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2019 Trends to Watch: TV and Video Super-Themes

The stakes have never been higher as big media consolidates to fend off FANG

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Summary

Catalyst

Megamergers of traditional media companies and unprecedented competitive pressure from scaled, multinational digital platforms, namely Facebook, Amazon, Netflix, and Google (FANG), are rapidly reshaping the entertainment industry. Traditional players have huge legacy businesses reliant on pay TV and commercial broadcast to sustain themselves while they attempt to reduce reliance on external distributors by investing in owned-and-operated direct-to-consumer (D2C) video platforms.

Ovum view

In 2018, the entertainment industry has been balancing the opposing requirements of preserving the cornerstones of traditional TV, in pay TV and commercial broadcast, while investing in winning market share in the growth segments of OTT subscriptions and AVOD. By 2019, we will know the initial results of the various transactions taking place that will transform the industry, namely AT&T's completed acquisition of Time Warner and the various potential transactions between Sky, Fox, Disney, and Comcast. These strategies represent the latest attempts to enable the media establishment to compete more effectively with the digital platforms – but there are no guarantees they will work. One thing is certain: the stakes have never been higher.

Key messages

- **Skinny bundles will solve pay TV's problems with subscriber growth, but ARPU and revenues will suffer.** 2019 will be the first year that skinny bundles drive overall subscription growth across pay TV and OTT in the US, reversing a near-decade-long trend.
- **Ongoing TMT megamergers will concentrate content spending across fewer platforms, owned by a handful of global giants.** The supersized entities likely to emerge from the current wave of M&A will focus on keeping their most wanted shows and movies exclusive to their own D2C platforms in order to better compete – or at least coexist – with FANG.
- **Alliances to jointly launch and operate OTT platforms will help broadcasters compete more effectively for AVOD market share.** There are, however, significant governance and execution challenges to address. YouTube and Facebook Video currently dominate AVOD revenue in markets such as the US, UK, Germany, Spain, and France, where any reorientation of market share will be hard won.

Recommendations

Recommendations for service providers and platforms

- **Ensure there is a clear path to commercial viability for skinny bundles.** Given the perilously low margins associated with the skinny bundle model, such servicesmight have to be positioned as loss leaders in the service of an adjacent business.

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- **Adopt a tailored approach to evolving markets with low OTT subscription uptake.** The flexibility afforded by AVOD and hybrid charging models may appeal to the larger free audience that can partially converted, over time, to a subscription-based model.

Recommendations for content providers

- **Focus content spending across fewer, strategically critical video services.** There are still too many OTT subscription video platforms: companies should focus original and exclusive content on their leading platforms to compete effectively.
- **Increase investment in original content production.** Differentiate video services in highly competitive markets through content. The hierarchy of content is increasingly being driven by its ability to stand out in a crowded catalog and attract and retain audiences.

Recommendations for technology vendors

- **Enable hybrid business models incorporating AVOD and subscriptions.** This will beparticularly important in emerging markets where OTT subscription uptake is low.
- **Focus on business models that help customers keep video platform launch and ongoing costs low.** We are entering a periodof intense competition and there is likely to be a shakeout of nondifferentiated and nonviable platforms: vendors will likely be asked to help some of their customers survive.

Skinny bundles will offset challenges to pay-TV subscriptions, but not to revenue

Survival amid pressure on pricing and from D2C launches

Growth in skinny bundle subscriptions masks the declines in traditional subscriptions, but skinny bundles are much less valuable in terms of both ARPU and commitment periods, meaning churn rates are markedly higher. Additionally, paying carriage for enough recognizable channels to be competitive means that at sub-pay-TV pricing levels, you are almost certainly teetering on a razor-thin-to-negative margin. The US will see combined subscription growth (both pay TV and skinny bundle) in 2018 for the first time this decade; however, combined revenues will continue to decline to 2022. Skinny bundle revenue growth will not be not sufficient to offset declines in traditional pay-TV revenue.

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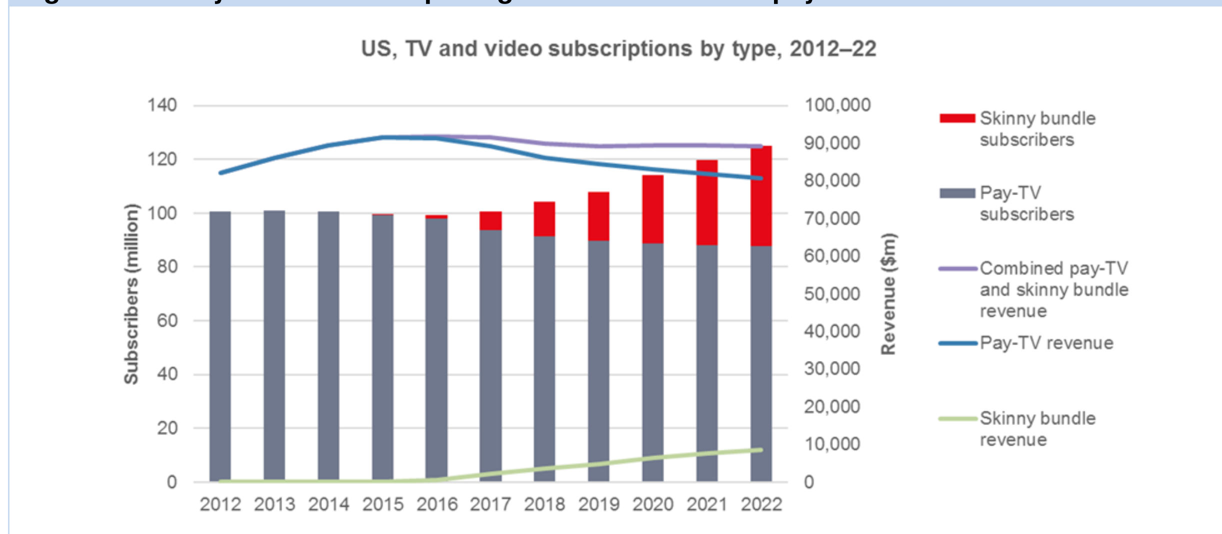
Figure 1: Skinny bundle subscription growth will not offset pay-TV revenue declines in the US



Source: Ovum

The implications for premium visual entertainment distribution

In 2019, we will see more OTT pay-TV services launch, particularly outside the US. We expect their impact to be less than in the US market, where pay-TV ARPU is very high and there is more scope to undercut the prices of traditional pay-TV subscriptions. Outside the US, pay-TV ARPU rates are much lower, so there is less wiggle room for price cutting and the erosion of the central value proposition of skinny bundles. Sky Europe, for example, is looking to graduate subscribers to its Now TV-branded skinny bundles to pay TV via promotional offers marketed via the user interfaces of its Now TV apps and media streamer device. Heavily discounted DirecTV Now access has also been used as an inducement to sign up to AT&T mobile, while AT&T Watch is offered "free" to the most valuable mobile subscribers. OTT pay TV is looking increasingly like a loss leader for adjacent businesses. If this is the case, multiple withdrawals are likely from companies offering this deceptively challenging video business model, by the end of 2019.

Supersizing content investment

Most of the world's Anglophone content will be created by a handful of gargantuan companies

The current wave of M&A means that content spending is increasingly coming from the coffers of fewer and fewer companies. Traditional media giants realize that they are, in their current forms and size, incapable of competing meaningfully against Netflix and Google for subscription and ad-funded OTT video market share. Even entertainment distributors and brands as recognizable as Disney are struggling to stake their claim. The latest response has been to combine, meaning that the content spending of each of the three largest entities potentially emerging from the current wave of US M&A – AT&T Time Warner (AT&W), Disney–Fox, and Comcast–Sky – would likely be more than double that of their nearest competitor in 2017 – which was, incidentally, Netflix. In 2019, more content investment will be focused on fewer platforms, as the supersized entities make big bets on D2C

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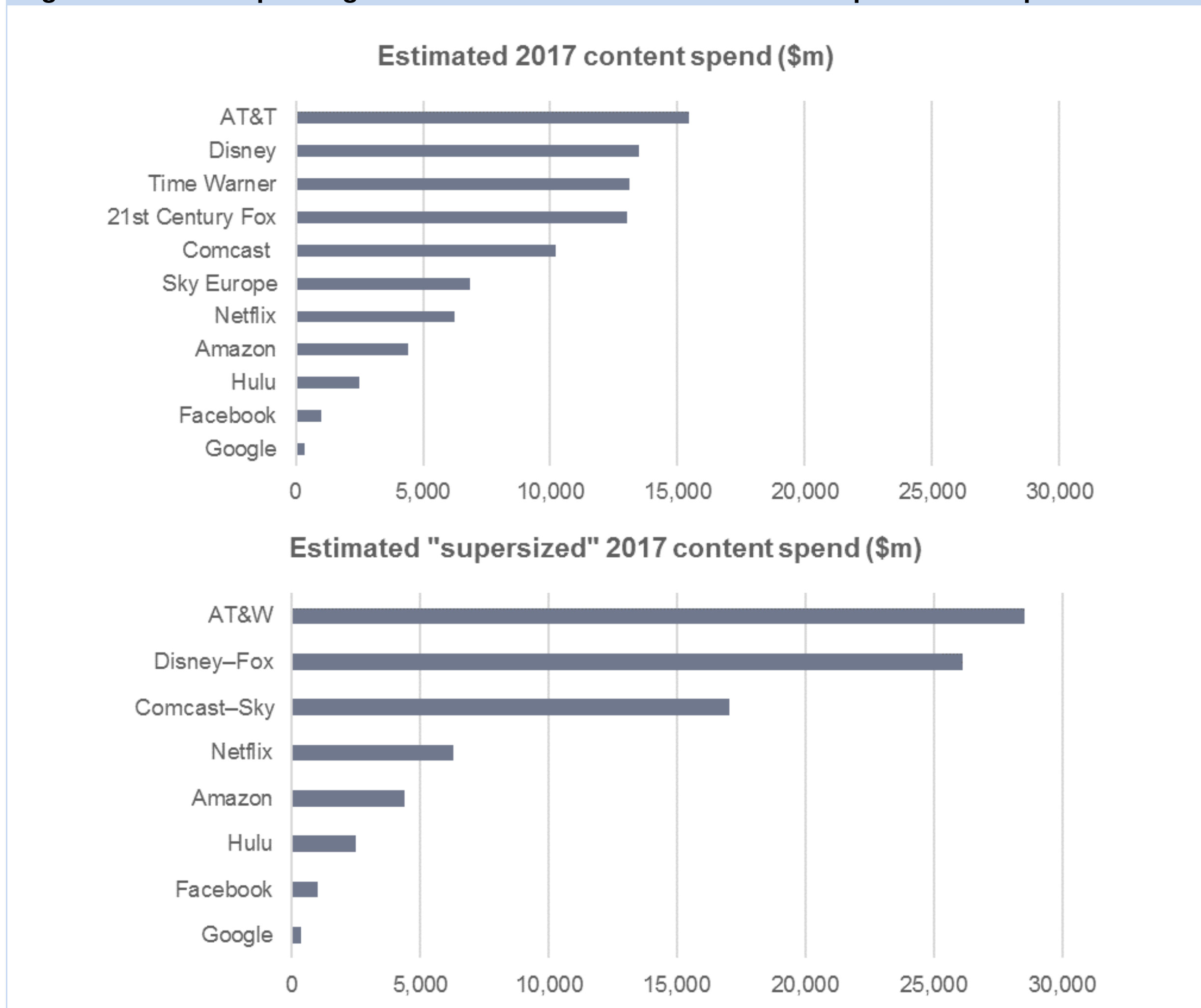
platforms to compete more effectively with Netflix and Amazon. HBO will be a prime beneficiary, with its existing annual budget for original productions expected to at least double. Disney's D2C platforms will also benefit substantially.

Figure 2: Content spending will become concentrated in a few ultrapowerful companies' hands



Source: Ovum

The shift to owned-and-operated D2C video platforms

An increasing number of shows and movies will be made for owned-and-operated D2C platforms as these platforms seek to compete with the digital platforms. Despite being able to spend more than Netflix, Facebook, or Google on original content, each of the supersized companies has many more outlets to populate, across TV channels and OTT video platforms, with diverse audiences to address, from sports nuts to anime fans. Netflix only makes shows for Netflix and its firepower is concentrated on the core platform. The combined entities will not be able to meaningfully scale more than one or two D2C video platforms each; hence their content spending should be concentrated in the key services, such as HBO Now for AT&T and Time Warner.

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FANG competition drives broadcasters to cooperate to compete

Broadcasters acknowledge that going it alone with OTT video isn't working

Broadcasters have started working together, jointly launching owned-and-operated OTT platforms that combine their respective content libraries, linear broadcast TV streams, and media sales capabilities. This is to attract bigger digital audiences, gather better data, and compete more effectively with the digital giants for digital advertising and subscription revenue. Broadcaster joint ventures and current M&A activity relies on this idea, with few alternative routes left, but this strategy is unproved. In 2019, we will be able to determine whether broadcaster alliances and the resultant OTT platforms can compete more effectively with YouTube, Netflix, Amazon, and Facebook for audience share, viewing time, and advertising and subscription revenue.

Figure 4: A growing number of major broadcasters are partnering on digital video

Broadcaster alliances in the US and Europe, Sep-18

Country	Broadcasters involved				Combined platform brand	Business model
US	NBCU	Viacom	Turner	Fox	OpenAP	Audience, data aggregation
Spain	RTVE	Mediaset Espana	Atresmedia		LovesTV	SLIN
France	France Télévisions	M6	TF1		SALTO	SLIN
Netherlands	NPO	RTL	SBS		NLZiet	SLIN
UK	BBC	ITV	Channel 4		Unconfirmed (Kanga-Two?)	SLIN
UK	Guardian	Telegraph	Sun	Times	The Ozone Project	Audience, data aggregation
DE/EU	ProSiebenSat.1 Media SE	Discovery	SPORT1	Axel Springer	7TV	AVOD now, SLIN later

Source: Ovum

The problem is the significant market share earned by the digital platforms in the two key growth narratives for TV and video distribution: subscription and ad-funded OTT video. Netflix and Amazon dominate the former while YouTube and Facebook Video routinely dominate the latter, with the two players' combined share of revenues in both cases exceeding 50% in most markets. Previous efforts to broach this dominance have not worked as well as hoped, hence the current focus on cooperation.

There is no doubt that the content offered by many of the broadcasters in these alliances is highly desirable to national audiences, given that many are among the most recognizable public and commercial TV brands in their respective markets. This strategy is, however, unproven and given the intensity of the competition between broadcasters, cooperation may be challenging to achieve. There is also no guarantee that the increased scale will enable broadcasters to take market share from the digital platforms. Much more needs to be revealed regarding the platforms' capabilities and go-to-market strategies before we can make a definitive comment on their prospects. But the short history of competing against native digital does not engender optimism.

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Appendix

Methodology

Drawing on Ovum's forecasts and research on global TV and video service providers, this report identifies the key competitive trends in global TV and video distribution in 2018 and 2019.

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