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Global Research Unlocked

Next episode of the growth narrative for streaming video companies

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Media and Entertainment
United States

Thomas (T.J.) Thornton
Head of Research Marketing
BofAS
+1 646 855 2449
thomas.thornton2@bofa.com

Jessica Reif Ehrlich
Research Analyst
BofAS

Key takeaways

- BofA Global Research analysts join the podcast to discuss emerging risks, opportunities, and growth themes in global markets.
- The shift to more ad supported streaming content is an important driver of subscribers, revenues and bunding opportunities.
- Jessica joins to discuss various ways that streaming services can continue to grow, and when content investment might slow.

Bundling, targeted ads among streaming growth drivers

Streaming video choices have ballooned over the last decade and leading streamers are already reaching well over half of US households. But there are still a number of compelling growth drivers. The crackdown on password sharing is underway and can boost subscribers, so can bunding deals, such as those with wireless companies and there's still room for much better ad targeting. Meanwhile, streaming companies are slowing their investment in content, another positive for profitability. But it's important to weigh these positives against the headwinds from a declining linear TV business, which is problematic for some of the integrated media companies. Jessica Reif Ehrlich joins us to discuss her outlook for this dynamic group. *Global Research Unlocked can now be found on public podcast platforms, including Spotify, Apple Podcasts, Google Podcasts, and Amazon Music. These podcasts are first released to clients and then to the platforms.*

Refer to important disclosures on page 6 to 8.
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Full Podcast Transcript

T.J. Thornton, Head of Product Marketing: Hello and welcome to Global Research Unlocked, where we discuss what's rising from growth industries to rising risks and opportunities in global markets. I'm T.J. Thornton, Head of Product Marketing at BofA Global Research, and we're recording this episode on Monday, December 18, 2023.

Our view is since Advertising Video on Demand really just launched in the last year or so, this will be a driver for the industry for at least the next 3-5 years, if not longer. And that's going to be a very important driver of profits for the entire industry.

- Jessica Reif Ehrlich

Streaming video has been through a lot of change over the last several years from hyper growth, to stepped up competition, to price hikes, to a pandemic fueled boom in subscriptions, from sharing one's password with an entire dormitory to in some cases not even sharing with your spouse. Joining us today to discuss all this is Jessica Reif Ehrlich, Head of US Media and Entertainment Research here at BofA Global Research. Thank you, Jessica, for joining us today.

Jessica Reif Ehrlich, Head of US Media and Entertainment Research: Thank you so much for having me.

T.J. Thornton: Traditional linear cable TV has been losing subs for years as streaming gained, but in the US how much growth do you think is left for streaming subscribers?

Jessica Reif Ehrlich: Well, it's not clear where cable TV or pay TV levels off. We're currently roughly 60 to 65 million households down from a peak of 100 million. And streaming, of course, has grown dramatically over the last few years. And depending on the provider, I'd say the most mature is probably close to 70 million, and many are way under. There is probably room for even the most mature to grow, and some of the drivers of subs would be the crackdown on password sharing that we're starting to see. Netflix has started, Disney+ will be instituting it, others will as well, and that should help in terms of just driving paying subs. New content TV series will start to come back probably by mid '24, production stopped as a result of the multiple strikes. And then movies are a big driver of subs and acquisition and the movie slate won't be replenished because of the strikes, will not be replenished until mid '24, so there are many things that should drive subs over the course of ‘24 and ‘25.

T.J. Thornton: Okay. And Jessica, despite this growth in subs for the streamers, I know a lot of them still lose money, so could we get the latest there? How many are still losing money and are there any that are profitable?

Jessica Reif Ehrlich: T.J. you are so right. They're basically all except one are losing money. The peak losses were in 2022 and actually they probably should have been '23. But again, production stopped because of the two strikes and so it just stopped the content spend. It also gave everyone a chance, all of the providers a chance to rethink their content strategy. And that's what they're doing. I think they're just figuring out how much content do you really need to keep churn down and keep your subs on the platform. You need a certain amount of originals, whether it's episodes or sports or something else to reduce churn, so we're starting to see that. We're seeing a cut in spending, but the losses as it peaked in '22, and '23 and '24 will still be fairly significant in terms of losses for most of the direct to consumer players.

T.J. Thornton: Okay. You mentioned rethinking strategies around content spend, but you also said that losses are still going to be pretty steep, even in '24, so when do we start to see that lower spend potentially narrow losses?

Jessica Reif Ehrlich: We're starting to see productions ramping up, but companies will produce less than they were pre-strike, and we'll start to see that. Content amortization takes a while before you see the impact on the P&L, but from a cash basis we're starting to see that. But what will drive growth, in our view, will be bundling of some of these services. In Pay TV, we've all gotten used to having one big bundle - sports, news, entertainment - for one price. And with the growth of streaming, it's been an à la carte choice. You either take Max or Peacock or Paramount+, etc., and so to get that overall package, we're all forced to buy many services. And what we think will happen, over the course of the next year, will be bundling of various services that may not be related, but will help reduce both churn and SAC (Subscriber Acquisition Cost), which is the marketing. As an example, Verizon just announced that they will bundle Max and Netflix for their advertising tiers. And that's pretty significant. We'll see more of that, whether it's Disney and Hulu. We will see that as '24 progresses.

T.J. Thornton: Okay. Another thing that's changed, you mentioned bundling, but is these ad supported options? Is this widespread among the streamers now, this optionality for consumers to pick the cheaper ad supported version? And what has that done for profits?

Jessica Reif Ehrlich: T.J., this is just beginning. The bundling, that I had just mentioned, offering their AVOD or Advertising Video on Demand here, so it's the lowest price. And the way the deal works is Netflix and Max will get a subscriber fee, and Verizon may take a cut, but the advertising portion they will keep 100% of. AVOD is just getting traction. These platforms need scale, which they don't have at the moment, but we already can see what AVOD will do. It's premium video content. It's uncluttered. Many of these services, they'll have 4-5 minutes an hour on their AVOD tier, versus 15-20 minutes in linear, a huge difference in the number of ads. It will be targeted for different demographics, different demo, different interest levels, different cohorts, and it will be premium video, so they will get premium CPMs (cost per thousand). Our view is since AVOD really just launched in the last year or so, this will be a driver for the industry for at least the next 3-5 years, if not longer. And that's going to be a very important driver of profits for the entire industry. And we'll see, as eyeballs are shifting to streaming, dollars follow eyeballs. First these companies need scale, which they're getting because they're pricing. The ad tiers are $6 or $7, they're lower priced, and then the subscription-only without ads are being priced at mid to high teens. It's really encouraging a lot of people to go into the ad tier and with scale the money will follow.

T.J. Thornton: Got it. And I use one of the big, over the top TV providers at home. I've noticed the ads have become much more targeted, not just to my demographic group, but clearly the ads are also based on search history and things like that. Are many of the streamers doing this, and how much of an opportunity is that when you think about where ad pricing could go versus where it is now for these streamers?

Jessica Reif Ehrlich: This is a huge opportunity. It is absolutely huge. Having the ability to not only target, but make these ads addressable, so that it's actually something that's relevant for you, for me, this is the Holy Grail for advertising, and it's really just the tip of the iceberg. This will be a big driver for a long period of time. Linear was very effective for brands, and our view is that brands will move over to streaming, where they have that capability to reach the consumer that they want to reach. And what we're starting to see already, even though it's super early days, is that the advertising portion of the ARPU, the Advertising Revenue Per Unit, actually exceeds subscriptions. If one of these streamers has a lower priced AVOD tier, very often the advertising contribution plus the low subscription fee exceeds their basic tier, the next level, the $16 or so. That will be a big driver and it also takes the burden off of the consumers from funding streaming directly. This is a long-term driver as money moves from linear and maybe even from some of the digital social media platforms over to premium video.

T.J. Thornton: Got it. And just a follow up on the ad question, we've mostly focused on the US here, but how much of an opportunity is international? Thinking about your names, the US names, is there a lot more growth in subscribers outside of the US and then also, is the ad opportunity earlier or later, when we look outside of the US?

Jessica Reif Ehrlich: The US is the biggest advertising market and the largest single country, but there's tremendous opportunity outside the US and many of these companies haven't even really rolled out yet. Max will roll out in Latin America in Q1 and in Europe before the Olympics in Q2. We're seeing other streamers roll out in additional countries, local languages driving subs globally. And there are certain really big developed markets for advertising that will contribute, so this really is a growth opportunity for both global rollouts and advertising probably for the next 5-10 years. But of course, all of this is replacing the decline in linear, so it's a balance.

T.J. Thornton: Got it - which is more of an issue for some of the incumbents that have this linear programming that they may lose out on versus those that are newer and that don't. The price per month, outside of the US, it is quite a bit lower though, right?

Jessica Reif Ehrlich: Pricing generally is lower. The US prices tend to be higher for everything, whether it's video streaming, audio streaming. Even if you look at the linear bundle, we are the highest priced country in the world, but still a lot of this content is used globally, which means that the profits for most of these companies, there's this tremendous leverage in having these global ad tech platforms and advertising the content.

T.J. Thornton: Okay. Do you think the market expects profits to improve at the streaming businesses? Because we've talked about a couple positives; one, rethinking the content strategy and then also just continued growth in subs, as well as the opportunity in advertising. As far as you can see, and from your analysis of what's priced into these shares, do you think the market gives these streamers credit for that?

Jessica Reif Ehrlich: Not entirely. I guess an analogy for many of these companies would be to look at the music industry, when it started to decline because of Napster and the unbundling of albums, there were a lot of things that drove it. And the music industry declined from the late nineties and probably bottomed in the teens 2014, 15. And it feels like the decline of linear were probably in the 2010 timeframe, we're almost there, but not quite, so transitions are difficult. They're not getting the credit because it's unclear how much is incremental versus how much is lost profit from a really good business model that's going away. It's been difficult. Having said that, we don't know what ultimate margins are, and if these companies are careful or more careful, everyone was spending like drunken sailors in 2020, '21, '22. And I think with the step back now, much bigger focus on costs and marketing on content spend, they can be very profitable and these can be actually very good businesses. In addition, we do believe that some of the smaller scale players will be forced to combine, so if we wind up with a handful of industry giants, it can actually be a very meaningful business.

T.J. Thornton: Okay. I wanted to talk about sports rights. It seemed that the numbers for sports rights continued to increase, some huge price tags paid for deals. Has that slowed at all? Has there been any tapering of this sort of war for sports content? If these deals are not profitable, and I think some of them have not been, do you think that will ultimately impact companies' willingness to pay?

Jessica Reif Ehrlich: Yeah, there's a lot of aspects to that question. I think you have to divide it up into premier sports, which are NFL, NBA and NCAA. College sports, basketball and football would be in there. And then there are secondary and tertiary sports. The next big contract that comes up is NBA this spring. And it's a critical sport. It has a very long season, which is very helpful to balancing out schedules. The audience can be younger. There's a very wide demographic fan base, but it's a sport that's growing in popularity globally. It's a very big part of culture, so NBA undoubtedly will get a huge increase, and the current contracts worth roughly $25 billion. We've said in the past the next go round; we believe will get $50 billion, so it'll get a double, but maybe not quite a triple. There's speculation that some of the traditional media companies will try to get back in. NBA aside, the question then is what happens with other sports? And you're 100% right T.J., some of these are not economical and the amounts paid, we're starting to see that some sports renewals have been at 40% increases when the market expected 50%. And it really depends at the end of the day, is there more than one bidder because that will drive the price up? And there's a moment in time when a streamer needs content or a platform needs content to get off the grounds. And a good example would be when Amazon bought Thursday Night Football, they paid more than double what Fox had been paying and Fox was losing $400 million a year on that contract. It really just depends who needs what at any given time. We are starting to see, interestingly, sports rights come down in Europe because they have a different model. They really pay much more directly for sports, but no doubt will evolve over time. In the US, I think the big question is, will there be a sports aggregator? It's so hard for consumers to know, where's this game on? Where's that game? Will somebody aggregate all the games? You can buy it through either one app or just figure out where to go.

T.J. Thornton: Okay - last question, related to the sports question and a lot of what we're discussing today - time spent. We know that time spent on social media over the last several years has continued to rise. I think for some of the other video apps as well, that are not expertly produced content, we've seen a rise as well, so where does that leave streamers? Are they fighting for time and will that be a headwind to what those businesses will ultimately be worth? Is there any sign that maybe the time spent on social media has started to plateau?

Jessica Reif Ehrlich: Yeah, it's amazing that time spent, if you added up someone's day, anyone's day, it's more than 24 hours, which is insanity, but people seem to be multitasking. What's interesting, if you look at, let's say gamers, heavy user, heavy gamers probably watch more TV than non-gamers. Heavy video users are heavy across the board. All of the data that we've seen, all of the surveys, basically the amount of viewing time for linear and streaming, so premium video is over five hours per day, which is a lot, and it's been pretty steady. Social media has grown, but again, a lot of that is done at the same time. It doesn't feel like the premium video industry has to worry yet about time declining or time being taken away by social media. And I think, again, as production ramps up and as some of these companies consolidate, the quality ramps up. Viewing has been really steady over the last few years and with new content, if anything, more likely go up than down.

T.J. Thornton: Thanks Jessica for a great discussion. Appreciate the time.

Jessica Reif Ehrlich: Thank you for having me.

T.J. Thornton: There are a lot of positives still ahead for streaming video. One is subscriber growth, both in the US and the rest of the world, which is driven partly by the crackdown in password sharing. Subscribers could also be helped by new content, which had slowed because of the strikes, but will be back by mid-2024. Bundling with say wireless providers helps too, especially the ad supported tiers. And then there's the advertising opportunity, which Jessica believes is still fairly early, especially when it comes to more precisely targeted ads. There are signs too that content spending has become more rational, but especially for incumbent players, that's partly offset by a linear TV business that's excellent, but that should continue to erode, making stock picking critical. Thanks for joining us today.

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