Zacks INVESTMENT MANAGEMENT

Market Insights by Mitch Zacks

6 Stock Ideas for Investors to Entertain

By Mitch Zacks
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In one of their trademark launch-events, Apple Inc. [AAPL] unveiled plans last week to start a new music streaming service pitting them against Spotify and Pandora, perhaps opening profitable new doors for their iTunes business. Apple plans to market the service to ~500 million customers in over 100 countries at a cost of $9.99 per month. Run some quick numbers and you'll realize this could become a cash cow for the $735 billion company.

Apple's announcement is another example of how the entertainment industry (music and movies) is rapidly evolving from traditional ownership (buying CD's, DVD's, paying monthly cable bills) to internet-based accessibility. It seems likely that in 2015, revenue from downloading and streaming video will outpace DVD sales — and then could overtake movie theater revenues within two or three years. It's incredible growth.

So, in a few years' time, all or most of the entertainment content we consume will be cloud and internet-based. It's cheaper, easier, and you don't have to block off six hours in a day for your cable guy to maybe show-up.

Here are six companies positioning themselves to be players—if not leaders—in the ever-changing world of content.

1.) Netflix, Inc. [NFLX] – Netflix has amassed over 60 million subscribers worldwide, but CEO Reed Hastings thinks he can get 90 million subscribers in the U.S. alone. Global numbers would be massive. The stock is pricey though, having risen over 400% in the last five years and trades at around 170 times earnings. That's a lot to pay, but there's some interesting news in the offing—the board is seeking approval to increase

its number of shares by 30 times, bringing the trading price down to about $20 per share from where it is now in the $600's per share. This doesn't make the company any cheaper, but it can help attract more retail investors, driving the price even higher.

2.) Alibaba Group [BABA] – This Chinese juggernaut is fixated on Hollywood, and is aiming to compete. They are planning on building China's version of Netflix and HBO in a new service called Tmall Box Office. The potential revenues dwarf what Netflix could expect from a U.S. customer base since Alibaba can market to 600 million eager customers. The value of the Chinese online video market is estimated to nearly triple to 90 billion yuan by 2018, and Alibaba wants all of it.

3.) Apple, Inc. [AAPL] – There are few reasons not to own Apple. It trades at a very reasonable multiple of around 15 times earnings and the company relentlessly innovates. The announcement of the streaming service coupled with a news service, that could be coming soon, shows that Apple is interested in content just as much as hardware—and content is king in today's world. The iWatch may not propel the company to new heights, but I have little doubt that Apple will, in due time, come out with multiple products that will.

4.) Amazon.com, Inc. [AMZN] – 'Amazon Prime' has extended its array of benefits beyond just free shipping, and now has a deal with HBO that allows Prime members to stream HBO content as part of their membership. Prime has around 20 million subscribers, is growing at a steady clip, and gives Amazon a solid base for which to market their other products like e-Readers, tablets, and streaming boxes.

5.) Comcast Corporation [CMCSA] – Comcast fits in as a blue chip player in the field, a media behemoth that would be hard to knock off in any line of business. The interesting aspect to focus on with Comcast is broadband, not necessarily their cable, phone or media operations (they own Universal, which distributed Jurassic World's record-breaking $520 million opening weekend). Comcast is keenly aware of the evolution to streaming, and since 83% of Americans get their internet connection through their cable company, the market is huge. When you think about it, their proposed merger with Time Warner Cable wasn't about cable at all—it was about high-speed Internet. A combined company would have controlled 60% of all broadband connections in the country.

6.) Walt Disney Co. [DIS] – Don't forget Walt! This iconic company has touched the hearts of many and driven nice returns over the long-term. I could see both of those qualities continuing well into the future. Disney has nicely outpaced the S&P 500 over the last year, and with the Star Wars and Marvel franchises on deck for years of movies and merchandise, the future is bright for sales. What's more, Disney has a dividend payout ratio of only around 25%, so they have plenty of room to notch up their dividend in the future to accompany their growth.

The Bottom Line for Investors

Like with any stock investing, make sure you thoroughly research a company before buying shares and avoid having too concentrated a position in any one company, no matter what your conviction. Investors are often tempted to go "all-in" on an individual stock they really like, but it can go both ways at a moment's notice.

Entertainment is a formidable and growing industry, and it tends to do well when consumers are doing well. But the opposite can be true too, so it's important to pay heed to economic cycles on a macro level when thinking about these investments.

-Best Regards, and Better Returns!
Mitch

About Mitch Zacks

Mitch is a Senior Portfolio Manager at Zacks Investment Management. Mitch has been featured in various business media including the Chicago Tribune and CNBC. He wrote a weekly column for the Chicago Sun-Times and has published two books on quantitative investment strategies. He has a B.A. in Economics from Yale University and an M.B.A in Analytic Finance from the University of Chicago.

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