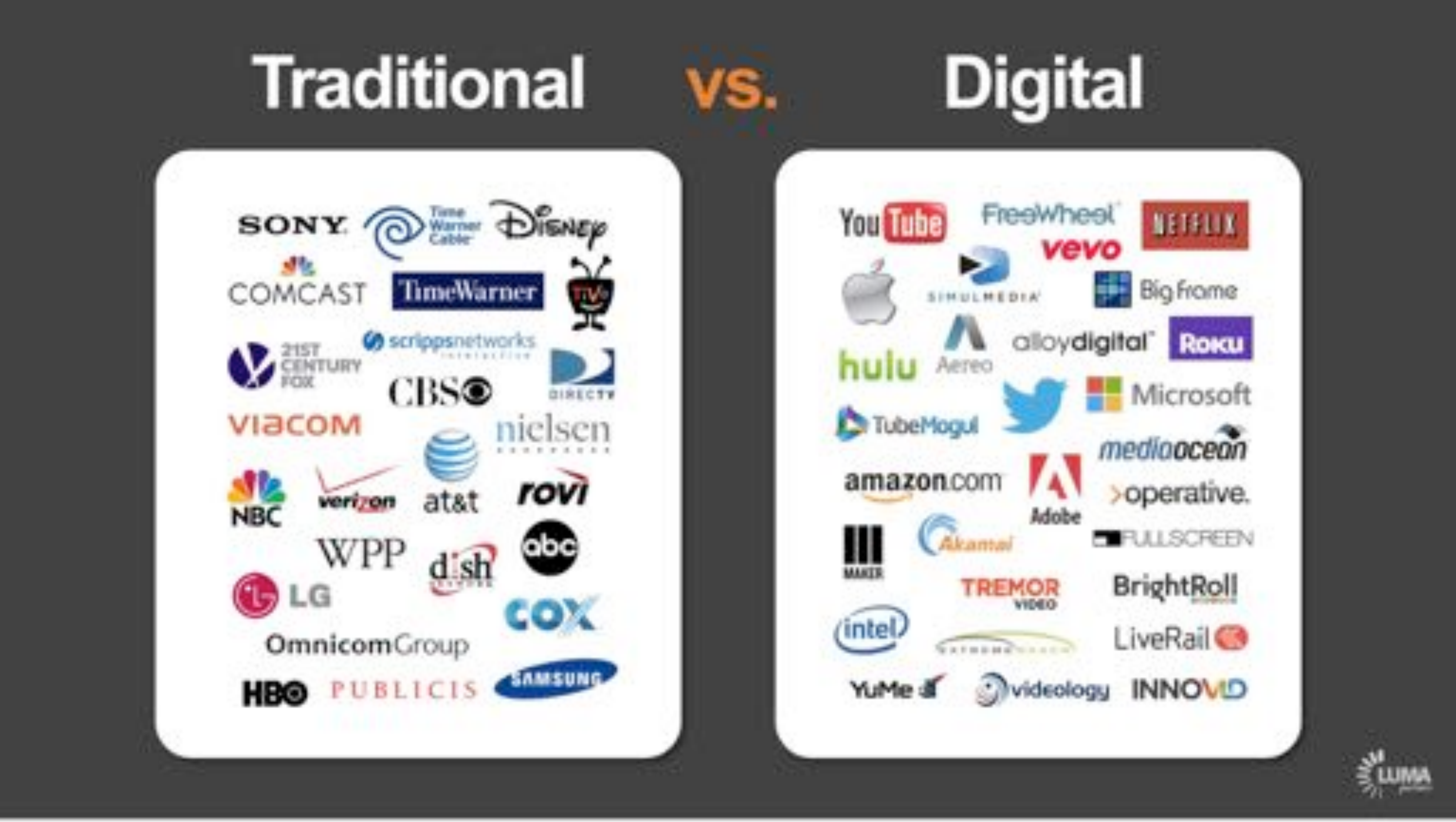
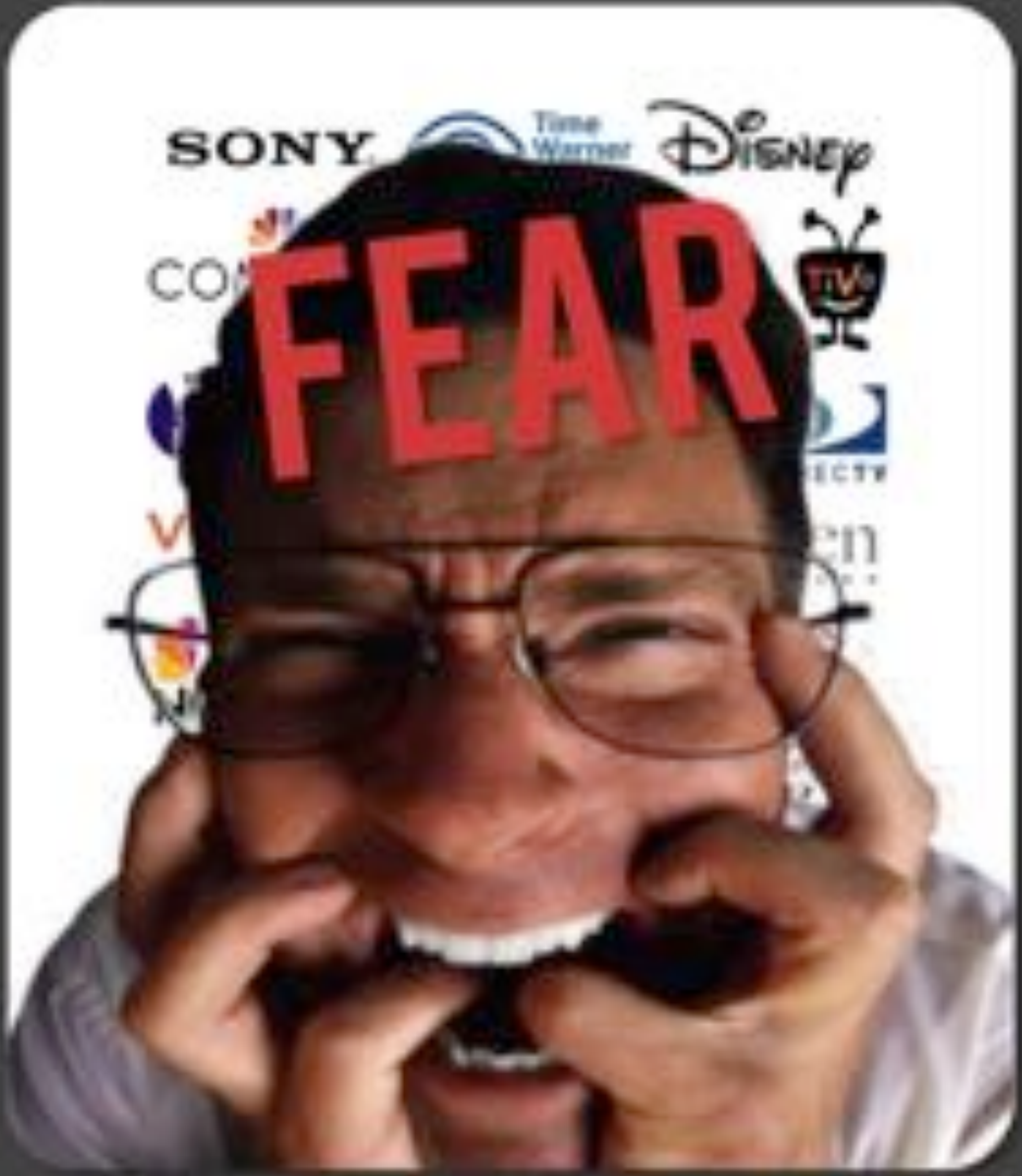
LUMA believes there is a great opportunity in video, yet there are misconceptions on how the convergence of TV and digital video will take place. We spent the last year collaborating with the leading companies in linear TV, OTT and digital video to create our thesis on convergence. It is a working draft as we continue our collaborative meetings. We hope you enjoy it.

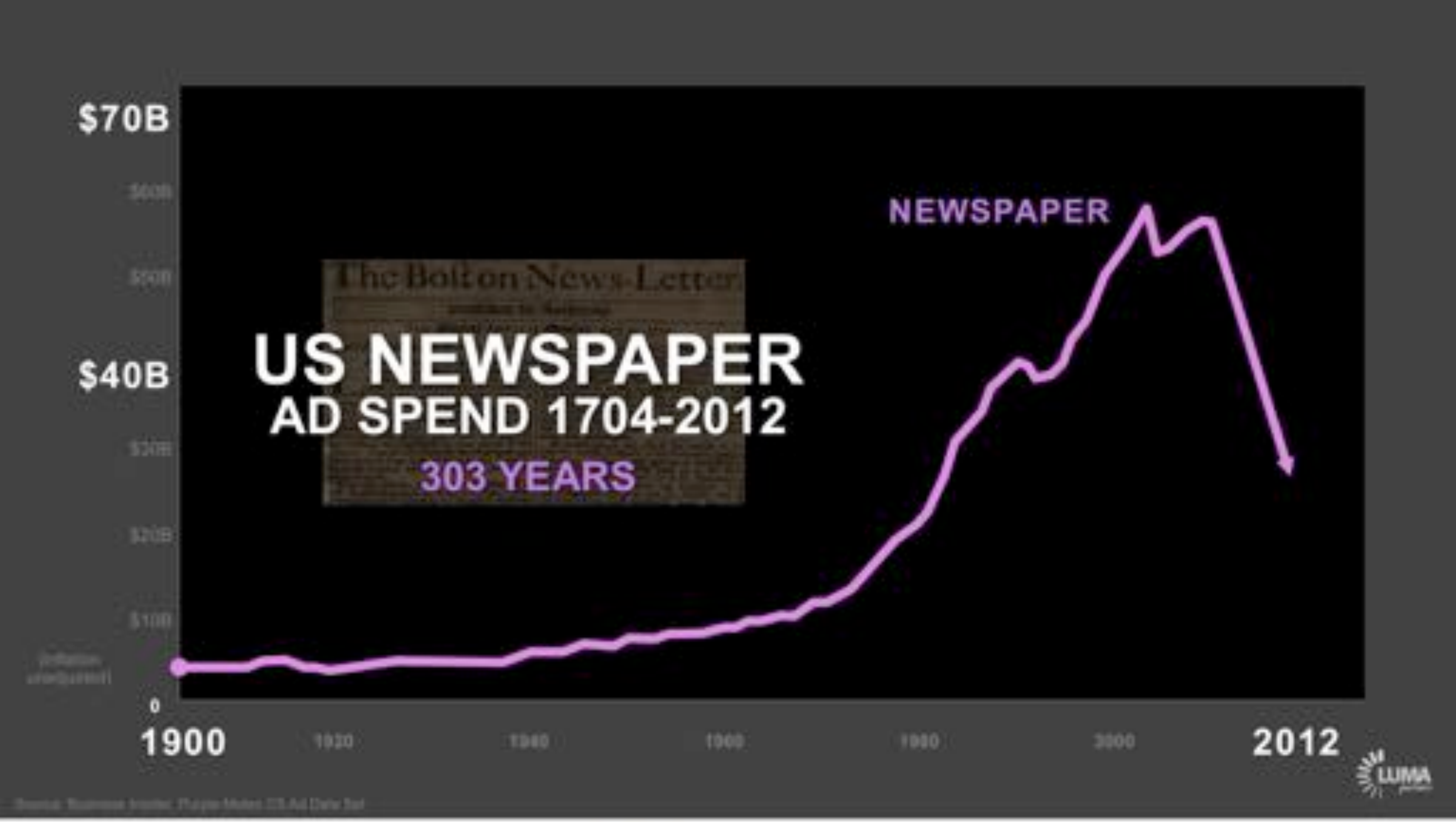


The dialogue around convergent TV seems to be taking place in silos. The traditional players until recently have not been that concerned about digital largely because they don't count in numbers that small. The digital players are equally ignorant and assume they will crush TV just like what happened in music or newspapers. This is decidedly not the case.

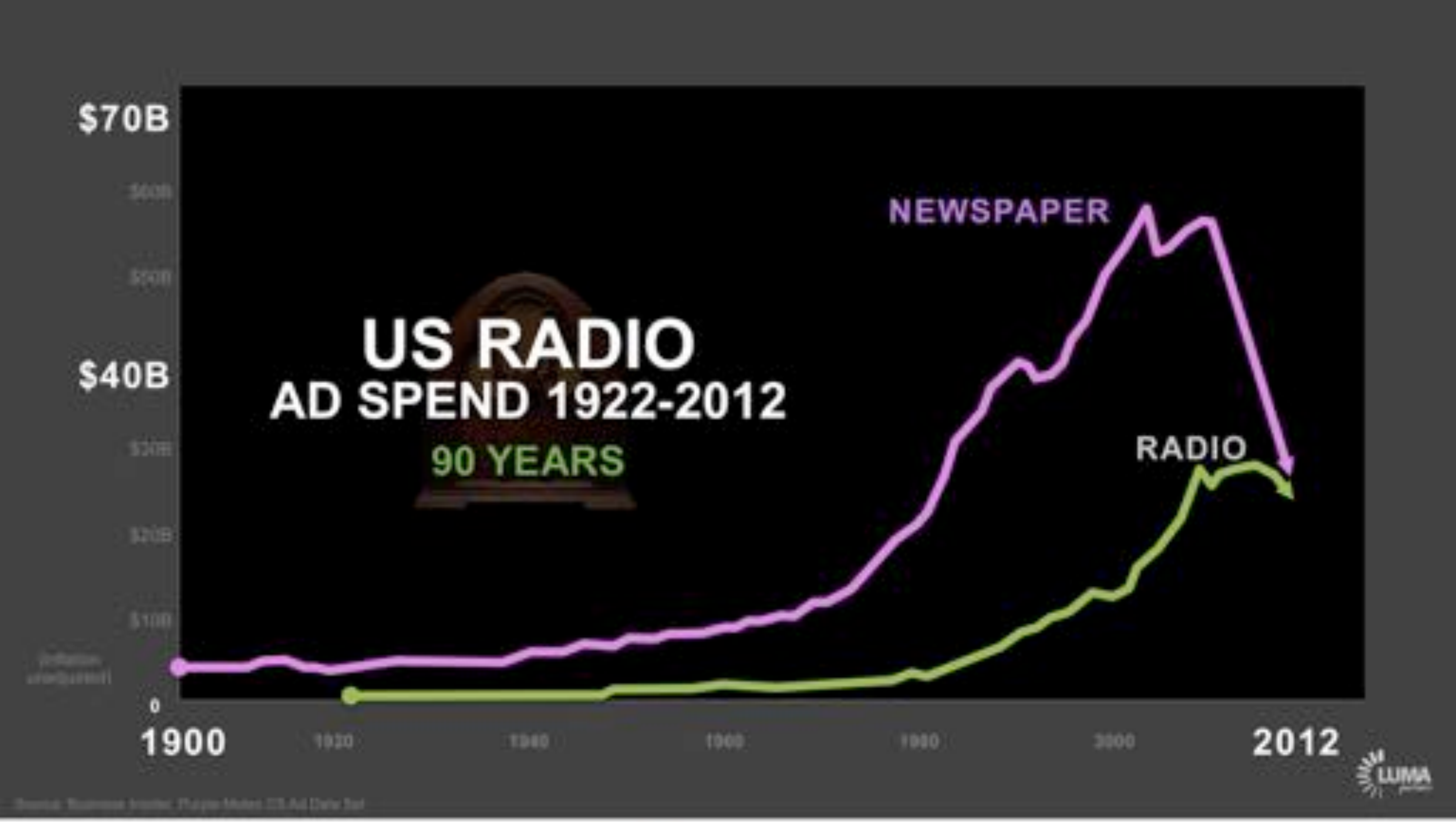
Traditional vs. Digital



The motivations of traditional TV and digital video players differ vastly.. Traditional TV guys are worried about losing share of their large, incumbent business whereas the digital guys see the $70 billion in TV spend and want a piece of the action.



We need to look back at all of the traditionally ad-supported industries to understand how we got to where we are today. The newspaper industry has suffered greatly with digital disruption. There has been a significant downturn in the industry's profits and the traditional business models are being challenged.



Radio and the music industry have suffered a similar mass disruption from digital.

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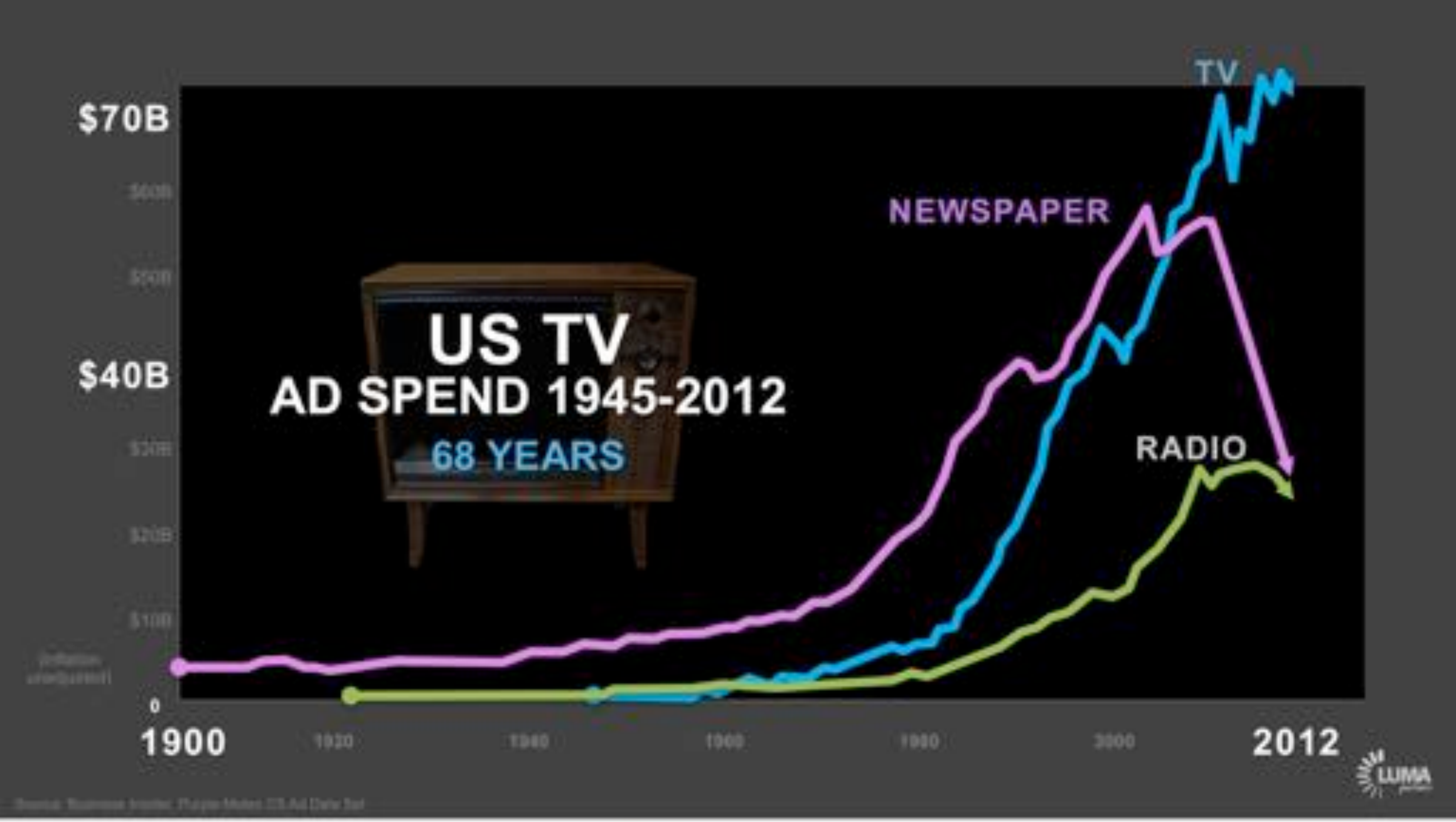
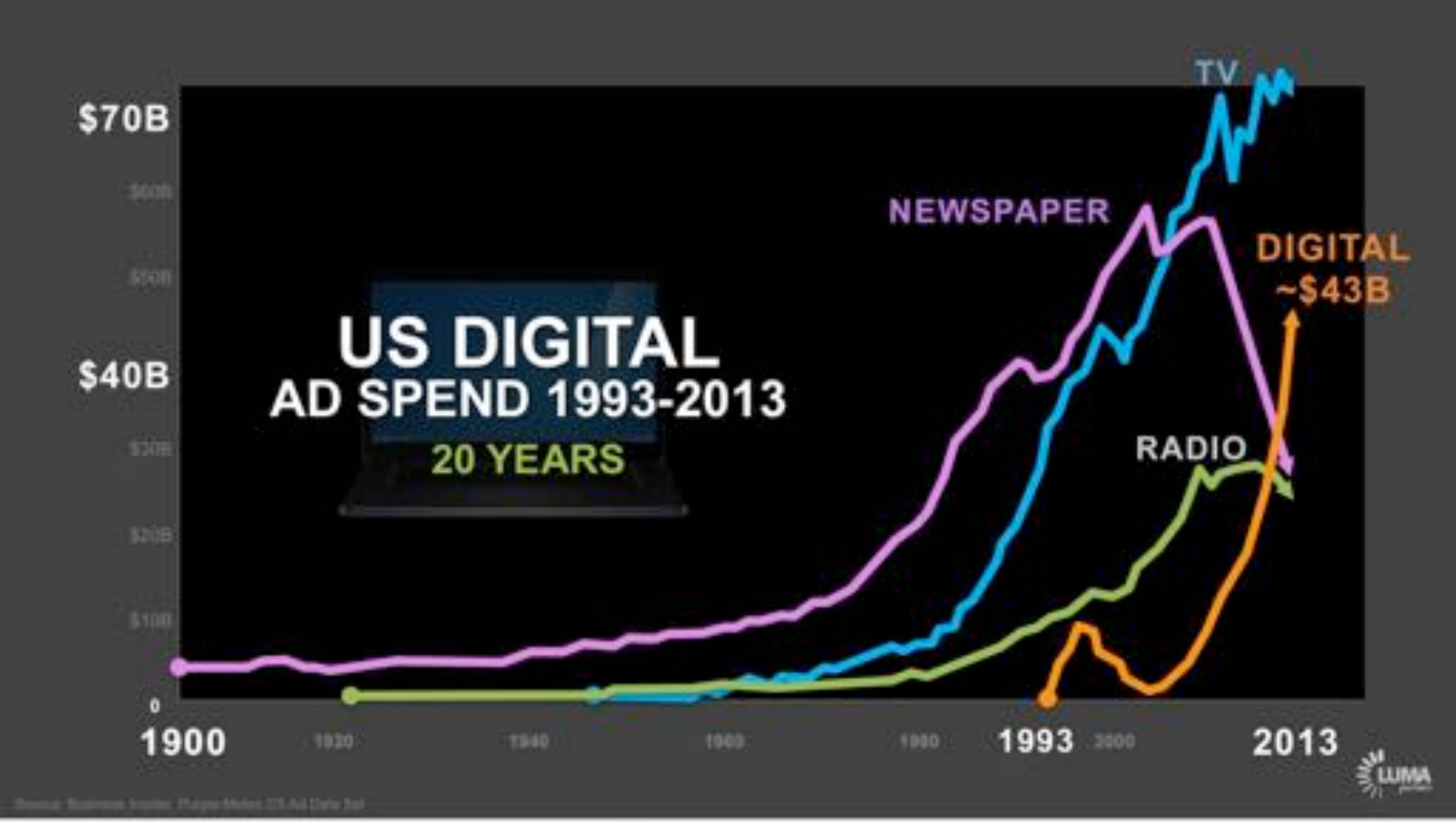
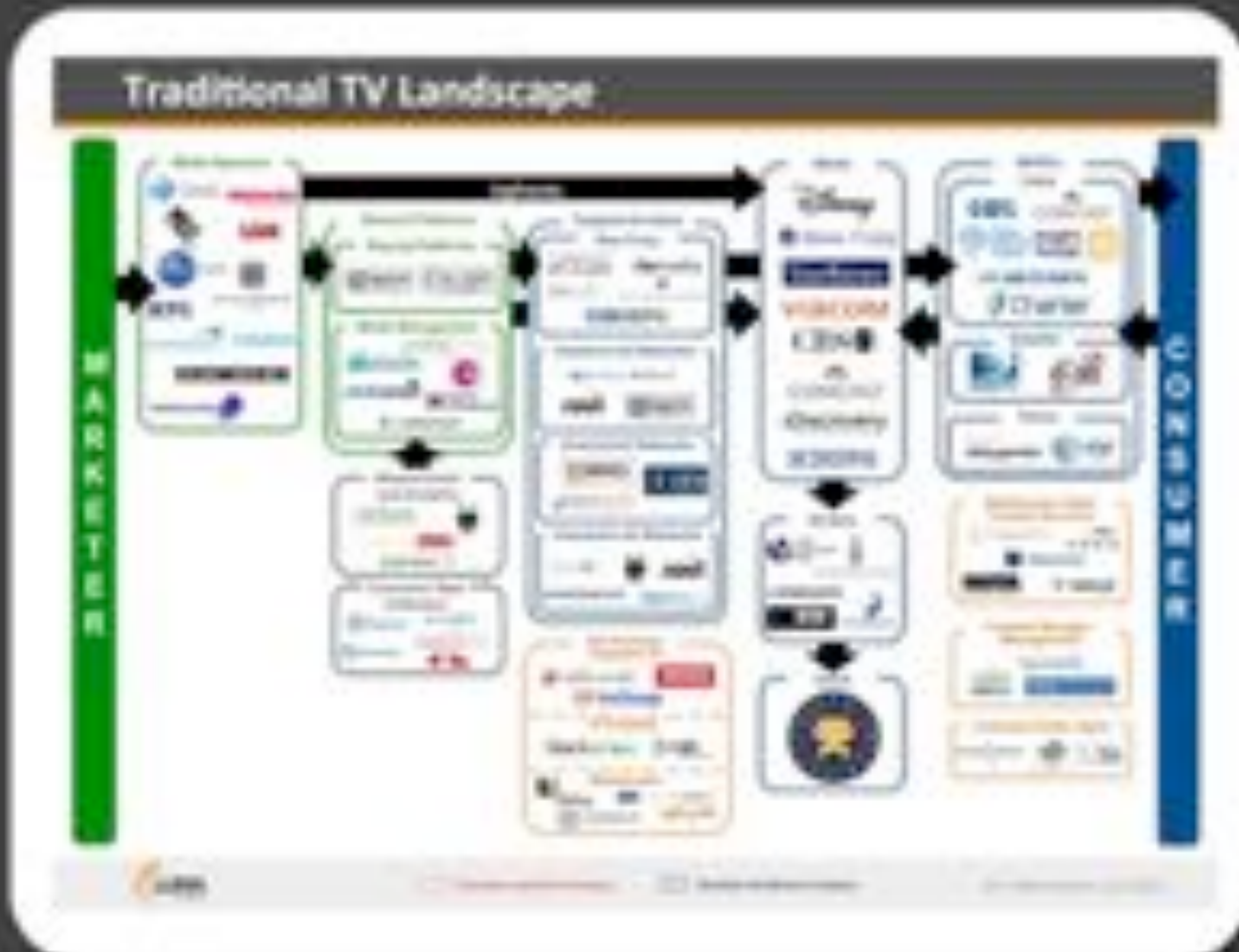


However, TV continues to grow.



… and digital is on fire. So the notion that TV will be cratered by the advent of digital video is simply untrue.

Traditional TV vs. Digital Video Players



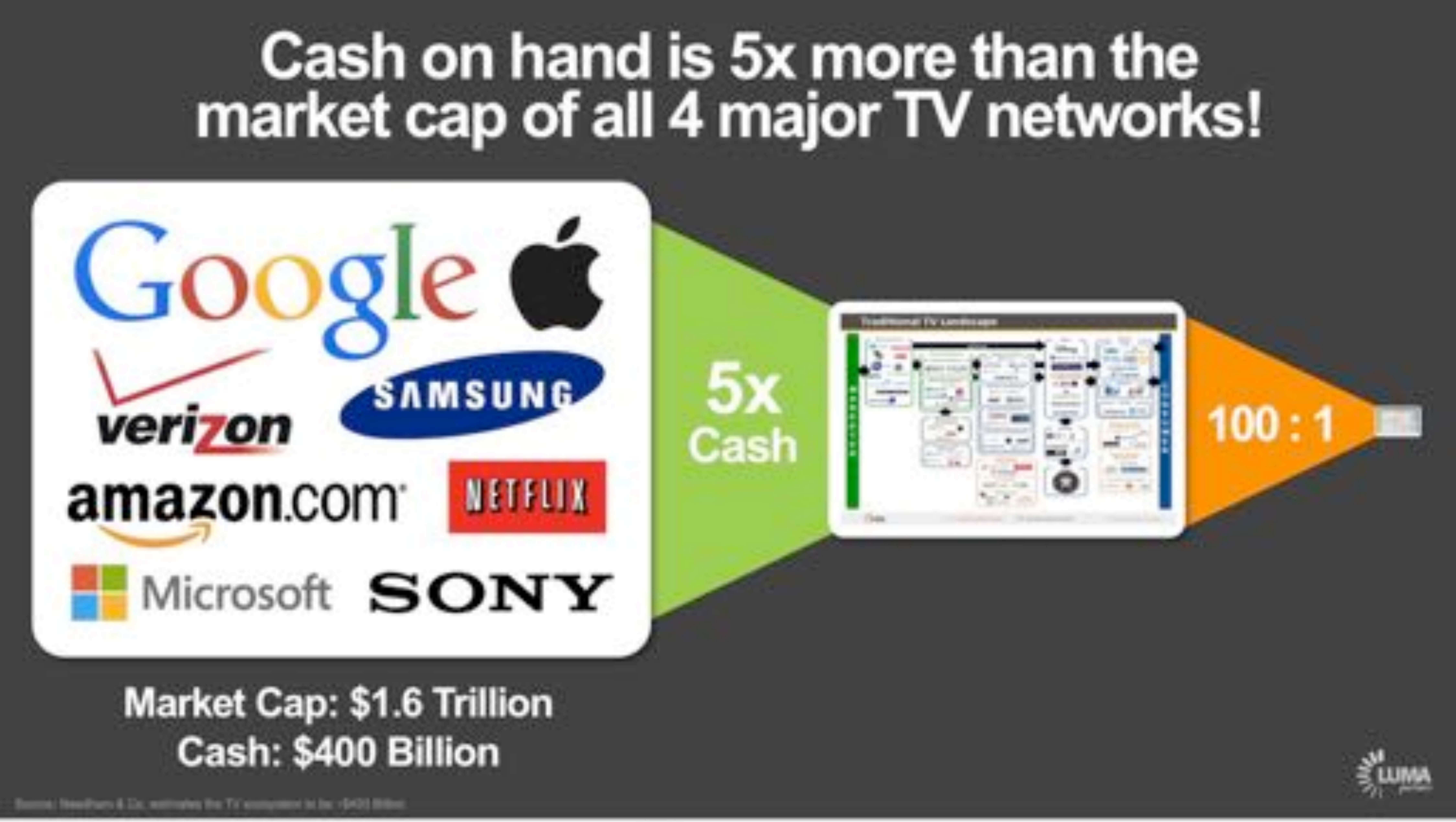
19	Buckets	36
~ 100	Companies	~ 400
$150 billion	Total Spend	$6 billion
$1.5 Billion	**$ / Company**	**$15 Million**

Traditional TV and digital video are two fundamentally different ecosystems. The traditional TV landscape has half as many categories of companies and a quarter of the number of players as compared to digital video.

Traditional TV vs. Digital Video Players

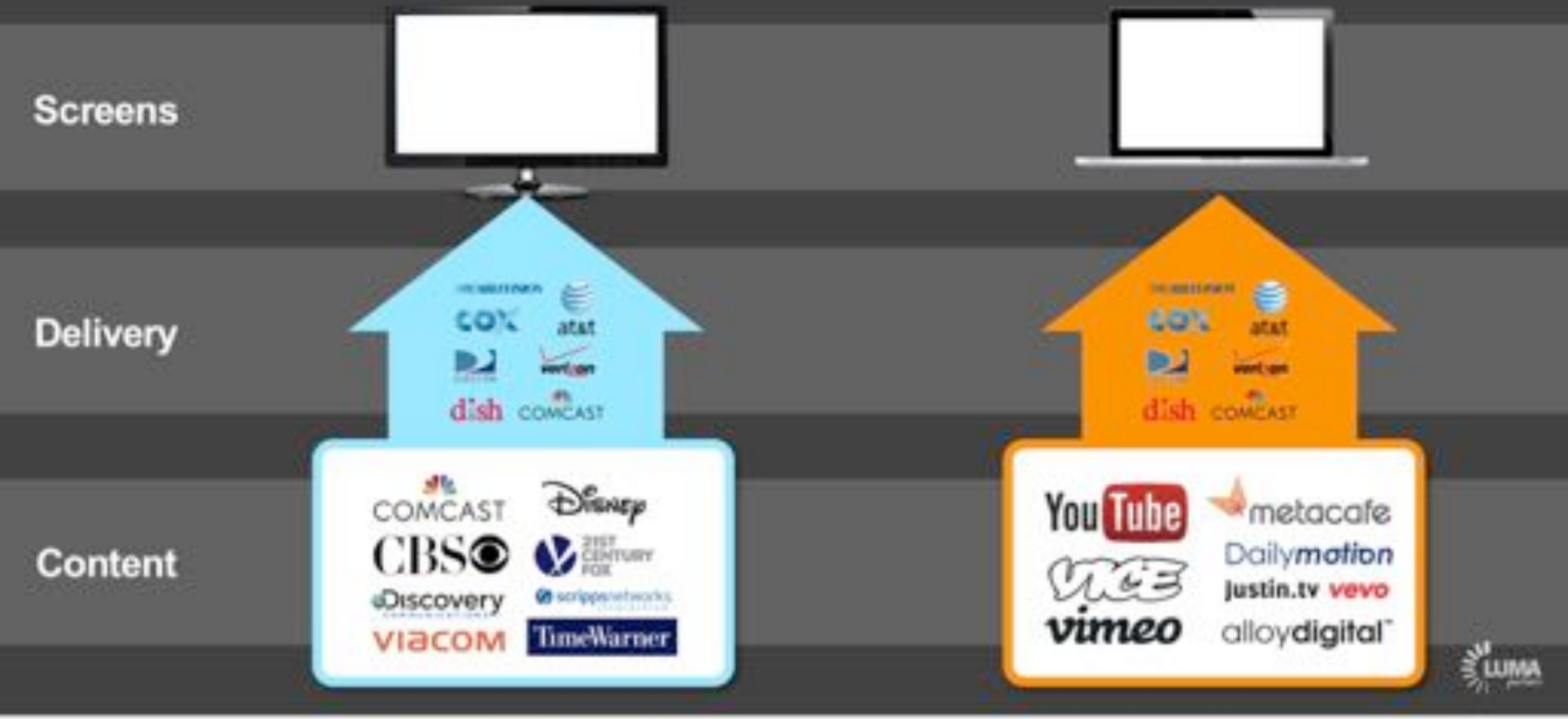
19	Buckets	36
~ 100	Companies	~ 400
$150 billion	Total Spend	$6 billion
$1.5 Billion	$ / Company	$15 Million

When you factor in the amount of spend per company in each of these ecosystems it's a 100 to 1 ratio between traditional TV and digital video. So the great change we're all expecting might not necessarily come from the smaller, VC-backed companies.

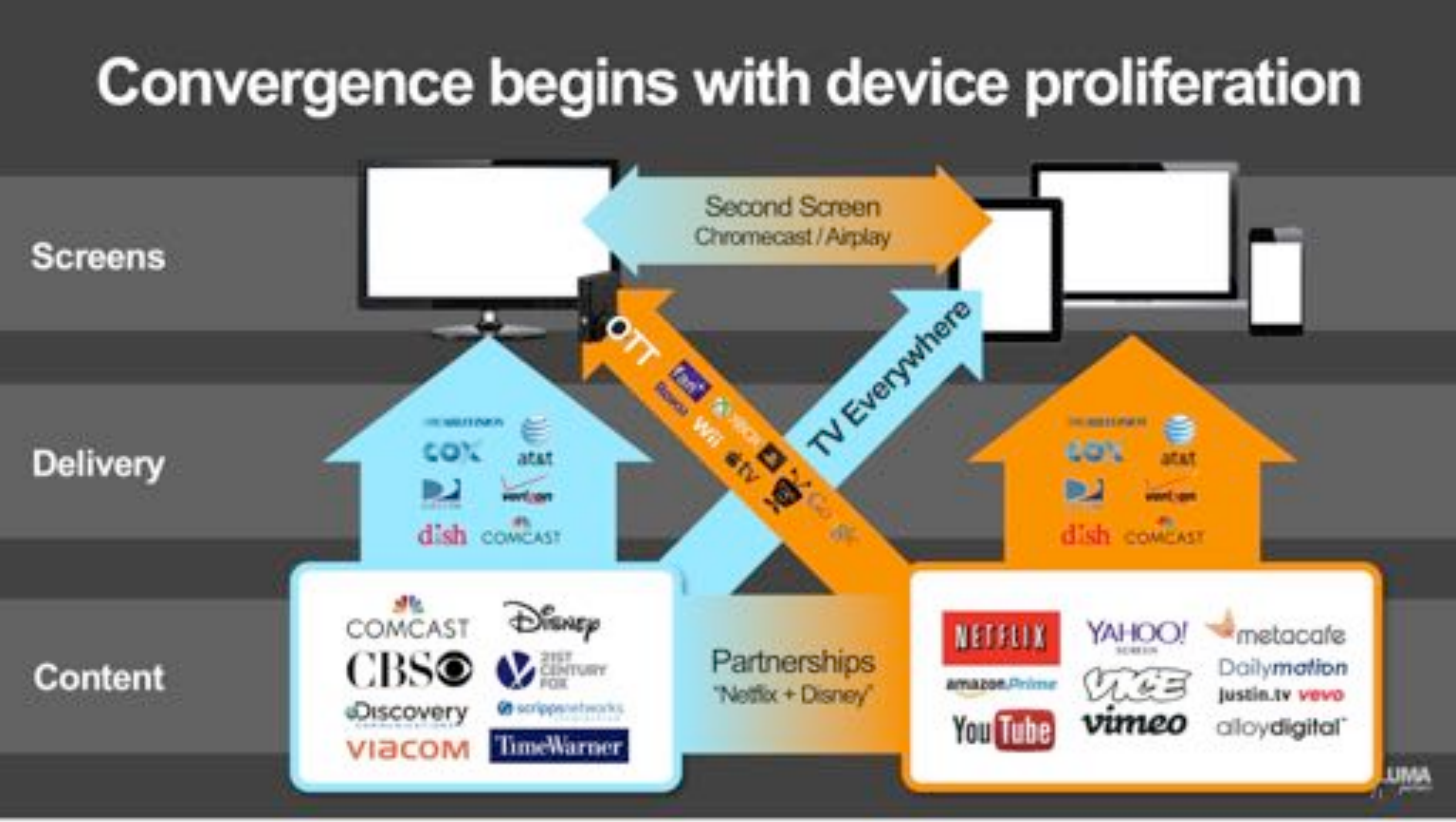


However, there are some new entrant that are very powerful. These are household names like Google, Apple, Verizon, Samsung, Amazon, Netflix, Microsoft and Sony that have combined market caps and cash that are multiple times greater than the entire traditional TV market.

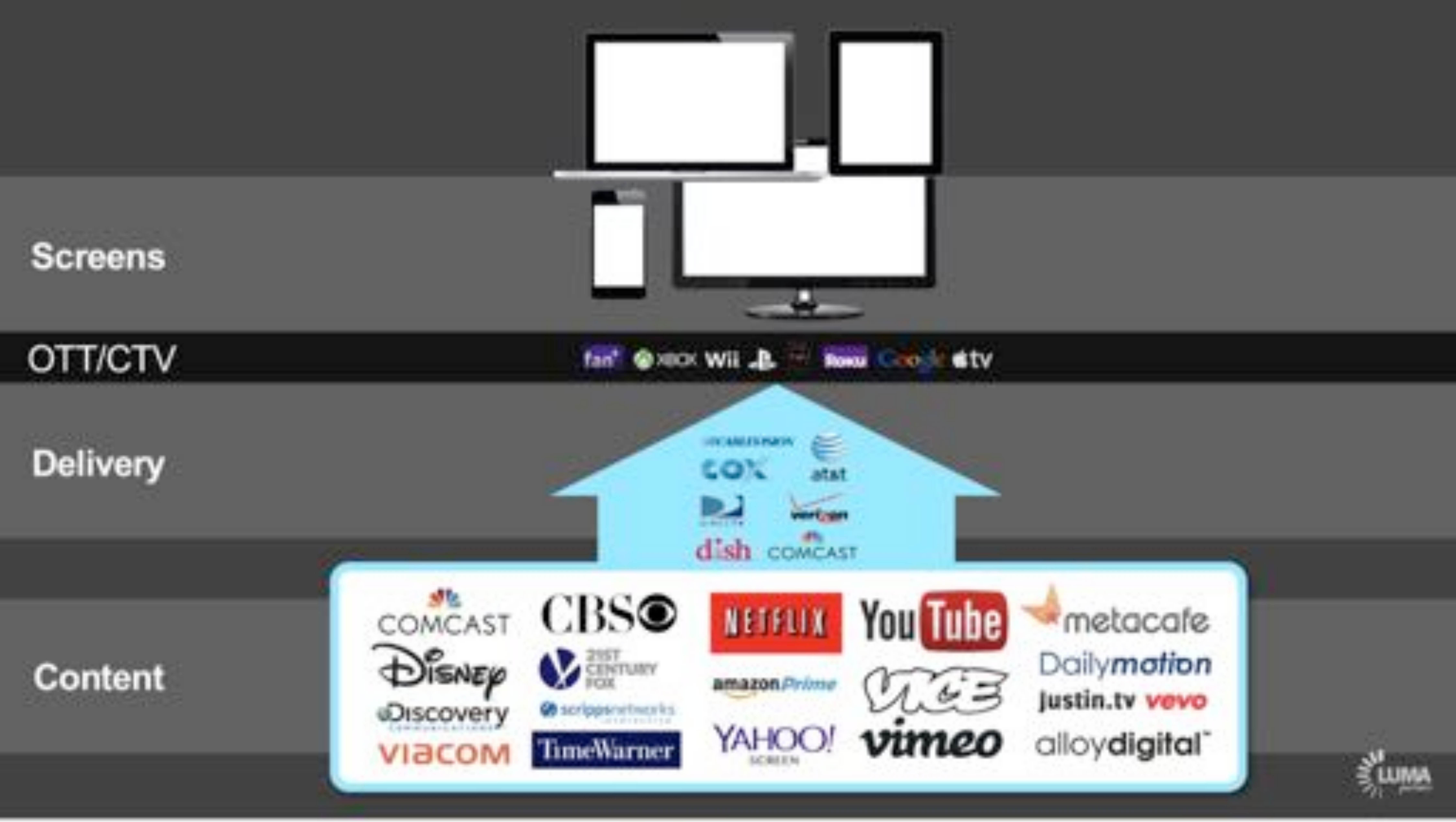
2008 was so simple: Traditional & Digital Silos



The world used to be simple. TV content was consumed on televisions and digital content was consumed via digital channels. It was straightforward and bifurcated.



Then came the adoption of multiple screens. With this we saw the beginnings of content partnerships between traditional and digital-first players. OTT emerged as a means to bring digital content to traditional screens. This was then complemented by TV Everywhere to bring television content to digital screens.



LUMA believes the future looks like a happy marriage between the traditional and digital players where there will be little distinction between what was previously thought of as traditional linear and digital delivery.

Kevin Spacey at Edinburgh TV Festival

"Studios and networks who ignore either shift, whether the increasing sophistication of story telling or the constantly shifting sands of technological advancement, will be left behind."

- Kevin Spacey, Keynote at Edinburgh TV Festival

A Collaborative Effort With Industry Leaders

LUMA is collaborating with the major constituents of both the linear and digital ecosystems to garner their expert input on this analysis. Accordingly, you can expect it to evolve as we have more meetings. If you have a perspective you would like to share and would like to schedule a meeting, please contact us at info@lumapartners.com

TV Business	Trends	Issues	Theses
Facts		Analysis	

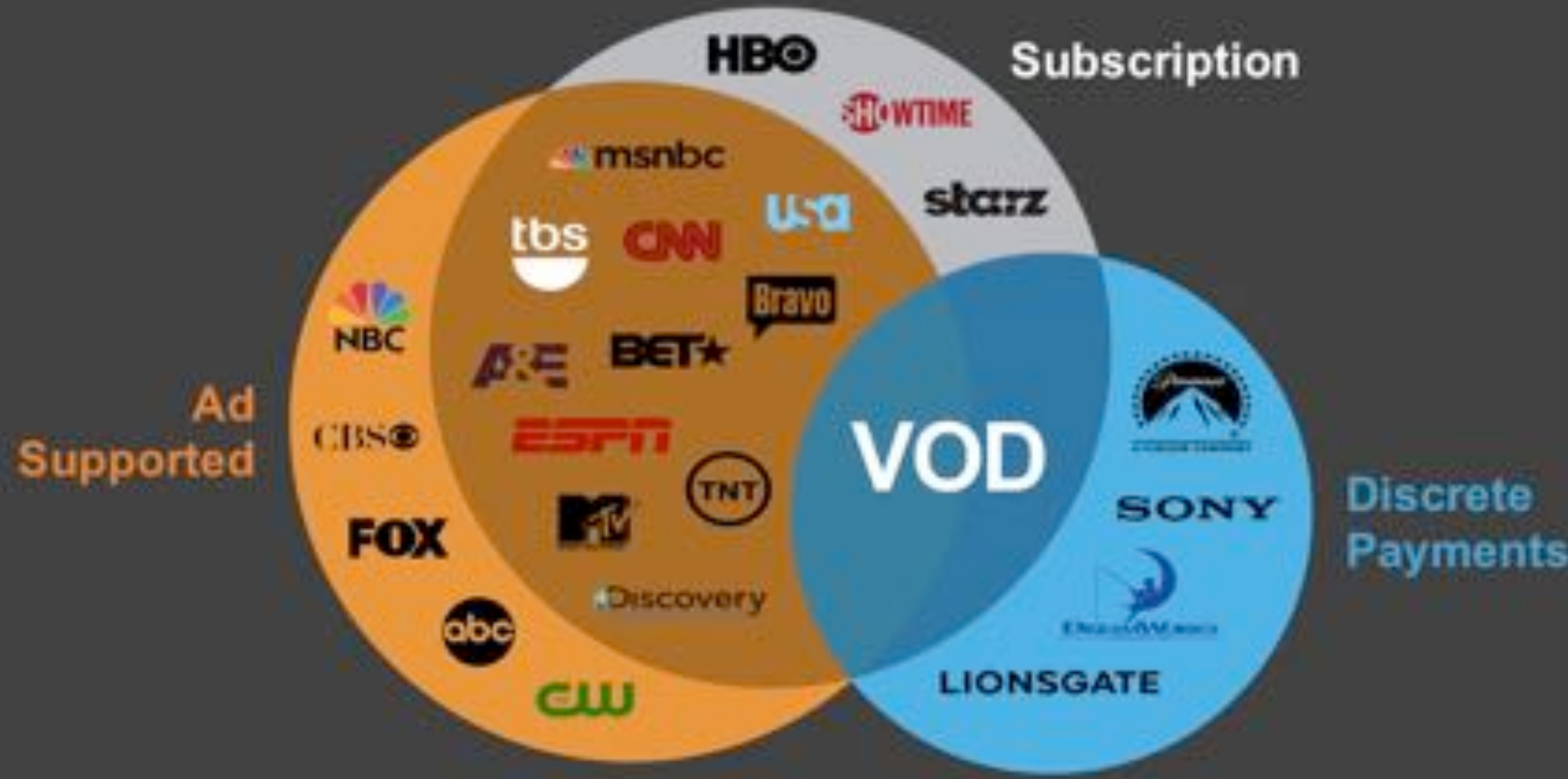
The deck is composed of four sections in two categories

TV Business | Trends | Issues | Theses

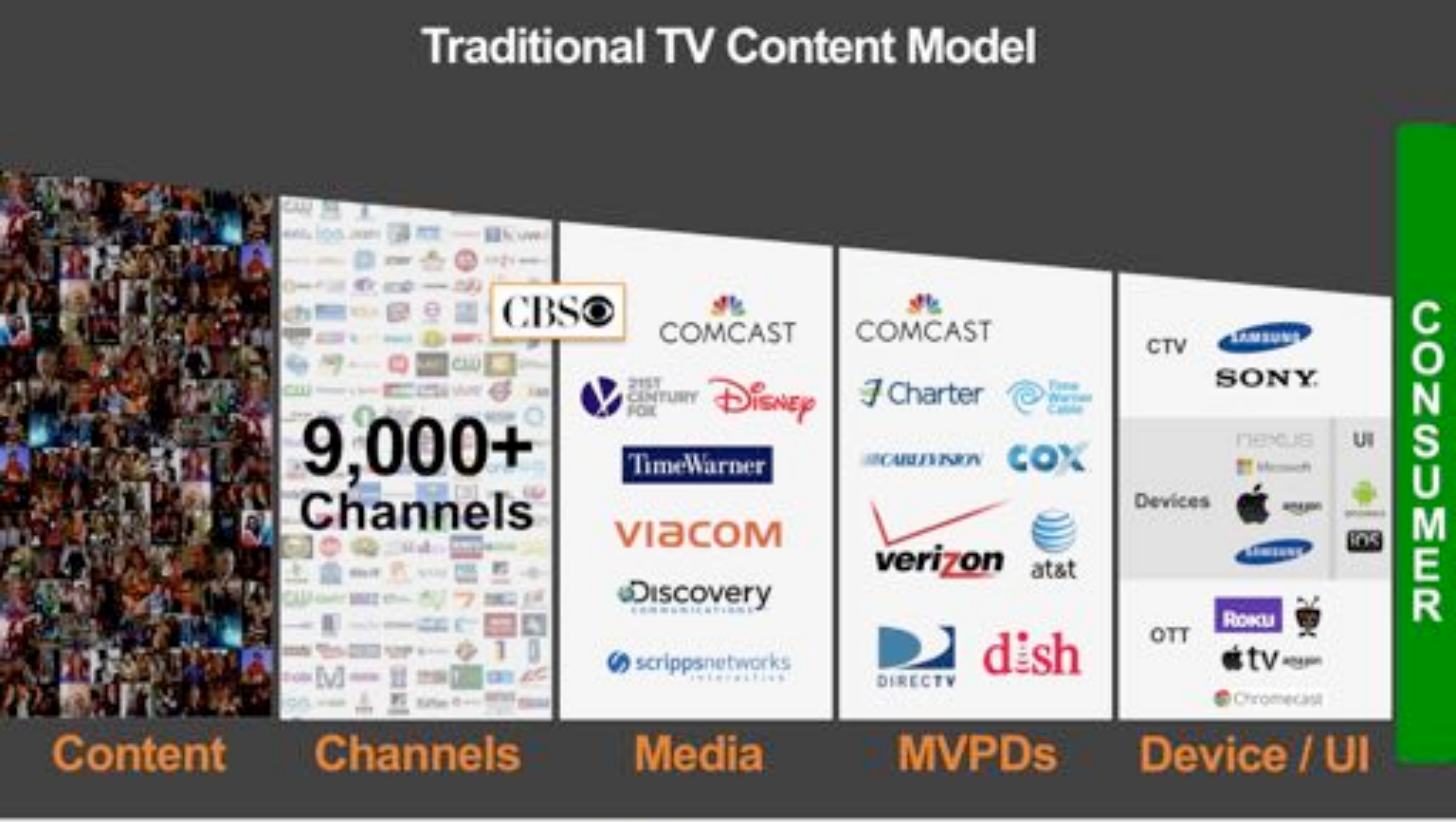
1. Business Models
2. Content Pre-Funding
3. Standardized Measurement
4. Inertia / Trust

LUMA partners

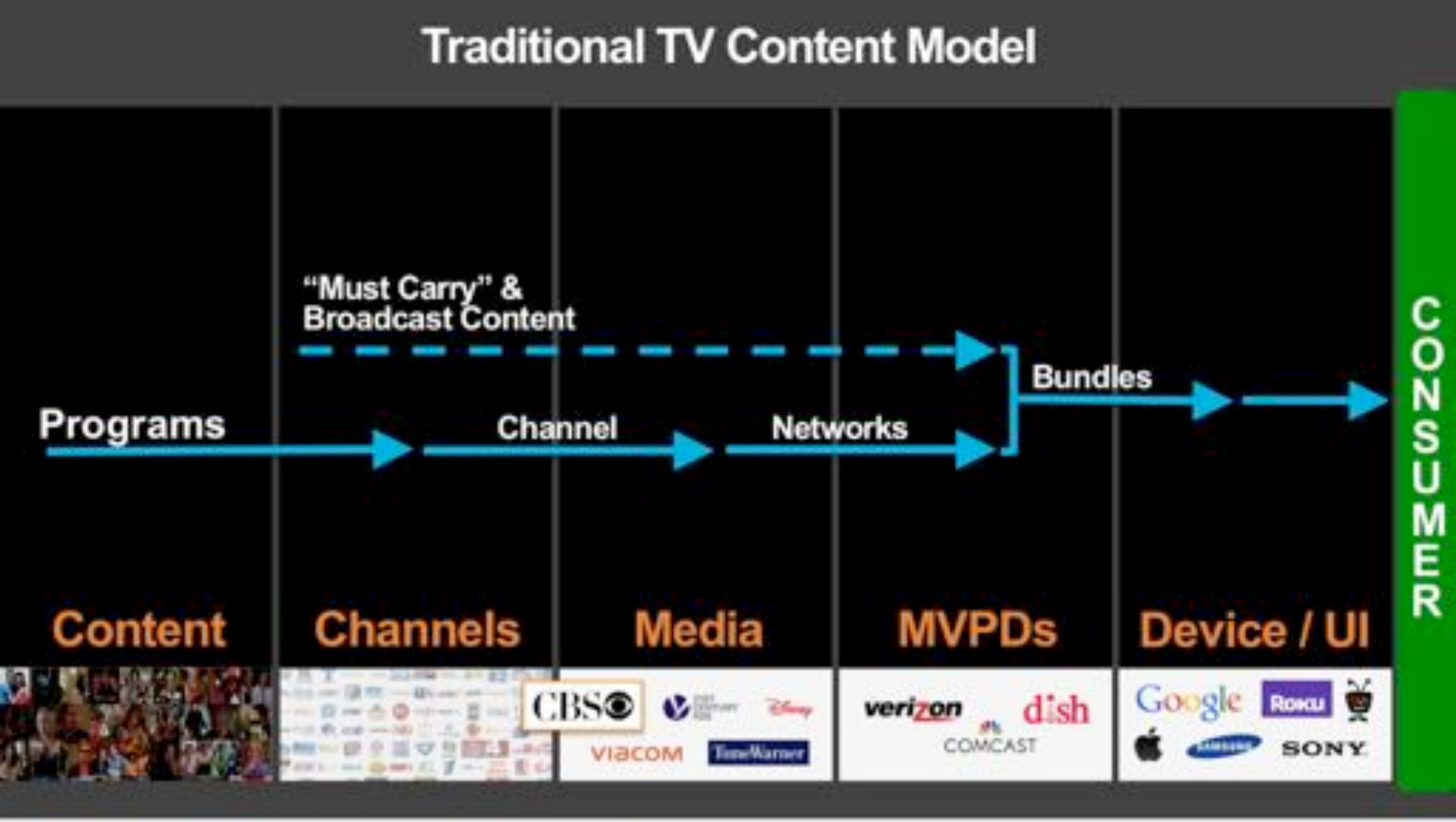
The Traditional Business Models



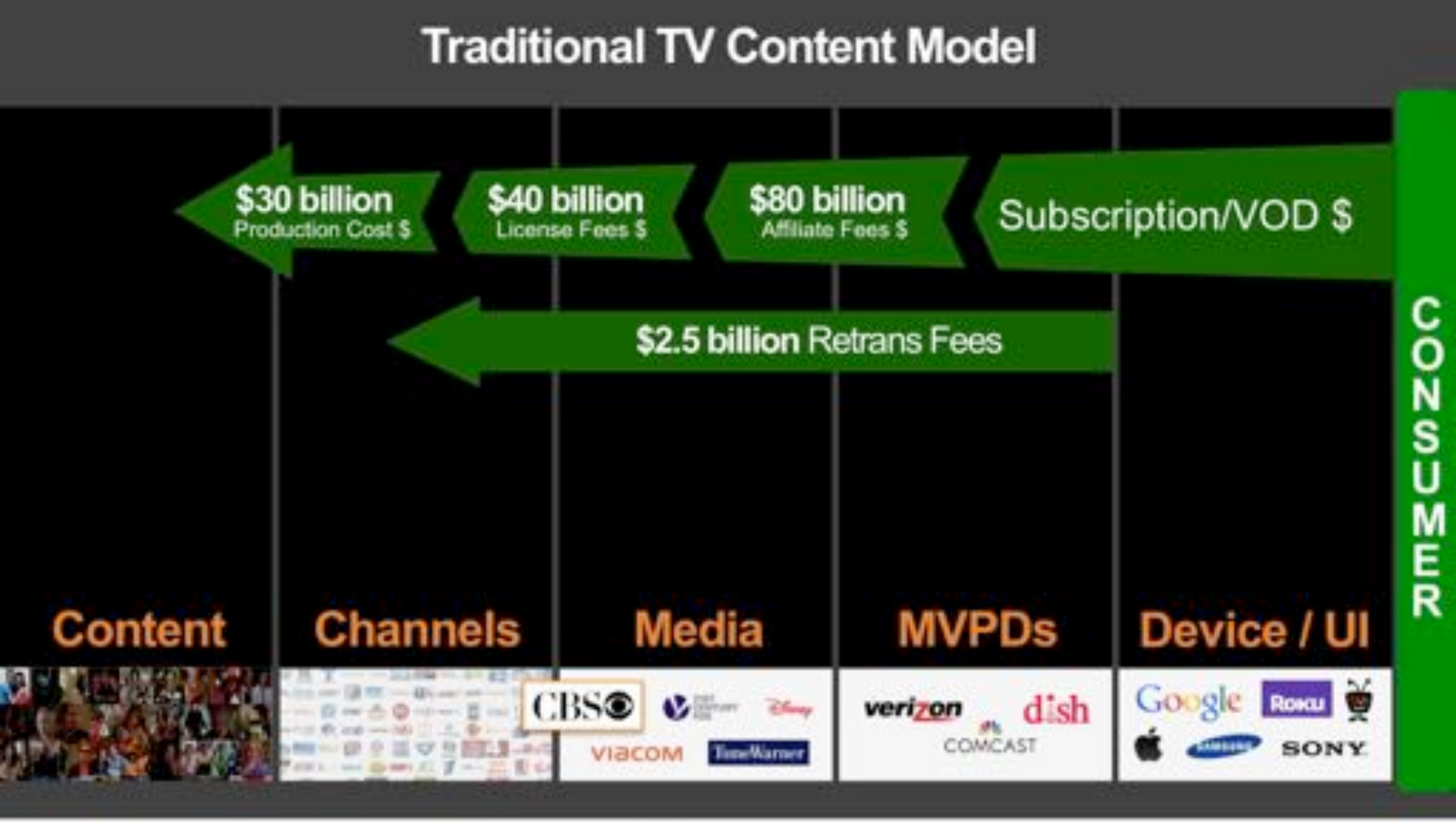
The TV business has a fundamentally different business model than digital video. While TV is the single largest ad spend category at $70 billion, this is only one of TV's revenue streams.



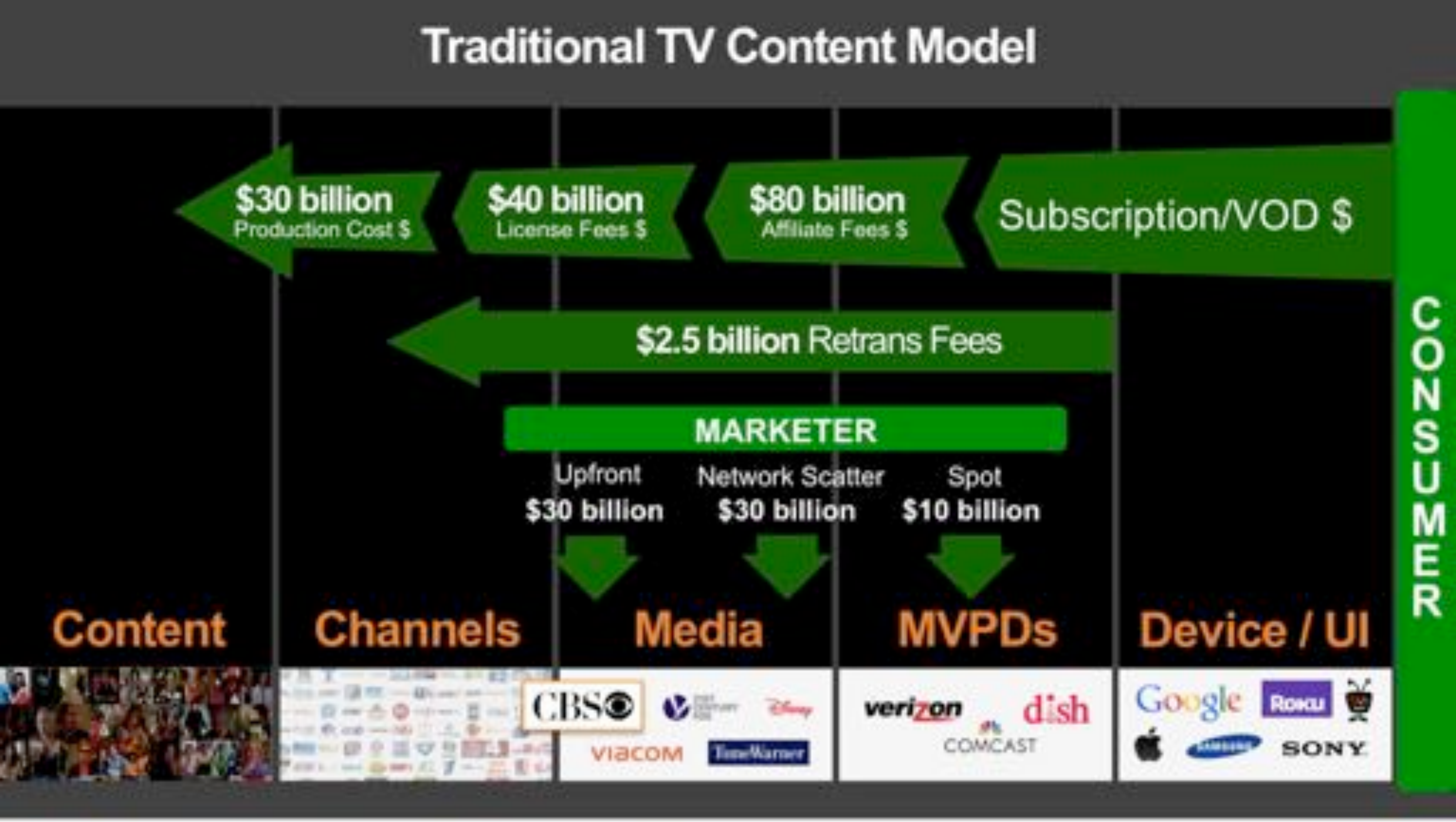
The traditional TV content model can be boiled down to the following: Content gets grouped into channels, which then get packaged by media companies, that are then again packaged and delivered by MVPDs, which ultimately gets viewed on the consumer's devices.



This is another way of looking at how the content flows to the consumer.



The return path is dollars. The $80 billion of subscription dollars gets shared between the delivery companies, the media companies and all the way back to the beginning to fund the creation and production of new high-quality, long-form content.



The marketing dollars are a separate, additional revenue stream. The $70 billion of TV ad spend comprises $30 billion of upfront buys that are committed to at the beginning of the year, $30 billion in network scatter for inventory that is not bought on an upfront, annual basis, and $10 billion in spot buys reserved for local markets.

TV Business | Trends | Issues | Theses

1. Business Models
2. **Content Pre-Funding**
3. Standardized Measurement
4. Inertia / Trust

Bundling Enables Pre-Funding of Content

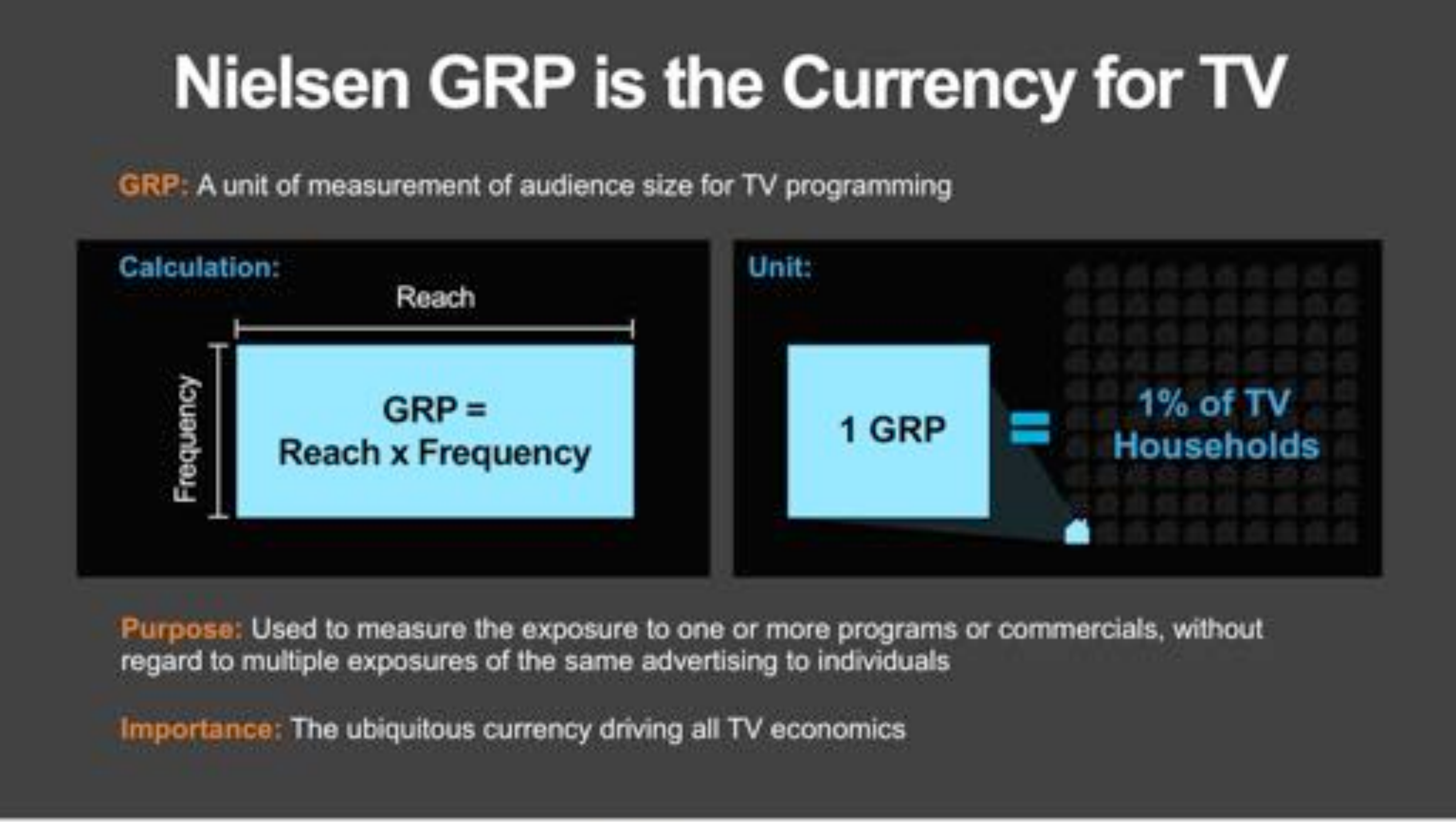
Media companies use the revenue committed upfront towards investing in new content. Traditionally, high-quality content has been very expensive as only a small minority of pilots produced may be picked up to actually air on TV. This means that the 10% that is picked up supports 100% of what is created.

Bundling Enables Pre-Funding of Content

This economic model differs from digital because in digital the publisher only gets paid well after an ad actually runs. There is no upfront payment.

TV Business | Trends | Issues | Theses

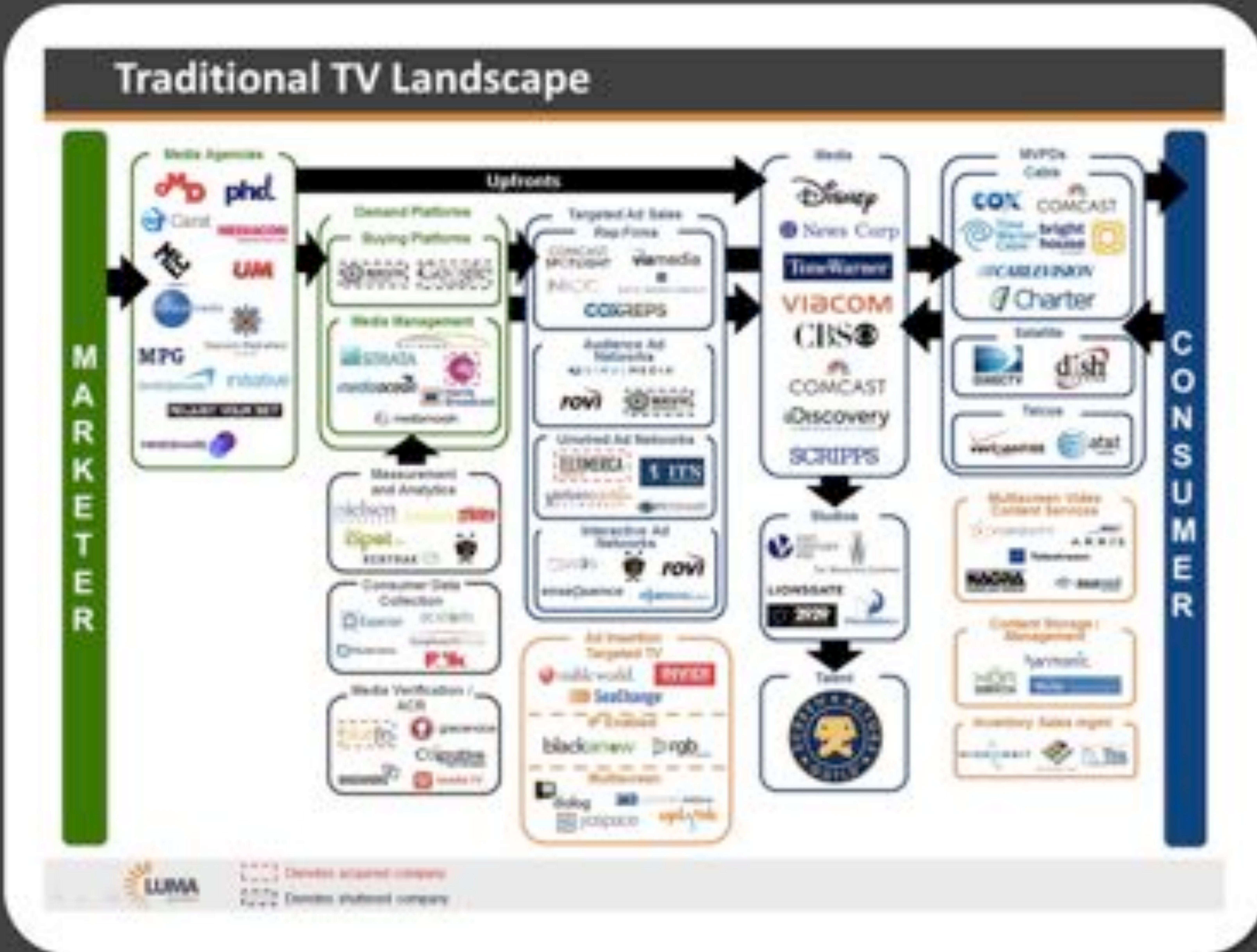
1. Business Models
2. Content Pre-Funding
3. Standardized Measurement
4. Inertia / Trust



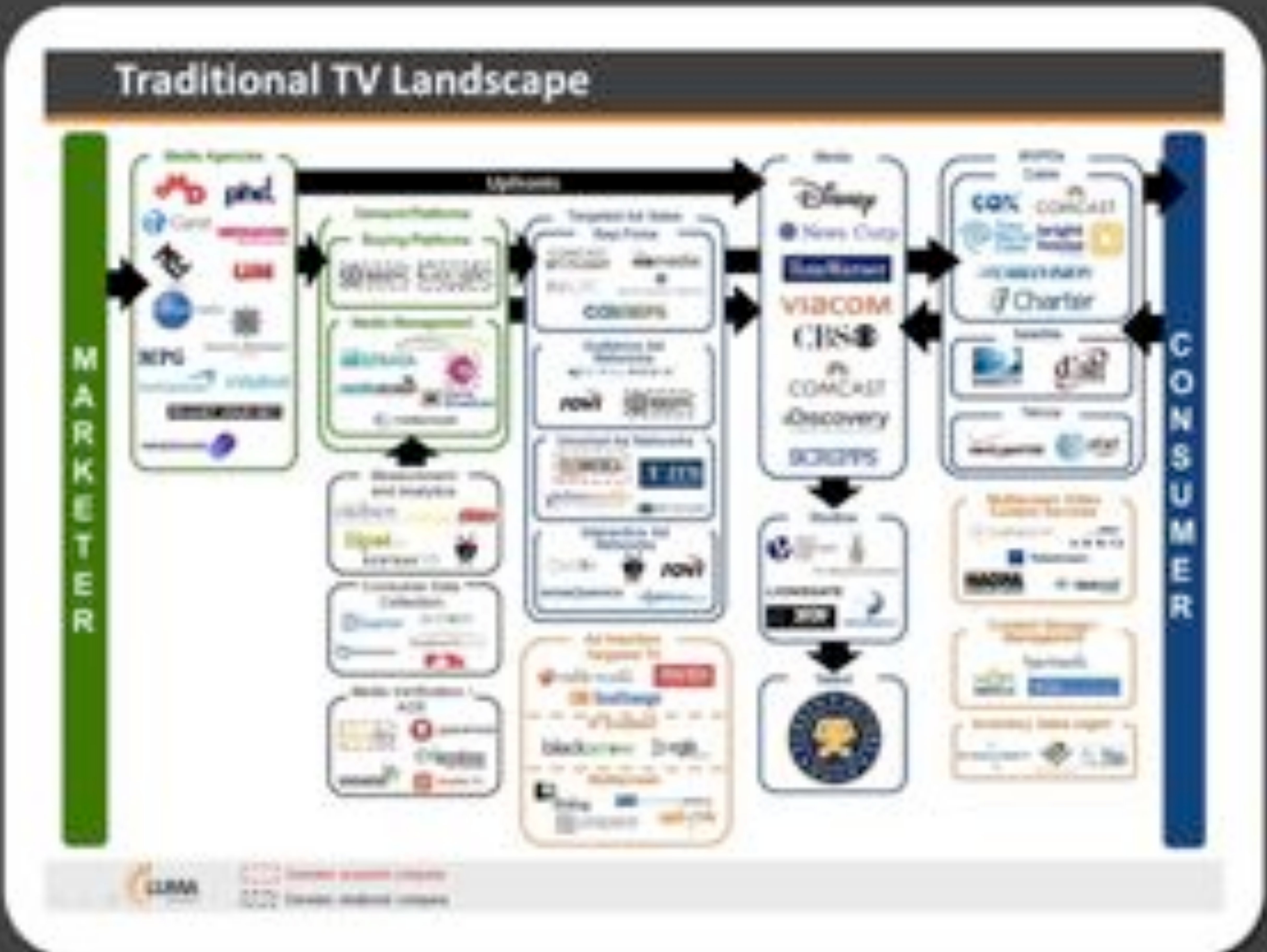
TV also has very different standards for measurement. Nielsen's GRP (Gross Rating Point) has long served as the single form of measurement / currency for all TV buying. This certainly differs from digital, which has multiple measurement metrics and multiple companies that perform those measurements.

TV Business	Trends	Issues	Theses

1. Business Models
2. Content Pre-Funding
3. Standardized Measurement
4. Inertia / Trust



There's a deep sense of inertia and trust that exists in the traditional TV ecosystem since the industry is mature and the same players have existed together for decades.



Observations

MATURITY of Ecosystem

SCALE of Audience

TRANSPARENCY of Data

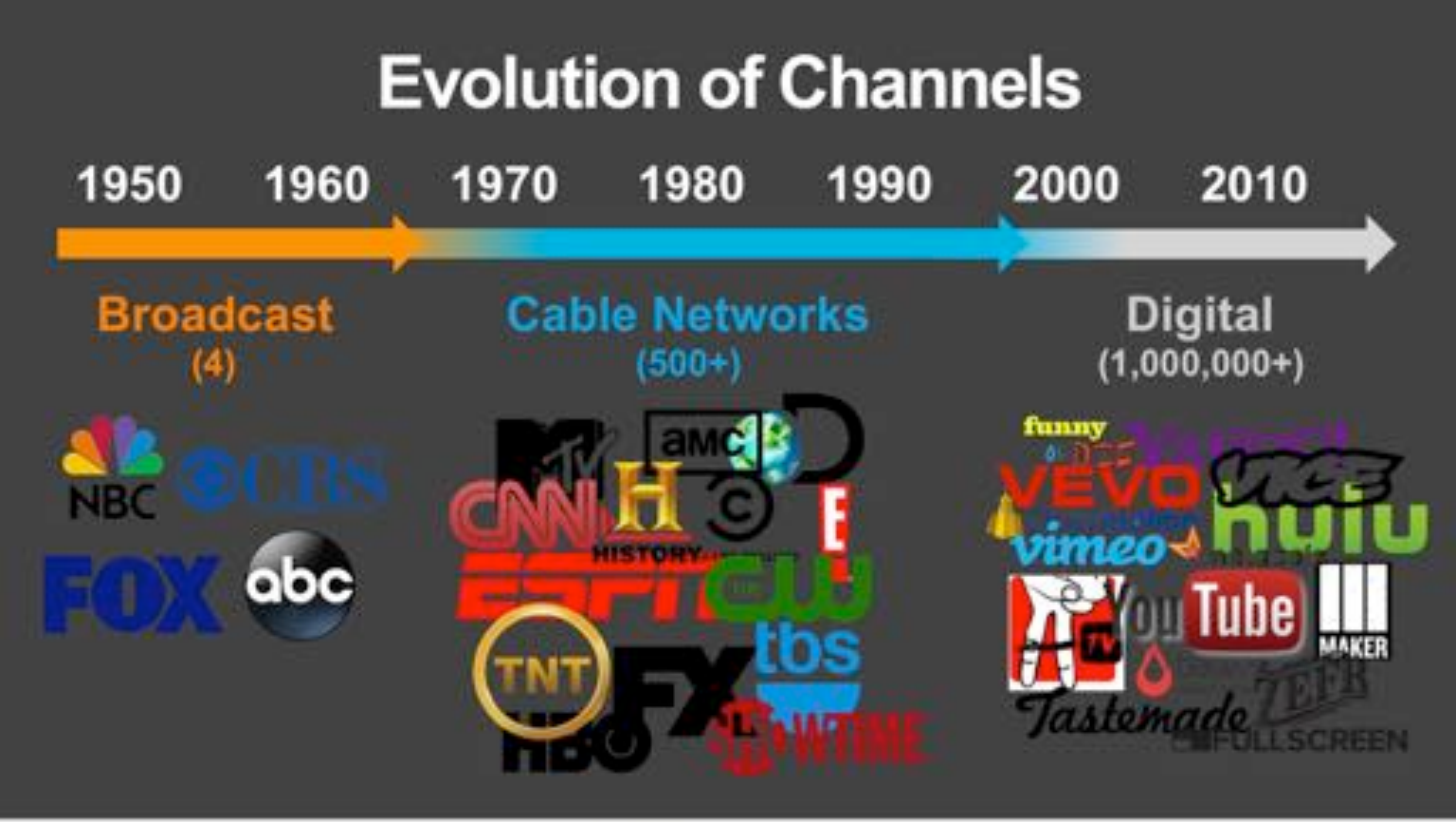
SIMPLICITY of Workflow

PRE-FUNDING of Content

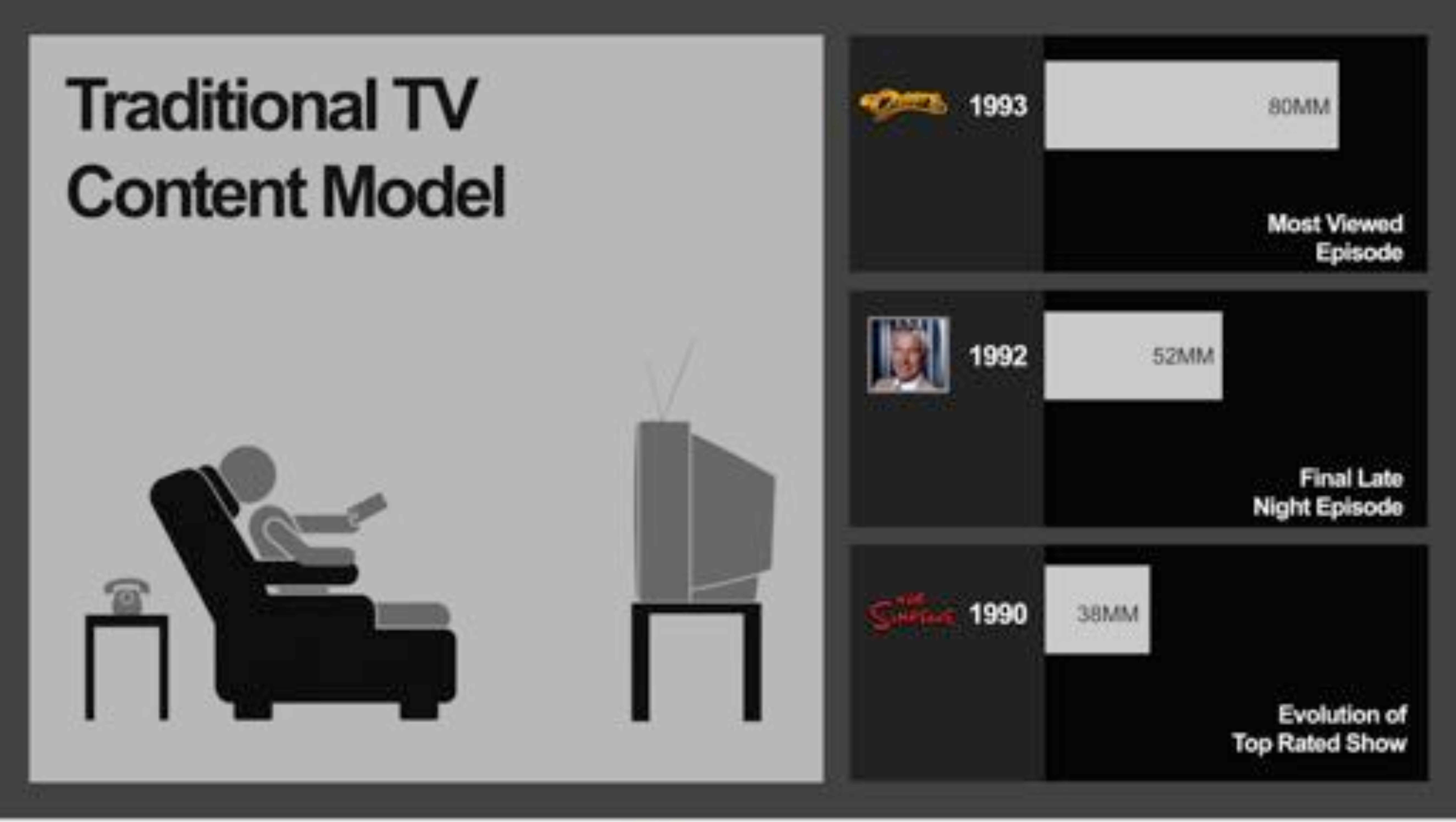
TV Business	Trends	Issues	Theses

1. Fragmentation
2. Device Proliferation
3. Second Screen
4. New Entrants
5. Original Content Production

LUMA partners

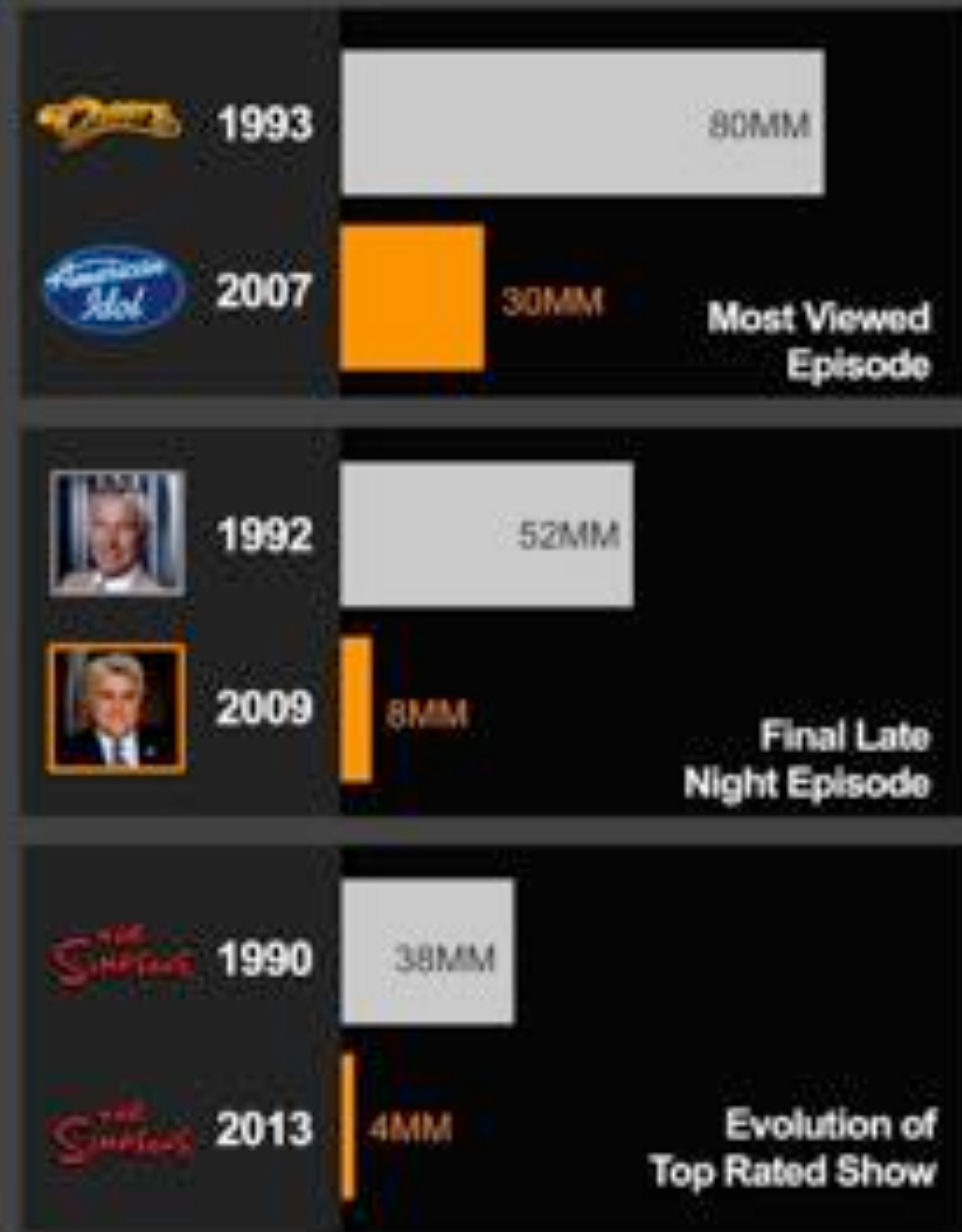


As television has evolved, the channels available to consumers have proliferated exponentially with each new medium. Cable networks brought consumers new, fresh programming across a variety of channels, while digital has provided nearly limitless options to consumers.



Hit shows used to deliver enormous audiences. This meant that it was easy for a marketer to reach an audience at scale at a specific time in conjunction with a specific event / show.

Cross channel devices killed the television star!



Fast forward twenty years and the hit shows don't even have a fifth of the audience they once had and many don't even have a fraction of the audience they once attracted. Increased choice in what and where to consume video content has lead to audience fragmentation.

TV Business | **Trends** | Issues | Theses

1. Fragmentation
2. **Device Proliferation**
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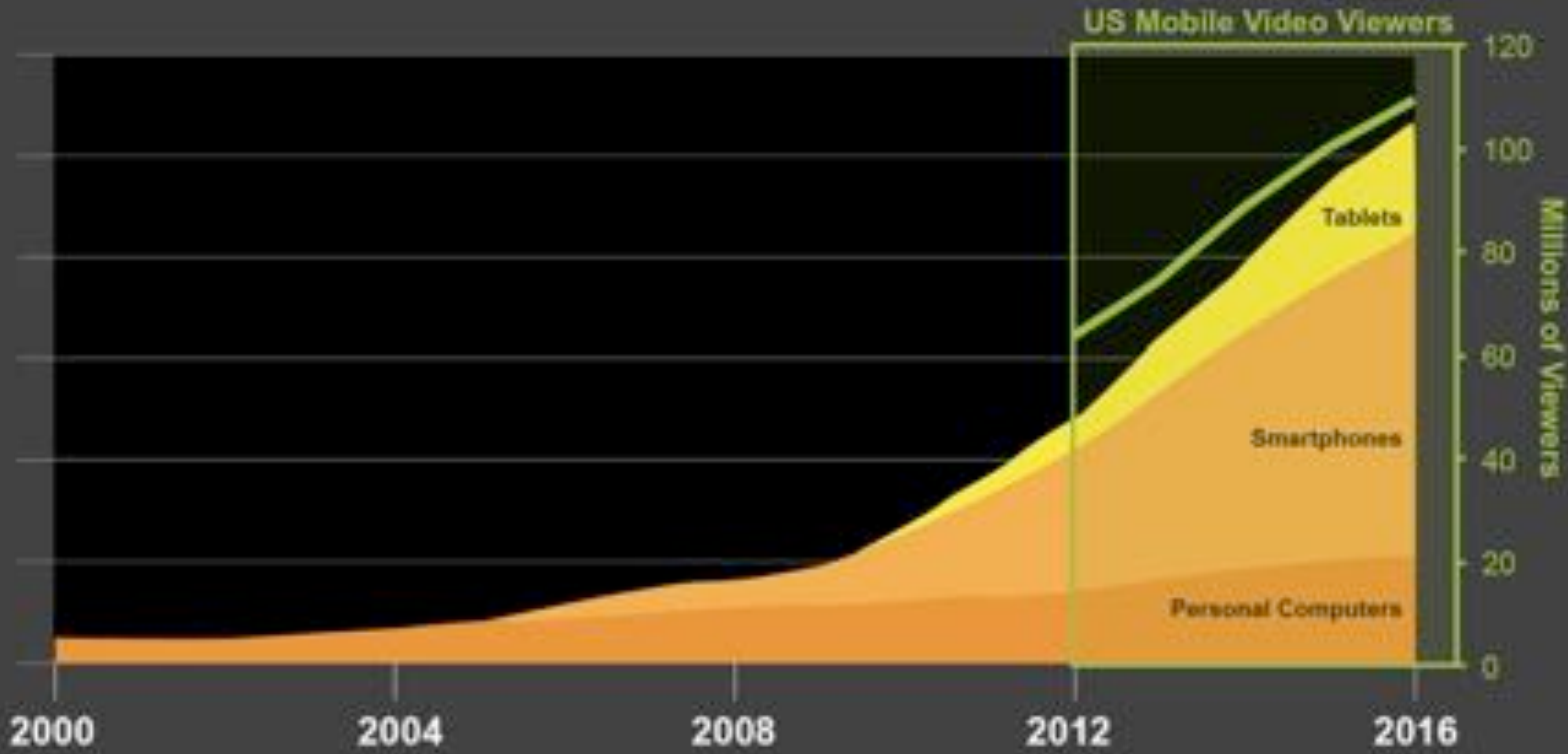
5. Original Content Production

Global Device Sales

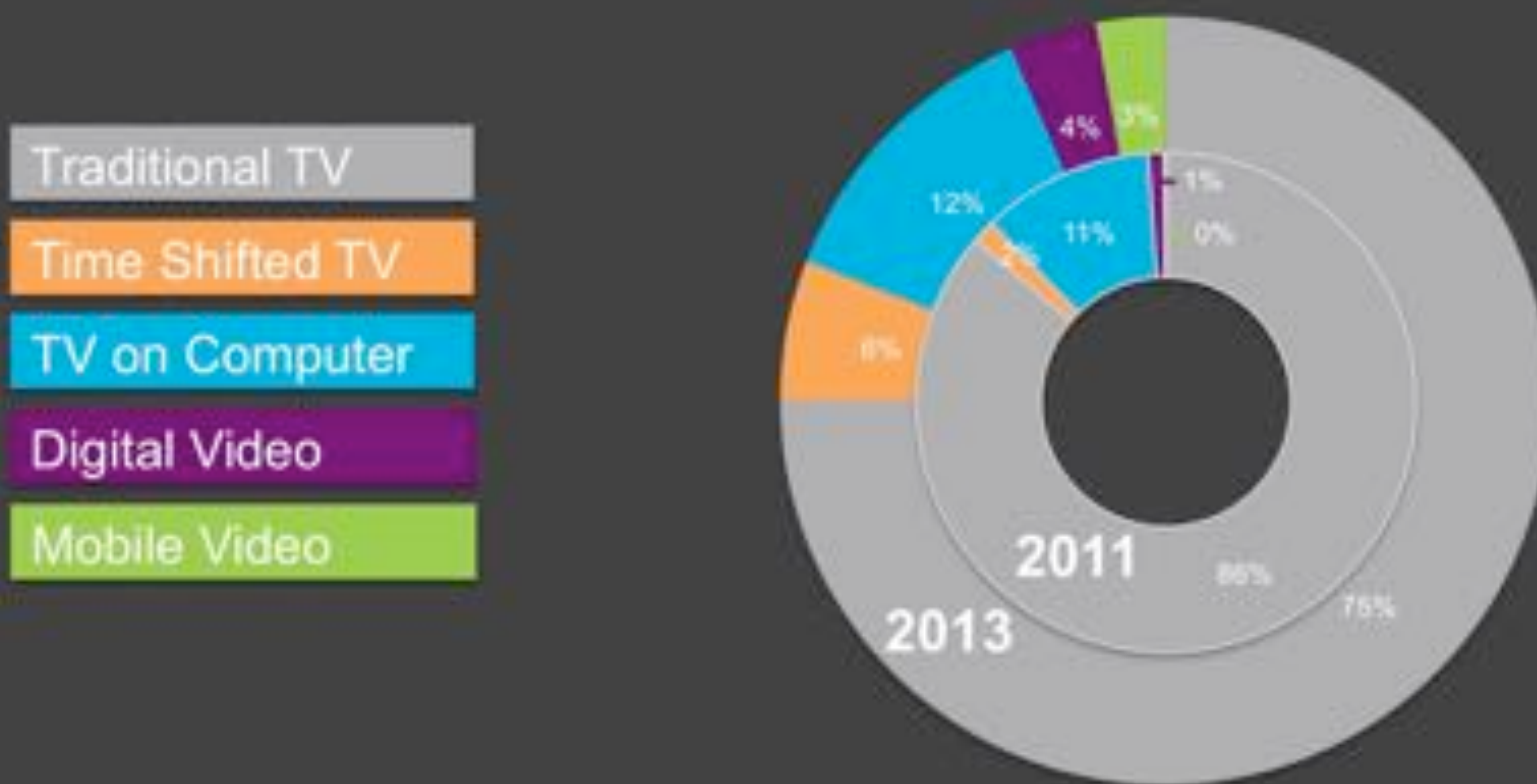


Source: Gartner, IDC, Strategy Analytics, Company Filings, BI Intelligence estimates, eMarketer

The number of devices per household has increased rapidly. We've seen an explosion in smartphone and tablet sales. In line with this device proliferation and bandwidth availability, consumers are spending more time watching video on their mobile devices.

Time Spent is Continuing to Fragment Quickly

Time Spent by Format / Device



Viewing has also timeshifted. People will watch what they want, <u>when</u> they want. We expect this trend to become more pronounced over time.

TV Business	Trends	Issues	Theses

1. Fragmentation
2. Device Proliferation
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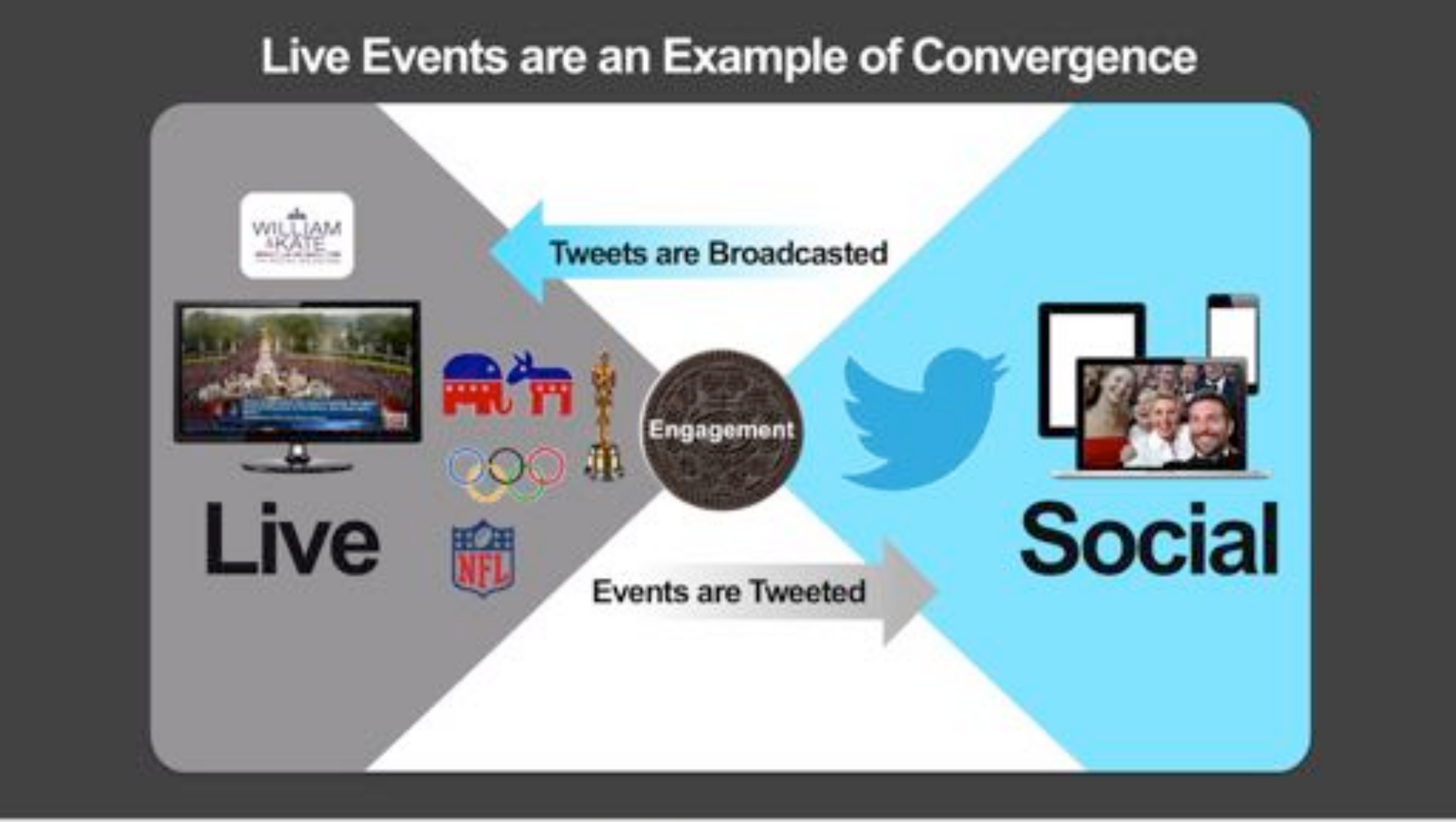

The growing use of a second screen is most effective for live TV, allowing a water cooler effect on steroids. While the second screen provides a great engagement opportunity for advertisers, it doesn't have a significant impact on TV ad revenue.

TV Business	Trends	Issues	Theses

1. Fragmentation
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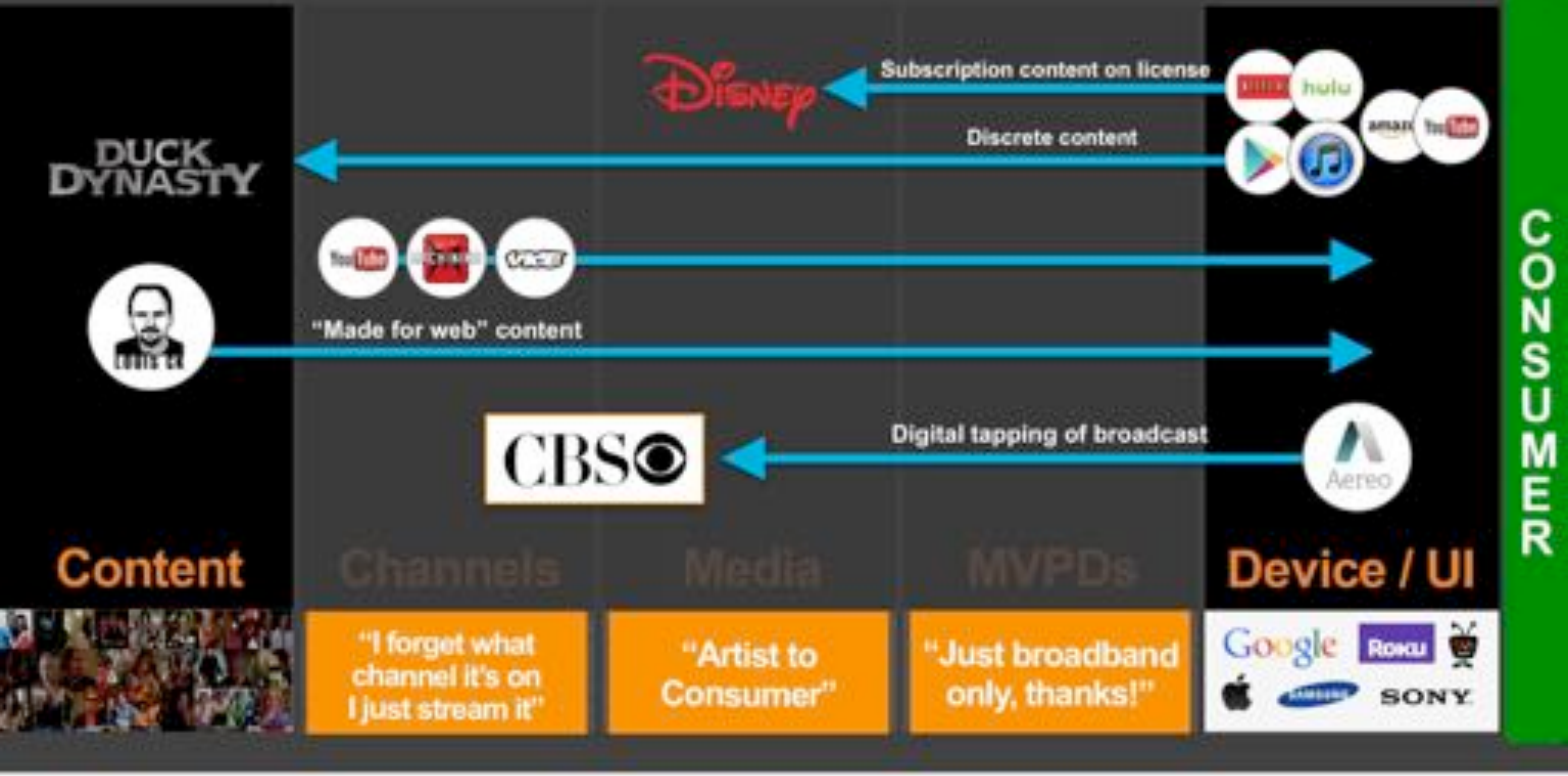
5. Original Content Production

New Entrants: Pursuing Different Strategies

The various new entrants take unique approaches to the opportunity with assets deployed across the spectrum from hardware, software, content and consumer services

The four players with potentially the most impact have lined up assets to capture the converged TV market.

New entrants open different distribution and content strategies

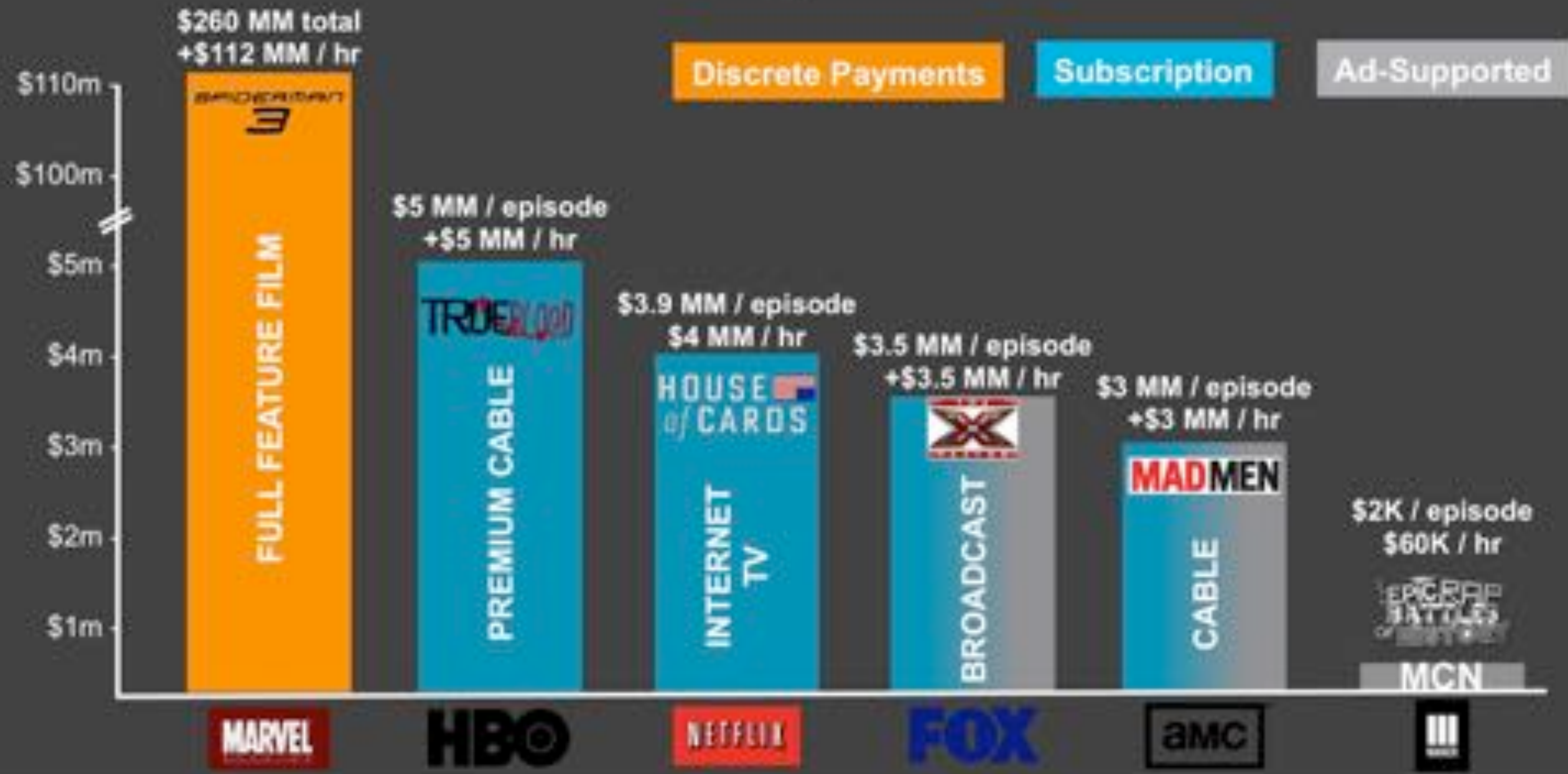


New entrants have varying disruption strategies. Some are coming forward with content solutions while others are focused on delivery, new pricing models or hardware. Netflix and Hulu are disrupting delivery but partnering with the traditional content players while others are bringing their own content directly to the consumer, bypassing all others in the middle.

TV Business | **Trends** | Issues | Theses

1. Fragmentation
2. Device Proliferation
3. Second Screen
4. New Entrants
5. **Original Content Production**

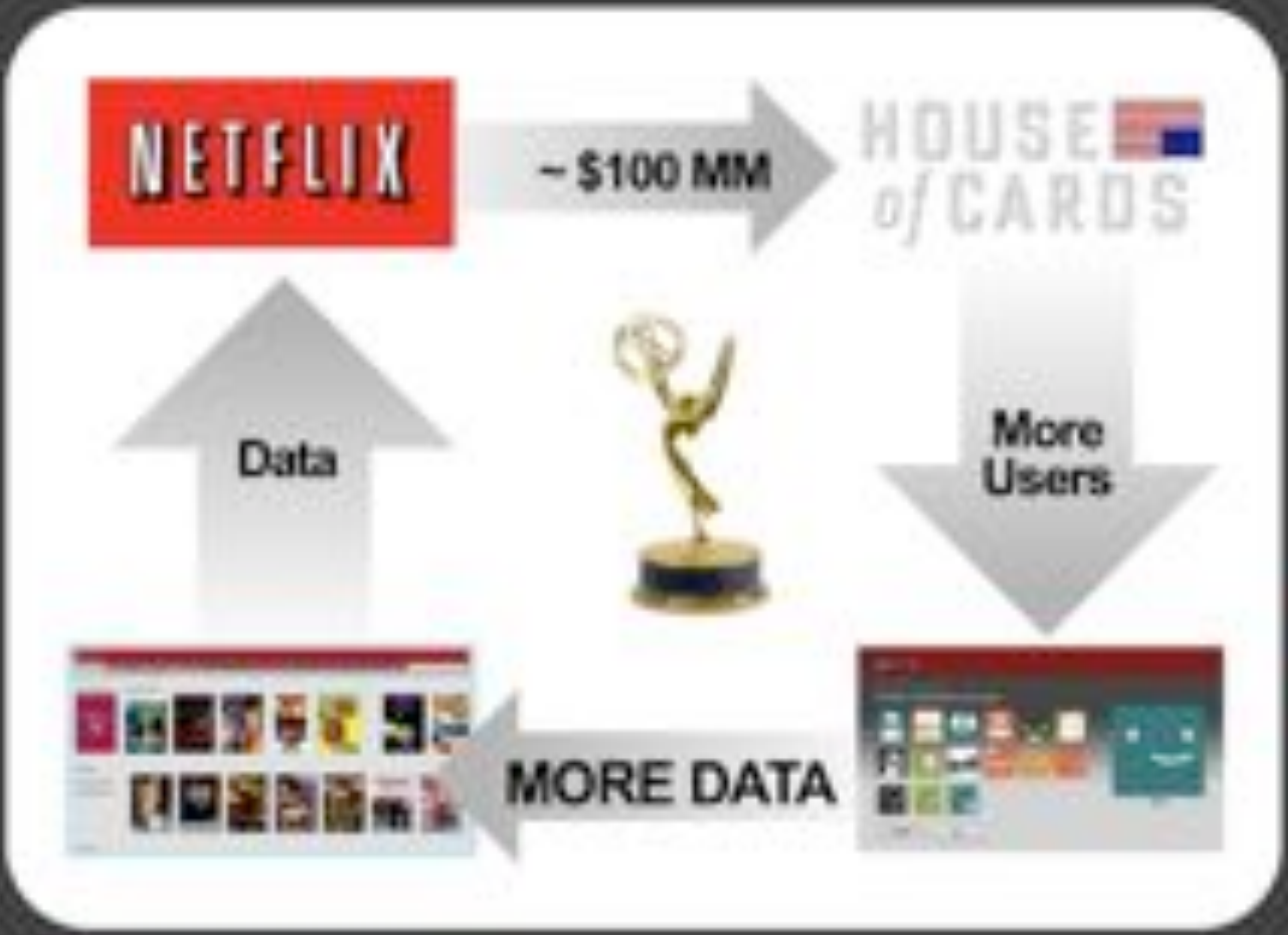
Production Costs per Hour of Content



Production costs have come down substantially for high quality content produced for digital and OTT distribution.

Digital has brought data-driven decisioning to video content creation. A great example of this is Netflix making a two season commitment to House of Cards without seeing a single pilot.

Fundamental reduction in risk to launch pilots and tier 1 shows



NETFLIX

amazon instant video

Amazon is also leveraging data but in a different manner. It is crowdsourcing ideas for pilots then creating mini-pilots that they then test with their actual consumer base. The constant feedback loop that this creates reduces risk and increases the efficiency of creating high-quality content that consumer want to watch.

New entrants launching 20+ new tier 1 shows in 2014

This data-informed approached has opened the door for other players to move into content creation. The names above are not the the usual suspects that come to mind when you think of Hollywood-quality content.

These new tier 1 shows are backed by serious tier 1 talent on the set

These new content creation models have caught the eye of tier-one talent who are not only lending their names to but also funding these new ventures.

Premium UGC = TV

Very Soon	**Household Name**	Yes
Yes	**Lead Role Celeb Status**	Yes
1.1 million	**Episode Views**	3.3 million
$7.60 (overall) $23.03 (in-stream)	**Average CPMs**	$15.63 (cable) $44.11 (network)
~$60K per hour	**Avg. Production Cost**	$3 - $5MM per hour
Yes	**Available on Guaranteed Basis**	Yes

Additionally, as User Generated Content ("UGC") has continued to improve, a new tier of "Premium UGC" has evolved that features characters that begin to look more like TV in terms of celebrity status, viewership and advertising income potential… except at significantly lower production costs.

TV Business | Trends | **Issues** | Theses

1. Digital Disproportionism
2. Antiquated UI/Navigation
3. Standardized Measurement
4. Audience Targeting

What we do online

Search

Buy

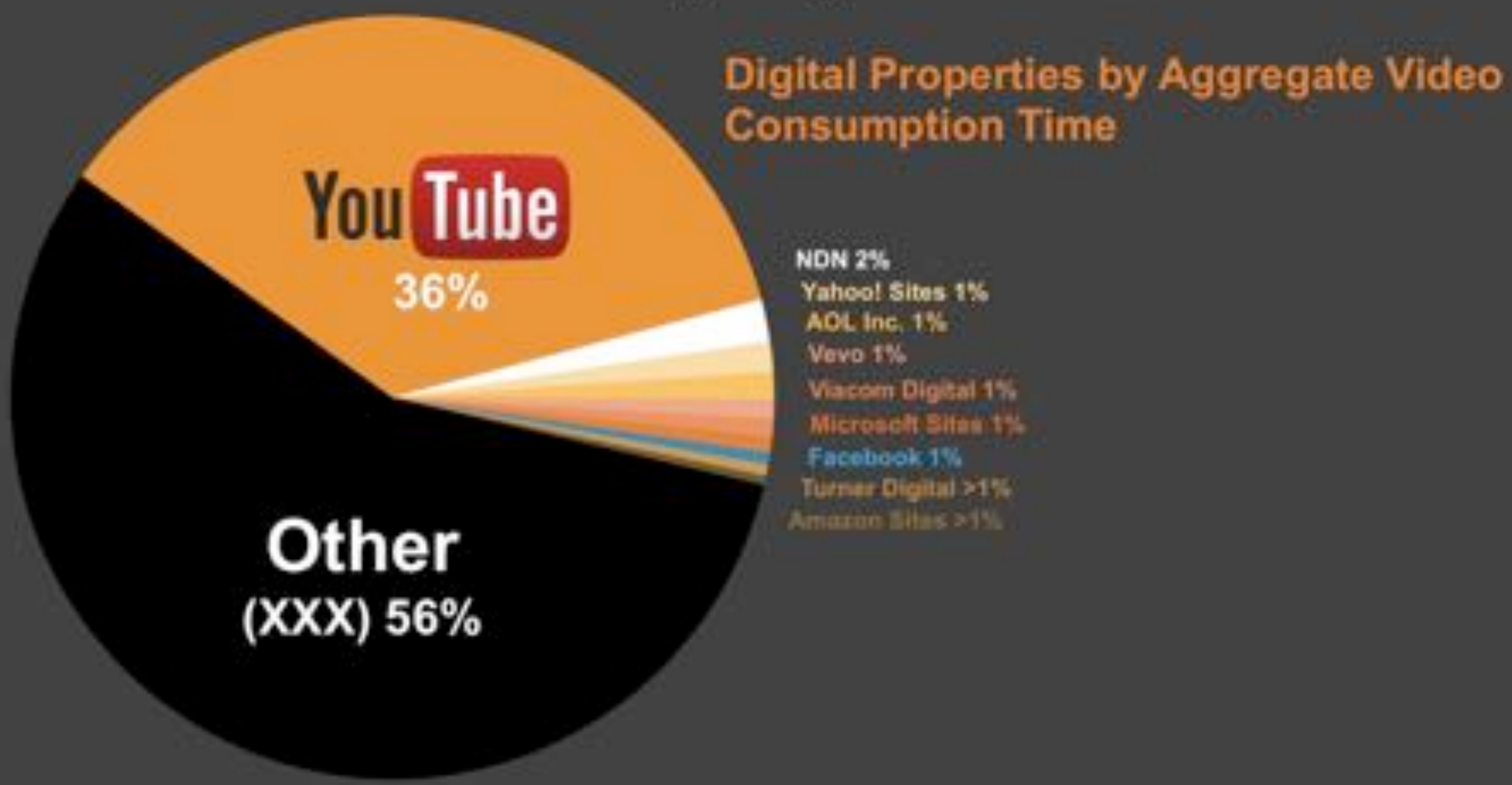
View

Share

LUMA partners

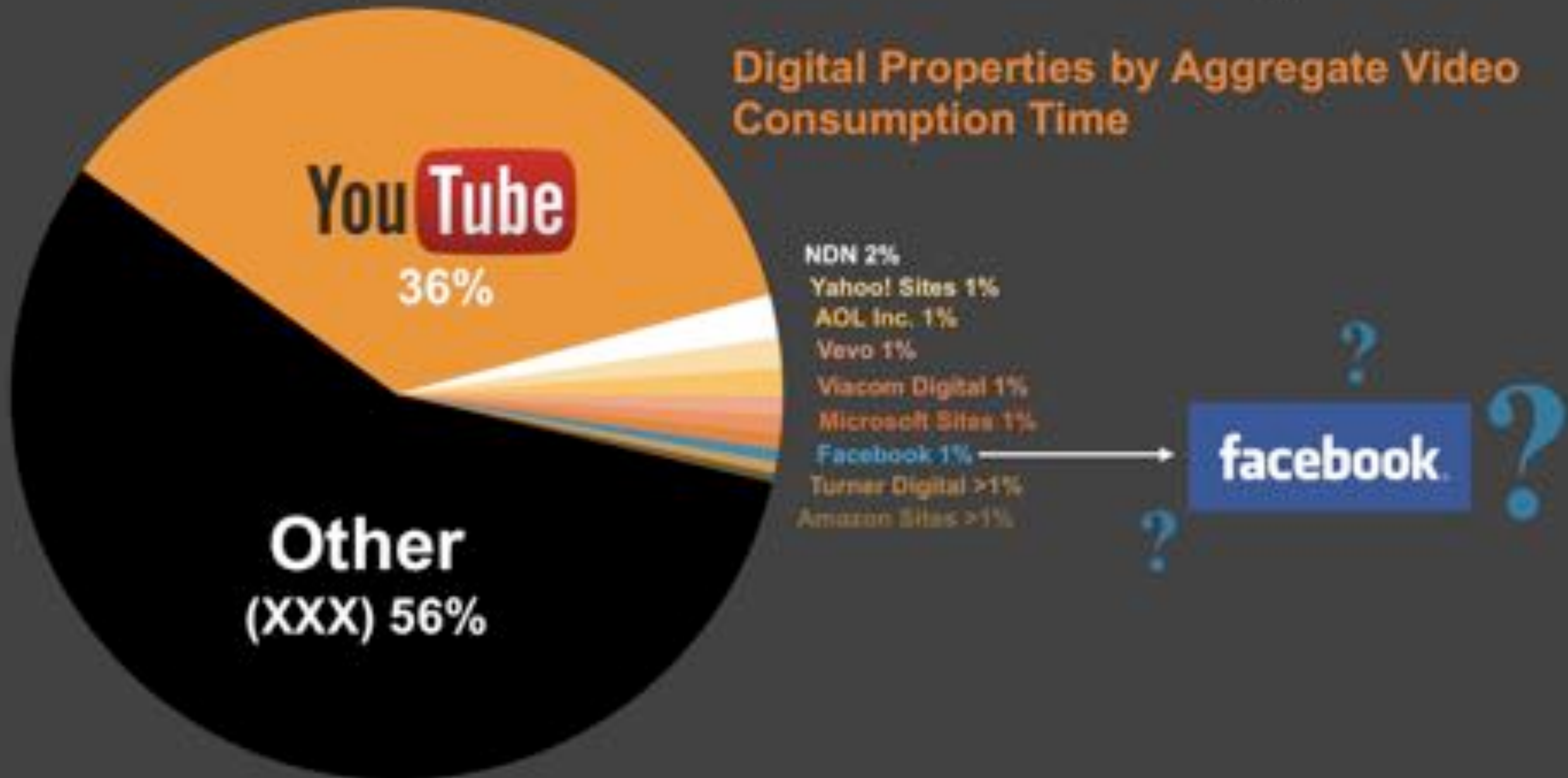
Our concept of digital disproportionism stands for the proposition that often when a channel is dominated by one player, it tends to have a material dampening effect on the entire ecosystem.

Video Disproportionism

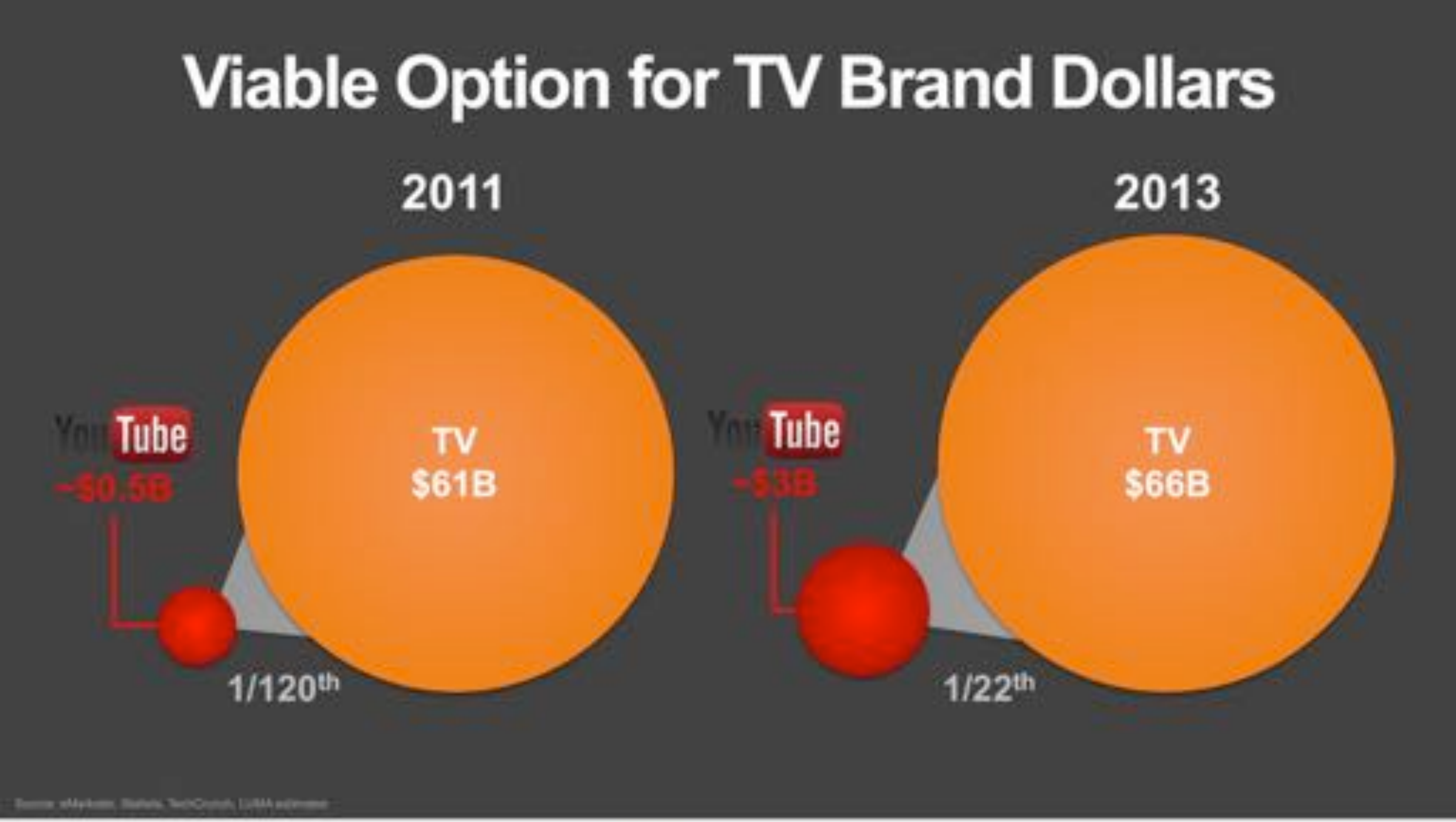


YouTube accounts for over 1/3 of all digital video views, whereas the next largest online property only accounts for 2%. It would likely help the ecosystem if there were a second and third player that were closer in scale to YouTube.

Video Disproportionism – A Rising Force?



All eyes are now set on Facebook as it has recently made a variety of video-related product announcements. Given Facebook's 1.1 billion users, it is a strong contender to be the next large digital video property.



Over the last few years, YouTube has positioned itself as a viable option for TV brand dollars. YouTube advertising revenue has increased by six-fold from 2011 to 2013 and its scale relative to that of the US TV advertising market has grown significantly.

TV Business | Trends | **Issues** | Theses

1. Digital Disproportionism
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Navigation plays a crucial role in the content discovery process. When the discovery of content evolves from linear navigation (old school remotes) to more software-based search and recommendation-driven, it will fundamentally change the economics. A large percentage of ad budgets go to tune in but this will change as consumers go directly to the content.

Consumer is in Control

Control in the digital realm

Consumers now have choice and we might soon see the day when they flip between tabs on their TVs just as they do today on their laptops, let alone skip ads.

TV Business	Trends	Issues	Theses

1. Digital Disproportionism
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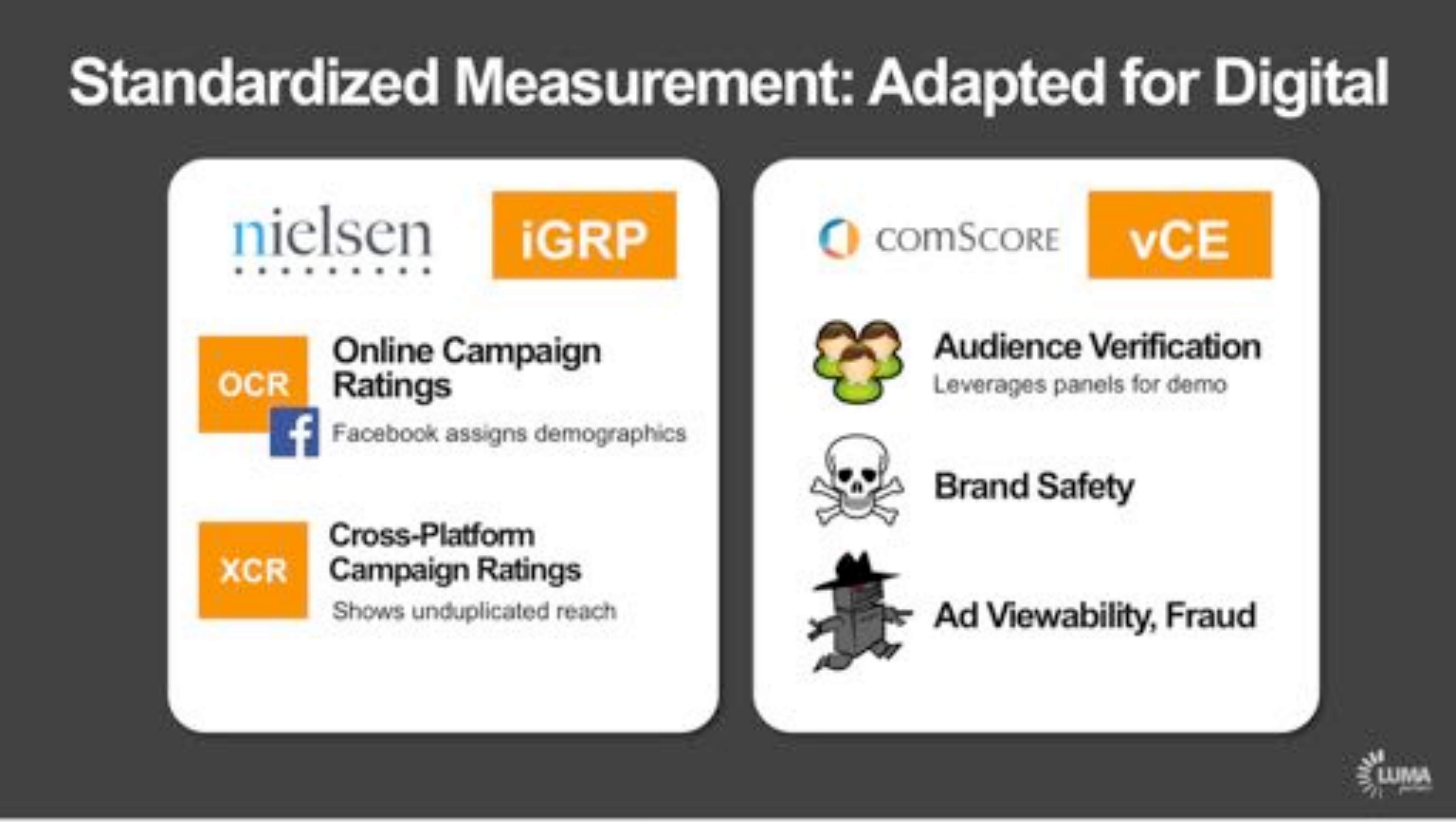

Nielsen owns the currency when it comes to traditional TV. In digital video there are two leading competitors, Nielsen and comScore, with products that help measure audiences with actual census data. The emergence of one clear standard will help accelerate the convergence of TV and digital video.

TV Business | Trends | **Issues** | Theses

1. Digital Disproportionism
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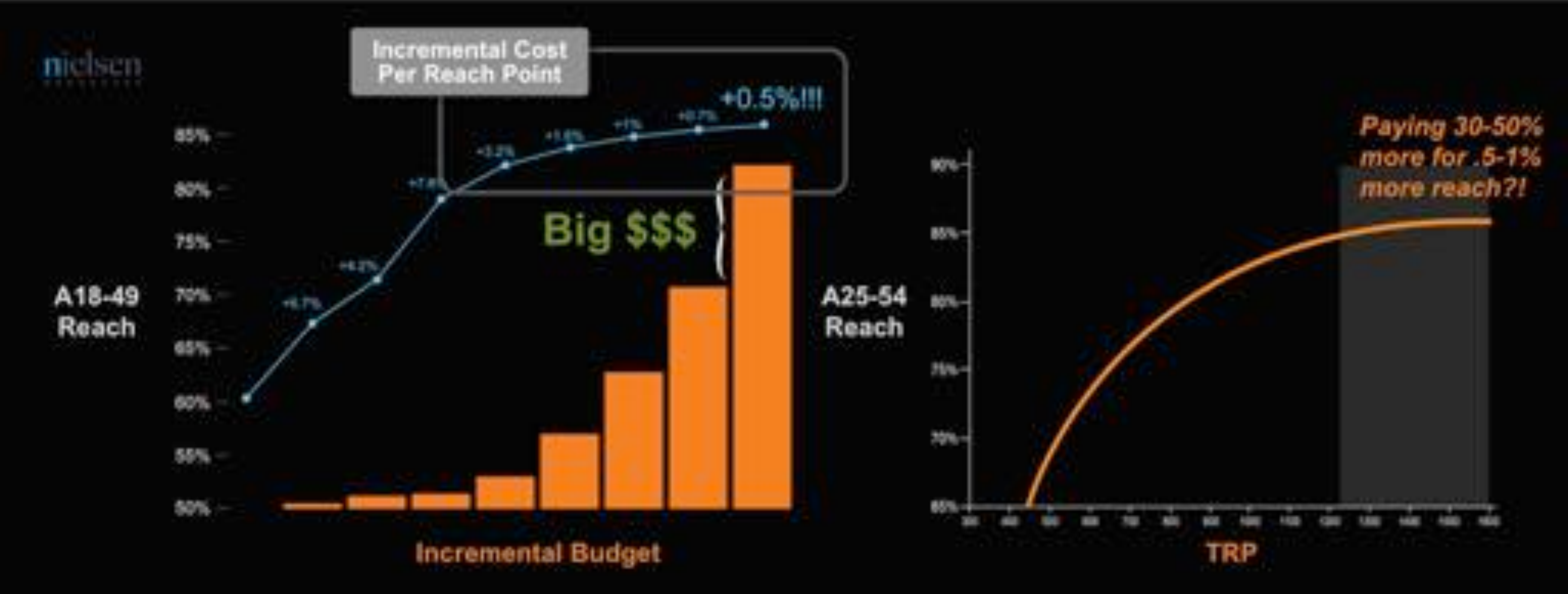
3. Standardized Measurement
4. Audience Targeting

Incremental is increasingly expensive on TV!



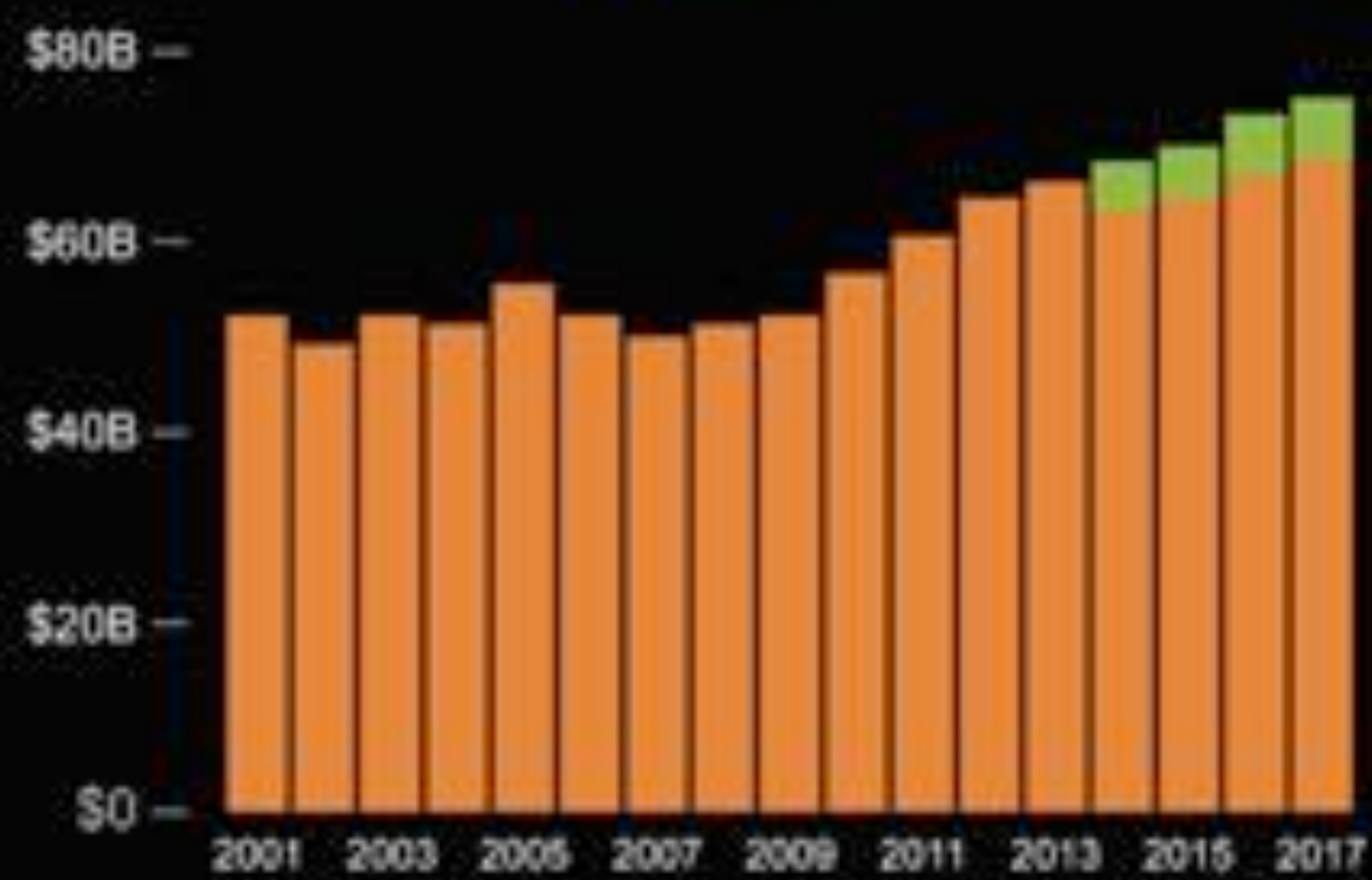
The last GRP, the marginal GPR, is the most expensive. So, with TV fragmentation increasing, so has cost of advertising in an effort to gain the same, large audiences.

Yet TV Dollars aren't slowing…

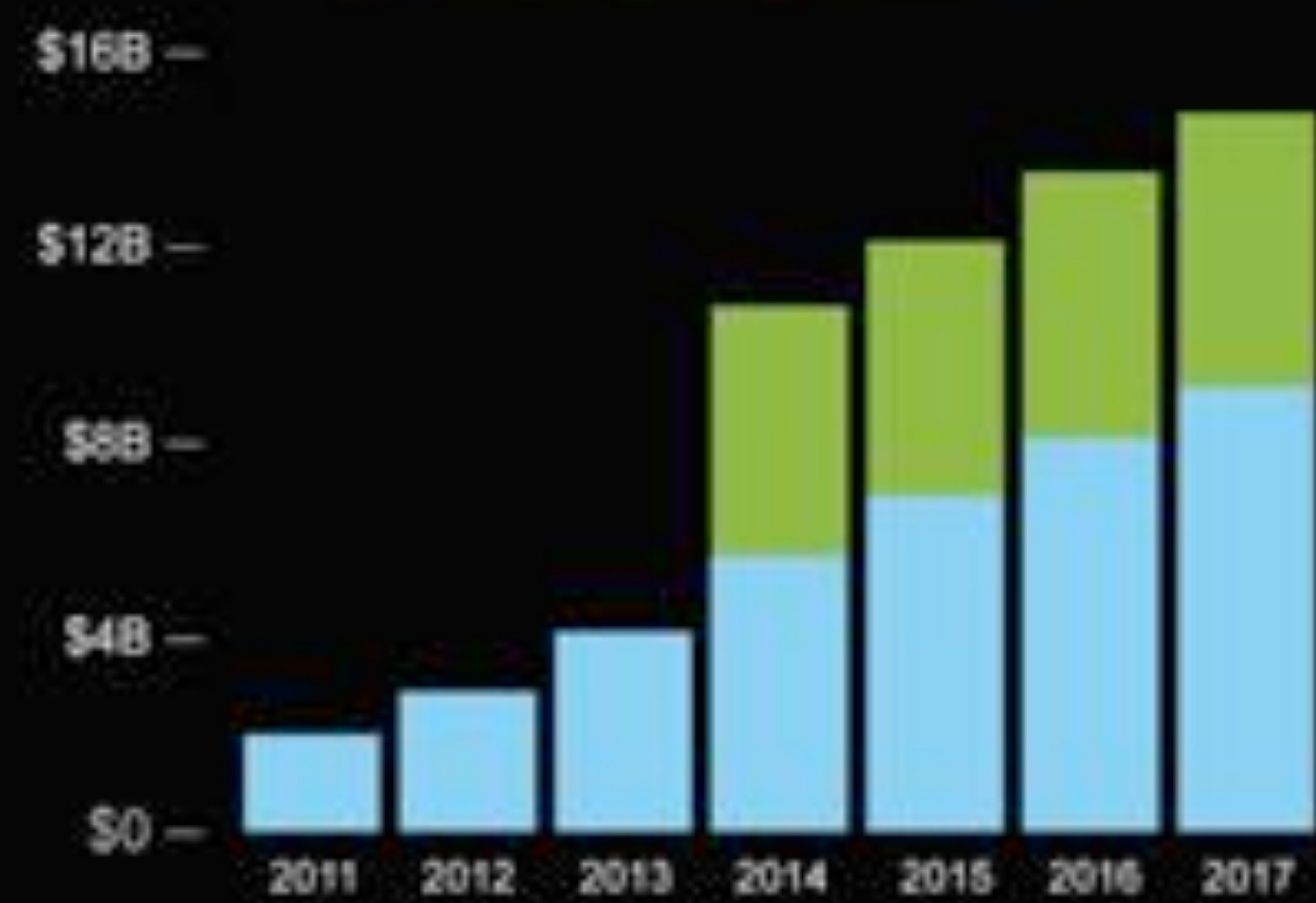
And even with the increasing cost to reach the same audience, TV spend shows no sign of slowing down. Linear television, the one everyone says is going to die, is a growth industry. In fact, television is growing more in absolute dollars than the size of the entire digital video industry.

Digital Video Doubles overnight if 7% inefficient TV is shifted to Digital Video!!!

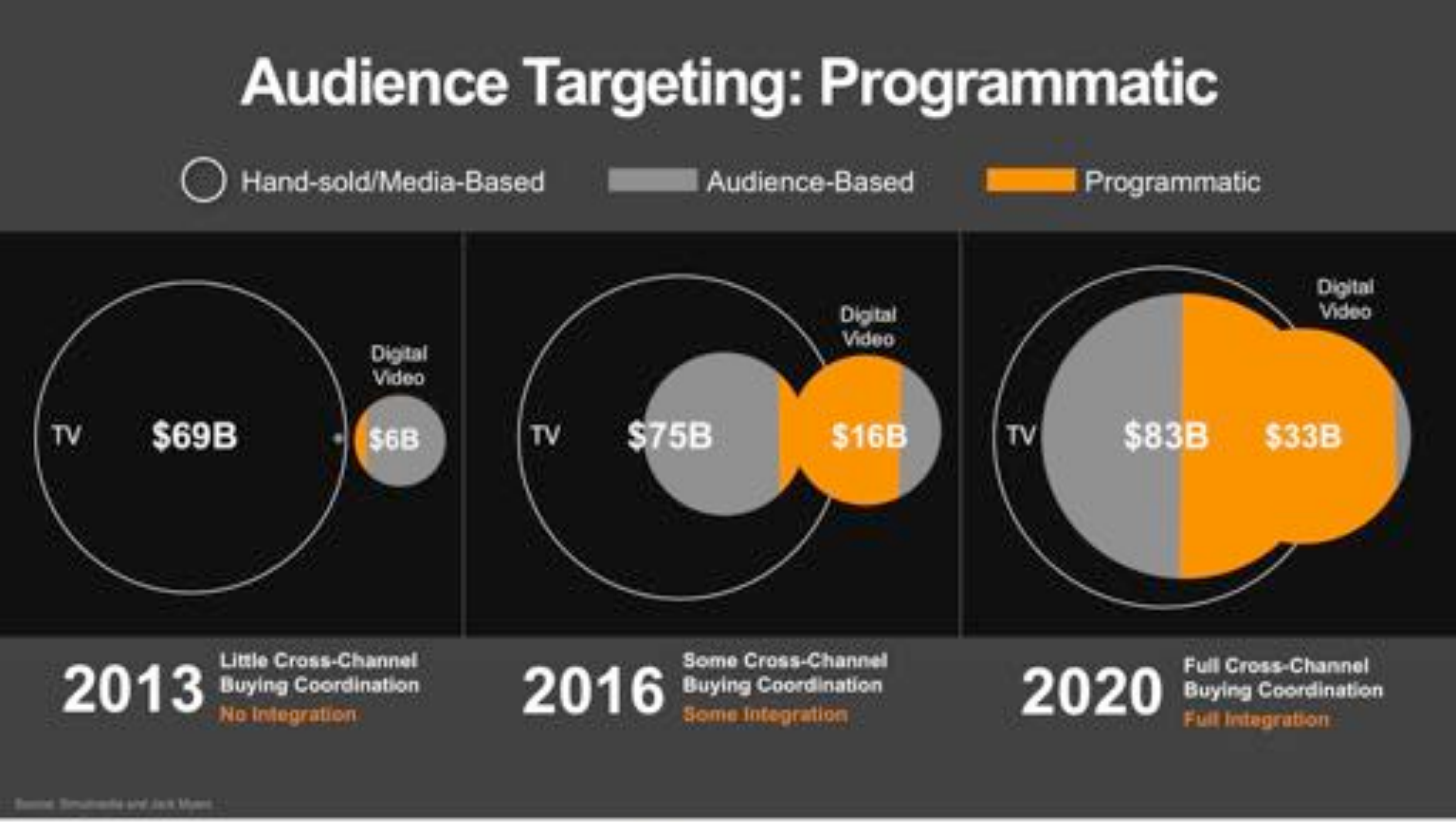
eMarketer TV Spend Projection



eMarketer Digital Video Spend Projection



If you were to take the last 7% of television spend, which is arguably the most inefficient due to getting the least scale per dollar, and apply it to digital, you would double the size of the digital video market. Some studies would argue that up to 25% of that TV spend would be more efficiently used in the digital channel.



Simulmedia and Jack Myers produced a study of what video would look like in the future. They predict that both will be growing and both will leverage programmatic. By 2020, video will be fully addressable so marketers will be able to buy traditional and digital as one.

TV Business | Trends | Issues | **Theses**

1. Convergence
2. Change & Convergence Drive M&A

TV Media Planner

A Tale of Two Planners

Digital Media Planner

The first challenge of convergence is how media is bought in each channel. Today, digital video and traditional are bought very differently and by two very different types of planners.

Their buying goals differ vastly. The TV planner cares about two things: age and gender. The digital planner, on the other hand, is focused on targeted attributes and performance.

How you sell to these different personalities needs to be tailored as they have different incentives.

Convergence changes workflow

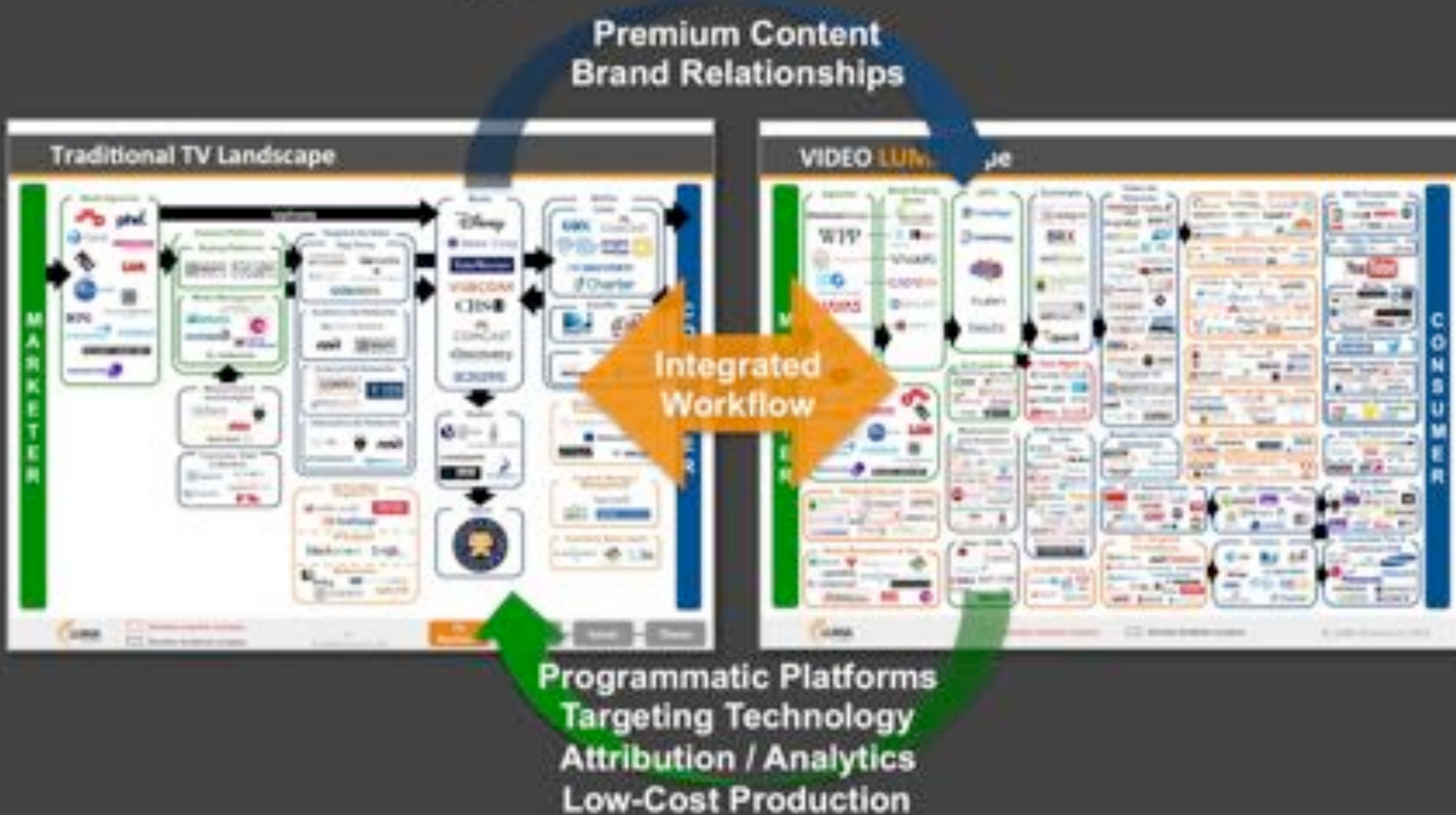
(1) Based on Extreme Reach's customers

Video is the only media format where the exact same creative can be utilized both on large-screen, traditional TVs as well as any other screen. However, the workflow for buying through each of these channels is different and will need to converge.

TV Business | Trends | Issues | **Theses**

1. Convergence
2. Change & Convergence Drive M&A

Convergence of Two Worlds



A key to this convergence will be M&A. The traditional linear TV world brings premium content, brand relationships and a sense of standardization to digital. The digital players bring targeting, attribution, programmatic capabilities and innovative, lower-cost content production. What will ultimately fuse them together will be an integrated workflow.

Convergent TV via M&A

All you have to do is look at recent activity to see that M&A will be the way traditional TV and digital video converge.

Thank You.

@tkawaja

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