



The Pay-TV Funnel

When I was growing up, I looked forward to *The Boston Globe's* Sunday newspaper so that I could read

the Wrigley Spearmint Gum's "Fun Facts to Know and Tell" at the bottom of the first page of the comic section. Inspired by these memories from decades ago, here is a 'Fun Fact' from recent LRG surveys: **More households in the US dropped Netflix in the past year than dropped a pay-TV service in the past year.**

This may seem unusual given the

fact that Netflix reported a net gain of nearly 5 million paying streaming subscribers in the US in the past year, and that the top pay-TV providers had a cumulative net loss of over 700,000 subscribers in the past year.

Both "facts," however, are possible. Looking at those who dropped a service is only focusing on those who are exiting out of the bottom of the funnel. Net additions also account for those who are entering or reentering into the top of the funnel.

About 5% in an LRG survey from earlier this year said that they do not currently get Netflix but had it in their household in the past year. This is nearly twice the rate of those who do not currently get a


pay-TV service, but paid for one in the past year. Clearly, Netflix is currently putting more subscribers into the top of the funnel to make up for those leaking out the bottom, while the pay-TV industry is not.

Later in these *Research Notes*, pay-TV declines are shown in terms of the number of subscribers as well as the penetration of pay-TV in the US. **But it is inaccurate to attribute these declines solely to being a function of those who dropped a service in the past year (often simplistically called "cord-cutters").** The declines in subscribers and penetration are from three main sources:

1. Those exiting the category

Overall, about 2.6% of TV households paid to subscribe to a traditional pay-TV service in the past year, but currently do not.

This exit rate in the past year is actually fairly similar to the rate in LRG's survey from a decade ago of 2.0% in 2006 (before Internet-delivered video services really even existed).



LRG Fun Fact

Wrigley's chewing gum was the first product ever sold with a barcode

In this issue:

The Pay-TV Funnel

82% of TV Households Subscribe to a Pay-TV Service

Major Pay-TV Providers Lost About 665,000 Subscribers in 2Q 2016

59% of U.S. Households Have an SVOD Service

Industry by the Numbers

2. Those entering/reentering the category

While about one-in-seven of all pay-TV subscribers have been with their current provider for under a year, the majority of those with a new provider are 'new' because they switched providers or moved.

Overall, about 1% of pay-TV subscribers were new to the category in the past year – this is down from 3.5% a decade ago.

Given a saturated pay-TV market; more options for video than in the past and some pay-TV providers not as aggressively pursuing lower-value customers as they used to, the rate of new households coming into the category is as low as it has ever been.

3. An increase in rental housing (a factor in the decline in penetration)

The US Census Bureau reports that occupied housing in the US increased by nearly 5 million units over the past five years and by 7.7 million units in the past decade.

Yet, all of the housing growth over the past decade has been in rentals rather than owner-occupied housing.

Renters are comparatively more likely to be younger, lower income, and movers – groups that have always been less likely to subscribe to pay-TV than home owners. Consequently, penetration of pay-TV in residential households has decreased in recent years.

Frequently an image of scissors cutting a cable wire is used to illustrate the state of the pay-TV industry. While this image is striking, it does not show the nuances of what is happening in the

market. A more appropriate picture of the market would be a funnel with a greater number of customers flowing out the bottom than going into the top, and still nearly 100 million subscribers in the middle.



LRG Fun Fact

About 6% of all TV households have never subscribed to a pay-TV service

82% of TV Households Subscribe to a Pay-TV Service

Leichtman Research Group, Inc. finds that about 82% of TV households nationwide subscribe to some form of pay-TV service. The percentage of TV households that subscribe to a pay-TV service is down from 87% in 2011, and similar to 82% in 2005.

Among TV households that do not currently subscribe to a pay-TV service, 14% paid for a service in the past year. Overall, about 2.6% of TV households paid to subscribe to a traditional pay-TV service in the past year, but currently do not – compared to 2.5% in 2015, 3% in 2014, 1.5% in 2011, and 2% in 2006.

While those who stopped subscribing to a service in the past year is similar to last year and to a decade ago, the study found that about 1% of pay-TV subscribers were new to the category in the past year – compared to 1% in

2015, 1% in 2011, and about 3.5% in 2006.

These findings are based on a telephone survey of 1,206 households from throughout the United States, and are part of a new LRG study, *Cable, DBS & Telcos: Competing for Customers 2016*. This is LRG's fourteenth annual study on this topic.

Other related findings include:

- Overall, about 3% of TV households last subscribed to a pay-TV service 1-3 years ago, about 6% subscribed over 3 years ago, and about 6% never subscribed to a pay-TV service
- 7% of current pay-TV subscribers did not subscribe to a TV service for more than a month at some time over the past two years
- 25% of those who moved in the past year do not currently subscribe to a pay-TV service – a higher level than in previous years
- 12% of pay-TV subscribers are likely to switch from their provider in the next six months – similar to 11% in 2015, and 12% in 2014
- 6% of pay-TV subscribers are likely to disconnect from their provider and not subscribe to any TV service in the next six months – similar to 7% in 2015, and 7% in 2014
- Mean reported monthly spending on pay-TV service is \$103.10 – an increase of 4% in the past year (the lowest annual increase in five years)

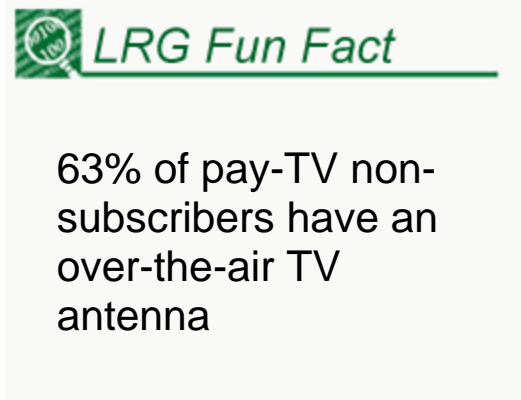
About 82% of households that use a TV currently subscribe to a pay-TV service. This is down from where it was five years ago, and similar to the penetration level eleven years ago. The rates of those exiting the category, or intending to leave, are actually similar to recent

years. The decline in penetration is also due to a lack of those who are coming into the category, and the industry not keeping pace with movers and related rental housing growth.

Major Pay-TV Providers Lost About 665,000 Subscribers in 2Q 2016

Leichtman Research Group, Inc. found that the eleven largest pay-TV providers in the US – representing about 95% of the market – lost about 665,000 net video subscribers in 2Q 2016, compared to a loss of about 545,000 subscribers in 2Q 2015.

The top pay-TV providers account for 93.75 million subscribers – with the top six cable companies having 48.9 million video subscribers, satellite TV companies having 34.0 million subscribers (including about 710,000 from DISH's Internet-delivered Sling TV), and the top telephone companies having 10.8 million subscribers.



LRG Fun Fact

63% of pay-TV non-subscribers have an over-the-air TV antenna

Other key findings for the quarter include:

- The top six cable companies lost about 225,000 video subscribers in 2Q 2016 – compared to a loss of about 340,000 subscribers in 2Q 2015

- Top cable MSOs losses were the fewest in any second quarter since 2006
- Satellite TV providers added 61,000 subscribers in 2Q 2016 (including gains from Sling TV) – compared to a loss of 214,000 in 2Q 2015
 - DirecTV's net adds of 342,000 in 2Q 2016 were more than in any quarter since 1Q 2009
- The top phone providers lost about 500,000 video subscribers in 2Q 2016 – compared to a gain of about 10,000 subscribers in 2Q 2015
 - AT&T U-verse's 391,000 net losses in 2Q 2016 were the most losses ever in a quarter by any provider (for the second consecutive quarter)


The top pay-TV providers lost about 665,000 subscribers in the traditionally weak second quarter, with net losses in 2Q 2016 surpassing the previous quarterly low set in last year's second quarter. Over the past year, the top pay-TV providers (including DISH's Sling TV) lost about 705,000 subscribers – compared to a loss of about 380,000 over the prior year.

59% of U.S. Households Have an SVOD Service

Leichtman Research Group, Inc. finds that 59% of all US TV households have a subscription video on-Demand (SVOD) service from Netflix, Amazon Prime, and/or Hulu – up from 47% in 2014.

SVOD services are particularly popular among non-subscribers to a pay-TV service. Seventy percent of all non-subscribers with a TV have an SVOD service (including 82% with a broadband

Internet service at home) – compared to 57% of pay-TV subscribers.



LRG Fun Fact

Overall, 52% of TV households get both a pay-TV service and an internet-delivered SVOD service – while 11% get an SVOD service but no pay-TV service

These findings are based on a survey of 1,209 households nationwide and are part of a new LRG study, *Emerging Video Services X*. This is LRG's tenth annual study on this topic.

Other related findings include:

- Among those who have an SVOD service, 47% have more than one service
- 19% with Netflix agree that their Netflix subscription is shared with others outside their household
- 49% of adults stream an SVOD service at least monthly – up from 41% in 2014
- 73% of ages 18-34 stream an SVOD service monthly – compared to 53% of ages 35-54, and 24% of ages 55+
- On a daily basis, 41% of adults watch video on non-TV devices (including home computers, mobile phones, iPads, tablets, and eReaders), and 62% weekly – up from 27% daily, and 53% weekly three years ago

SVOD services are in the majority of US households, and along with video to non-TV devices, have become core components in allowing pay-TV non-

subscribers to cobble together a variety of viewing options. On a daily basis, 49% of all non-subscribers with a TV stream an SVOD service, compared to 19% of pay-TV subscribers.

About 190,000 Added Broadband in 2Q 2016

Leichtman Research Group, Inc. found that the fourteen largest cable and telephone providers in the US – representing about 95% of the market – acquired about 190,000 net additional high-speed Internet subscribers in 2Q 2016. These top broadband providers now account for 91.9 million subscribers – with top cable companies having 57.0 million broadband subscribers, and top phone companies having 34.9 million subscribers.

Other broadband findings for the quarter include:

- Overall, broadband additions in 2Q 2016 were less than in any quarter in the past fifteen years (since LRG began tracking the industry)
 - The past seven second quarters account for the seven fewest quarterly broadband net adds over past fifteen years
- The top cable companies added about 550,000 subscribers in 2Q 2016 – 139% of the net additions for the top cable companies in 2Q 2015
 - Cable broadband net adds were the most in any second quarter since 2008
- The top phone companies lost about 360,000 broadband subscribers in 2Q 2016 – compared to a loss of about 150,000 in 2Q 2015
 - Telco providers have had net broadband losses in four of the past five quarters
- Over the past year, there were about 3,025,000 total net broadband adds – compared to about 2,970,000 over the prior year about 10,000 broadband subscribers in 1Q 2016 – compared to a gain of 160,000 in 1Q 2015

While Telcos lost more broadband subscribers in 2Q 2016 than in any previous quarter, cable companies added over 550,000 subscribers in the traditionally weak second quarter. Over the past year, cable companies have added about 3.5 million broadband subscribers, while Telcos have had net losses of about 500,000 broadband subscribers.



LRG Fun Fact

76% of pay-TV subscribers agree that there are specific channels or packages that are “must haves”

Industry by the Numbers

Top Pay-TV Providers in the U.S.

<i>Cable Companies</i>	Subscribers at End of 2Q 2016	Net Adds in 2Q 2016
Comcast	22,396,000	(4,000)
Charter*	17,312,000	(143,000)
Altice**	3,639,000	(25,000)
Mediacom	842,000	(11,000)
CableOne	338,974	(11,602)
Other major private companies***	4,330,000	(30,000)
TOTAL TOP CABLE	48,857,974	(224,602)
<i>Satellite TV Companies (DBS)</i>		
DirecTV	20,454,000	342,000
DISH^	13,593,000	(281,000)
TOTAL TOP DBS	34,047,000	61,000
<i>Telephone Companies</i>		
AT&T U-verse	4,869,000	(391,000)
Verizon FiOS	4,637,000	(41,000)
Frontier^^	1,340,000	(70,000)
TOTAL TOP PHONE	10,846,000	(502,000)
TOTAL TOP PAY-TV PROVIDERS	93,750,974	(665,602)

Sources: The Companies and Leichtman Research Group, Inc.

* Charter completed the acquisition of Time Warner Cable and Bright House Networks in 2Q 2016

** Altice includes Cablevision (acquisition completed in 2Q 2016) and Suddenlink

*** Includes LRG estimate for Cox

^ DISH totals and net adds in 2Q 2016 include its Internet-delivered Sling TV service (which began in 1Q 2015)

^^ Frontier is an LRG estimate (following the Verizon transaction completed in 2Q 2016) and does not include DBS subs

Company subscriber counts may not solely represent residential households

Top pay-TV providers represent approximately 95% of all subscribers Top cable companies do not include overbuilder WOW with 524,300 subscribers

Top Broadband Internet Providers in the U.S.

<i>Cable Companies</i>	Subscribers at End of 2Q 2016	Net Adds in 2Q 2016
Comcast	23,987,000	220,000
Charter*	21,815,,000	227,000
Altice**	4,105,000	24,000
Mediacom	1,128,000	14,000
WOW (WideOpenWest)	725,700	3,400
Cable ONE	508,317	(107)
Other Major Private Companies***	4,745,000	15,000
Total Top Cable	57,014,017	553,293
<i>Telephone Companies</i>		
AT&T	15,641,000	(123,000)
Verizon	7,014,000	(83,000)
CenturyLink	5,990,000	(66,000)
Frontier^	4,552,000	(77,000)
Windstream	1,075,800	(16,200)
FairPoint	311,440	117
Cincinnati Bell	296,700	4,300
Total Top Phone	34,880,940	(360,783)
Total Top Broadband Providers	91,894,957	192,510

Sources: *The Companies and Leichtman Research Group, Inc.*

* Charter completed the acquisition of Time Warner Cable and Bright House Networks in 2Q 2016

** Altice includes Cablevision (acquisition completed in 2Q 2016) and Suddenlink

*** Includes LRG estimate for Cox

^ Frontier is an LRG estimate (following the Verizon transaction completed in 2Q 2016) and does not include wireless subs

Company subscriber counts may not represent solely residential households, and reporting adjustments

Top cable and telephone companies represent approximately 95% of all subscribers



LRG

Leichtman Research Group

Leichtman Research Group, Inc.
www.LeichtmanResearch.com
(603) 397-5400