Cutting the Cord

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Pay TV’s New Worry: ‘Shaving’ the Cord

BY KEACH HAGGY
AND SHANTINI RAMACHANDRAN

The biggest U.S. cable-TV channels are experiencing a troubling trend: Their reach into American households is shrinking.

Over the past four years, the top 40 most widely distributed channels in 2010—household names like CNN, ESPN and USA—have lost an average of 3.2 million subscribers, or more than 3% of their distribution, according to a Wall Street Journal analysis of data from measurement firm Nielsen.

Some in the industry point to consumers who are “cutting the cord,” ditching their cable and satellite-TV connections in favor of more affordable online video options like Netflix and Hulu. But the numbers don’t add up.

Last year the pay-TV industry lost 156,000 subscribers, accounting for research firm MoffettNathanson LLC. While that was the first annual decline on record, it isn’t enough to account for the subscriber declines of the biggest cable channels.

Indeed, the data and interviews with a range of cable-TV industry executives suggest that something else is going on: subscriber growth. Pay-TV providers face significant risks, too. If more people downgrade to skinny bundles, it could pressure

3.2 million

The average number of households lost by big channels since 2010

CBS and HBO launching TV streaming services

OCTOBER 17, 2014, 7:15 AM
Credit: cbsnews.com
• **Background**
  – Digital has disrupted other media in the past
  – General consumer dissatisfaction with the traditional TV (cable and satellite)
  – Increased digital TV content and devices (esp. mobile) and increased access to broadband
  – Some are “cutting the cord” and unsubscribing traditional TV
  – Some are “shaving the cord” and some (esp. millennial) are “cord nevers”

**Transition to digital is inevitable and a tipping point will happen in the next 3-5 years**
• Several layers of bundles forced on consumers

• Al a carte
• Internet access mostly through cable

TV Ecosystem

Content

Channel Grouping

Media Packaging

Service Provider Bundling

Consumer

Internet TV

Internet Provider

Content Aggregators

Content Companies

Internet

Free Internet

WiFi Hotspots

Starbucks

Digital Content

Movie Studios

Online courses
• $150B (Ads + Bundling Subscription)
• $70B revenue goes to the “majors”
• Symbiotic commercial relationship

$30 billion Production Cost
$40 billion License Fees
$80 billion Affiliate Fees
Subscription/VOD

Content
Channel Grouping
Media Packaging
Service Provider Bundling

Traditional TV

Movie Studios
Content Aggregators
Internet Provider
Free Internet

Internet TV

Content Companies
Internet Provider
WiFi Hotspots
Starbucks

Digital Content
Online courses

• $6B (Ads)
• À la Carte Subscription
• Internet providers still make money
• Some trends have started to emerge in this tug of war for viewers and dollars

• Four key areas:

1. Use of Mobile Devices for video (2\textsuperscript{nd}/3\textsuperscript{rd} screen)

2. Premium Content availability online (unbundling)

3. Change in Viewership (demographics)

4. Digital Ad growth (2\textsuperscript{nd} order effect)
1. Shift in viewing habits to mobile screens

- The number of devices per household is on the rise.
- The number of mobile viewers is on the rise.
- The number of hours of long format video is increasing -- viewing habits are changing.

Types of Video Content Viewed on Smartphones and Tablets

<table>
<thead>
<tr>
<th>Type of Content</th>
<th>March 2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Movies</td>
<td>24.5%</td>
</tr>
<tr>
<td>News</td>
<td>20.8%</td>
</tr>
<tr>
<td>TV show previews, movie previews</td>
<td>20.1%</td>
</tr>
<tr>
<td>Reruns/previous seasons of TV shows</td>
<td>18.0%</td>
</tr>
<tr>
<td>Sports clips</td>
<td>11.5%</td>
</tr>
<tr>
<td>Live TV shows</td>
<td>11.5%</td>
</tr>
<tr>
<td>Sporting events</td>
<td>6.0%</td>
</tr>
<tr>
<td>Tablets</td>
<td>5.6%</td>
</tr>
<tr>
<td>Smartphones</td>
<td>4.6%</td>
</tr>
<tr>
<td>Tablets</td>
<td>6.4%</td>
</tr>
</tbody>
</table>

- Sources: Cisco/Business Insider, DigitalSmiths, marketingcharts.com

- Mobile video traffic is surging

- Mobile engagement is seen higher with apps than sites.

- Video consumption is growing

- 44% of smartphone users and 61% of tablet users regularly watch video on these devices; and

- 45% of smartphone viewers and 71% of tablet viewers watch long-form content, be that TV, movie or sports.

- Mobile engagement seen higher with apps than sites.

- # of devices per household is on the rise

- # of mobile viewers is on the rise

- # hours of long format video is increasing -- viewing habits are changing
2. PREMIUM CONTENT AVAILABILITY ONLINE

2008:
Traditional and Digital Silos

2014:
Content Partnership by means of OTT & TV Everywhere

- Cross pollination of content across digital and traditional eco systems
- Just last week HBO and CBS announced OTT offerings (a la carte )

Source: http://www.slideshare.net/tkawaja/lumas-the-future-of-digital-tv
3. Change in Viewership -- OTT Increasing

Digital Viewership is proliferating

Streaming is the dominant form of viewing for millennials

Sources: HarrisInteractive, marketingcharts.com
With the current rate of growth, Digital expected to overtake TV by 2018.

Digital Ad Revenue Increasing
Video Ad revenue still small but increasing along with overall rise in Digital Ad spending.

2014 AD Spend
- Traditional $70 billion, 3-4% year to year growth
- Digital $6 billion, ~20% year to year growth

Sources: Pricewaterhousecoopers/marketingcharts.com, Wall Street Journal/emarketer.com
• Powerful Incumbents

• Oligopolistic practices by Broadcast Internet providers
  – Netflix vs Comcast

• Legal/Regulatory uncertainty
  – Net Neutrality
  – Aereo ruling

• Sports content availability
  – Necessary for OTT success

• Content creators are not as financially incentivized in existing digital ecosystem as in TV ecosystem

• Fractured Online ecosystem
  – Still evolving

• **Now- < 1 year**
  - Lot of content is already available (this domino has fallen)
  - Broadband penetration is high, both mobile and cable (this domino has fallen)

• **Short Term - 1-3 years**
  - Sports content will follow suit

• **Medium Term - 3-5 years**
  - Broadcasters will get squeezed and provide OTT offerings
  - Ad money for digital video will reach critical point (~25%)
  - Consolidation will happen in Digital Ecosystem to remove fracturing

• **Long Term - > 5 years**
  - Digital Ad revenue will equal or exceed traditional
  - Over time, traditional Telco/Cable companies will become mostly Broadband providers
  - Production cost will decrease substantially due to online data driven model
  - Alternate high speed broadband access (Fiber to the home, etc.) will emerge to compete with Cable

Sources: ncta.com/industry-data
• After initial success set-top-boxes will get absorbed into IPTVs (3-5 years)

• Satellite providers will resort to servicing mostly the niche/urban segments (3-5 years)

• Current multichannel Pay TV Package (for the home/family) will get split into Individual personal subscriptions
  – A new bundling opportunity will emerge in the digital space

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<tbody>
<tr>
<td>1.</td>
<td>apple</td>
<td>$614 BILLION</td>
</tr>
<tr>
<td>2.</td>
<td>google</td>
<td>$360 BILLION</td>
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<tr>
<td>3.</td>
<td>verizon</td>
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<tr>
<td>4.</td>
<td>facebook</td>
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<td>at&amp;t</td>
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<td>6.</td>
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<td>7.</td>
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<td>8.</td>
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<td>9.</td>
<td>fox</td>
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<tr>
<td>10.</td>
<td>time-warner</td>
<td>$66 BILLION</td>
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<td>11.</td>
<td>time-warner-cable</td>
<td>$39 BILLION</td>
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<tr>
<td>12.</td>
<td>directv</td>
<td>$38.9 BILLION</td>
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</table>
• Traditional TV ecosystem will continue to resist change

• But the transition to digital is inevitable…

• Dominos are starting to fall, and a tipping point will happen in the next 3-5 years
Backup
• Multiple Revenue streams ($150B)
  – Subscription & VOD $80B
  – Advertisement $70B
  – 66% comes from the 6 “majors”

• Bundling
  – Three levels of fortressing
  – Enables pre-funding for content
    • For every “A” movie there are 10 “B” & “C” movies

• Inertia/Trust
  – Industry is mature and players have worked together for decades
  – Clarity and simplicity of areas of focus for each part of ecosystem
  – Transparency of data

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<table>
<thead>
<tr>
<th>The Media Conglomerates</th>
<th>Film Studios</th>
<th>TV Production &amp; Distribution</th>
<th>US Cable Networks</th>
<th>Broadcast Networks</th>
<th>Film &amp; TV Revenues</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time Warner</td>
<td>Warner Bros. New Line Cinema</td>
<td>Warner Bros. TV Cartoon Network Studios</td>
<td>HBO CNN</td>
<td>WB</td>
<td>$20,784 m</td>
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<tr>
<td>Walt Disney</td>
<td>Walt Disney Studio Miramax</td>
<td>Buena Vista Television Touchstone Television</td>
<td>ESPN Disney Channel</td>
<td>ABC</td>
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<tr>
<td>Viacom / CBS</td>
<td>Paramount Pictures</td>
<td>CBS Paramount TV King World Production</td>
<td>MTV Showtime</td>
<td>CBS UPN</td>
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<tr>
<td>NBC-Universal</td>
<td>Universal Pictures</td>
<td>NBC Studios NBC Universal TV</td>
<td>Sci-Fi Bravo</td>
<td>NBC Telemundo</td>
<td>$13,789 m</td>
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<tr>
<td>News Corp.</td>
<td>20th Century Fox Fox Searchlight</td>
<td>Fox TV Studios 20th Television</td>
<td>Fox News Fox Sports Net</td>
<td>Fox</td>
<td>$13,931 m (1)</td>
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<tr>
<td>Sony</td>
<td>Sony Pictures Columbia Pictures</td>
<td>Sony Pictures Television</td>
<td>International</td>
<td>International</td>
<td>$6,640 m (2)</td>
</tr>
</tbody>
</table>
• Average $ spend per company is 100 to 1
• A lot of fracturing of the business on the emerging digital video
Parallels - Tipping Point between bundled Music vs Individual Choice

Charts & Data Credit: Tom Silverman, Tommy Boy Records
Opportunity for new Pandora or Spotify - Digital Advt based on preference

Digital Music Sales Decrease For First Time in 2013


Music streaming doubles in 2013, as album sales fall
Streamimg now accounts for 10 per cent of record label revenue

Read more at http://www.nme.com/news/various-artists/74657#jxQ6mXZYF3oGFCKw.99

IP TV Converters May Go Away

Smart TV Share of Global Flat Panel TV Shipments

<table>
<thead>
<tr>
<th>Year</th>
<th>Share</th>
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</thead>
<tbody>
<tr>
<td>2013</td>
<td>33%</td>
</tr>
<tr>
<td>2014</td>
<td>44%</td>
</tr>
<tr>
<td>2017</td>
<td>73%</td>
</tr>
</tbody>
</table>
Opportunity - But Roku and others may license their Software to make the experience easy

Roku TV: A Smart TV That Helps You Cut Out Cable

Low-Priced HDTVs With the Brains of the Popular Streaming Box

http://online.wsj.com/articles/roku-tv-a-smart-tv-that-helps-you-cut-out-cable-1409083779
Cloud Computing will thrive -

Content Providers will either build their own Cloud or will use Public Clouds

Data Needed..