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Business Guidelines for a Magical Media

Seeking the Way Forward

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From a lean back belly laugh over a pratfall on Saturday Night Live, to leaning forward in disbelief at live shots of the 9-11 tragedy, the ever changing images on television continue to capture our attention and to mesmerize. All the while this multi–faceted media is itself undergoing an ever more rapid makeover and transformation. From on–demand TV as in VOD, to digital recording and 'trickplay' viewing as in DVD–R and PVR, to viewing digital TV with an HDTV, the methods keep changing, only our fascination with television remains constant. As with the rest of us, such a metamorphosis often seems beyond the capability or even the imagination of its managers and their regulators to fully grasp. A real problem when there is an ongoing need to adjust and reconcile the many factors that impact the competing and conflicting commercial, governmental and private interests. It is an ever–changing puzzle driven by a multitude of technological changes that continue to challenge the accepted business and viewing paradigms. TV advertising in particular, as a major financial underpinning of television, is being challenged. Yet overall a more beautiful butterfly seems to be emerging.

"TV advertising in particular, as a major financial underpinning of television, is being challenged."

Are there some useful fundamental rules we can apply to help steer the TV enterprise away from chaos and toward greater success during this period of dramatic change? Beyond the usual bromides, what business compass is there to guide the venturesome television businessperson on his or her way? In today's TV world this appears to be a basic question that can only be ignored at one's own peril. Herein, we attempt to address this matter and sketch out a few prospective navigational rules.

Given the current financial challenges facing television, especially its cable arm, one might wonder why such a popular media has so much difficulty making money steadily and consistently. The answer it seems relates in part to the inherent difficulties associated with managing business enterprises within competitive markets that experience very rapidly changing circumstances. For an

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CMS NewsLine

"Validating the Middle Ground"

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example, think back if you will to the oil fields of East Texas early in the twentieth century when wildcatters and entrepreneurs vied for oil leases and drilling platforms. The upheavals caused by the cycles of boom and bust that followed led to the creation of the all–powerful Standard Oil Company. The U.S. government was then obliged to step in and break up Standard Oil into Exxon, Chevron and the rest. Thus in the early U.S. oil business very rapid change caused chaos that Rockefeller, the wily attorney, exploited. Short of the 'force majeure' of government action, the free market failed. Is today's TV business as well as broadband headed toward similar difficulties?

RULES OF THE ROAD

Soon after WWII Dr. Hans Friestadt, the German scientist, immigrated to the U.S. along with such famous Nazi personalities as Dr. Wernher Von Braun, mastermind of the World War II V1 and V2 rocket programs. The good doctor professed a way of dealing with truly difficult issues. He advocated avoiding most complexities as they lead to frustration; and, instead, going after the first principles on which they rest. He noted that most complexity grows like an inverted pyramid from its source, the basics or first principles that underlie most things. Perhaps it would pay to give this rules–based approach a closer look.

"…complexity grows like an inverted pyramid from its source, the basics or first principles…"

What do we have to lose? With that great pioneer Ted Turner leaving the cable business this may be a good time to reflect on the past and carefully reconsider the future. With rumors that AOL Time Warner may soon face a takeover attempt from the likes of Viacom the overall electronic media platform seems somewhat unsettled. At the same time we have just witnessed a bitter little feud between Kevin Martin and Michael Powell of the FCC regarding the application of ORCA™ (open revenue channel access), to AT&T and other broadband companies on the Baby Bells telephone networks. During such a period, first principles may be needed and helpful to bring back order to the bubbling cauldron of change that we are witnessing.

Such basics may emerge out of a re–examination of the primary functions of television along with each of their perceived strengths and weaknesses. This process should also illuminate those elements that don't fit in properly or that may need to be reconciled in order to harmonize with the changing nature of TV itself. Such principles are needed to help us manage TV's technological changeovers in ways that contribute to the interests of the public, the commercial houses and the investor community alike.

Of course it would be presumptuous for anyone, including CMS NewsLine, to proclaim that this or that underlying concept, idea or principle indeed belongs as one of these basic underpinnings of the television business. With that in mind, all that is offered herein are a few rules as candidates for inclusion as first principles. These are a few (suspicious) prospects that must be carefully scrutinized and, as necessary, discarded. Then, after much field–testing, perhaps some half dozen or so practical rules will emerge. Their primary function would be to help steer TV toward better ways and away from pitfalls and the risk of failure.

TV HIPE — THE BASICS

A place to begin is a review of the nature of the basic Home Information, Promotion and Entertainment (HIPE) elements that make up the TV experience. If only television were able to deliver these HIPE elements in a manner that satisfies the viewers while providing a suitable profit for the service providers, then everyone might be rightfully pleased. In an era of slow or modest change, or in a business that is highly restrained by governmental or other regulations such an outcome would not be unexpected. On the other hand, with the current state of affairs in the television business, where even the wisest of prognosticators are unable with any degree of accuracy to forecast the direction or the steepness of major trend lines, such an outcome is surely not the case. Confusion often reigns supreme and vast investments, as in AOL Time Warner, are fraught with opportunity, uncertainty and danger.

These are indeed the manifestations of a revolutionary time in the TV business. This is a period characterized in part by the many false alarms heralding true understanding of this or that new technology or service only to find out that it is but false or transient knowledge. The thoughtful media manager or financial analyst or prognosticator has come to expect that challenges that may have appeared for a moment to be resolved, can often dematerialize again into a state of uncertainty. Think if you will of the bumpy evolution and lack of understanding on our parts of such new things as ITV, VOD, SVOD, and VoIP — all examples of the ever–changing face of new TV technology as it transits toward profitable new services.

"One possibility is to heavily regulate the TV industry and thereby slow it down to a more controllable level…"

With many of TV's parts in constant flux, it is very easy to be misled or deceived by initial trend lines or early manifestations of any new technology. Think of the rise and then downfall of Microsoft TV or Microsoft Ultimate TV. What is a media company to do? One possibility is to heavily regulate the TV industry and thereby slow it down to a more controllable level, but that would also steal away its mojo, its mystery and its magic, the very things that ultimately excite the public and make money for the providers.

FOLLOW THE MONEY

One popular approach is to 'follow the money' in search of better TV models. That is, to take a hard look at the Promotion aspect of HIPE and see how it can be improved. After all, the varieties of advertising and promotion represent a major portion of the funding of the television enterprise. Herein we may include all TV advertising, also the promotion of premium channels such at STARZ and HBO, the selling of transactional services such as VOD and PPV and the vending of subscription services such as VoIP, DTV, PVR, SVOD and broadband. If the TV media could only maintain the past success of this 'wedged–in' aspect of its TV economic model, its ongoing viability would be assured. Unfortunately for the MSOs this is no longer the case, as new technology has gotten in the way of the old model. New forms of television are threatening to erode away some of TV's major sources of revenue, especially in the TV advertising arena. Notice that in the acronym HIPE, the P is wedged in between Information and Entertainment, and that is how it should be.

Principal 1: Consumers Buy Convenience.

One strong candidate for selection as one of the first principles of the TV business — that also applies to consumer electronics — is consumers buy convenience! In that sense, a clear problem exists today with much TV advertising and promotion due to the inability of the viewing public to switch from an advertising to a transactional (or subscription) model on the fly. As a result, the viewer can become frustrated whenever he or she would prefer to eliminate the ads by paying a fee in lieu of acquiescing to untimely advertising interruptions and delays. For example, a viewer watching an exciting movie may well on a one–shot basis prefer to switch from an advertising sponsored mode to PPV and simply pay a fee in lieu of the distracting advertising. Today he does not have such a choice, at least not in real time. Yet, consumers buy convenience, so such an alternative would probably pay off handsomely for the TV MSOs.

IS IT COMMON SENSE?

What happens when consumers are not allowed to conveniently buy what they want? That is a key $64,000 question. Oftentimes what is perceived as illicit behavior, stealing, or even piracy by the likes of a Jamie Kellner or Jack Valenti is simply the public seeking ways around obstacles that limit its enjoyment of a service they have already paid a heavy usage 'tax' to access. Contrary to the opinion of some cynics among us, Americans typically prefer to pay a fair price for what they get, and they seldom stake out what does not belong to them without just cause. It is only when the public is frustrated in its attempt to satisfy rightful wants and needs that it can stray toward improper behavior that may victimize some commercial interests. For example, in the absence of a way to readily switch from one viewing mode to another via an effective quick–pay–service system, some individuals may feel that it is proper for them to copy TV content without permission. For example, by making a copy of a PPV film onto a DVD or PVR for later viewing.

> *"…with all the new on–demand and trick play technologies, a different revenue model is what is needed."*

Now that the most able defender of the established TV advertising catechism Jamie Kellner of Turner Networks has left the field, it may no longer be considered a crime to go to the bathroom or to the refrigerator during a TV commercial. But making a DVD copy of a movie you paid a VOD or PPV service to view — so that you can take it with you on your holiday, or watch it in a different room of your house — is a bona fide crime. Thanks for this are due Jack Valenti and the MPAA and others including a few misguided fellow travelers in the TV pantheon who left their brains in Sigmund Freud's secret place.

EARLY TO BED, EARLY TO RISE AND ADVERTISE

Let us now turn to the fact that it takes a lot of money to make television go. For in all the change that is taking place, at center stage in the coming upheaval of television is TV advertising and its future that is at risk. It is the gadgets that followed the VCR, such as the PVR and the DVD–R, that have now placed TV advertising's very survival in some doubt. Billions of dollars of advertising revenue could soon be lost to the television business, moneys that cannot readily be replaced. The net result could be a great drop in the variety and quality of available TV programming as well as the ongoing viability of scheduled TV to compete with VOD, DVD rentals, the Internet, PVR and other non–linear forms of electronic entertainment. Perhaps that would not constitute a great loss, but it would certainly represent a dramatic restructuring of TV's economic model. In this area the TV industry needs to thank the same intrepid Jamie Kellner for his mighty clarion call regarding this approaching danger.

One way to look at it is to conclude that technology has empowered the viewing public with the means of 'stealing' content in far more advanced ways than simply turning ones head, muting the sound or going to the refrigerator during commercials. On–demand TV in all its many varieties such as PVR and VOD is much more powerful than that! Yet, in the sense that the glass is half full not half empty, a better way to look at this challenge to classical TV is to observe that with all the new on–demand and trick play technologies, a different revenue model is what is needed. For there is little to be gained by lamenting what is already gone. In our view, a more flexible interactive TV revenue model that allows mixed modes of advertising, pay–per–view and the like can render the system viable once again. Classical TV advertising is now a flawed and outmoded commodity — face it and move on. But the idea of advertising as part of the economic model that underpins TV is neither outmoded nor flawed.

With a properly designed real–time pay for services on–the–fly system the viewer would be able to switch among the subscription, transactional and advertising modes, in part or in whole. Viewing in this manner will financially enrich the TV media business while, at the same time, removing barriers that block subscribers from watching TV the way they may prefer. Greater choice for the individual buyer and greater profit for the service providers, what an idea! Let's call it nouveau TV capitalism and see if it flies. It is reasonable to suppose that with such an approach a great deal of TV advertising can survive and prosper. Of course it may appear in slightly different and newer forms, but consumers buy convenience and they always will.

"TV advertising is now a flawed and outmoded commodity — face it and move on."

A somewhat more advanced alternative, one that goes beyond just changing the billing method on–the–fly, would include revenue models that give viewers a greater choice as to what commercials are shown, the number of such commercials per hour and the context and the form in which they are presented. Somewhat more questionable would be the use of a split screen to show commercials, as a way of multi–tasking the viewer's attention, a method the TV Guide Channel may already be overcooking. With an improved balance between commercial messages and entertainment content and a greater choice as to how it actually appears on the screen, we may indeed be in position to create new gateways for TV advertising, ways that might work better for all concerned in a non–linear TV world.

The technology is available today to enable such improved systems to incorporate a real time capability of selectively adding or removing commercial and other interruptions and distractions at will and on–the–fly while substituting a PPV transaction or some other pay mode into the process. The net upshot would be to give the viewer greater freedom to have his content served–up as and when he chooses. It would also allow the commercial interests to benefit, as they would get fully paid for their hard work, their content and their contribution. It's a win–win situation — based and derived from the first principle that leads us to:

Principle 2: The Transactional Modes Must Satisfy The Subscribers.

The 90 million U.S. subscribers to cable and satellite TV shell out some 50 billion dollars per–year to an industry that regroups and repackages itself as it navigates the turbulence caused by one technology–based makeover after another. Each such passage is then declared a great victory: cable system upgrades, DTV, PPV, VOD, VoIP, PVR and now HDTV and networking, with ultra wideband (UWB) soon to follow. All the while, the public that loves the basic TV product hangs on, although troubled by TV's many machinations, reformations and odd transactional forms. Yet consumers appear willing to try just about anything in the hope of improving the experience and enhancing the way basic HIPE is delivered to them. Consider the savings to be reaped by MSOs if only a fraction of the cable TV subscriber churn were eliminated. Everything possible must be done to prevent this tolerant public from tiring of the TV game of switch and pay. Conclusion: the transactional modes must satisfy the subscribers! So far PPV is only a partial success, and ITV is mostly a failure.

RULES OF THE ROAD

Here for your consideration and critique are a few more candidates for the role of first principles. These are rules of the road that may be useful during this current period of rapid technological and regulatory change in the TV business. At this time it is too early in the process, and we have far too little knowledge to compile even a preliminary list of first principles. All we can do is conjure up some prospects that we believe have merit. The following are but a few such rules that may be the precursors of the real first principles needed to underpin the ever–changing TV business.

Rule 1: Strive to Minimize Viewer Frustration, Confusion & Wasted Time.

There is a fundamental need to minimize the frustration, confusion and wasted time of subscribers as they try to relax and enjoy TV. The starting point for further improvements in this area rests with such things as better organized TV channels, improved information within programming guides, and even means for viewers to multi–task as they watch TV. This is an important part of the Information component of HIPE. When effective useful information leads the viewer to a better TV experience by reducing his wasted time, confusion and frustration everyone benefits. Interactive programming guides are a big help, also effective ways to toggle between and among programs. TV Guide and the TV manufacturers are making real progress in this arena, but much more remains to be done, such as the inclusion of a 'volume leveling' device that balances the decibel level between channels and within programming and advertising segments.

"Everything possible must be done to prevent this tolerant public from tiring of the TV game of switch and pay."

Rule 2: Remember that Viewer Choices are Both Relative and Absolute.

This rule addresses the proposition that TV programs are selected on both an absolute and a relative basis. This relates to the Entertainment component of HIPE and the way viewers make their selections day–by–day and hour–by–hour when limited to linear TV. The public wants to watch what it wants, when it wants to, and whenever possible prefers to avoid all programming it does not rank highly, even some of the best–in–class shows at times of the day that offer only limited alternatives. With scheduled real time TV, programming choices are limited in this regard and selections are made mostly on a relative basis by picking best–in–class in a given time slot.

Not so with on–demand non–linear TV — as with VOD, DVD and PVR — where choice is absolute and one elects to watch what one really prefers from a larger, time independent, class of programming choices. This kind of TV viewing is beginning to downgrade some of the marginal programming now being watched somewhat reluctantly by the public during off–hour time slots. In counter point, this process will tend to up the value of those shows people like to watch the most. Thus the rich programs will get even more successful and the less attractive ones may have even greater trouble surviving. After all, the public has only so many hours to watch television and they would, if they could, prefer to concentrate their time on their preferred fare. This principle will greatly impact the economics of future television.

Rule 3: Foster the Creation of TV Communities.

This rule states that TV viewers like to join cohesive groups or communities of like–minded viewers who share common interests in such things as cooking, history or golf. Therein they share a common purpose which tends to increase their level of enjoyment as well as their desire to participate more fully than with one–way TV. Therefore, within such special TV communities various forms of ITV are likely to prosper. Also the value of advertising within such selected populations is much greater. Ads are seen as much more effective by the advertisers and therefore CPMs are likely to be much higher in the long term. The Food Channel and the Golf Channel are excellent current examples of this community concept in action. This approach is gaining ground because of the fractionation occurring as a result of the proliferation of TV channels, alternate forms of entertainment and other access points.

Rule 4: Keep in Mind that Work Modes and Play Modes Don't Really Mix Well in Electronic Media.

Here is a rule that warns us that lean–back and lean–forward activities need to be kept mostly separate. Such a preference in behavior is indeed endemic with most people and can only be ignored by TV content and services providers at their own risk. In self–delusion some computer companies, including Microsoft, continue to deny this preference claiming instead that only a generational gap exists. While there is indeed a generational preference, the differences between lean–back and lean–forward behavior cannot and must not be denied. Attempts to meld work and leisure activities on electronic media have only succeeded to a very limited degree, and mostly when there was little choice. Students watching TV in their dorms and office workers doing the same do not violate this principle. To think otherwise can lead to financial woes as demonstrated so clearly by the declines of many ITV enterprises, such as WebTV, Open TV, Wink and the like. The alternative to work and play goulash is to offer the public effective migration paths between the various forms of multimedia including the TV experience and the Internet. In particular, to allow the TV viewer and the PC user to migrate from one to the other as needed, without forcing the style of the one onto the behavior of the other. Caveat GUI designers: the right tool for each job.

Rule 5: The Home is the Viewer's Kingdom — Violators will be Punished.

This overriding first principle candidate warns that all outside agents are intruders in the home and must therefore learn to play the role of the good guest or risk being uninvited. This applies with special force to programming that contains gratuitous sex, violence and profanity as well excessive noise or shock value such as the graphic depiction of startling scenes of war, accidents or social discord. To fail to appreciate this fact of life is to lose sight of the reality that the public at large can regulate the TV industry back down to a small unprofitable little business whose economic weight will then match its lack of moral authority. The sanctity of the home and the family is not subject to the commercial wishes of the TV industry, either with regard to content or to advertising. First the public must be willing to invite the TV providers into the home, and then the latter may have an opportunity for economic gain. Caveat Venditor: let the seller beware!

Of course there are many other good choices for rules that can perhaps become valid first principles. Rules that guide greater choice for consumers, more effective copyright rules for content owners, better subscriber–MSO interfaces and the like come to mind. The important thing is to seek them out so that the public, the services providers and the governmental regulators can apply them. When true first principles become the basis of our actions, the television business will be more vital, more successful, more stable and more profitable.

[Don't miss Kalsow's Back–Channel; turn to the last page. —Ed.]

About CMS NewsLine

CMS NewsLine is published monthly by Alvairi-Derfler Associates, a Market Development company, which specializes in assisting corporations with:

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KALSOW'S BACK-CHANNEL: *"Validating the Middle Ground"*

TV Violence update: No sooner had we inked Rule 5: *The Home is the Viewer's Kingdom — Violators Will Be Punished* in this month's lead article than we came upon the Associated Press article of 3/10/2003: *Study: Children's Viewing Linked to TV Violence.* Sometimes we as an industry do seem as thick as mud. If the media industry does not regulate the excessive violence shown to children on TV, it will indeed be severely punished. We also do not need another First Amendment battle royale in our courts.

The coming of MystroTV by AOL Time Warner, as reported in the NY Times, is indeed a leap forward. Sure it may coop much TiVo technology and some of its magic. But it also addresses a number of major concerns coming from commercial interests regarding the impact of the PVR on many aspects of the TV revenue model. Most of all it is an acknowledgment that non-linear TV is now locked-in as part of the DTV experience. While there may be drawbacks to a system like Mystro, such as the limitations of headend PVR; we applaud the coming of Mystro TV. In the end it will as usual come down to how the public elects to change its viewing behavior. TV advertising? Don't worry about it, for it will surely survive and thrive after a few little adjustments.

Watching TV on your PC, is it good or bad? Media PCs such as the new ones from HP are a step forward. For those of us who cannot readily watch TV on our TV sets — say in a college dorm or at one's desk at work — they can be of value. However, the idea that TV viewing is really as enjoyable on a PC still requires a great deal of proof. For more on this see the September 2002 Issue of CMS NewsLine entitled: *From Convergence to Interoperability.* For an understanding of the value of combining DVD and PVR functionality, see the December 2002 Issue entitled: *A Most Satisfying Experience — When DVD and PVR are Combined.* That said, we applaud HP, Gateway, Toshiba, Sony and the other PC makers for addressing the PC side of news and entertainment.

Our comments in last month's column regarding the departure of Ted Turner from AOL Time Warner's active management drew the greatest response we have ever had. Clearly many in high tech, entertainment and elsewhere, along with the general public, share our view that a true pioneer has departed the scene. But if such persons are still made valuable and noteworthy by the current impact of their past counsel and great deeds, then, through the actions of others the positive impact of Ted Turner's legacy will continue to be felt in television and throughout the electronic media. Say, when bold action is needed, or when real imagination and courage are called for, or when one's convictions must be followed by stout deeds and resolve.

Kevin Martin versus Michael Powell — what a little power struggle we seem to be having within the FCC! We too were a bit shocked by the temerity of it all. Is it right and proper for a young upstart, though a Republican to the core, to take on the media regulatory establishment? Young Martin has the nerve to question why the Washington politicos are backing the baby bells against AT&T and the other broadband companies demanding ORCA, open revenue channel access? Shame on him for backing free enterprise against back room deals and for supporting competition instead of well entrenched special interests. And what about the tradition of pay to play? Bravo we say!

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