

Research Notes

3Q 2003

Actionable Research on the Adoption and Impact of Broadband Media

On-Demand Marathon

On April 22, 1980 Rosie Ruiz was the first woman to cross the finish line at the 84th annual Boston Marathon. Ruiz's time for the more than 26 mile race was the third fastest ever

recorded by a woman, yet when she finished the race she was barely sweating. The reason why this unknown runner was able to accomplish such an amazing feat was that she had not actually run the race, but had snuck her way in less than a mile before the finish.

Like a marathon, the race to win consumer acceptance of video on-demand (VOD), and digital video recorders (DVRs), are long ones that cannot be won by simply jumping in at the 25th mile.

Much of the requisite training for the VOD marathon has taken place. In the past few years the infrastructure to deliver VOD has made tremendous strides, while cable operators in the U.S. have simultaneously built a base of over 20 million digital cable

subscribers. Many cable operators have already installed VOD systems, and today nearly 10 million digital cable households have the ability to order some form of VOD. This means that about 40% of all cable subscribers are connected to a cable system that currently delivers VOD.

Now the actual race begins. A recent Leichtman Research Group (LRG) consumer research study conducted in four U.S. markets where VOD is available found that, while awareness of VOD is growing, there are still many obstacles ahead. A few results of the study include:

- 82% of all cable subscribers have heard of video on-demand, compared to 60% in a recent nationwide LRG survey
- One-quarter of digital cable subscribers, and half of analog cable subscribers are not aware that VOD is currently available
- Just 35% of DBS subscribers in these markets are aware that the cable company in their area provides VOD
- While usage rates vary, overall about 30% of all digital cable subscribers in the four markets studied have used VOD

This data exemplifies the challenges that cable operators are facing in this stage of VOD deployment. On-

In this issue:

- *On-Demand Marathon*
- *HDTV Attracting a Growing Audience*
- *Video On-Demand Footprint and Awareness Growing*
- *Justice, Tranquility and 100 Channels*
- *High Speed Internet Growth Slowing Down?*
- *Industry by the Numbers*

demand TV is not as simple as “build it and they will come.”

Many operators have been slow to aggressively market VOD for several reasons. Operators may be concerned about not having enough (or the right) content; they may worry about generating too many simultaneous users for the system to handle; or perhaps they feel that VOD is inferior to DVRs. Yet if a VOD service rolls out in the forest and there is no one there to hear it does it generate revenue and reduce churn?

Written by Bruce Leichtman, president and principal analyst for Leichtman Research Group. Reprinted with permission from August 06, 2003 issue of SkyREPORT.

HDTV Attracting a Growing Audience

Adoption of high-definition television (HDTV) sets in the US has risen to 4% and further growth will be driven by higher-income consumers spurred on by falling prices of the sets. LRG research found that current HDTV owners have an average household income 73% above average, and those most likely to purchase an HDTV set in the next year have an average income 54% above average.

These findings are based on a telephone survey of 1,250 randomly selected households throughout the United States in areas where cable television is available, and are part of a new research study, ***HDTV: Awareness, Interest and Intent to Purchase.***

Other key findings include:

- 9% of DBS subscribers in areas where cable TV is available say that they currently own an HD-capable set, compared to 4% of cable subscribers
- An additional 13% of DBS subscribers say that they are very familiar with HDTV, compared to 8% of cable subscribers
- 43% of those who have an HDTV set, or are very interested in getting an HDTV set in the next year, would be very likely to spend \$9.95/month for an HD programming package
- 26% of consumers who plan to purchase a TV set in the next year expect to spend over \$1,000

*About one-third of households with high-definition sets are satellite subscribers in areas where cable is available, according to Leichtman Research Group, a market-research firm. That is **double the market share** that satellite has among households with traditional sets in cable-served areas.*

- Wall Street Journal
July 24, 2003

With over 275 million television sets in US households, it will be many years before HDTV sets become the norm. Yet with prices decreasing, purchasing an HDTV set is becoming

a default for the high-end TV buyer rather than an active decision to get an HDTV set. This will result in the sale of millions of HDTV sets in the next few years, with the total number of HDTV-capable households in the US forecasted to grow to 33 million by the end of 2007.

HDTV Awareness, Ownership & Interest by Annual Income*	<\$75,000	>\$75,000
Have heard of HDTV	69%	89%
Have an HD-Capable Set	2%	12%
Very Familiar with HDTV (but don't have an HDTV set)	6%	13%
Investigated getting and HDTV set in the past six months	4%	11%
Expect to spend over \$1,000 on a new TV set in the next year	3%	7%

Source: Leichtman Research Group, Inc.

* Based on stated annual household income. Percentages are within each group.

Video On-Demand Footprint and Awareness Growing

Video on-demand (VOD) availability and consumer awareness is growing, but the service still remains a long way from achieving widespread consumer acceptance. New research conducted in four markets where VOD is currently available found that over 80% of cable subscribers have heard of video on-demand, yet many subscribers are not aware that VOD is actually available in their market, and the majority of subscribers have yet to use the service.

Key findings of this new study include:

- Overall awareness of VOD is high: 90% of digital cable subscribers in the four markets studied where VOD is available have heard of video on-demand. This compares to 69% of digital cable subscribers nationwide.

- Awareness of the availability of VOD is more limited: About one-quarter of digital cable subscribers, and one-half of analog cable subscribers in the four markets studied, are not aware that VOD is currently available in their market.
- Use of VOD is moderate: About 30% of all digital cable subscribers in the four markets studied have used VOD.

These findings are based on a telephone survey of 1,400 total households in four markets where VOD is currently available and are part of a new research study, ***Consumer Opinions in Four VOD Markets***. Additional nationwide results are based on a survey of 1,250 households throughout the United States in areas where cable television is available, and are part of a recently released research study, ***On-Demand TV: A Nationwide Study of Consumers' Perspectives***.

VOD is now potentially available to nearly 40% of cable subscribers, yet making VOD available is just the first step in building the business. Intensified marketing efforts, along

with increased content offerings, will be significant factors in growing consumers' use and appreciation of VOD.

“VoD users particularly like the ability to start movies and programs when they want to watch them,” Leichtman notes. “While price is often given as an excuse for not having used VoD, it is more a lack of knowledge of the VoD offering, or the overall cost of cable that consumers may be concerned about rather than the specific cost of VoD.”

- Internet News
August 21, 2003

Justice, Tranquility and 100 TV Channels

Over 210 years ago the Constitution of the United States was ratified, and to this day the nation remains guided by most of these Articles. While the original “founding fathers” were able to establish guiding principles that have stood the test of time, unfortunately they were not able to foresee the dilemma that our nation now faces – the cost of cable TV.

For the better part of two decades trepidation over the price of cable TV has generated outcries to exert government control on the industry. These concerns led to the passage of the Cable Act of 1992 that established regulations on the cable industry, and also resulted in the first override of a

veto by then President George Bush (Sr.).

Over a decade later there is still limited wireline competition to cable (primarily because it is prohibitively expensive to wire an entire franchise community as a second player), and politicians from both parties still find it prudent to voice their consternation about cable rate increases. Like the floating of the huge Underdog balloon that is part of Macy's Thanksgivings Day Parade, the rising price of cable TV controversy is once again making its annual flight. Today's marketplace for multi-channel video, however, is far different than the market in 1992.

The Direct Broadcast Satellite (DBS) industry in the US recently celebrated both its 10th anniversary and its 20 millionth subscriber. DBS has moved well beyond being a service largely for rural households where cable is unavailable, or those early adopters who wanted the latest electronics toy. Today, over one out of every six households where cable TV is available choose to subscribe DBS.

Nearly 80% of all households in cable passed areas subscribe to either DBS or cable. With the market for multi-channel video highly saturated, DBS now seems to be having a particularly strong impact in providing market regulation of the cable industry.

- In the past 18 months, the ten largest cable operators combined have lost over 800,000 cable TV subscribers, while DBS providers

have added 3.2 million subscribers.

Leichtman Research Group (LRG) research on consumers throughout the US finds that the average cable subscriber spends about \$47 per month on cable TV – an 8% increase over last year. Yet it is important to note that cable subscribers have largely segregated into two groups: digital subscribers and analog subscribers.

- For the top ten cable operators, one-third of consumers have elected to subscribe to more channel-rich, and more expensive, digital cable offerings
- This group of digital cable subscribers spends on average close to \$59 per month on cable TV, while the average spending for analog subscribers is 40% lower
- Comparatively, the average DBS subscriber in cable areas spends about \$49 per month

While the cost of cable TV has increased, the vast majority of consumers in the US have a realistic choice of multi-channel video providers today, and consumers are exercising their choices based on price as well as other criteria. We the People of the United States have the ability to decide if cable is priced correctly. If consumers feel cable prices are too high they can downgrade their service, or they can switch to DBS, or (believe it or not) they can actually choose not to get Spike TV, Fox News, Lifetime and

dozens of other channels and dust off the old rabbit ears to take advantage of free broadcast channels.

Written by Bruce Leichtman, president and principal analyst for Leichtman Research Group. Reprinted with permission from September 3, 2003 issue of SkyREPORT.

High-Speed Internet Growth Slowing Down?

In the second quarter of 2003 the major US cable and DSL providers added a combined total of 1.55 million high-speed Internet subscribers. Net additions for the quarter were the smallest since the second quarter of 2002. As of the end of the second quarter of 2003, the leading cable and DSL providers in the United States accounted for nearly 20.7 million high-speed Internet subscribers.

*According to Leichtman [Research Group], top cable operators served **13.2 million** broadband customers at the end of the second quarter. The top telephone companies that provide high-speed DSL service accounted for **7.4 million** subscribers.*

- Rocky Mountain News
August 9, 2003

Other key findings include:

- DSL had a greater share of the net additions than in previous quarters. DSL providers had 625,000 net subscribers added in the quarter representing 40% of

the net high-speed Internet additions for the quarter. The top cable companies added 930,000 subscribers in the quarter, 320,000 fewer additions than the record-setting growth of the first quarter of 2003.

- The top cable operators maintain a 64% share of the overall market versus DSL and now account for over 13.2 million high-speed Internet subscribers, however, every cable provider reported smaller net high-speed Internet growth in the second quarter than in the first quarter of 2003.
- SBC was the only provider to

report significantly more net additions this quarter than in the previous quarter, adding 304,000 subscribers in the second quarter - 33,000 more than it added in the first quarter of 2003.

With the addition of over 1.5 million net new subscribers in the second quarter of 2003, high-speed Internet remains a very healthy business. While caution should be shown in making major assumptions based on the quarterly figures, there were some interesting changes from previous quarters that should be watched closely to see if these results become trends.

Industry by the Numbers – (as of the end of 2Q 2003)

Top 10 Cable MSOs in the U.S.

	Passing	Subscribers	Availability	Penetration	Net Adds 2Q 2003	Net Adds 2Q 2002
Basic Cable	105,000,000	58,900,000		56.1%	(130,000)	(228,000)
Digital Cable	102,500,000	19,750,000	98%	19.3%	588,000	1,020,000
Broadband Internet	89,250,000	13,050,000	85%	14.6%	920,000	935,000
Telephone	14,800,000	2,283,000	14%	15.4%	9,000	175,000

DBS

	Subscribers	Net Adds 2Q 2003	2Q 2003 Total New Subscribers	Average Sub. Acquisition Costs	Average Rev. Per Sub Per Month
DirecTV	9,950,000	181,000	633,000	\$595	\$60.90
Pegasus	1,233,000	(43,000)	32,000	\$609	\$54.69
Other NRTC**	377,000	3,000	20,000		
DirecTV Total	11,560,000	141,000	685,000		
EchoStar	8,800,000	270,000	700,250	\$408*	\$51.60
Total DBS	20,360,000	411,000	1,385,250		

Sources: The Companies and Leichtman Research Group, Inc.
Broadband Internet data does not include RCN.

* Subscriber acquisition cost reported by EchoStar excludes leased equipment and un-returned boxes and includes a reimbursement for a litigation settlement – without these factors, Average Sub. Acquisition Costs would be \$505.

** NRTC total new subscribers are estimates.

Top Broadband Internet Providers in the U.S.

Broadband Internet Provider	Subscribers at end of Q2 2003	Net Adds in Q2 2003
Cable		
Comcast	4,388,300	350,900
Time Warner	2,856,000	170,000
Cox	1,674,835	112,452
Charter	1,349,000	76,700
Cablevision	921,105	68,270
Adelphia	781,000	69,264
Bright House Networks*	560,000	30,000
Mediacom	234,000	20,000
RCN	184,265	10,875
Insight	179,500	10,140
Cable One	106,600	10,800
Total Top Cable	13,234,605	929,401
DSL		
SBC	2,774,000	304,000
Verizon	1,931,000	101,000
Bell South	1,225,000	103,000
Qwest	560,000	9,000
Covad	453,000	36,000
Sprint	223,000	38,000
ALLTEL	105,178	17,178
Cincinnati Bell	87,000	4,000
CenturyTel	68,000	8,000
Total Top DSL	7,426,178	620,178
Total Broadband	20,660,783	1,549,579

Sources: The Companies and Leichtman Research Group, Inc.

* Bright House Networks totals are estimates.

Company subscriber counts may not represent solely residential households.

Top cable and DSL providers represent approximately 98% of all subscribers.



LRG
Leichtman Research Group

Leichtman Research Group, Inc.

3 Ellison Lane
Durham, NH 03824

(603) 397-5400
(603) 397-5410 (Fax)

www.LeichtmanResearch.com

Copyright© 2003, Leichtman Research Group, Inc.
All Rights Reserved