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The Battle for Video

By Jesse Cryderman

When I grew up, video wasn't an entertainment category as much as it was a television, or if you were lucky, a movie screen. Families didn't watch "videos," they watched television shows or movies, and there was no pause button on the remote control. The commercialization of home video arguably ushered the word "video" into the popular lexicon, and sparked a shift to a consumption model that, for the first time, was not appointment based. In response to demand, soon after came DVRs and VOD, then OTT services and IPTV, and now robust mobile video offerings.

As someone old enough to recall these trends and the pre-internet "dark ages," I'm what some would call a digital immigrant. The future, however, belongs to digital natives: those born into an on-demand world with global access and a pause button.

If technology trends have taught us anything, they've shown us how much we value video. As Ira Gorelick, Verizon, recently remarked at 4GWorld, "We are a graphical society; people want graphics, they want video, and that's what drives the need for more bandwidth and much lower latency."

In fact, I would argue that most advances in computing over the past 15 years have been spurred on by a demand for a better video experience. High speed DDR memory and multi-threaded chip topology began life in video cards. Hard drives would probably still be labeled in megabytes, if it weren't for video

and high-resolution image file sizes. The "need for speed" is really an outgrowth of a desire for a high-quality video experience.

Research from numerous outlets confirms the mammoth demand for video, and tells us demand is increasing. Given these facts, how are telcos, MSOs, and OTT players faring in the battle for the video customer of today, and more importantly tomorrow?

The Landscape

Video offerings from telcos Verizon (NYSE: VZ) and AT&T (NYSE: T) have made significant inroads into the video market, and despite signs of slowing growth in the third quarter of 2011, the concomitant decline in subscribers on the historical "cable guys'" financial reports paints a picture of a changing video landscape in the U.S. The most recent data on subscriber change from the major players (fig. 1) indicates the customer exodus from cable in favor of other video offerings is continuing unabated.

Second Quarter 2011 Video Landscape

Operator	Subscriber Growth	Subscriber Total
Netflix	1,800,000	24.6 million
Comcast	-238,000	22.5 million
DirecTV	26,000	19.4 million
Time Warner	-130,000	12.6 million
Dish Network	135,000	14 million
Verizon FiOS	184,000	3.8 million
AT&T U-Verse	202,000	3.4 million
Cablevision	-23,000	3.3 million

Verizon and AT&T have also released numbers for Q3. Verizon saw an increase of 131,00 new pay TV subscribers in the third quarter, up to 4.0 million FiOS TV subs, and A&T reported its pay-TV subscriber base grew by 176,000 to 3.6 million. Both telcos saw their pay-TV growth slow a bit since Q2 2011, but storm

outages and subsequent delays in installation were partially to blame, say AT&T and Verizon. For example, Fran Shammo, CFO, Verizon, told the press that East Coast storms cost the company nearly $250 million, and significantly slowed FiOS installations, which would impact subscriber additions. Nevertheless, both telco-TV and satellite TV have eaten away at the cableco subscriber base. And cheap offerings from OTT players like Netflix have obviously attracted subscribers in droves.

So it's clear we're living in a new video age, but what is driving this transformation, and how can carriers and their vendors stay competitive in this changing game? After talking with several Tier 1 carriers and top vendors, four main factors emerge that play a role in influencing the success of a video offering: quality, delivery, price, and content.

Quality

Consumers, especially digital natives, expect a high level of service quality that extends across multiple devices. Ira Gorelick, Verizon, commented at 4G World 2011 that these future end users want mobile video, for instance, "to look like their desktop experience." As a result, ensuring a high-quality video experience is a crucial part of the puzzle for everyone involved with video, but some service providers are better equipped than others to deliver and monitor quality. Whereas an OTT like Netflix must adapt the bit rate resolution of a video stream in response to dips in bandwidth, carriers (provided they have the tools in place to differentiate packet data by service type) are uniquely positioned to actively distribute capacity in response to video stream degradation.

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Presumably, this is why FiOS and U-Verse have made such strong strides. In part, by effectively leveraging network intelligence, telco video offerings from both Verizon and AT&T ranked ahead of cablecos in the J.D. Power and Associates 2011 U.S. Residential Television Service Satisfaction Study. In fact, AT&T U-Verse has ranked the highest for overall satisfaction in the Western and Southern regions of the US for four consecutive years.

In terms of multi-screen quality, every player we're covering in this article knows how to transcode video for multiple screen sizes, select the nearest video server, and monitor network quality on a general level, but thats doesn't tell the whole story. A provider can get all of these things right, and yet the Quality-of-Experience (QoE) can still suffer. Ultimately, to fine tune the quality metric, providers must have real-time visibility along the entire signal pathway, from the content delivery network right to the screen. It's

not enough to know packet loss and jitter data. To compete on quality, and reduce churn, a provider must optimize the video experience for the end user, across multiple devices.

Delivery

Video delivery has grown far past the television, and now, new data from Sandvine says it's grown past the PC as well (Sandvine Report). For digital natives, video is anywhere and everywhere, and providers must have a strategy in place to deliver the multi-screen experience, or risk becoming a VHS-like video relic.

Jim Benz, VP Business Development, Content Direct, CSG International, sees multi-screen video delivery platforms as crucial to competitiveness. "It's pretty clear now in the pay TV and online video markets that TV Everywhere offerings are table stakes," says Benz. "If you aren't allowing customers to extend their subscriptions out of the set-top and onto mobile devices and connected TVs, it's going to be tough to compete."

In terms of delivery innovation, Netflix (NASDAQ: NFLX) is far ahead of the pack. The company not only delivers video to PCs, connected TVs, and Android and iOS devices, but also extends the Netflix viewing experience to game consoles, Windows 7 devices, Facebook, and various set-top boxes. The sheer number of outlets through which a customer can access and view content is impressive, and has clearly played a major role in building Netflix's huge subscriber base.

Time Warner (NYSE: TWC) and Comcast (NASDAQ: CMCSK) are probably the best positioned among MSOs for multi-screen delivery. Both have second-generation iPad Apps, and Comcast also has a neutered Android App (it's unable to stream programming). Comcast XfinityTV also allows subscribers to watch and download content through an internet portal on desktop or laptop. From the telco camp, Verizon is the leader, with FiOS FlexView, which not only enables subscribers to watch Verizon content on televisions, tablets, mobile devices, and computers, but also allows customers to upload their own content. So your embarrassing birthday video can exist alongside commercial offerings in your On-Demand content library.

Part of the value of OTT services is their device ubiquity. To stay competitive in the video market, carriers have to move quickly to deliver new services to new devices, while being careful not to roll out a service that is only half-baked. As Ira Gorelick from

One area of content that carriers could focus on that could generate new revenue is exclusive live programming.

Verizon pointed out, "The worst thing is to bring out a service and not have it work." This is probably why neither Comcast nor Time Warner offer live or on-demand video content on an Android tablet; with such a wide-degree of hardware variations, these carriers who compete on quality can't (at this point) guarantee a high-quality experience on Android tablets.

Since game consoles are now the most commonly used portal for viewing OTT content, carriers would be wise to explore similar partnerships with Sony, Microsoft, and Nintendo, and leverage their deeper content libraries head-to-head with their OTT competitors. Think about it: a customer could login to their Netflix account to watch last year's season of Dexter, or login to Comcast's Playstation3 App to watch the latest Dexter episode the day after it aired.

Price

As you can see in fig. 2, finding the magic price point

Operator	Representative Monthly Cost
Netflix	$4.99 (DVD only) to $29.98
U-Verse	Video (single play) $29
FiOS	2-play from $69.99, 3-play from $89.99
DISH	$19.99 to $49.99, upcharge for premium and BB Moviepass
DirecTV	$29.99 to $83.99
Cablevision	iO TV $29.95 to $103.95
Time Warner	Digital TV + HD $49.99
Comcast	Xfinity TV for $29.99 to $99 for triple play
Cox	$57.99 to $64.99 for TV only

for video content is an evolving science, especially in a world with free, ad-supported options. (As someone remarked at the Real Time Communications Conference last month, YouTube is wildly popular because it has figured out the right price point.)

Video providers compete aggressively on price, and sometimes, in their race to add new subs with attractive introductory pricing, they anger long-time customers. Regardless, most peg the barrier to entry at $29.99 for monthly paid-TV service. Removing OTT from the equation, at the ends of the cost spectrum are most expensive FiOS and least expensive DISH.

For OTT players, price is the main influencer. With a sub-$10 sticker, the barrier to entry for most OTT services is very low, and the since subscription doesn't require a long-term contract or hardware installation, adding new subs is a relatively easy sale. But mess with the subscription price and you face customer exodus. Netflix lost 800,000 subscribers in the third quarter after announcing a change to its pricing structure.

Content

While most video carriers offer a full line of basic and premium channels, differentiation occurs across local programming, channels with VOD content, first-run movies, number of HD channels, and streaming content library size.

There are roughly four areas providers compete on with regard to content: breadth of catalog (how many total channels); depth of catalog (how many On-Demand offerings); exclusive live content (sports, concerts); and niche programming.

Licensing deals with major studios to provide exclusive or first-run distribution of video content have also proven to be successful strategies, but this is an expensive tactic and it doesn't always pay off. Time Warner announced last month that it struck a deal to release Trespass on the same day it launched in theaters. Did you know Trespass stars Nicholas Cage and Nicole Kidman? Probably not, because the movie was a bomb, earning nearly unanimous ridicule on website, Rotten Tomatoes.

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One area of content that carriers could focus on and then generate new revenue is exclusive live programming. In the realm of music, some bands are already packaging and selling live concert streams, for $10 to $20 per concert, and currently carriers aren't capitalizing on this market. Another content strategy might be to extend greater personalization to customers, with matching pricing, instead of current "buffet" models that focus on the number of channels available (as if anyone could every stay abreast of 500+ channels of content).

Competitive Strategies

The cheapest paid video service we're looking at in this article—Netflix—has the lowest ARPU and a significant churn rate. In the third quarter of 2011, Netflix ARPU slid to $11.56, and churn climbed to 6.3%. By comparison, Time Warner also passed on price increases to its customer base, and yet boosted ARPU to over $90.

Certainly MSOs should offer multi-screen, on-demand viewing options, but how much money should they spend actively courting customers who are fickle and

contribute little to the bottom line? Or is a focus on attracting and retaining high-ARPU, loyal customers a better long-term, strategy? This is an important question that each carrier needs to consider.

On the other hand, Jim Benz of CSG International says it doesn't have to be an either/or situation—it can be both:

> In the digital content world, you can go direct to consumers anywhere – not just within your own network footprint. You can deliver services globally; effectively be an over-the-top player yourself. That game is less about ARPU, and more about profitability. Even if you have a low margin, high volume digital content business, you can drive a lot of profit through that line of business to an addressable market of billions of people worldwide. In that case, everyone is fair game. You can use the same infrastructure to deliver and monetize lower quality, lower priced content that is targeted to "lower ARPU" customers as well as high-quality, premium content to "high ARPU" customers. In that case, it's really more about the direct to consumer model and being able to deliver content globally to any kind of device and do so profitably at a range of price points.

Some service providers are innovating in other ways in order to monetize their assets. While most MSOs have squared off against OTT, Cox Communications moved the opposite direction, and licensed its VOD content catalog to TiVO's Premier set-top box. This means Cox content will sit alongside offerings from Amazon, Netflix, and YouTube.

Verizon has taken the battle for video a step further by launching Verizon Digital Media Services. The carrier has developed an end-to-end "digital media utility," which is based on the premise that streaming video needs to be transcoded and packaged for delivery. If, say, the Chicago Bears wanted to deliver their own content on demand through a variety of channels, Verizon Digital Media Services could enable and deliver this service. Depending on the customer, this strategy can put Verizon in a position to profit from an OTT offering, even if it's not delivered on the Verizon network. Pretty slick!

Even without Verizon's horsepower, carriers can leverage solutions like CSG International's Content Direct to further monetize their content. Content Direct enables content owners to rapidly launch, scale, promote, and evolve their video assets through multiple channels. It's an innovative solution that enables direct-to-consumer video offerings—something OTT has excelled at. Content Direct also incorporates social media, intelligent advertising, and can deliver video to multiple screens and devices. Similar offerings are available from Cisco (Content Delivery System) and SmithMicro (Vidio).

As a percentage of revenue, video is still king for the cablecos, but it's slipping each quarter, and even though cable has balanced these losses with broadband services, they also must evolve to remain competitive, and that means more screens and innovative partnerships.

Video providers of all types must provide a high-quality video experience across many devices; this is what the digital natives expect in a world of TV everywhere. In terms of price, providers don't need to neglect the low-ARPU customers who flock to OTT, but instead should find ways to leverage their content catalogs with direct-to-customer offerings. Carriers could benefit from offering more personalized content models and integrating with game consoles as well. At the end of the day, multi-screen delivered content, priced correctly and delivered with appropriate quality for the targeted customer base—and there are several—is the difference between a successful video offering and a pixelated failure.