Remarks to

FCC WORKSHOP ON THE STATE OF THE VIDEO MARKETPLACE

Challenges Faced by Online Video Distributors

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It is a great pleasure to participate on this panel at this workshop for several reasons. The first is simply that the issues already discussed and to be discussed at this panel translates to my entire professional life. In an earlier time, before I became involved in the broadcast and media industries, I was an antitrust economist with the FTC working on some of these same competitive issues, such as the impact of vertical restraints on the level of competition in a particular industry.

The second reason is the incredible dynamic nature of this industry. For those of you who are on Twitter and other social media apps, we have been in the workshop for about 4 hours – has there been any new entrants announced in the OVD or OTT space? I say this partly in jest, but certainly there is no day goes by without some company in this arena not announcing something or some competitive company such as a cable MSO responding to some action by an OTT or OVD service.

The third reason I am so pleased to be here is the mere fact that the FCC is asking for input on these important questions. While some of us might differ as to the need of FCC involvement in this burgeoning industry, it is extremely gratifying to see this agency asking these questions. The FCC has somewhat different goals than other government agencies, such as program diversity, and it is important to assess whether the marketplace is working towards those other goals.

So, let’s begin. What are the major hurdles facing these OVDs and OTT services? At first glance they do not seem to be very much given the increased entry just in the past few weeks. While there are some very popular networks out there attracting significant audiences and being distributed by MVPDs, some of these OTT and OVD services are entering this marketplace and prospering without them. In fact, some are entering this marketplace with original content, some of which, as Commissioner Pai noted in his comments on the recent NOI, is programming that provides an incredible amount of diversity. What seems to be emerging in this marketplace are consumers purchasing subscriptions to multiple services to get *their mix of desirable programming when they want it*. What an incredible move to consumer empowerment!

What is also significant about the question of “must have” programming is the response by the MVPDs of slimmed down programming bundles. While the cable and satellite distribution industries have not moved to a pure a la carte model, they are providing consumers with fewer channels for a lower price in order to retain these customers. Simply put, there are much fewer “must have” channels that what these MVPDs been offering as a combined bundle for many years.

With respect to OVDs access to local broadcast stations, I think the jury is still out. Of course, some of these OVD customers can possibly access these signals via over-the-air reception, though some cannot. So, to be a full alternative to MVPDs, some of these OVDs may wish to provide those local signals. But, it might not fit their business model if the retransmission consent payments are too much. Some may actually prefer to be a source of alternative programming as they are now.

There are other potential entrants who are considering entry into the OVD market with a collection of local over the air television stations. The pending rulemaking at the FCC on the definition of an MVPD might lead to this new entry, adding yet another wrinkle.

Additionally, remember that one such OTT service, HULU, is a collection of many of the popular broadcast network programming series. While that does not include local news and other programming, it does provide an option for some consumers to access that desirable programming. And, CBS's All Access is providing that local programming in addition to the network programming. Clearly, the OVD and OTT services are springing up to provide what consumers want and are willing to pay for.

A final consideration of the availability of “must see” programming is the incentives of the network providing that programming. Of course, they want to maximize whatever subscription revenue they generate. Providing access to an OTT or OVD service may affect those revenues from MVPDs. Yet, they have a tremendous incentive to get as much distribution as possible to sell advertising. Given the fixed cost nature of the production of this programming, any additional households that have access to the program could lead to increases in advertising revenue and substantial increases in profitability.

Moreover, that advertising pool available is growing as more nation broadcasters wan to target local consumers, something that the OVD and OTT services can provide. In fact, a representative of HULU noted at one of our BIA/Kelsey conferences a while back that 30% of their advertising revenue was from targeted advertising for specific local markets in lieu of a nationwide advertising buy. We see that movement of national brands targeting local markets as only increasing, providing more opportunities for these OVD and OTT services.

Selling that advertising is a bit of a challenge for OVD and OTT services. While these services have information on the direct connection of their subscribers, that is not an independent source of audience information that is necessary for advertisers. Of course, comScore ratings are available and are used. And, one could easily expect that the recent acquisition of Rentrak by comScore could easily lead to more thorough audience estimates.

Finally, there has been several questions concerning the impact of most favored nations (MFNs) and alternative distribution methods (ADMs) clauses in the contracts that programming companies have made with MVPDs and other distribution services. As I mentioned in the beginning of my talk, I studied these types of vertical constraints during my time at the FTC. In fact, these contract provisions have been studied for quite some time, with Supreme Court cases going back to the 1940s discussing the impact of these types of provisions. Many an economic dissertation and journals have analyzed if and when these types of provisions lead to pro and anti-competitive results.

With respect to the programming sources that entered into these MFNs and ADMs with the existing distribution companies at that time several years ago, they may be hampered now in expanding that distribution with the new OVDs and OTTs services. But, that does not mean that these provisions were or are anticompetitive. These new programming services may not have been able to get distribution at their initial launch without having those provisions. Steve Salop and Fiona Scott Morton, both serious and experienced antitrust economists listed in a 2013 article some conditions that would suggest that MFNs are less likely to raise antitrust concerns and one seemed very relevant to new programming:

*Input has uncertain value for innovative new product with resulting potential for delays and holdout problems.*

In other words, the uncertainty surrounding new programming networks might have been too great at the time of debut that the existing MVPDs at that time would not have ever carried them. And, we might not even be thinking about these programming services and their expanding into OVD and OTT services without those contract provisions.

In conclusion, as has been discussed during this entire day, these OVD and OTT services have seen incredible acceptance by consumers, and has prompted important competitive responses by the existing program distribution systems. While there could be instances where particular OVD and OTT services may have some difficulty in securing certain type of programming, it does not seem those difficulties have severely hampered their growth.