The Future of Broadcasting V
The Search for Fundamental Growth

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In last year’s issue, *The Future of Broadcasting IV*, we observed that market optimism within broadcasting had soared, and asked where growth would come from to justify these lofty future values. This year market expectations have continued to climb, despite a $130 billion plunge in the value of the wider media market in August 2015. The widening gap between future value and current value makes the search for fundamental growth increasingly pressing for broadcasters.
In this year’s edition two other financial trends have emerged. A number of broadcasters have made a strategic shift to content production, generating revenue from international licensing deals and global/local syndication, in order to protect themselves from slowing growth in advertising revenues. Other broadcasters have looked to achieve scale through consolidation, as demonstrated by increased M&A activity.

In response to these financial trends, we have identified three opportunities for value creation: how to capitalize on service as a point of differentiation, how data analytics can be used as a strategic tool for content decisions, and how incumbent broadcasters can exploit the “broadcast advantage.” We believe these value-creation opportunities will help broadcasters in their search for new sources of fundamental growth.

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 Media.
Growth in the broadcasting industry has been slowing. Industry revenues increased to $413 billion in 2014, but fell short of the $418 billion analysts had forecast last year. That shortfall of $5 billion, although small in relative terms, represents a 19 percent reduction in projected revenue growth. This slowdown in growth may not have registered yet, but its impact is likely to be felt soon, with industry revenues in 2018 ($501 billion) set to be $43 billion lower than analysts’ projections last year.

In the 2015 edition of *The Future of Broadcasting* we outline the findings of Accenture’s annual broadcasting value analysis and identify three financial trends that are shaping developments in the broadcasting industry. We also assess the implications of these trends and share three value-creation opportunities that we believe broadcasters should act on to improve fundamental growth.

**TREND 1: Market optimism continues but increases in current value yet to be seen.**

The future value of broadcasters has now reached an all-time high and, for the first time, accounts for almost half of enterprise value. Despite shares in media companies plunging by $130 billion in August 2015, broadcasting future value has grown by 14 percent since last year. The gap between expectations and performance is widening, raising some crucial questions. How will current value rise? And, if it doesn’t, will further market correction be inevitable?

**TREND 2: Content strategies pay off.**

To create value, some broadcasters have invested in original content production/commissions and maximized revenues from international rights deals and local/global syndication. These content-led broadcasters have achieved higher levels of capital efficiency and higher operating margins than their peers who rely on advertising income alone.

**TREND 3: Consolidation for scale drives M&A activity**

Broadcasters have sought to create value from M&A activity. We have seen consolidation take place at both ends of the value chain—in content creation and distribution—with broadcasters looking to achieve scale. We have also observed broadcasting organizations acquiring multi-channel networks (MCNs), to reach new audiences and advertising revenue pools.

We also propose three opportunities for value creation that we believe will help in the search for fundamental growth. First, we argue that, thanks to the proliferation of new content platforms, service has become a key differentiator, and broadcasters need to develop a multitude of heavily tailored offerings to meet customers’ needs and their willingness to pay. Secondly, we look at how broadcasting organizations can use data analytics as a strategic tool to inform content-commissioning decisions and programming choices. And finally, we analyze how incumbent broadcasters can “exploit the broadcast advantage” to compete against digital natives entering the broadcasting ecosystem.
The Future of Broadcasting peer set

In this latest edition of the series, our value analysis focuses on fifteen broadcasters, representing 52 percent of the industry based on revenue. Broadcasters were selected to ensure a variety of geographies, revenue models and company sizes are represented. Their operations span the broadcasting value chain from aggregators to operators. Only broadcasting organizations who make their financial data publicly available are included in the peer set. Our objective is to provide a robust and representative perspective on the broadcasting industry.
Market optimism continues but increases in current value yet to be seen

Market expectations within broadcasting have continued to climb, with the future value of broadcasters now at an unprecedented level. Despite shares in media companies plunging by $130 billion in August 2015, broadcasting future value has remained high. The gap between broadcasters’ future value and current value is widening, raising some crucial questions.

How will current value rise? And, if it doesn’t, will further market correction be inevitable?

**EV = CV + FV**
Enterprise Value = Current Value + Future Value

**Enterprise Value** is the sum of market capitalization plus net debt—intuitively, it’s what you would pay if you were to purchase a listed company. It is comprised of two components:

**Current Value** is the value of the firm, or group of firms, today. It is calculated by dividing profitability (NOPAT or Net Operating Profit After Tax) by cost of capital (WACC or Weighted Average Cost of Capital).

**Future Value** represents the market’s expectation of a firm’s (or group of firms’) ability to grow above current operations.

In last year’s issue, The Future of Broadcasting IV, we identified a widening gap between the future value and current value of the broadcasters tracked in our analysis. This year that gap has continued to widen, with future value, which grew at 31.4 percent per year⁶ between 2012 and 2015 (see Figure 1), now accounting for 50 percent of enterprise value, up from 44 percent last year.

At the same time, the wider media market has seen a substantial fall in value. In just three weeks, $130 billion was wiped off the Dow Jones Media Index—a fall of 16 percent—after Disney issued revised guidance in August 2015 relating to subscriber losses at its sports cable network ESPN.⁷ However, the impact on the broadcasting market⁸ has been moderate. Over the same three weeks (when global markets were also affected by a significant crash of the Chinese market), the enterprise value of the broadcasters we track decreased by approximately 5% (or ~30 billion only). Only three of these broadcasters saw a decline in enterprise value greater or equal to 10 percent (and, in one case, this was the result of a currency devaluation).

The moderate impact on the broadcasting market can be explained by the diversity of our peer set, whose members are spread out across the globe and the broadcasting value chain. Only four of the fifteen broadcasters we track are based in the US market and our peer set includes both content aggregators and platform operators. This combination of geographic and operational diversity has left the peer set better protected against the threat of cord cutting.

Strong expectations in the broadcasting market raise two important questions.
With broadcasting future value at an all-time high, how will current value rise? And, if it doesn’t, will a market correction be inevitable?
Content strategies pay off

With growth in advertising revenues weakening, broadcasters who have adopted a content strategy have prospered. Our analysis found that those broadcasters who earn 20 percent or more of revenue from content production and licensing have out-performed their peers who rely on advertising income alone, achieving higher levels of capital efficiency and larger operating margins.

For the majority of Pay TV broadcasters tracked in this analysis, the slowing growth of advertising revenues has become significant. Between 2011 and 2014 most broadcasters in the peer set saw their advertising revenues fall as a share of overall revenue, in one case by as much as 10 percent.

A number of broadcasters have successfully made up for this shortfall by generating more revenue from content (acquired from a combination of international rights deals and local or global syndication). Some broadcasters in the peer set have traditionally produced content, but others have developed content strategies only recently. ITV, for example, has made a substantial investment in original content, creating a B2B “movie-studio” model (see case study below). This move has helped increase the contribution of ITV’s international business, as a proportion of total revenue, by 19 percent over the last five years.

Adopting a content strategy has been popular in the US for many years, where cable networks completely transformed their business by moving into content production and licensing. Recently, this approach has also gained traction in Europe, where it is considered a less risky option than digital for generating revenue. A broadcaster setting up a digital service, such as an OTT platform, has no guarantee that it will attract sufficient viewers to pay off the sizeable up-front investment in technology that is needed. A broadcaster moving into content production, however, will spread investment across different strands of content and have numerous options of broadcasters and platforms as prospective buyers. As we observed in our Pulse of Media 2015 report, broadcasters are enjoying a content “renaissance.”

Our value analysis found that content-led broadcasters achieved higher levels of return on invested capital (ROIC) than those who relied on advertising revenues alone. Superior performance can be seen both in terms of capital efficiency (between 20 percent and 50 percent for content-led broadcasters versus below 20 percent for advertising-dependent broadcasters) and operating margin (20 percent to 30 percent versus 5 percent to 15 percent respectively).
CASE STUDY | Content-led broadcasters

ITV

Five years ago ITV, a UK-based broadcaster, was heavily reliant on advertising income, with 69 percent of its revenue coming from advertising. This dependence left it vulnerable to the 2008 financial crisis, which saw a loss of advertising revenues contributing to a 7.3 percent fall in ITV’s 2009 revenue.

Falling revenues accelerated a change in strategy for ITV, which sought to rebalance its revenues and reduce its reliance on UK advertising income. In the last five years, the broadcaster has made a considerable investment in its production arm, ITV Studios, acquiring eleven production companies (and in talks to buy another, the TV division of UTV Media3). By investing in content, ITV has been able to increase the contribution of its international business, as a proportion of total revenue, by 19 percent over the last five years. Boosted by these investments, revenue (UK and international) from ITV Studios has grown by 68 percent over the same period (see Figure 2). As a result, the share of ITV’s revenue from advertising fell to 63 percent in 2014.

ITV’s content strategy is centered on the assembly of a large portfolio of successful series and formats with wide appeal. The broadcaster generally showcases new programs and formats on local linear channels before licensing them across multiple platforms in the UK and abroad. Thanks to the international success of shows such as Hell’s Kitchen and I’m a Celebrity..., ITV sold 36 formats around the world last year and has become the largest independent producer of unscripted content in the US.

More examples

Content-led broadcasters are making their shows and formats widely available across devices and geographies in order to achieve sustainable scale. Fox Studios, for instance, has increased the number of TV series it produces from 27 to 43 over the last five years. Consequently, these broadcasters are likely to continue placing their premium content on as many devices and platforms (including streaming services such as Hulu, NOW TV and Sling TV) in as many regions as possible.

Other broadcasters have also been turning to content strategies to diversify their revenue streams away from advertising. RTL, a major European broadcaster, has invested in content by acquiring American production company 495 and a 25 percent stake in Corona Television, a new UK-based drama producer.
Consolidation for scale drives M&A activity

The value of media-sector M&A deals this year is set to exceed the combined value of transactions completed over the last four years. This upswing in deal value is being propelled by the creation of two new broadcasting behemoths—AT&T/DIRECTV and Charter Communications/Time Warner Cable—and by two significant trends in M&A activity. First, consolidation is taking place at both ends of the value chain, in content creation and distribution. Secondly, broadcasters are acquiring multi-channel networks (MCNs), to reach new audiences and advertising revenue pools.

After a quiet period in 2014, M&A activity in the media sector is forecast to hit $165bn in 2015. This projected deal value is greater than the sum of all the transactions completed over the last four years. As of August 2015, total year-to-date transaction value was $75 billion, with a pipeline of $90 billion set for approval by the end of the year.

Two trends in recent M&A activity stand out: consolidation to provide scale and the acquisition of MCNs.

1. Consolidation to provide scale is being seen at both ends of the value chain. Content companies are acquiring other content companies. The Fox/Time Warner deal in 2014, in spite of the bid ultimately being withdrawn by Fox, sought to support Fox’s strategic imperatives of investing more in quality content, breaking out of traditional TV cycles and processes, and innovating in development, marketing and distribution. At the other end of the value chain, consolidation in distribution and channel ownership (for instance, Sky Europe) can be used to maximize investment in content.

In the broader ecosystem, the AT&T/DIRECTV deal has increased AT&T’s market share of TV subscribers from 6 percent to around 28 percent. If the deal between Charter Communications and Time Warner Cable is approved, the combined entity will have an 18.2 percent share of US TV subscribers and will achieve 3rd position in TV subscriber market share.

2. Acquisition of MCNs. Although transactions involving MCNs have been smaller in deal value (estimated to be in the range of $1.6 billion in 2014), the increased popularity of MCNs among content providers, traditional broadcasters and telecom companies is likely to have a significant effect on the market. This impact is likely to be felt in a number of ways, as MCNs:

- can provide direct access (B2C) to new global audiences who are beyond the reach of saturated domestic markets and may have given up on traditional TV
- allow broadcasters to take advantage of existing relationships with media buyers to increase advertising revenues
- enable broadcasters to develop and experiment with new formats
- support access to burgeoning advertising revenue pools.

The last point has substantial significance for future revenues. YouTube’s annual advertising revenue stands at approximately $4 billion, while Facebook, Twitter and Snapchat have all underlined the importance of video to their strategies. Moreover, mobile advertising still has substantial room for growth, especially relative to the amount of time that consumers spend using their mobile devices.

Source: Bloomberg, Accenture analysis
CASE STUDY | Traditional broadcasters and MCNs

ProSiebenSat.1 and Collective Digital Studios

German broadcaster ProSiebenSat.1’s acquisition of a majority stake in Collective Digital Studios is a recent example of a traditional broadcaster assuming control of a major MCN. With an investment of $83 million in July 2015, the broadcaster increased its interest in the MCN from 20 percent to 75 percent, enabling it to merge Collective Digital Studios with its smaller in-house MCN, Studio 71. The combined entity, known as CS71, is valued at $240 million and set to attract 2 billion video views a month.

What is a Multi-Channel Network?

Multi-Channel Networks (MCNs) are a new type of player in the broadcasting industry, whose innovative business model has sprung up in the wake of YouTube’s explosive growth. MCNs team up with digital talent to produce video content skewed towards younger viewers, which is then distributed, promoted and monetized through partnerships with YouTube or other video-streaming platforms.

MCNs vary in scale but the biggest control thousands of YouTube channels, have millions of subscribers and attract billions of views a month. One of the largest MCNs, Maker Studios, has more than 650 million subscribers and its content is viewed over 10 billion times a month.

ProSiebenSat.1 joins RTL (which owns MCNs Broadband TV and StyleHaul), Disney (which acquired Maker Studios in a deal valued at $500 million) and DreamWorks (owner of AwesomenessTV after a $95-million transaction) as the largest groups on YouTube.
Opportunities for value creation

Our value analysis has identified three important financial trends. The widening gap between future value and performance makes the search for fundamental growth ever-more pressing. Broadcasters have—with some success—turned to content strategies to improve performance.

At the same time, broadcasting organizations have sought to create value through increased M&A activity and consolidation in the industry. But it is unlikely that these initiatives alone will be sufficient to close the gap between expectations and performance. We have identified three opportunities for value creation, which we believe will help broadcasters in their search for new sources of fundamental growth.
1. Service is king

Digital natives have redefined customer experiences and expectations, not just in broadcasting but across every customer-facing industry worldwide. At the same time, the proliferation of new content platforms has meant that consumers now have far more choices in where to spend their entertainment dollars. (This is especially true for video-on-demand transactions, where the same content can be on multiple platforms.) This has meant that the service itself becomes an integral part of the customer experience, with the potential to make content more accessible, attractive and engaging. In this new world, high-quality content is indispensable, but “service is king.”

At the same time audiences will continue to want what they want, when they want. A recent survey discovered that consumers abandon video streaming if it is delayed by more than two seconds. Broadcasters, now more than ever, have to be able to offer content anywhere (on and off network), anytime (live or time-shifted) and on any device (laptops, PCs, tablets and smartphones), at a low latency and in an easy-to-use, intuitive format.

The unbundling of packages and the establishment of direct-to-consumer models (such as EROS’s and Lionsgate’s OTT streaming services) have contributed to an increase in transactional video on demand. Despite this, transactions have seen relatively slow growth, as subscriptions have remained the dominant form of video on demand, both in transaction numbers and value. It has, however, accustomed consumers to being more selective over the content they want, which is affecting consumer attitudes toward subscription services. More and more, consumers want bundled services but with the option of customizing these packages to provide what they consider to be best value for money.

Price, alongside content and service, has become crucial in an increasingly competitive market. This is a difficult task for any broadcaster. Some broadcasters such as Verizon FiOS—Custom TV, Sky—NOW TV and Dish—Sling TV have created stand-alone OTT and direct-to-consumer offerings. These broadcasters offer “skinny bundles,” providing customized packages at a low price (Custom TV starts at $10 a month, NOW TV at £6.99 and Sling TV at $20). These bundles have had some success to date: Sling TV, for instance, has nearly 250,000 subscribers, and Now TV has attracted 1 million subscribers within two years of its launch. While this poses a significant risk of cannibalization to legacy businesses, the risk of complacency is bigger. Can broadcasters afford to ignore consumer demands in this competitive environment? Kodak was killed by incumbency, not by the digital camera.

The key for broadcasters looking to create value is to develop a more fragmented market with a mixture of propositions tailored to customers’ needs and their willingness to pay. The use of analytics, driven by the collection of accurate usage, content-preference and subscription data, provides an opportunity for broadcasters to truly understand segment dynamics and offer segment-only propositions based on deep insights. This enables broadcasters to establish direct-to-consumer models and offer low-cost bundles, attracting “cord nevers” and “cord shavers” while minimizing cannibalization from cord cutting. If successful, the net impact of these innovations would be to increase the size of the broadcasting market by attracting consumers who would never have subscribed to a traditional broadcast package.

Over the last few years, efforts to meet service expectations have centered on content discovery through mining insights to improve personalized recommendations. This has been a long-time differentiator for Netflix and other digital natives. Broadcasters now need to develop this concept further, not just to meet service expectations but to better understand their customer base. This knowledge can then be used to drive advertising revenues and inform a segment-driven approach to pricing propositions.
2. Content decision-making

Uncertainty exists around many aspects of the future of broadcasting, but we can be confident that two trends will continue. First, audiences will continue to favor high-value content and, secondly, technological advances will enable better-quality access to content across a greater number of devices. Over the coming years, these trends are likely to fuel demand for content, which, in turn, will boost its cost. Supporting content investments in these circumstances poses a challenge to broadcasters. For those that have acquired content capabilities of their own, the increased cost of content signifies a higher opportunity cost for failure, and for those that have not, it means the stakes are raised when it comes to making programming decisions.

To meet this challenge, broadcasters need to become better at exploiting and analyzing the data they collect. Analytics is vital in meeting service expectations and supporting pricing propositions, but it also provides a strategic tool for content decision-making. Insights about how viewers engage with content can help broadcasters with crucial decisions: whether to build or buy in a new series or re-commission an existing show, what talent to attach to projects, what genres (scripted versus non-scripted, sports versus drama) to build content strategies around, and how best to format and distribute content (exclusive versus exhaustive, binge-watching on OTT versus Sunday evening network primetime).

The use of analytics to inform content strategies was pioneered by Netflix when determining whether to green light its original production of House of Cards. Netflix’s recent decision not to renew its deal with Epix (which means popular films like The Hunger Games: Catching Fire and World War Z will disappear from Netflix) was also likely informed by insights from predictive analytics of its users’ content-consumption patterns.

A silo’ed approach to analytics will not lead to an improved return on content investments. Only a tightly integrated analytics strategy, driven by coordinating content strategy, viewing recommendations for users and audience measurement, will boost the returns on content investments, while also building customer satisfaction and brand loyalty.

3. Exploiting the broadcast advantage

The broadcasting ecosystem continues to expand rapidly beyond traditional broadcasters, as digital natives increasingly use content to drive growth within their wider business (as illustrated by Amazon’s loss-leading Prime bundle, Rakuten’s acquisition of Wukai.tv, and Alibaba’s announcement of the launch of Tmall Box Office).

While growth in enterprise value across the broadcasting industry has increased, a typical broadcaster’s average market capitalization still stands at just over 10 percent of an average super platform’s (see Figure 4). This is a significant disadvantage in an industry where cash for investments in high-quality content and the best platforms or services to showcase it on, coupled with scale to access new and far-reaching audience bases, are major differentiators.
Moreover, as Accenture’s recent report *Bringing TV to Life V* highlighted, the uniquely digital heritage of these new entrants to the broadcasting industry gives them an inherent understanding of how digital consumers behave and what they want. Digital natives, such as super platforms, also possess a mastery of the capabilities needed to target and serve consumers effectively on a global scale.

At first sight, the picture looks bleak for broadcasters who, having evolved from traditional terrestrial networks, tend to lack the agile operations and digital skills of their new competitors. But broadcasters have two significant advantages over other industry players.

The first can be summed up in one word: trust. Most broadcasters have been at the heart of their national cultural life for decades, and audiences have grown up with them in their lives. Accenture’s Digital Consumer Survey found that a greater number of respondents (31 percent) trusted broadcasters to provide a high-quality service than internet-video providers (15 percent) and social-media service providers (5 percent) combined. Furthermore, consumers show a clear preference for obtaining digital services from one provider, rather than several. Broadcasters have a significant opportunity to use this customer trust and preference for bundled services to increase their share of customer wallet.

The second advantage centers on a broadcaster’s greatest asset: its people. Human curation is vital. Digital natives are likely to have the edge in deriving insights from analytics, but they may lack the human input needed to make content and services emotionally resonate with audiences. For broadcasters, this human element is second nature, as it has been at the heart of decisions about content commissioning, scheduling and advertising inventory for many years.

In addition, consumers increasingly value real-life experiences (as demonstrated by the enduring appeal of live concerts and sports events in the age of digital and social media). Broadcasters can use their employees to create shared real-life moments for viewers, which help forge deeper relationships and trust with audiences.

Broadcasters wishing to exploit the human advantage must re integrate people into the interface, providing human interaction and curation at the points that really matter. To achieve this, they will need to strategically consider which services are appropriate to manage with machines and which with humans. They need to ensure that human interaction makes a fundamental difference at the points along the customer journey where they matter most: when things go wrong, when viewers need help deciding what to watch, and when customers are considering leaving.

This will require a shift in organizational culture and performance management. However, early adopters of human curation are seeing success. MUBI, a curated online cinema streaming service, has been fusing insights from analytics with those of their in-house film buffs to bring an element of human curation to their audiences. Every day they introduce a new film curated by their experts which can be watched by users over the subsequent 30 days.

To succeed, broadcast employees will need to become more open to using data in decision making and become accustomed to combining art with science. To achieve this, broadcasters need to value their people for that undefinable “human” element and measure them on the quality, and not the quantity, of their interactions with consumers.
Appendix

The Future of Broadcasting series is now in its fifth year. Since 2011 we have charted the rapid evolution of the broadcasting industry.

In the first edition of The Future of Broadcasting we saw the market’s clear preference for pay broadcasters’ subscription-based models over the advertiser-funded free to air (FTA) model. By the second issue, enterprise value across the sector had increased significantly with all broadcasters enjoying a recovery in value. By 2012/13 the distinction between FTA and pay business models had become even less relevant, with investors looking for all broadcasters to embrace more sophisticated strategies adapted to an era of constant change. Last year we saw the distinction between business models continuing to disappear and noted another large increase in enterprise value (up 43 percent from 2012), fueled by future value, signifying rising market optimism within broadcasting.

This year we observe that the gap between future value and current value is widening, with future value at an all-time high. We also assess the strategies that broadcasters are implementing to create value: investing in content production and licensing, and achieving scale through consolidation.
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Endnotes

1 In our analysis market optimism and market expectations are represented by changes in the total future value of the broadcasters in our peer set. See enterprise value call-out box for an explanation of our future value calculation.
2 Between August 4th and 23rd the value of the Dow Jones Media Index fell from $811 billion to $681 billion
3 Forecasts were based on analysis of data from SNL Kagan.
4 Before the correction in the media market, broadcasting future value had increased by 25% since last year (May 2014 to May 2015).
5 As measured by Compound Annual Growth (CAGR), which is used throughout this analysis to represent annual growth rates.
6 Over the past six months, the Pay TV industry has lost about 500,000 subscribers, according to analyst Craig Moffett. While small in comparison to the total number of subscribers (100 million), this loss still marks one of the worst periods in cable history. Until 2010 the industry had never experienced a quarter of net subscriber losses.
7 As represented by our broadcasting peer set.
8 We define content-led broadcasters as those who earn 20% or more of their revenue from content production and licensing
9 As reported in August 2015
10 Enders analysis report: From MCN to next generation media company Part 1: Funding
11 State of the Internet, 2015, Akamai.
12 In Accenture’s Annual Digital Consumer Survey, 2015, 79% of respondents stated they would prefer a bundled solution from the same provider.
13 Kodak actually invented the first digital camera in 1975, but it was Sony who first introduced an electronic camera to the consumer market in the form of the Sony Mavica in 1988. Kodak, on the other hand, focused its digital technology on high-end, niche markets because they could not imagine a world in which selling one digital camera to a few power users would be more profitable than selling analog cameras and rolls of film to the mass market.