The Future of Broadcasting, Issue IV – Preview
A New Era of Optimism
A New Era of Optimism

After several challenging years that saw disruption from new competitors, digital technologies and changing consumers, the broadcasting industry is settling into a new era of cautious optimism.

At a macro level, the global economy has improved. Consumer entertainment and advertising demand have made a rebound supported by new online channels. Latest broadcasting projections suggest revenues will hit $579 billion by 2018, from $453 billion today. A rise of 6.3 percent compound annual growth rate (CAGR).1

Many of these themes and trends are being discussed online. If you would like to contribute to the discussion, please join us online at Pulse of Broadcasting.
At an industry level M&A activity has been buoyant. Average deal values and deal volumes have been rising over the last few years. In 2012, 589 deals took place at a total value of $72 billion. By 2013 deal count had risen to 615 deals and total value was up 27.7 percent to $92.1 billion dollars.²

The need for broadcasters to increase scale has been a major driver of M&A activity. The breakdown of geographical regulation and advancement of broadband capabilities have created a truly global competitive environment with lower barriers to entry. This has opened the gate for new, larger, more aggressive competitors to enter the broadcasting ecosystem.

These new competitors dwarf the average broadcaster. In terms of market capitalization, the average size of a top 20 broadcaster lags behind that of a cable company, is less than a third of a telecoms operator, and a meagre 10 percent of a super platform.¹

Broadcasters have become the smallest players in their new pool of competitors (see Figure 1).

At the same time subscriber rates have been reaching saturation across Western markets growing at just 0.2 percent CAGR in North America (2010 – 2018).³ In an attempt to hold their own, broadcasters have been forced to come together; consolidation has been a survival tactic for broadcasters globally.

The past three years have seen the potential creation of behemoths such as AT&T/DirectTV. This trend looks likely to continue. Plans to aggregate the Sky businesses to create Sky Europe, which will be the continent’s largest pay TV provider by subscribers, are underway and 21st Century Fox may well reengage in a takeover bid for Time Warner.

M&A activity has not been limited to large-scale deals. Investment decisions have included content production capabilities and digital businesses. Broadcasters understand that involvement in all aspects of the value chain, from content creation to consumer access, provides the greatest control. At the same time revenue growth is important and must come from new as well as traditional sources.

The market has responded positively. Future values have increased at an unprecedented rate to three times their value in 2012. While a few broadcasters have contributed more significantly to this increase than others it is still reflective of the industry direction as a whole. No other industry comes close to this rate of growth (see Figure 2).

While this signifies optimism in the industry it also highlights a crucial question: Where will growth come from to justify these lofty future values?

This report looks to help answer that question. We outline the findings of our annual Broadcasting Value Analysis and share four value creation themes that we believe broadcasters should act on to meet rising market expectations. At the same time we give consideration to the challenges along the way: a war on talent ignited by the glamor of tech start-ups and super platforms, increasing competition from global subscribers that has made premium content even more sought after, and a pressing need to ensure content investments align with consumer demand.
**Figure 2: Expected Future Values by Select Industries**

Expected Future Value (USD mn): This shows the market expectation for a firm with regards to its ability to grow above current operations (2012 - 2014)

<table>
<thead>
<tr>
<th>Industry</th>
<th>2012</th>
<th>2014¹</th>
<th>CAGR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aerospace &amp; Defence</td>
<td>490,549</td>
<td>692,484</td>
<td>25.8%</td>
</tr>
<tr>
<td>Consumer Goods</td>
<td>324,176</td>
<td>552,577</td>
<td>42.7%</td>
</tr>
<tr>
<td>Enterprise Technology</td>
<td>271,719</td>
<td>479,190</td>
<td>62.9%</td>
</tr>
<tr>
<td>Telecom</td>
<td>247,373</td>
<td>387,864</td>
<td>32.9%</td>
</tr>
<tr>
<td>Utilities</td>
<td>233,262</td>
<td>308,038</td>
<td>20.4%</td>
</tr>
<tr>
<td>Superplatforms²</td>
<td>221,207</td>
<td>232,602</td>
<td>-4.0%</td>
</tr>
<tr>
<td>Airlines</td>
<td>169,810</td>
<td>231,769</td>
<td>23.0%</td>
</tr>
<tr>
<td>Retail</td>
<td>128,606</td>
<td>167,701</td>
<td>123.2%</td>
</tr>
<tr>
<td>Pharma</td>
<td>69,074</td>
<td>155,814</td>
<td>13.6%</td>
</tr>
<tr>
<td>Comm Tech</td>
<td>62,982</td>
<td>125,663</td>
<td>61.4%</td>
</tr>
<tr>
<td>Broadcasting</td>
<td>50,299</td>
<td>51,310</td>
<td>56.6%</td>
</tr>
<tr>
<td>Cable</td>
<td>30,410</td>
<td>21,215</td>
<td>-55.8%</td>
</tr>
</tbody>
</table>

Source: Bloomberg, Accenture analysis

Notes: ¹2014 – refers to the latest period in 2014 as per earnings release of companies; ²Super platforms: Facebook, Google and Amazon;

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**Breaking Down Enterprise Value**

**Enterprise Value** is the sum of market capitalization plus net debt. It is broken down into two components:

- **Future Value**: Represents the market's expectation for a firm (or group of firms) with regards to its ability to grow above current operations
- **Current Value**: the value of the firm, or group of firms today. It is calculated by dividing profitability (NOPLAT) by the cost of debt (WACC)
The New Face of Broadcasting

The fourth edition of our Future of Broadcasting series, Accenture’s annual value analysis of 15 broadcasters (representing 47 percent of the industry based on revenue), identifies three key trends that are shaping developments in the industry.
1. Rapidly Increasing Market Expectations

Our analysis of the sector highlights an unprecedented increase in market expectations. These market expectations, illustrated by increasing industry enterprise value, rose 43 percent between 2012 and 2014. During this period current value remained relatively constant while future value fueled growth by tripling from $50.2 billion in 2012 to $167.6 billion in 2014 (see Figure 3).

One of the drivers of future value is revenue growth. In contrast to enterprise value, which has a CAGR of 15.7 percent (2009-2014), industry analysts are predicting broadcasting revenue growth rates will grow at 6.3 percent CAGR to 2018.

At this rate of growth the average margins in the industry will have to increase by at least 300-basis points to meet future value expectations by 2018. While there are a number of factors which, taken together, can partly explain the steep rise in future value—such as overall improving macro-economic conditions, previously undervalued assets and M&A activity—they by no means account for the whole increase.

Our research indicated, through constant current values, that linear cost cutting to date has paid some dividends but not enough. If the market is not to be proved wrong, broadcasters will need to focus on generating incremental value from their fixed assets while undertaking more significant cost restructuring.
Figure 4: Capital Structure Impact

Total Return to Shareholders is made up of increases in fundamental value of a firm, multiples (market expectations), dividends and capital restructure (the use of debt and equity). Multiples and capital structure were the largest contributors to the success of high performing broadcasters.

(Jun 2009 – Jun 2014)

| Source: Accenture value analysis of 15 broadcasters |

<table>
<thead>
<tr>
<th>Quartile</th>
<th>ProSieben</th>
<th>Netflix</th>
<th>CBS</th>
<th>IT</th>
</tr>
</thead>
<tbody>
<tr>
<td>TRS CAGR</td>
<td>63.5%</td>
<td>60.5%</td>
<td>57.0%</td>
<td>42.1%</td>
</tr>
<tr>
<td>Revenue Growth</td>
<td>2.4%</td>
<td>5.6%</td>
<td>14.8%</td>
<td>2.7%</td>
</tr>
<tr>
<td>Change in Margin</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Change in EV/EBITDA</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dividend Yield</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in Capital Structure</td>
<td></td>
<td></td>
<td></td>
<td>22.2%</td>
</tr>
</tbody>
</table>

2. Balancing Operations and Investments

The leading performers in our analysis share two common characteristics; they have raised capital and continued to invest in content. When we rank leaders by total return to shareholders (TRS), ProSieben occupies the top position, followed by Netflix, CBS and IT. For this top quartile, changes in capital structure were the largest contributor to TRS. This was achieved by reducing share of net debt, to which investors responded favorably.

This theme was seen throughout the peer set. Nine of the fifteen companies included in our Value Analysis saw share price increases arising from the positive impact of changes to their capital structures. This includes both the reduction in debt and investor response toward restructuring activity (see Figure 4). These leaders’ significant investments in content, either through joint ventures or direct production, establish a clear link between content investment and performance. And the market believes that they will continue on that trajectory—with a strong track record of returns on invested capital.

3. Segment is not a determinant of performance

When Accenture first started its Value Analysis in 2007, Pay TV broadcasters emerged as the higher performing segment. In subsequent analyses the mix of high performers by segment became more dispersed. In this year’s analysis, that dispersal has further increased.

The blurring of segment boundaries, as more Pay TV providers offer FTA services and vice versa, is partly responsible for this performance dispersal. We found more FTA broadcasters (four), than Pay TV broadcasters (two), in the top half of our TRS performance scale signifying individual strategies and respective investor responses are more influential determinants of success than any overarching preference for a specific segment. Going forward, our prediction is that scale will also be an important contributor to performance providing a greater audience share and a more diversified portfolio of products and services.

More broadly, economic conditions have squeezed consumer disposable income globally and, for Pay TV broadcasters, saturation of subscriber numbers in the main markets of North America and Western Europe has had its toll.

However, segment specific conditions mustn’t be overlooked. Pay TV broadcasters are currently within an investment cycle as they develop more sophisticated on-demand features. They have also had to make substantially greater investments in distribution than their FTA counterparts.
The industry themes we have identified enable us to draw out four value creation themes that broadcasters will need to focus on in order to meet the market’s future value expectations. Understanding consumers and ensuring decision-making is centered on consumer insights will be key to success.

This relentless focus on the consumer will have an impact on all elements of a broadcaster’s business: from content decision-making and technology investments to operating model updates and global expansion plans.
Value Creation Theme 1: Premium and Cost-Efficient Content

A rise in the volume of content being produced has led to an increase in costs for high value, quality content. The appeal of premium content is clear. It can increase subscriber numbers, drive up revenues and offer a way to introduce other services. However, with the cost of premium sporting rights known to increase by more than 50 percent each time they are renegotiated, the high cost of premium content can adversely impact profits. In addition, building a subscriber base around premium content also carries the risk of rapid audience decline in the event sports rights are lost to a competitor.

While broadcasters seek ways to monetize rights through the introduction of other offers, (e.g. one-off pay per view deals or by using premier content to reward loyal consumers) they need to do more to offset the increasingly large costs of premium content. In April 2014, Netflix announced plans to raise its pricing by $1-2 per month, initially for new users only, but eventually everyone. The company plans to use the increased revenues to “acquire more content and deliver an even better streaming experience.” Netflix is anticipating that consumers will accept the trade-off between the modest rate increase and a significantly improved user experience.

A focus on new approaches to content production is fundamental in this environment, especially given that new engagement methods have become essential, content sources and competition are becoming global and disruptive competitors have large cash reserves.

Creativity will enable broadcasters to find ways to acquire and create content more cost effectively. The recent upsurge in M&A activity between broadcasters and TV content creators (e.g. Liberty Global’s stake in ITV, or Disney’s acquisition of Maker Studios for $500 million) illustrates one way of becoming cost effective. Crowdsourcing and user generated content is another way. BBC News and CNN utilize user-generated content to supplement content at relatively low costs.

However embracing creativity in a sustained and continually cost effective method requires broadcasters to go one step further. They must both internalize and protect those creative skills that have been abandoned over the decades in favor of less risky rights acquisition strategies. This requires embracing new digital production processes that involve a ‘digital from day 1’ attitude, including increasing interactions while shortening production cycles. And in adopting these processes, intellectual property management must be given appropriate consideration.

Warner Bros.’ investment in digital end-to-end capabilities has transformed its entire film and television production, post-production and distribution to an entirely digital process. This has enabled considerable savings in management and distribution costs at the same time as more than doubling annual film deliveries—all in two years. In terms of securing content for use across multiple channels and devices, cable and content providers have secured rights for TV everywhere service that aim to counter consumer need for OTT offerings (such as Netflix and Hulu) and to develop the foundations for a future IP-streamed multichannel subscription package.

Whatever decisions they make about selecting and investing in new content, understanding consumers will be essential for all broadcasters. It will help them to understand specifically how much and for what consumers are willing to pay. This, in turn, should increase the likely success of future investments. However, the ‘right’ content is only part of the story. Putting these assets to best use is just as important as what they acquire.

Value Creation Theme 2: Consumer Optimization

Consumers have high expectations of media experiences set by players such as Google, Apple and Netflix. These businesses, and others like them, operate directly to the consumer. The strength of those relationships enables these organizations to develop an increasingly detailed picture of consumer preferences and behavior. This in turn drives a lucrative circle of greater insights that can direct additional investments to further engage consumers’ attention—and their wallets.

These players’ show mastery of two key capabilities:

a. They customize content by users

By using advanced analytics these firms are able to make continuous and increasingly relevant content recommendations to individual consumers and provide a joined up experience through seamless multi-device viewing. While a number of competitors have tried to replicate this success, by building connected device ecosystems and providing the content alongside them, their success to date has been limited.

An understanding of user preferences is therefore extremely important for broadcasters. Beyond relevant content recommendations, user preferences coupled with technological advances enable even the most niche content to find an audience. This opens up a whole world of consumers for new and existing content.

b. They engage everywhere

The ability to engage beyond content provides a new way to both retain existing consumers and attract new ones. Examples include branded interactive games that integrate live sports with fantasy team stats and live gambling opportunities based on content.

The top performer in our analysis, ProSieben, acquired Aeria Games Europe to provide access to new markets and areas of new growth. ProSieben’s gaming community is now 77 million strong, with a portfolio of 29 licenses, and the company publishes games in 35 countries. While the acquisition of gaming assets is not a trend being seen across the broadcasting industry, the gaming sector’s 8 percent CAGR provides a clear potential growth strategy.
Converged Operating Models

For content investments to really pay off, broadcasters need to challenge current operating models and move from vertical structures into horizontal, converged organizations. This will enable the optimization of key capabilities such as sales, content creation, consumer insight, product development and technology solutions. These capabilities need to be organized across channels or geographies to support a global audience base at a lower cost-to-serve.

In defining new operating models, the traditional channel structure has to be challenged along every dimension — technologies, distribution methods, access devices, monetization models, marketing techniques, advertising paradigms, rights acquisitions and management, organization structures, talent and skills. Broadcasters must also consider how they can facilitate the continued journey into the digital era whilst maximizing content value and building audience insights.

Operating models should support broadcasters in making consumer-centric decisions and ensure information can be rapidly shared across business units. New ideas and concepts must be quickly replicable to all channels regardless of geography, P&L accountability and internal control structures.

This requires operating models to be lean, agile and nimble. They must be ready to take advantage of advances in digital capabilities and replicate these globally. With M&A activity expected to continue, structures must be capable of accepting acquisitions, supporting mergers and rapidly realizing expected synergies.

To achieve this, flexibility must be built into support functions. Some support functions will need to be specific whilst others can be brought together in cross-product shared services. IT and engineering capabilities, for example, will need to be consolidated to create service-oriented architectures capable of continuous delivery at scale with decreased time-to-market.

The role of technology cannot be overestimated in the quest for a more agile and cost effective operating model. Broadcasters need to become media technology companies, learning from the success of new Internet-based entrants, or risk getting left behind. The adoption of cloud shows that broadcasters are at different stages of this evolution. 27 percent of broadcasters are deploying cloud-based solutions and while most cloud initiatives involve private cloud solutions, reflecting the embedded culture of controlling technology in-house and concerns over security of core content and customer data, there is a trend toward hybrid, more cost effective models. These models incorporate some public cloud services, while keeping more sensitive data in private clouds, and increasingly use encryption and anonymization of data in public clouds.

As highlighted in the Accenture point of view, “How Cloud Computing Changes the Game in Media & Entertainment,”
the benefits of a cloud-based approach are abundant:

- Faster speeds to market, closing the gap on OTT delivery cycles
- Scalability to support spikes in workload and surges in the popularity of new services
- Data collection to enable consumer optimization becomes feasible
- Ongoing service innovation through constantly iterative, agile development

If successful, converged operating models can lead to a unified commercial organization with improved rights management, content and ad sales. As brands operate across channels they improve the experience offered to consumers and can drive additional sales. In addition, brands operating across channels can drive down costs and support faster, more successful, innovations.

Value Creation Theme 4: Monetization

One of the ways analysts expect broadcasters to unlock future value is by monetizing their existing assets to increase profits. For example, enhanced advertising prospects (e.g. dynamic ad insertion, wrap around content ads and content access ads) provide opportunities for broadcasters to generate further revenues. With digital advertising providing the greatest CAGR growth, advanced advertising should be part of a broadcaster’s strategy. Here again, the ability to understand consumers is important in order to provide a more compelling offer to advertisers.

Others are looking to launch new services that focus on business-to-business markets, for example, deals with hotels, jails, hospitals and stadiums.

These opportunities, and those included within in all of our value themes, are limited by the overall growth available in developed markets, many of which are reaching saturation. Looking further afield, and in particular to developing economies, can offer the possibility of faster growth rates. To that end, broadcasters are seeking to reach new, global audiences with their content. This has been a successful strategy for many top performers in our analysis; for example, ITV, Netflix, and the BBC have global revenues making up a substantial part of their total revenues. Netflix recently acquired exclusive global rights to the Warner Bros. Batman series Gotham. The deal provides Netflix with premium content to service its growing international subscriber base. Other broadcasters such as Canal +, Direct TV and RTL with CBS in Asia have expanded infrastructure through acquisitions, joint ventures and alliances in new markets.

With subscriber numbers reaching saturation in developed markets, emerging markets offer a potentially attractive space into which broadcasters could profitably expand. Consolidation activity has supported this expansion, providing broadcasters with a larger footprint and therefore, naturally enough, larger audiences.
Turning Today’s Optimism into Tomorrow’s Returns

Over the past four years, our Future of Broadcasting series has tracked the fundamental shift in the broadcasting industry, from an insular environment dominated by a Pay TV business model, to a dynamic industry that’s adapted to digital disruption, expanded competition and changing consumer needs.

Responsive business strategies, new content experiences and a series of technology innovations have been part of this evolution, achieved through a combination of organic and inorganic growth. The market is impressed. Our research shows that the expectations for the broadcasting industry have never been higher. In order to deliver the needed growth, broadcasters have to keep raising their game.

Success will depend on increasing revenues and controlling costs through balanced investments in content, optimizing the consumer experience, developing innovative approaches to monetizing existing assets, and establishing a content-centric operating model that supports flexibility at low cost. The market is willing to invest in sound strategies and reward those that can execute. Are you ready to make your next move?
References

1 Accenture Research, PwC’s Global M&E Outlook, 2014-2018; SNL Kagan’s Multichannel Database
2 Bloomberg
3 Accenture Research, PwC’s Global M&E Outlook, 2014-2018; SNL Kagan’s Multichannel Database
4 As in previous years our analysis is grounded in a value analysis of key players in the global broadcasting industry. Our work around the world with broadcasters and other media, entertainment and consumer technology companies (most of which are now in the video content space) allows us to build on the fundamentals of our value analysis to draw a set of “moment in time” conclusions about this rapidly evolving sector.
7 Bloomberg, Accenture Research
8 Devoncroft Big Broadcast Survey 2014
1 Super platform cohort includes Amazon, Google and Facebook

About Accenture
Accenture is a global management consulting, technology services and outsourcing company, with more than 293,000 people serving clients in more than 120 countries. Combining unparalleled experience, comprehensive capabilities across all industries and business functions, and extensive research on the world’s most successful companies, Accenture collaborates with clients to help them become high-performance businesses and governments. The company generated net revenues of US$28.6 billion for the fiscal year ended Aug. 31, 2013. Its home page is www.accenture.com.

Authors
Gavin Mann
Global managing director
Accenture Broadcasting
Francesco Venturini
Global managing director
Accenture Media & Entertainment
Ekta Malhotra
Senior manager
Accenture Strategy, Communications, Media & Technology

About the Series
Accenture’s “Future of Broadcasting” series is grounded in our Shareholder Value Analysis (SVA) of key players in the global broadcasting industry. Our work around the world with broadcasters and other media, entertainment and consumer technology companies allows us to build on the groundwork of the SVA to draw a set of “moment in time” conclusions about this rapidly evolving sector.

In this latest issue we address the value creation themes required to deliver on the significant market expectations for future growth in the broadcasting industry.

Acknowledgement
We’d like to acknowledge the significant contributions of the following individuals:
Bouchra Carlier, senior manager, Accenture Research. Bouchra leads Media and Entertainment research globally. Dominik Michaelis, senior manager, Accenture Media & Entertainment.

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