www.cablefaxdaily.com, Published by Access Intelligence, LLC, Tel: 301-354-2101

4 Pages Today

Cablefax Daily™

Thursday — July 16, 2015 | What the Industry Reads First | Volume 26 / No. 135

Netflix 2Q: Record Sub Adds; Support for Charter Deal Filed

It was an eventful Hump Day for **Netflix**. Earlier in the day Netflix shares started trading at a post-split price of around $100 following a 7-for-1 stock split that occurred late Tues. And after market closed, the streaming company reported a record 3.3mln new sub additions in 2Q, compared to 1.7mln a year ago. That puts the company's total sub count at 65mln, which includes 42mln US subs and 23mln international subs. And during the day, Netflix, a vocal opponent of the **Comcast/Time Warner Cable** merger, voiced its support for the Charter/TWC deal in an **FCC** filing. Pleased with Charter's no-fee interconnection policy that lasts through the end of 2018, Netflix said the practice is "a welcome and significant departure from the efforts of some ISPs to collect access tolls on the internet." And applying the policy across the new Charter footprint is "a substantial public interest benefit and will support scaling the Internet to meet consumers' growing demand… Accordingly, Netflix supports the proposed Charter-Time Warner Cable transaction if it incorporates the merger condition proposed by Charter," Netflix said. The company struck peering deals with several major ISPs including Comcast last year. If the merger goes through, other SVOD companies will benefit, said CEO *Reed Hastings* during the earnings call. During 2Q, the company gained 0.9mln new subs in the US and 2.4mln members internationally. However, profit fell more than 63% YOY as programming costs increased. Profit was also impacted by a strong US dollar, which lowers the value of international revenue. In the US, revenue grew a solid 22.4%, driven by a 5% YOY gain in average subscriber profit. That's partly thanks to an uptake in Netflix's HD 2-stream plan. The company continues to target a 40% US contribution margin by 2020. It's forecasting 3Q US net adds of 1.15mln, slightly higher than the year-ago period. A big part of the earnings interview was on international expansion. Netflix plans to launch in 200 countries by the end of next year, with Portugal, Japan, Italy and Spain slated to join before year-end. Citing **Hulu**'s initial unsuccessful attempt to launch in Japan, Hastings said Netflix will price its service more aggressively and will include local content. "Japan is a unique market because it's brand sensitive… But it might be our best market in the long-term" once Japanese consumers embrace the Netflix brand, Hastings said. He noted several Japanese consumer electronics companies such as **Sony** and **Toshiba** are interested in integrating Netflix with their platforms. When it comes to a potential China launch, "we still need to figure a few things out," Hastings said. With more pay-TV ops offering skinny TV programming options, will Netflix be part of the bundles? Probably not. "We would

CABLEFAX DAILY (ISSN 1069-6644) is published daily by Access Intelligence, LLC ● www.cablefax.com ● 301.354.2101 ● Editorial Director: Amy Maclean, 301.354.1760, amaclean@accessintel.com ● Associate Publisher: Michael Grebb, 323.380.6263, mgrebb@accessintel.com ● Editor: Joyce Wang, 301.354.1828, jwang@accessintel.com ● Sr Community Editor: Kaylee Hultgren, 212.621.4200, khultgren@accessintel.com ● Advisor: Seth Arenstein ● Dir. of Business Dev.: Rich Hauptner, 203.899.8460, rhauptner@accessintel.com ● Jr. Acct. Exec: Olivia Murray, 301.354.2010, omurray@accessintel.com ● Dir of Market Dev: Laurie Hofmann, 301.354.1796, lhofmann@accessintel.com ● Production: Joann Fato, jfato@accessintel.com ● Diane Schwartz, SVP Media Comms Group, dschwartz@accessintel.com ● Group Subs: Laurie Hofmann, 301.354.1796, lhofmann@accessintel.com ● Sub Questions, Client Services: 301.354.2101, clientservices@accessintel.com ● Annual subscription price: $1,649/year ● Access Intelligence, LLC, 4 Choke Cherry Road, 2nd Floor, Rockville, MD 20850

always want to be separately priced," Hastings said. Meanwhile, Hastings is bullish on UltraHD. Over time, he expects a significant percentage of Netflix subs to upgrade to the UHD service as more UHD TVs become available. Finally, did we mention that Hastings wore a BoJack Horseman (Netflix's adult-oriented animated series) sweater on the earnings call? "The most important thing about this call is to let you know that... BoJack Horseman season two launches on Friday… So we hope everyone will have a great binge weekend on one of the most incredible shows," the Netflix co-founder said.

All-Star Blackout: Last week came the wind-up and the pitch as **Mediacom** petitioned the **FCC** to update retrans rules. The crack of the bat came Tues when **Media General** stations in 14 markets went dark at 6pm ET, just before the start of the **MLB** All-Star Game on **Fox**. This retrans blackout, the 2nd in the past month for Mediacom, impacted 17 stations, including the Fox affils in Topeka and Terre Haute, IN. Something notable about this dispute—it's happening in the back-yard of **Sen Communications** subcmte chmn *John Thune* (R-SD) as it impacts the **CBS** and **MyNetworkTV** stations in the Sioux Falls, SD, market (his constituents). Thune was a backer of the Local Choice proposal last year, which would let consumers choose to pay for local broadcast stations, similarly to how they pay for premium nets such as **HBO**. Not all Media General stations are dark on Mediacom because the stations that expired Tues were previously owned by **LIN Media**. The rest of Media General's stations come up for Mediacom later this year, with the broadcaster seeking to combine the agreements into 1 new contract that includes the LIN stations the broadcaster acquired in Dec. As usual, price seems to be the factor. "We are disappointed in the outcome of our negotiations, especially since we have successfully reached deals with every major cable, satellite and telecommunications company that recognizes our fair market value," Media General said. Mediacom issued an open letter to customers, declaring that the broadcaster wants twice the price it paid them for the prior 3 years. "If we agreed to Media General's demands, [NBC affil in Davenport, IA] **KWQC** would have become the most expensive broadcast channel in all of the 1,500 communities that Mediacom serves across 22 states. Further, other broadcasters would follow and begin demanding to be paid the same as Media General, driving up costs for other channels on your lineup," said the letter from Lincoln Region vp *Todd Curtis*. Mediacom is moving some networks in higher tiered packages, including **Hallmark Channel** and **NBCSN**, into the broadcaster's channel slots. While the LIN stations have a new owner, there's a history between the 2 with the same stations going dark for 6 weeks on Mediacom in 2011. On May 31, Mediacom lost **Granite Broadcasting** stations for nearly 2 weeks as the companies hammered out a new agreement. Mediacom's retrans pitch to the FCC includes preventing blackouts unless signals are available free OTA or via Internet streaming to 90% of homes in a relevant market. Last year, the MSO filed a petition on forced bundling and programming costs. Mediacom subs have company in blackout land: **Dispatch** stations have been dark on **DISH** since June 16.

HUD, Obama and Broadband: Pres *Obama* along with the **Department of Housing and Urban Development** announced on Wed the **ConnectHome** initiative, which is aimed at bringing high-speed broadband to more families. The pilot program will begin in 28 communities around the nation, with participating providers including **Cox, Google Fiber, Suddenlink, Vyve Broadband** and **CenturyLink**. Google Fiber will offer free monthly home Internet service to select public housing residents in Atlanta, Durham, Kansas City and Nashville, while Vyve, Suddenlink, **Pine Telephone** and **Cherokee Comm** are working together to offer low-cost Internet to the Choctaw Nation of OK. CenturyLink's offer in Seattle and across it footprint is for $9.95/month the first year and $14.95 the next 4 years. Cable already works to provide low-cost Internet to families with students who qualify for free lunch through **Connect2Compete**. Cox led that initiative by voluntarily offering low-cost Internet to students who qualify for free lunch back in 1999. Cox noted that while the HUD program is only in 4 cities in its footprint, it will continue to offer its $9.95/month program in all 18 states it serves for families who qualify for free lunch. Comcast isn't part of ConnectHome, but continues its Internet Essentials program, offering deeply discounted Internet to free and reduced lunch families. Comcast said it welcomes the administration's efforts to connect more low-income Americans to broadband. "Comcast has the country's largest and most comprehensive low-income broadband adoption program, having already connected more than 1.8 million Americans," read a company statement. "We also note that studies show that the main barrier to broadband adoption is a complex set of relevance, digital literacy, and awareness issues, and we've been working in local communities to overcome those issues and look forward to these additional efforts." **Charter** also isn't a part of ConnectHome, but it has announced plans to expand and enhance a broadband adoption program currently offered by **Bright House** as a condition of its acquisitions of **Time Warner Cable** and Bright House.

Incentive Auction: Turns out the **FCC** won't consider 2 spectrum incentive auction items at Thurs' meeting after all. Chmn

BUSINESS & FINANCE

Tom Wheeler opted to postpone their consideration until the Aug 6 open meeting. Earlier this week, **House Commerce** chmn *Fred Upton* (R-MI) and Communications subcmte head *Greg Walden* (R-OR) wrote to Wheeler and urged him to delay the vote, saying the agency lacks the data needed for a rulemaking. **NAB** isn't happy with the postponement. "The FCC's original incentive auction order fashioned a careful compromise allowing licensed wireless microphones and unlicensed users to operate in the duplex gap. The FCC could easily have voted tomorrow on an order maintaining this balanced approach and not delayed the process," said a spokesman.

People: **House Commerce** chmn *Fred Upton* (R-MI) named *Mike Bloomquist* deputy staff dir, succeeding *Alexa Marrero,* a longtime Hill vet who's leaving the committee to relocate to Chicago. Bloomquist previously served as the committee's general counsel, before joining the private sector. -- **BBC Worldwide North America** appointed *Dawn Williamson* to svp, ad sales and *Tim Wastney* to vp, ad sales. Williamson will report to *Carolyn Gibson*, evp of BBC Advertising, and *Nick Ascheim*, svp of consumer digital, BBC Worldwide North America. She was most recently vp at **CNN International** ad sales, Americas. Wastney will report directly to Williamson. He was formerly vp of global business intelligence for BBC Advertising.

Cablefax Daily Stockwatch

Company	07/15 Close	1-Day Ch
BROADCASTERS/DBS/MMDS		
DIRECTV:	93.01	0.35
DISH:	69.05	(0.2)
ENTRAVISION:	7.94	(0.21)
GRAY TELEVISION:	17.09	0.06
MEDIA GENERAL:	16.75	0.27
NEXSTAR:	55.77	1.35
SINCLAIR:	29.74	(0.07)
TEGNA:	32.49	0.38
MSOS		
CABLE ONE:	394.68	4.32
CABLEVISION:	27.49	0.69
CHARTER:	181.00	3.92
COMCAST:	63.75	0.51
COMCAST SPCL:	63.35	0.35
GCI:	17.98	(0.12)
LIBERTY BROADBAND:	53.98	0.90
LIBERTY GLOBAL:	51.74	1.01
SHAW COMM:	21.12	(0.21)
SHENTEL:	34.42	(0.46)
SHENTEL:	34.42	(0.46)
TIME WARNER CABLE:	186.00	2.53
PROGRAMMING		
21ST CENTURY FOX:	33.93	0.27
AMC NETWORKS:	85.61	0.17
CBS:	55.37	(0.03)
CROWN:	4.64	0.03
DISCOVERY:	33.92	(0.09)
DISNEY:	118.30	0.45
GRUPO TELEVISA:	36.24	0.16
HSN:	71.90	(1.54)
LIONSGATE:	37.29	(0.11)
MSG:	83.26	(0.84)
SCRIPPS INT:	66.31	0.09
STARZ:	45.48	0.53
TIME WARNER:	90.48	0.49
VIACOM:	61.62	(0.53)
WWE:	16.96	0.11
TECHNOLOGY		
ADDVANTAGE:	2.25	0.01
AMDOCS:	56.40	0.06
AMPHENOL:	55.00	(0.15)
APPLE:	126.82	1.21
ARRIS GROUP:	31.51	(0.14)
AVID TECH:	13.15	0.15
BLNDER TONGUE:	0.91	0.11
BROADCOM:	52.79	(0.06)
CISCO:	28.11	0.08
COMMSCOPE:	26.02	0.06
CONCURRENT:	6.39	0.13
CONVERGYS:	25.83	0.03
CSG SYSTEMS:	31.55	(0.32)
ECHOSTAR:	47.86	UNCH
GOOGLE:	560.22	(0.88)
HARMONIC:	6.95	(0.04)
INTEL:	29.69	0.04
INTERACTIVE CORP:	82.19	(2.4)
JDSU:	11.15	(0.13)
LEVEL 3:	51.93	(0.68)
MICROSOFT:	45.76	0.14
NETFLIX:	98.13	(2.24)
NIELSEN:	45.56	(0.04)
RENTRAK:	70.49	UNCH
SEACHANGE:	7.24	0.02
SONY:	27.92	(0.38)
SPRINT NEXTEL:	3.84	(0.16)
TIVO:	10.32	(0.14)
UNIVERSAL ELEC:	50.71	0.17
VONAGE:	4.85	0.04
YAHOO:	38.38	(0.25)
TELCOS		
AT&T:	34.73	(0.39)
CENTURYLINK:	29.67	(0.31)
TDS:	29.17	(0.31)
VERIZON:	47.33	(0.08)
MARKET INDICES		
DOW:	18050.17	(3.41)
NASDAQ:	5098.94	(5.95)
S&P 500:	2107.40	(1.55)

Think about that for a minute...

Glut

Commentary by Steve Effros

You can never have too much of a good thing, right? Wrong. The industry may be in the middle of a cycle of so many extraordinarily "good things" being delivered that when the pendulum starts to swing in the other way it's going to get ugly.

From the consumer's point of view the "good things" are starting to come fast and furious. There are so many new competitors seeking to get the consumer to use their service for video delivery, for instance, that the list of available options is never accurate by the time the ink dries; cable, satellite, Roku, HBO, Hulu, Netflix, Chromecast, Xbox, Playstation, Apple TV, Amazon Instant Video, etc. They're all offering different ways for the consumer to choose and view video product.

The problem is, now that there's full-throated competition to be the aggregator of video content, the competitors have to start differentiating themselves in order to justify their offerings. Given that most are not actually the one delivering the products (hence the consumer has to buy both the aggregated content and a delivery company... read cable, broadband or satellite) and at the same time many of the competitors have very similar program lineups or libraries of films and many television series, differentiation comes down to locking up exclusive product. Hence HBO has "Game of Thrones" or Netflix has "House of Cards." I've discussed this before and won't go into the new business models for creating that programming such as Amazon's. It's important, but not here.

The issue here is that folks, after they consume the "exclusive" material, are left with a very large library of alternatives, some of which are really good, and a lot which failed in their first outing, and deserved to. The first challenge is to figure out which is which. To be sure, you could use a measure of what is most "popular." But that doesn't work for many of us. You could also rely on reviews, or "recommendation engines" like TiVo's. However, no matter how those choices are made, what you will find with all that backlogged syndicated product is that there is far more material out there than you have the time, or in most cases the willingness to view. There's a glut.

I fear that just as with the real estate bubble, or the stock market bubble, the rapidly inflating bubble of available programming for viewers is going to, sooner rather than later, result in the "bubble" bursting. What does that look like? Well, there are several aspects to this. Just as with cable in the early days, when we heard "57 channels and nothing to watch," we are starting to hear the same thing about, for instance, the Netflix film library. Sure, there's a lot there, but "...I've already watched all the good ones." The same is true for the "original" material, especially if it is released all at once. After you've watched the whole series in a marathon session, then what? As any programmer can tell you, creating the really good stuff is hard and only happens occasionally. Look at all the Netflix series you've never heard of to appreciate that point.

So what happens? More money for more exclusive product? That will result in a lot of the current "players" consolidating or falling by the wayside. The big get bigger? Probably. Increasing costs for promotion rather than product? Likely. Higher prices? Sure. These are not "unintended consequences." They're predictable, and those who insist "more is better" are going to be responsible for the results.

Steve

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