, however, failed to gain significant traction in its original test market.⁷ In particular, cinema exhibitors were concerned about how the subscription model might affect the industry. Although MoviePass paid theatres full price for every movie ticket its members ordered, the perceived devaluation

of ticket prices was an unattractive prospect to the theatres.⁸ However, despite the initial setback, the service was immediately considered to be the “Netflix” of the movie theatre industry and one of the top 25 disruptive apps by *Business Insider*.⁹

In 2012, MoviePass relaunched with a subscription price of \$30–\$34 a month, this time using a prepaid debit card to purchase movie tickets.¹⁰ Customers would pay MoviePass a monthly fee, download the app, and receive a MoviePass debit card. After choosing the movie showing from their app, customers would pay for admission at the theatre using the debit card. If customers’ subscription fees did not cover the cost for the movie they watched, MoviePass paid the difference. In addition, a new geo-location feature was included for security purposes and to stop individuals from lending their card. For the geo-location service to work, the subscriber’s phone and card needed to be close to each other and within 100 yards of the theatre where the ticket was reserved.¹¹ This revised model led to rapid growth of the company. In 2014, MoviePass began a partnership with AMC Theatres (AMC), which was no longer able to dismiss the rising popularity of the subscription-based service.¹²

Lowe was named CEO of MoviePass in June 2016, but prior to joining the company, he had worked for Netflix and RedBox Automated Retail LLC (RedBox). At Netflix, he served as the entertainment domain expert and vice president of Business Development and Strategic Alliances. He later became president of RedBox, a digital versatile disc (DVD) and video game rental company. According to Lowe, MoviePass was “Netflix for the movie theater” and would “make it easier for passionate moviegoers and casual fans to see films the way they’re meant to be seen—in the theater.”¹³ Drawing on his experience at Netflix, Lowe affirmed that MoviePass was “changing the way consumers think about going to the movies by making it possible to experience a broader array of films—from the latest summer blockbuster to a critically acclaimed documentary—through a subscription model.”¹⁴

In August 2017, H&M acquired a controlling stake in MoviePass. H&M was a data and analytics firm traded on the NASDAQ Capital Market. The company offered a broad range of information technology services to retail, education, health care, and government.¹⁵ Following the acquisition, MoviePass immediately slashed the monthly fee to \$9.95, which caused membership to swell from 20,000 subscribers to three million in less than a year. The rapid growth generated significant publicity that hailed MoviePass as a disruptive force in the movie industry. According to MoviePass, its subscribers bought approximately one in every 17 movie tickets sold in the United States in 2017.¹⁶ Its membership program was accepted at more than 91 per cent of theatres across the United States in 2018, making it the nation’s largest theatre network.¹⁷

However, unprecedented growth led to substantial financial losses at MoviePass. The cost of covering the full price for each ticket quickly burned through MoviePass’s cash holdings, and the company lost \$98.3 million on \$48.6 million of revenue in the first quarter of 2018.¹⁸ The company requested an emergency loan of five million dollars to keep the business operational in July 2018. MoviePass temporarily ran out of money in the summer of 2018 and announced that subscription prices were going to be increased to \$15.¹⁹ Subscribers were unimpressed, and one week later the company retracted the statement and maintained the original price of \$9.95. Instead, MoviePass decided to set a limit of only three movies per month and required customers to upload photos of ticket stubs as proof that they were not seeing the same movie multiple times.²⁰

MoviePass also continued to look for other streams of revenue, including selling data (collected from subscribers) to movie producers, distributors, and other related businesses.²¹ For example, the location feature in the MoviePass app (removed in March 2018 due to privacy concerns) allowed the company to see where customers were spending their time before and after the movies.²² This information could help the company coordinate a night out at the movies with vendors, like restaurants, as a way to generate revenue.

Almost 60 per cent of users cancelled their subscriptions in 2018.²³ In November 2018, some subscribers filed class action lawsuits with regard to the high number of theatre blackouts. Theatre blackouts occurred when there were no longer any tickets available for a viewing at a selected time. While MoviePass promised access to any three films per month, theatre blackouts prohibited members from using their pass.²⁴ In August 2018, Jeffrey Braxton filed a lawsuit on behalf of hundreds of investors who lost money in the venture, stating that “those that put stock in the company feel as though they were misled and lied to about the MoviePass business model.” The attorney for the plaintiffs argued that “there was no reasonable basis to believe MoviePass could monetize the model to a degree that could be maintained before being too buried in debt to survive.”²⁵

Since August 2018, stock prices of H&M had been under \$0.10. As a result, the company was in danger of being delisted from the NASDAQ for the failure to maintain the minimum price of \$1 per share. In addition, its market capitalization was approximately \$26 million, significantly below NASDAQ’s requirement of \$35 million. The company attempted to address the problem with a reverse stock split in July 2018. The board had tried to approve a second reverse split to increase the stock price, but had delayed the meeting twice. A meeting had now been scheduled for March 2019 and was seen as one of the only ways to halt the delisting process.²⁶

In addition to MoviePass, H&M also controlled three other entities—MoviePass Films, MoviePass Ventures, and Moviefone. MoviePass Films was a majority-owned joint venture between H&M and Emmett Furla Oasis Films and supported independent filmmakers and distributors by jointly acquiring equity stakes in films to enhance performance during the theatrical release window.²⁷ The company joined with the Orchard in acquiring *American Animals*, a critically acclaimed movie, in June 2018.²⁸ It aimed to produce between 10 and 12 films per year and acquire or co-produce eight to 10 films per year.

MoviePass Ventures was a wholly-owned subsidiary that primarily jointly acquired films with film distributors.²⁹ Moviefone provided a telephone service that originally helped users to find show times but had since evolved into an online guide for all types of entertainment. H&M acquired Moviefone in April 2018 to complement MoviePass. Moviefone served as a platform to recruit subscribers for MoviePass and expand its advertising business.³⁰ In the long run, H&M aspired to create a MoviePass “ecosystem” that also included partnerships with ride-sharing companies, malls, local retailers, restaurants, and other related businesses.³¹

NETFLIX

In 2016, an average American spent \$2,172 on entertainment (including fees and admissions, audiovisual equipment and services, and other entertainment supplies).³² According to a 2017 survey by the Bureau of Labor Statistics, watching television (TV) was the most popular leisure activity, accounting for over half of all leisure time (see Exhibit 1).³³ Many leisure activities took the form of subscription services, including traditional media and entertainment like newspapers, magazines, and cable TV. Other service providers also employed subscription-based models, such as gym memberships, breakfast clubs, art supplies and stationery (e.g., PaperGang), food delivery (e.g., Expack), and even air travel (e.g., Surf Air).³⁴ A prime example of successful adoption of the subscription model was Netflix.

Netflix started in 1997 as a pay-per-rental mail-order video rental company. At the end of 1999, the company settled on a subscription-based model that offered unlimited rentals with a flat fee. A decade later Netflix had 13 million members across the United States and offered over hundreds of thousands of titles from around the world. Instead of providing the latest content, the company offered offbeat movies favoured by movie aficionados. Continuous improvement of proprietary recommendation algorithms allowed Netflix to show customers content that was aligned with their interests, creating customer intimacy that became crucial to its success.³⁵

Online streaming became increasingly popular during the late 2000s, as the world of streaming became a new arena for competitors who fought to provide relevant content, seamless delivery to TV and mobile devices, and an attractive user interface to increase engagement.³⁶ With an increased focus on streaming and new communication technologies, Netflix began to direct its attention to platforms like computers (2007), consumer electronics (2008), and smartphones (2010).

Instead of purchasing content outright, Netflix negotiated licensing agreements with studios and distributors. For instance, Netflix signed a five-year deal worth nearly \$1 billion to stream movies from Paramount, Lionsgate, and MGM in 2010. Under this agreement, movies would appear on Netflix 90 days after their debut on premium pay TV and subscription video on demand (VOD) services.³⁷ Under this and similar agreements, Netflix would obtain content distribution rights to an unlimited number of viewers. For viewers, this meant that for a monthly fee they had unlimited access to Netflix's ever-growing and more personalized selection. The company began to develop its own shows, starting with *House of Cards* in 2013, to reduce its dependence on content providers. Netflix had since become an entertainment powerhouse, producing more than 70 shows in 2017.³⁸

In 2018, Netflix used a tiered pricing model based on how many screens consumers wanted to use at once and whether they needed access to high definition (HD). The basic plan cost \$7.99 and was available on one screen only. The standard plan at \$10.99 allowed access to two screens in HD, while the premium plan at \$13.99 allowed for four screens and included both HD and ultra HD features. Netflix's three business segments—domestic streaming, international streaming, and domestic DVD rentals—generated \$7.6 billion, \$7.8 billion, and \$366 million in revenues, respectively, for the fiscal year ended December 31, 2018. For the domestic and international streaming segments, expenses associated with the acquisition, licensing, and production of streaming content made up the majority of cost of revenues.³⁹

THEATRE INDUSTRY

Approximately 5,750 cinema sites operated in the United States in 2017, down from 7,480 in 1997.⁴⁰ AMC, Regal Entertainment, and Cinemark Theatres (Cinemark) were among the leading exhibitors and operators of multiplex cinemas. In 2018, 871 films were released in Canada and the United States.⁴¹ The typical moviegoer bought 4.1 tickets per year at an average price of approximately \$7.93.⁴² According to the Motion Picture Association of America, 12 per cent of North Americans were frequent moviegoers, attending the cinema once a month or more. This group of moviegoers was responsible for 49 per cent of all tickets sold. Two per cent of tickets were bought by infrequent attenders who went once in 12 months, while the other 49 per cent was purchased by occasional moviegoers who attended less than once a month.⁴³ After peaking in 2002, the number of movie tickets sold in North America had been declining (see Exhibit 2).⁴⁴

The making of feature films for international distribution had been dominated by Hollywood studios, such as Paramount Pictures, Warner Bros., Sony Pictures, Disney Studios, and 20th Century Fox. Movie distributors, which could be studio-owned or independent, planned the release dates and marketing strategy. Release windows maximized distribution revenue by minimizing competition among DVD, streaming, and in-theatre movie formats. The theatrical release window typically lasted about 16 weeks. This was followed by exclusive availability on home videocassette (VHS) or DVD for several months, VOD, and subscription pay TV. Free-to-air media like TV was usually the last window.⁴⁵

The most significant operational cost incurred by exhibitors was the film rental paid to distributors, which was typically negotiated for every film and could be renegotiated on second or third runs. Movie theatres also budgeted for labour, property taxes, facility lease expenses, utilities and maintenance, and compliance with

health and safety regulations. Covering these costs had become increasingly difficult as distributors shortened release windows to move the movie onto other formats and online platforms sooner. Shortened release windows caused theatre attendance to drop, which contributed to the closures of many movie theatres.⁴⁶

Subscription-based services like MoviePass provided exhibitors an opportunity to increase viewership by lowering the cost of a night out at the movies. Expenses for a night at the movies might also include transport, meal, snacks, and drinks. Cinemas typically generated a significant proportion of revenue from concession sales because they were often impulse purchases.⁴⁷ A 2018 report suggested that viewers were willing to pay \$51.39 for one person, \$101.49 for a date night, and \$148.96 for a family.⁴⁸ According to a survey in 2017, attending movies at theatres was considered an activity for richer-than-average participants, with over 50 per cent of individuals who attended movies making more than \$50,000 a year. Meanwhile, the percentage of individuals watching TV and movies at home was over 50 per cent for those with a yearly income of under \$50,000.⁴⁹ While MoviePass could help get people back to the theatre, forming and maintaining partnerships with cinema operators had been a struggle, especially with those who offered competing loyalty programs.⁵⁰

PARTNERSHIP AND COMPETITION

AMC THEATRES (AMC)

AMC introduced the first multiplex theatre in 1962 and was the largest movie theatre chain in the United States. Since its beginning in 2014, the partnership between AMC and MoviePass had not been smooth. AMC made it clear that MoviePass would not receive any concession revenue, a source of income that MoviePass had originally demanded. MoviePass also failed to persuade AMC and other exhibitors to provide discounts on tickets sold through its membership program. AMC believed that programs like MoviePass trained consumers to undervalue films and that the business plan was unsustainable. The rift between these two companies deepened in 2018 when MoviePass cut service to 10 AMC theatres.⁵¹ This combative tactic was meant to pressure AMC to give MoviePass a \$3 discount on each ticket and a 20 per cent cut of concessions. These requests were motivated by the fact that MoviePass provided AMC with approximately \$2 million of revenue per week.⁵²

In July 2018, AMC launched its own subscription service called Stubs A-List Plan, gaining over 600,000 users in just a few months. At \$19.95 a month, members of the plan received access to three movies a week in any format and for any show time, free upgrades on pop and popcorn, express services at the box office and concession stand, no online ticketing fees, and more. Members could earn 100 points for every dollar spent on tickets or concession and receive a \$5 credit for every 5,000 points earned.⁵³

CINEMARK THEATRES (CINEMARK)

In December 2017, Cinemark, another major cinema chain in the United States, launched Movie Club, a monthly plan that cost \$8.99. Members of the Movie Club could buy one movie ticket a month for a discount price without online fees and enjoy 20 per cent off concessions. The company's own research suggested that consumers preferred a monthly membership program with ticket rollover benefits that allowed them to accumulate credits, reserve their seats in advance, and enjoy significant discounts on concessions.⁵⁴ The plan also included options that allowed customers to add a companion ticket or upgrade for extra fees.⁵⁵ The program was poised to reach more than 550,000 members in early 2019.⁵⁶

SINEMIA

Sinemia was a movie subscription company that offered a range of monthly offerings from one movie a day for \$29.99 to one movie a month for \$4.99.⁵⁷ Founded in Turkey in 2015, this start-up capitalized on the hype around MoviePass to launch its service in the United States and Canada in 2018 and had a variety of fees besides the monthly payments, including an initiation fee, processing and handling fees, and debit card fees. However, this information was not as widely advertised as their cheap monthly plans. Many customers complained, and a “bait and switch” lawsuit against the \$1.80 processing fee was filed in October 2018. Nonetheless, Sinemia still claimed to have a competitive edge by offering “flexible ticketing options, Uber integration, preference and AI-based film recommendations, in-app social sharing, commenting, polling, and photo ops, access to exclusive discounts and events, fast and easy ticket reservations and search filtering.”⁵⁸ In November 2018, the company launched Sinemia Enterprise, a service that helped theatres set up their own chain-specific subscription plans. The company would handle “monthly or annual payment processing, customer relationship management, fraud detection systems and management of an iOS or Android app through which subscribers could purchase tickets and reserve seats.”⁵⁹

MOVIEPASS LOOKING AHEAD

In February 2018, MoviePass began partnerships with more than 1,000 movie theatres and several major Hollywood studios. The partners could market films directly to MoviePass’s subscribers through email and mobile push notifications and films displayed prominently in the app.⁶⁰ In addition, MoviePass was working to introduce a solution that could let exhibitors like AMC launch their own subscription programs using MoviePass’s platform and technology.⁶¹

Beginning in August 2018, subscribers were limited to three movies a month, a quantity that would satisfy over 85 per cent of subscribers.⁶² The remaining 15 per cent who watched over three movies a month were super-consumers. In addition to being heavy users, super-consumers tended to be highly engaged with a product category or a brand. Research showed that they accounted for three times as much growth as other consumers and were highly influential through social media and word of mouth.⁶³

At the end of 2018, MoviePass was considering launching a new subscription pricing menu with three different plans and prices that varied based on user location. The Select plan cost up to \$15 per month and allowed subscribers to choose from a limited selection of films. The All Access plan cost \$20 per month and included new releases. The Red Carpet plan, at \$25 per month, included one 3-D or IMAX screening per month. Customers were still limited to three movies per month in all of the plans.⁶⁴

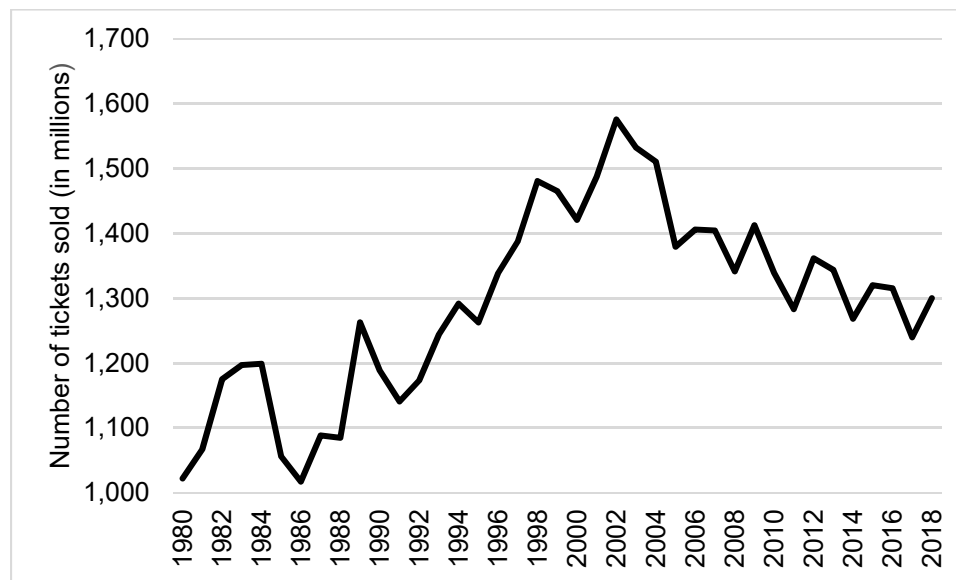
NEXT STEPS

In early 2018, MoviePass’s main strategic objective had been to stabilize, optimize, and grow. However, while Netflix’s stock remained above \$250 per share, H&M continued to trade for pennies, with a reported loss of \$130 million in the third quarter. The company’s leadership acknowledged that it was difficult to estimate the actual funds required to support MoviePass’s current business model.⁶⁵ Nevertheless, should the company implement the new pricing menu? What else could the company do to avert the downward spiral?

EXHIBIT 1: AVERAGE LEISURE TIME PER DAY

Activity	Time
Watching TV	2 hours and 47 minutes
Socializing and communicating	41 minutes
Playing games; using computer for leisure	25 minutes
Reading	19 minutes
Participating in sports, exercise, recreation	18 minutes
Relaxing and thinking	17 minutes
Other leisure activities	12 minutes

Note: Data were annual averages for 2015 and included all persons age 15 and over and all days of the week.
Source: "Leisure Time on an Average Day," United States Department of Labor: Bureau of Labor Statistics, December 20, 2016, accessed April 22, 2019, www.bls.gov/tus/charts/leisure.htm.

EXHIBIT 2: NUMBER OF MOVIE TICKETS SOLD IN THE UNITED STATES AND CANADA, 1980–2018 (IN MILLIONS)

Source: Amy Watson, "Number of Movie Tickets Sold in the U.S. and Canada from 1980 to 2018 (in Millions)," Statista, 2019, accessed April 22, 2019, www.statista.com/statistics/187073/tickets-sold-at-the-north-american-box-office-since-1980/.

ENDNOTES

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