Build Subscription Revenue

OTT DIGITAL CONTENT MONETIZATION

The term "over the top," or OTT, has had a workout in the media lately thanks to a rash of high-profile announcements by media giants, pay-TV companies and start-ups alike. And it's no wonder that these standalone, online streaming subscription services have become a trend; changing television consumption habits on the part of consumers have demanded it. But delivering what the eyeballs want is only one part of the picture, as it were; monetizing OTT is a persistent back-end challenge for OTT providers of all sizes, and business models continue to be in flux.

OTT IS HAVING A MOMENT

It's been a good autumn for OTT, with an ongoing groundswell of digital launches from large-scale, traditional media stakeholders. CBS made news with the All Access subscription service that will go for $5.99 per month and offer a raft of live and on-demand content from the network. It will also launch a Showtime standalone OTT service in 2015—which echoes big news from HBO that the premium cable leader is going online with a streaming service of its own in 2015.

AMC Networks meanwhile has said that it is exploring OTT as an outlet for niche content, particularly documentaries. And ESPN has said that it is mulling a strategy for offering online access to live Major League Soccer games as a way to add revenue without alienating its existing model of working solely with pay-TV operators for distribution.

Traditional pay-TV distributors are jumping in too; Verizon Communications has said that it may leverage its purchase earlier this year of Intel's OnCue digital video assets, combining the telco's FiOS IPTV and broadband offering with its mobile assets. The resulting mobile OTT service could launch in the middle of 2015, and the telco is already in the latter stages of negotiations with the major content providers ahead of the launch (Disney, NBCUniversal, Viacom, FOX, Time Warner and so on).

Pure-play OTT providers like Netflix and Amazon Prime, who have quickly taken on incumbency in the market, continue to add subscribers as well, which ups the ante for the more traditional johnny-come-latelies. In fact, Netflix now has 36 million subscribers in the United States, compared to premium channel HBO's 31 million, according to Bloomberg.

"This is changing so fast that many companies are jumping in, really just to get in, even if they don't have a strategy yet," said Fernando Elizalde, an analyst in the consumer services and applications and consumer technology and markets divisions at research firm Gartner.

And that lack of strategy is where the OTT discussion turns a bit darker.

Netflix kicked off the idea of content streaming via the Web back in 2008 with a partnership with Starz to offer an innovative service: on-demand streaming video. And in the next two years it grew the proposition, managing to kill off the movie-rental business as we knew it—RIP, Blockbuster. End users took to the service by the millions, and that also drastically changed the traffic patterns for broadband consumption; In fact, one could argue that Netflix single-handedly has driven the massive upgrades in residential broadband services across the U.S. by cablecos and telcos alike.

With better broadband comes better viewing experiences for video, and more uptake. And so, far from a perfect storm of opportunity, what Netflix started six years ago has become a crowded ocean of streaming video competition. The most recent tsunami of planned launches will mean an even bigger surfeit of consumer choice for programming how and when they want it—but the reality is that business models have yet to shake out. Put simply, the Netflix model of offering third-party content on demand across the Web is no longer enough to support a viable OTT business.

OTT'S COMPETITIVE CHALLENGES LOOM

There's a reason so many big names are jumping into the OTT space, business-model maturity aside. In 2014, the industry is projected to generate nearly $8.5 billion in the United States, according to PricewaterhouseCoopers. That is an increase of 102 percent from 2009. PwC is also projecting that the OTT business in the U.S. will grow another 101 percent between now and 2018, to total just over $17 billion in revenue.

So, there is clearly opportunity in the market, but the stick is equal to the carrot in this case when we delve deeper into the competitive realities of the market.

"This is changing so fast that many companies are jumping in, really just to get in, even if they don't have a strategy yet."

Fernando Elizalde, analyst in the consumer services and applications and consumer technology and markets divisions at research firm Gartner

For one, convincing consumers to opt for OTT exclusively—to cut the cord, as they say—is easier said than done, for now. Despite charging an average of $100 or more per month for basic entertainment, cable and other pay-TV segments have an advantage when it comes to consumer loyalty: access to premium channels like HBO, and exclusive access to things like major league sports. Especially in the latter case, the programming rights are so expensive that no OTT provider could hope to monetize them on the back of a $7.99 per month subscription—leaving it squarely in the purview of traditional TV.

It's no shock that CBS' new service does not include live sports content.

Also, traditional pay-TV provides other benefits, namely convenience. The set-top box (STB) acts as "input one"—and is an aggregation point for disparate content sources. Watching OTT, on the other hand, requires disconnecting the STB and plugging in some other box in order to get content on the big-screen TV, often at the mercy of whatever broadband connection is in place in the home. And, considering that no one OTT service has all of the content that a single pay-TV subscription does, it's likely that the consumer would be toggling between apps and paying for multiple OTT subscriptions to simply approximate what cable gives them all in one place, within one programming guide.

This is being played out in macro-trends: According to the latest informitv Multiscreen Index, the total number of subscribers across the top 10 pay-TV services was up by over 400,000 year-on-year as of

VINDICIA OTT MONETIZATION SOLUTIONS

To succeed in the rapidly evolving OTT marketplace, providers need to offer more than compelling content and reasonable value. To truly thrive, OTT providers must combine compelling content and value with enticing promotions, a broad reach, proactive retention processes, scalability, and continuous improvement.

However, many OTT providers find that traditional billing platforms can't support those objectives in a subscription setting. For example, adding a simple refer-a-friend promo to a traditional system can take weeks. Billing glitches lead to involuntary churn and reduced revenue streams. And OTT providers with international rights should be able to sell globally easily—but their billing systems may hold them back.

That's why many successful OTT players are monetizing their digital assets using proven subscription billing solutions from Vindicia that allow them to:

- Create agile, subscription-based and VOD business models that respond to customer demand.
- Maximize recurring revenue through pricing, packaging, bundling, campaigns and promotions.
- Retain customers longer by implementing frictionless payment strategies that reduce subscriber churn.
- Leverage subscriber analytics to gain knowledge about their customers and understand key trends, thereby enabling faster and improved decision-making.

Vindicia offers two solutions: Vindicia CashBox, a complete subscriber acquisition, billing and retention platform; and Vindicia Select, a customer retention solution that works with any existing billing system to resolve failed payment transactions. Both solutions were created from the premise that

August 2014, and by more than 1.5 million over two years.

Overall, OTT has been largely complementary to existing cable, satellite and IPTV subscriptions so far—and that means that a household is not likely to subscribe to more than one ancillary service. A subscriber has either Hulu Plus OR Netflix, Amazon Prime OR VUDU. So slicing up that $17 billion revenue pie may end up being an exercise in extreme fragmentation, as more choices enter the market.

But what about the 10 million broadband-only homes in the U.S.? That's a figure that's growing: Some 75 percent of U.S. homes have a broadband service, and of those broadband homes, 14.1 percent did not use a traditional pay-TV service in third quarter 2014. That's up from 8.6 percent three years earlier, according to research firm The Diffusion Group.

In a similar vein, it's clear that OTT will become more crucial as millennials continue to move into the video market. Consumers under 30 are much less likely to value a cable subscription than their older counterparts, so while the pay-TV picture remains good for now, traditional operators will not be able to hang onto success in the long term. According to nScreenMedia, 19 percent of millennials are living without pay-TV; out of those, 98 percent say they have no intention of getting it.

So this looks like a greenfield opportunity on the surface, but again, it's an open question as to how many under-$10 subscriptions these consumers are willing to pay for before the approach becomes a drag on their wallets (and patience). They may ultimately opt for a basic cable service or may go with just one or two OTT options.

And finally, it must be noted that companies jumping into OTT need to walk a very fine line between cannibalizing their bread-and-butter revenue sources and capturing additional opportunities. Media companies are concerned about alienating or undercutting existing distribution partners (i.e., pay-TV operators), while those same operators must be careful to protect their own subscription and advertising revenues.

strategic monetization is critical not just as an operational necessity for successful OTT service models, but also as a marketing resource that strengthens customer acquisition and retention.

VINDICIA CASHBOX

Vindicia CashBox is a comprehensive, SaaS-based subscription billing and recurring payment platform specifically designed for dynamic subscription business models favored by OTT service providers. The solution features integrated marketing and best practices that boost customer acquisition and optimize customer retention. CashBox lets OTT service providers quickly change pricing, introduce new bundles, support SVOD and one-time sales, launch flexible trial entry programs, and reach new audiences through coupons or promotion codes.

With CashBox, content owners, cable/satellite operators, and broadcasters/networks looking to capitalize on the growing popularity of OTT services can take full control of their new business models with detailed analytics and best practices to grow and sustain new revenue streams.

VINDICIA SELECT

For OTT providers who already have a billing system in place, Vindicia Select is an add-on solution that increases OTT subscriber retention to drive higher revenue and customer lifetime value. Incorporating Vindicia's patent-pending Advanced Retention Technology (ART™), Vindicia Select heals failed payment transactions, thereby dramatically reducing involuntary churn. The solution allows OTT providers to:

- Reduce involuntary churn by about 30% or more
- Boost revenue by as much as 5%
- Increase customer lifetime value through improved retention
- Improve customer service by keeping customers connected to OTT services

AMC's OTT concept is a long-tail play, for instance. Its top-flight network content, like Mad Men and the Walking Dead, will stay right where it is, on the cable channel's linear, on-demand and TV Everywhere outlets.

Conversely, start-ups/Web companies who jump in full-force to the online-only proposition effectively limit their wider options with bigger distributors. Apple, for instance, has been pursuing a relationship with pay-TV for years to become the middleware on STBs—a concept that cable and media alike has categorically refused to entertain because of the potential competitive ramifications in allowing Apple to control the user experience inside the home.

CONTENT: THE FINAL BATTLE

The answer to solving these competitive woes lies in one key element: content. The better the content, the more loyalty one wins. And this is where savvy monetization becomes a linchpin for any provider of OTT services.

"The biggest problem with subscriptions is you have to have enough content for people to want to pay a monthly fee," says Frost & Sullivan's Rayburn. "If a distributor comes out and says they are going to charge $9 a month, they are not going to get much interest if they have only 500 titles."

OTT leaders have been investing heavily in original content in order to compete not only with each other, but also with premium cable offerings. Netflix has famously called the HBO linear TV channel its "biggest competitor."

The problem of course is that content is not cheap, and many are feeling the effects of margin compression. It is unlikely that a subscription price much above the $10-$15 range will be considered a value when it comes to OTT, so there's a de facto pricing cap at work to begin with.

Consider Netflix, which has had great success with its original programming, like House of Cards and Orange is the New Black—both high-profile Emmy-bait and Twitter staples. Its content costs have risen from $3.9 billion in 2011 to $7.3 billion last year. Amortization expenses on Netflix's streaming library are following suit and grew $699 million to $2.1 billion over the same period.

So, in a nutshell: over the past two years, the company's revenues have grown by 17% compounded annually, while its costs have grown by 23% compounded annually, as of April. That prompted a $2 rate increase for new customers over the summer—which translated to lower than expected subscription additions for Q3, sending Wall Street into a frenzy, dumping stock.

> "The biggest problem with subscriptions is you have to have enough content for people to want to pay a monthly fee,"
>
> Dan Rayburn, principal analyst at consulting firm Frost & Sullivan and executive vice president of StreamingMedia.com.

"While 2013 was a positive year for Netflix in some respects… more evidence mounts that the Netflix business model is fundamentally broken," said David Trainer, a stock analyst at New Constructs.

Amazon Prime is working originals hard as well: it has launched the second season of its John Goodman political comedy Alpha House, along with new drama Transparent, which is generating Emmy-nomination buzz for star Jeffrey Tambor. Amazon also has an in-season VOD window deal for summer CBS hits Under the Dome and Extant. Another big coup for the service is the fact that all seasons of Downton Abbey are covered in an Amazon Prime exclusive starting in June — a deal that took the popular PBS series away from Netflix.

In all, Prime Instant Video offers more than 38,000 movies and TV episodes for Amazon Prime members to stream commercial free. Last year it paid upwards of $1 billion in content acquisition costs to be able to do that.

"The cost for that content is extremely high. We're talking billions of dollars. So that must be having an impact," analyst Colin Dixon of nScreenMedia said.

And, these figures don't even take into account the cost of subscriber acquisition and retention.

"Some [OTT companies] are making it, but the rest are still trying to figure out how to monetize this business," said Dan Rayburn, principal analyst at consulting firm Frost & Sullivan and executive vice president of StreamingMedia.com.

MONETIZATION APPROACHES: THE CUSTOMER IS KING

In a 2013 survey, StreamingMedia found that 54 percent of media executives said that the most successful revenue model for OTT is subscription, compared to 40 percent who believe advertising is the best approach.

Accordingly, OTT offerings have focused on subscriptions so far, but some are testing the waters with hybrid approaches that include advertising.

Hulu is owned in part by 21st Century Fox, ABC parent company Disney and NBC parent Comcast – and gets a break on the content costs accordingly. It's ad supported, with the subscription-based Hulu Plus acting as an additional revenue arm. CBS All Access is also using the subscriber-ad hybrid, charging $5.99 per month while serving ads at the same time.

But advertising, like subscriptions, has a top-end limit in its unvarnished form. "When the average CPM [cost to reach 1,000 consumers] is $25, which has not changed in years, it's hard to monetize that," said Rayburn. It would take many, many thousands of consumer eyeballs to cover costs in an ad-supported environment.

Targeted, programmatic advertising can bump up CPM rates, offering fresh promise, but it's an approach that's in its infancy. For now, "Why does someone get ads for insurance that's for people over 65 years old when they're half that age? Why would advertisers pay more for ads that are not targeted?" Rayburn said.

Given that subscriptions are and will continue to be the basic building block of the content-rich OTT model, perhaps the best monetization strategy is deceptively simple: customer retention and communication.

Third-party billing and management platforms are similarly supporting OTT clients to achieve a shared goal: Maximizing the average customer lifetime value (ACLV). This is the amount of revenue generated by a subscriber over the duration of their subscription—at some point, the amount that a subscriber pays in becomes more than the cost to acquire her; helping out the bottom line of the service.

Put another way, the longer a customer is paying for a service, the more of that subscription can be considered profit. It's a bit like a mortgage—the first years of payments go directly to the interest on the note. But later, the payments start to pay off the principal, and that's when equity begins to accrue.

Highly integrated billing platform partners bring to OTT partnerships a range of tools for making sure that subscribers stick around. Some are as simple as basic customer service—flawless refunds processes, for instance, or automated troubleshooting for managing payment failures. Offering options like alternate payment options can be the key to dramatically reducing subscription cancellations and churn.

There's also a revenue-generation piece to this: an OTT provider's best customer communication conduit is the billing process, because it's a monthly touchpoint. While the ideal scenario is to have billing occur seamlessly in the background, the relationship in and of itself allows OTT providers to offer carefully crafted, even personalized marketing or re-marketing messages that are triggered by specific billing events or customer actions, for instance.

Further, The OTT provider's customer roster offers the ability to create a highly targeted user base—with the right demographics capture and opt-in mechanisms at sign up, or in subsequent customer communications, it's possible to bring a better advertising proposition to brands; or to push ancillary services.

Also, bringing in additional ways to connect can add a wrapper of loyalty around a subscription.

"Smart customer experience teams will increasingly use customer data from diverse sources like social listening platforms, campaign management platforms, mobile apps and loyalty programs – to personalize and tailor experiences in real time so that they inherently adapt to the needs, wants and behaviors of individual customers," said Forrester analyst Michael Gazala.

Bottom line? Despite its challenges, OTT is going to happen

He added that as companies strive to break from the pack and gain a competitive edge, especially in what he calls "laggard" industries like video service, "see the battleground shift to new areas like emotional experiences and extended customer experience ecosystems."

Bottom line? Despite its challenges, OTT is going to happen—it's a multi-billion-dollar revenue opportunity, and the primary way that video providers will maintain their customer base as millennials grow up. But it's not an easy path to walk, being fraught with outsized cost centers, transitioning legacy businesses and intense competition. Going forward and as business models shake out, the most successful OTT companies will remember that the customer is, as ever, the pole star of the business model universe. ■