Sea Change for TV Broadcasters

By Douglas Ferguson, Ph.D.

Overview

With all the usual admonitions about forecasting, the near-term outlook for terrestrial broadcasting looks more challenging but still quite profitable in the United States. Changes are coming, momentous changes, but not for at least five years, closer to ten years.

One major premise of this paper is that interactive television in 2000 is where cable and home video stood in 1980. This is the calm before the storm. American broadcasters need to plan, not panic.

Most organizations use an introspective analysis for their planning cycles. This so-called SWOT analysis looks at strengths and weaknesses in the present and from within, along with threats and opportunities in the future and from without. The following is a brief overview of broadcast television's position.

Over-the-air television's foremost strength is its 99 percent U.S. household penetration, which makes it an unequaled avenue for commercial advertising. No other persuasive medium combines sight, sound, motion, and universal access. Advertising-supported cable networks presently reach 80 percent of American homes, but that number is not expected to grow much. Beyond the relative small amount contributed by DTH satellite, conventional cable television accounts for 68 percent penetration, a number that has not seen much increase in the last dozen years despite a homes-passed rate of 96 percent.

Public perception of broadcast television’s near-monopoly on local news content will keep it profitable at least through 2011. Broadcasters take great solace in the fact that the major television networks in the United States derive most of their profitability by operating local stations in heavily populated areas. Television broadcasting is still a steady revenue producer, and not likely to see any fluctuations before 2006.

The primary weakness of broadcast television is that it has too much competition: competition from technology and competition for leisure time. These areas are outlined later in this paper.

Broadcasters are not without great opportunity. The convergence of computers with TV portends a goldmine for ancillary services available on unused digital bandwidth. Companies like DigitalConvergence.com, Broadcast Digital Cooperative, iBlast, and Geocast offer new datacasting opportunities that capitalize on television's ubiquitous signals. My own view is that it will be hard for television owners to adjust to selling information, after years of giving it away in exchange for the audience's attention (and likely exposure to commercial messages). But what they lack in expertise can be hired or bought from the retail and direct-marketing world. The phone conglomerates have been able to learn the cable TV business by purchasing huge chunks of it. Group-owned stations need to form partnerships or strategic alliances with data providers.

The number-one threat to terrestrial broadcasters comes from technology that frees the viewer from program schedules: personal video recorders (PVRs) and video-on-demand. Although the real impact of these technologies are just arriving and not likely to pose immediate harm to broadcast revenues, the timetable will be swift—certainly starting no later than 2006. The loss of program schedules spells the loss of commercial breaks as we know them, because PVRs allow the viewer to "skip 30" seconds. Spot advertising will need to be more compelling than ever. It is doubtful that "product placement" within programming will take up much of the slack. The present system is based on real-time viewing constraints that simply won't exist in a world with PVRs, even if limited to affluent homes.

Another threat down the road and far less immediate is posed by the unusual media consumption patterns of Generation Y. This age cohort, though still quite young, has a disturbing lack of respect for content copyright and a voracious appetite for all things related to instant, online and wireless communication. Broadcast television will need to refocus some of its programming (and bandwidth) toward a highly-mobile audience.

Competition

Competition from technology poses a continuing threat to broadcast television: cable/PPV, DTH satellite, VCR/DVD, streaming video internet, VOD/NVOD/PVR commercial-free content. I foresee the widespread arrival of digital set-top boxes by 2002, especially those that incorporate the PVR, which will motivate people to *interact* with their television set. The audience will lean a little more forward in their seats—perhaps not to the extent of personal computing, but certainly less passive than the "lean back" couch potato of the past.

The other form of competition is for leisure time. Broadcasters have become accustomed to fighting each other for audience share. Now they must serious compete for their share of electronic leisure time. The next generation of video games will siphon more young adult and child viewing. I believe the "killer app" of the video game business will be a virtual world for adults, made realistic by online connections that get viewers to become cyber-contestants on programming in the *Survivor* mold.

Furthermore, I think gaming (online gambling) presents an opportunity for broadcasters. In its most benign form, local merchants will promote their goods and services through pseudo-lotteries that let viewers trade their attention for a chance to win (which is not a violation of FCC regulations). For example, contests could be based on product information available from commercials embedded in local broadcasts.

Timetable

The brave new digital world will be delayed by natural forces, like the product adoption curves for other innovations. Certainly demand for digital receivers will evolve by attrition, just as color TV took decades to catch on. The influence of policy regulations to roll out HDTV is already showing strains; it's difficult to legislate innovation. Still, I project that DTV will reach 50 percent penetration by 2011 at the earliest, driven largely by legislative fiat instead of consumer preference.

Standalone technologies like the PVR (Tivo, Replay, Showstopper) and system-driven innovations like digital set-top boxes are more likely to appear faster in American homes. PVRs will reach 20 percent penetration by 2002, before set-top boxes start integrating the storage capabilities, not unlike the adoption of VCR+ functions by VCR manufacturers.

Human Factors

With the exception of Generation Y and still-newer generations, the audience for interactive and on-demand television will be restrained by old habits. The traditional viewer wants it simple and cheap, meaning that complexity and expense works against adoption. Consumers will demand simple remote controls (not keyboards) and minimal cabling.

Given our experience with VCRs, the American audience will not want to read any instructions, learn any sequences or steps, or wait for their TV's operating system to boot-up. Manufacturers had better use firmware and downloadable updates, because my own research shows that television viewers still want to relax. The diffusion of computers in the last few years has been driven by simple browser software that substitutes a mouse for a keyboard. PVRs will succeed because they mimic the functions of VCRs and are easily installed.

The computer user who makes the transition to converged media will resist paying for services. Internet users want everything free, even if they have to trade away some of their privacy, receive junk e-mail, or stare at banners for the privilege. This situation will remain unchanged in the future. Furthermore, I foresee that the electronic media will emulate the way the grocery business uses scanning-cards, by starting to offer savings to consumers who apparently don’t mind trading their privacy for bargains.

Business Models

The question on everyone’s lips is what will the broadcast business model be in the longer-term future? How will advertisers reach customers who can avoid their commercials? The aforementioned contest model is a distinct possibility, as is the buyer-information-for-free-content model. I think the advertising-based model is safe for a while, certainly through 2011, but group-owned broadcast companies will need to find new revenue streams. For sure, they cannot count on interactive program guides (IPGs) because these will be controlled by the multichannel distributors, luring away some broadcast dollars.

My ideas? Create value from local personalities who "star" in media content. In many ways, this is a return to the 1950s when local media personalities (not journalists) were able to create excitement for local merchants through live remote broadcasts (the ultimate in product placement) and commercial endorsements. Regardless of technology, audiences want media to be a trusted friend. As the cocooning of America further disconnects people from interpersonal contact, these parasocial relationships will become crucial. One need look no further than the very recent success of real-people reality shows on CBS or real-people games shows on ABC in primetime. The old model of "programming vehicle plus limited choice plus spot avails" is dying. Not so soon that evolutionary adjustments can't be made, but not so slow that advertisers can continue to whistle in the dark.

The future of local news? I think it's flat, or downtrending. Pew Research reports that the mass audience is less and less interested in newscasts (and newspapers) because the news itself is more and more common (that is, continuously available from an infinite number of sources). National and international news has become merely a commodity. Local news may be unique, but it's no longer "special" because viewers are weary of regularly-scheduled news programs. They want the news, but they want it when it’s convenient for them, and they don’t want filler. With the PVR and on-demand internet streaming video, they can skip the stories they don’t want and make the content fit their lives. Personality-driven news, however, will survive and grow, while content-driven news will wither and die.

Existing Forecasts

Before I gaze anymore into my own crystal ball, let’s look at the conventional wisdom. For example, Forrester says:

> The use of personal video recorders (PVRs) will kill $18 billion in television advertising revenues by 2005, as consumers will use the disk-based devices to quickly skip commercials and thus erode the traditional spot-buying market. But by the same time, the television industry will enjoy $25 billion in new revenues generated by interactive services.

I agree, but not on the timetable. I think it will be 2007 before any appreciable revenues, with a similar offset of advertising losses. Forrester’s bullish predictions about PVRs coincide with my own.

On the negative side, there’s Charles Wilkinson, who wrote for Futurefile.com:

> People who watch Jerry Springer are unlikely to navigate the world of ISDN, ISPs, Internet protocols, and high bandwidth.

This audience, which has tremendous purchasing power, won’t go away without a fight. But, as much as some broadcasters will want to cling to predictions that the audience won’t change, I predict that the new technologies will bend over backwards to accommodate *Jerry Springer* fans, so that they won't need to know about bandwidth or protocols—they'll just swim in the digital stream without having to learn anything. All of this is predicated on good design of remote controls and smart set-top boxes, for which I am very optimistic.

Rick Ducey at NAB wrote last year:

> …broadcasters [should] redefine their basic business model in a couple of ways. First, broadcasters are in the spectrum bandwidth business. One use of this resource is traditional television. There are highly, highly valued spectrum bandwidth markets that are growing far faster than the traditional television market and indeed exceed its total value. Second, broadcasters can redefine their "retail distribution" network from dedicated, single-purpose devices known as television receivers to anything capable to detecting, receiving, decoding and processing encoded signals distributed via their spectrum emissions.
>
> The best long-term bet for broadcasters looking to not only hold their own but dramatically expand their market is to start thinking of client devices as the targets of their broadcasts and not just television receivers.

Amen. Group TV owners need to focus on their real asset: bandwidth. If they can deliver the brave new world, with or without advertising, over their excess digital capacity (or over the vertical blanking interval), these traditional broadcasters will stay competitive with the new challengers.

The Future Foretold

I predict more mergers. AOL, Microsoft and Microcast will likely dominate the online world. Streaming startups that survive the shakeout will be bought up by the existing distributors, both wired and wireless.

The public *will* learn to choose shows from on-screen menus (versus the old buffet-line system). Broadcasters will need to forge alliances with the IPG owners.

The public *will not* abandon its brand loyalties. The audience's ability to remember more than a dozen channels (channel repertoire) will remain constant. Also, it's hard to imagine more than 7 or 8 big content producers (from the old Hollywood Seven), with each angling to own a content packager (network). The companies with brand identities will get sampled first.

Content is king, and will continue to follow the whims of the public. But the audience will really appreciate the power of *choice*, much in the way online users with DSL or cable modems appreciate the power of continuous connection. And viewers will enthusiastically embrace *control*, as they clamor for buttons to pause live TV or instant-replay whatever video they want. If broadcasters can expand their view beyond the advertising-supported world, and beyond the "average viewer" world, they should do fine in the coming years.

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Douglas Ferguson, Ph.D.
College of Charleston
843-953-7854