

# Growing Pay TV Revenues in the Recession and Beyond

## The untapped portion of the pyramid

By Martin Horn, Brand-ID Europe, September 2009

In today's recessionary but increasingly competitive markets, TV Operators face many challenging questions:

- How can I increase the average revenue per user (ARPU) from my existing subscriber base?
- How can I mitigate the effects of churn from subscribers worried about their own income stability?
- How do I defend my business against new entrants with new technologies and attractive consumer propositions?
- How can I launch profitable new services when consumer finances are so stretched?
- How can I rapidly and significantly expand my customer base?

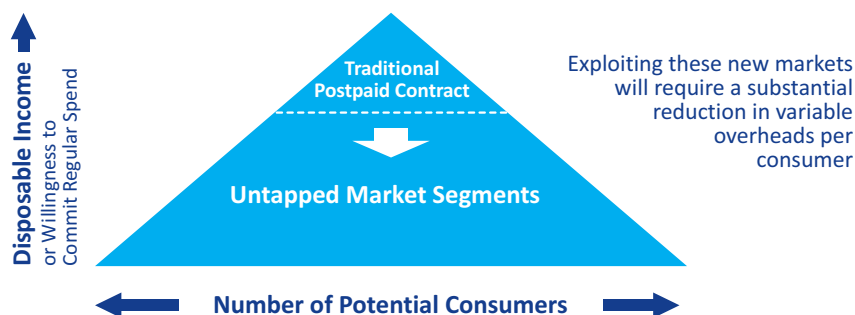
Solutions to many of these issues can be found by supplementing traditional Pay TV business models and embracing additional new business strategies, which are well-proven in other industries. These strategies are flexible and consumer focussed, they serve consumers with precisely what they want, when they want it, at a price they can afford. In short, offering more personalised flexibility and better value for money has proven in other industries to immediately access a larger market. The question is, how can this be achieved at a profit by Pay TV Operators who currently rely on a guaranteed regular income to offset the substantial marginal cost of acquiring and retaining each subscriber?

Some answers to these questions are explored in this paper, looking at:

1. The Expansion of the Traditional Pay TV Business Model
2. Lessons Learned from the Global Mobile Phone Industry
3. Key Opportunity Areas for Pay TV

## 1) Expansion of the Traditional Pay TV Business Model

Pay-TV operators have traditionally employed post-paid monthly subscription models to provide a stable revenue base, but in many countries these leave large market segments substantially untapped.



Traditional Pay TV business models are aimed at consumers towards the top of the economic pyramid, where disposable incomes are sufficient to ensure a stable commitment to pay a monthly subscription fee. Naturally, these higher-end consumers are also targeted by a wide range of other entertainment and technology providers who constantly compete for their attention (see Appendix A). In addition, the recession is causing some to look for options to cut back on regular monthly financial commitments; particularly towards the lower end of this "top triangle". Thus, Operators are rightly focused on ensuring the continued retention of these traditional consumers, but perhaps this is no longer the easiest, nor the only segment in which to expand Pay TV revenues.

*"In many markets, a substantial opportunity now exists to expand the Pay-TV market "downwards" into an increasing broader consumer base"*

In many markets, a substantial opportunity now exists to expand the Pay-TV market "downwards" into an increasing broader consumer base. Servicing these new consumers profitably will require a re-evaluation of the traditional Pay TV business model to allow the addition of new and complimentary offerings, but fortunately there is no need to re-invent the wheel.

## 2) Lessons Learned from the Mobile Phone Industry

The mobile phone industry began in the early 1990s following the post-paid subscriber model traditional to the fixed line telecommunications industry. This continued until 1996, when certain markets began to look saturated from this perspective. The overheads incurred in taking on and retaining each subscriber, combined with the onerous requirements for creditworthiness and access to formal banking services, conspired to restrict this market to a top triangle of between 2% and 20% of most national populations; depending on the economic profile of the country studied.

*"On a global basis more than 70%\* of all mobile phone users are now on some form of pre-paid model"*

New pre-paid business models were first launched in Italy, and then in South Africa. These proved so successful that they were rapidly rolled out worldwide. The size of the mobile phone market simply exploded. On a global basis more than 70%\* of all mobile phone users are now on some form of pre-paid model. Indeed, the use of mobile phones is now so ubiquitous that it is tempting to forget the genuine doubts and debates that preceded the introduction of pre-paid offerings that would be aimed lower down the economic pyramid: "Do lower income groups really need or want a mobile phone when they don't even have (or they already have) a fixed line phone at home?" "Can teenagers really become mobile phone customers?" "If they don't have a contract, how can the upfront cost of a handset and a SIM card ever be recovered?" "Can we really make a profit from serving consumers with much lower disposable incomes?" These questions may seem ridiculous now, but in 1996/7 they were very real.

*"Pre-paid offerings were supported by new and highly automated business processes for consumer acquisition, retention and payment collection"*

The new pre-paid offerings were supported by new and highly automated business processes for consumer acquisition, retention and payment collection at significantly lower marginal costs than those incurred per post-paid subscriber. Crucially, these processes did not rely on the use of call centres or any other staff to effect activation of new consumers, nor to recharge their accounts.

Appendix B discusses some case studies of this market expansion in the mobile phone industry and the details of how some of the practical challenges of upfront costs and new distribution channels were overcome. Finally, it examines how the initially lower ARPUs of these new consumers were maintained and driven upwards over time.

*"Sufficient parallels certainly exist to suggest that Pay TV Operators can derive some valuable lessons from the mobile market"*

Whilst not all of the experiences of this highly successful market expansion are fully analogous to the Pay TV industry, sufficient parallels certainly exist to suggest that Pay TV Operators can derive some valuable lessons from the mobile market:

- They challenged the traditional assumptions about which segments of the population were potential customers
- They introduced new, flexible pre-paid and hybrid business models to address the needs of the new market segments with far greater choice
- They introduced a much wider variety of services and bundles at different levels of cost and utility
- to existing high ARPU consumers, they substantially reduced the variable overheads incurred in obtaining and retaining the new pre-paid consumers to ensure that even lower ARPU consumers would be profitable
- They found innovative ways of removing or reducing the upfront barriers to entry represented by the cost of the handsets and SIM cards, thereby creating many new active and potentially active consumers
- They radically reduced the minimum purchase threshold at which any service could be accessed and made money from multiple smaller transactions per consumer per month
- they allowed natural market forces to ensure the widespread availability of recharge vouchers as and when needed by consumers
- Rapid growth came from re-activating churned consumers, winning business from competitors and, most of all, from a huge expansion in the size of the overall market serviced
- These new flexible offerings did not undermine their existing high-end client base, who still valued the convenience of a higher-end service that was always available

*"Rapid growth came from re-activating churned consumers and from a huge expansion in the size of the overall market serviced"*

At Brand-ID Europe we believe that Pay TV will experience rapid growth by following similar approaches.

### 3) Key Opportunity Areas for Pay TV

*"Viewers with flexible commitments will provide fluctuating and uncertain incomes, so the operator's servicing costs should be equally flexible"*

To attract substantial numbers of new viewers, Operators need to offer a wider range of flexible and easily adaptable package options. However, viewers with flexible commitments will provide fluctuating and uncertain incomes. In order to profitably service such viewers, the operator's servicing costs should be equally flexible. Furthermore, since the incremental revenue per extra viewer is likely to be lower than that currently received per contracted subscriber, the incremental cost incurred needs to be substantially lower as well. Brand-ID Europe has leveraged experience of highly secure pre-paid voucher services in the mobile telecommunications and electricity industries to create CHKVIEW, a comprehensive outsourced solution which supports a fully flexible range of new pre-paid business models for Pay TV Operators on a worldwide basis.

*"CHKVIEW is a comprehensive outsourced solution which supports a fully flexible range of new pre-paid business models for Pay TV Operators on a worldwide basis"*

Many consumers who can't afford or won't commit to a monthly subscriber fee will happily pay in advance (at a premium rate) for their preferred service by event, bundle or time period. The key growth opportunities for Pay TV Operators in many regions around the world now lie in the profitable servicing of these previously unreachable market sectors. The following are four examples of how this can be done. Individual Operators will no doubt be able to assess from their local knowledge which of these new segments represents the "low hanging fruit" in their particular market.

\* Informa reports 70.5% in 2008, set to grow to 74% by 2013

#### a) Expand the Subscriber Base for Existing Packages

*“CHKVIEW pre-paid vouchers can simply be used as an extra method of collecting the monthly subscription fee and activating the package. Established and widespread channels already exist in virtually every country for the distribution of such vouchers”*

In certain developing markets the growth of the existing Pay TV business model is constrained by poor or limited access to banking services, credit cards, etc on the part of potential consumers who would otherwise be able to qualify for and afford the existing package offering. In these cases, CHKVIEW pre-paid vouchers can simply be used as an extra method of collecting the monthly subscription fee and activating the package. Vouchers can be deployed in the form of PIN codes electronically delivered at point of sale and/or via a variety of physical scratch voucher products appropriate to the content packages being offered. Established and widespread channels already exist in virtually every country for the distribution of such vouchers (for mobile phone airtime, electricity, etc) via a variety of outlets such as supermarkets, petrol stations and many smaller stores. In this way, the use of an additional payment collection method like CHKVIEW can significantly increase the potential size of the market.

#### b) Re-activate Churned Consumers at Low Cost

*“Dormant set-top boxes represent "unsold capacity", rather like empty seats at a theatre show. Consumers can be profitably serviced even if they activate (& deactivate) their set-top boxes multiple times in a single month”*

effectively dormant set-top boxes and smart cards which they have previously provided into the market but from which they no longer receive any revenues. These set-top boxes represent "unsold capacity", rather like empty seats at a theatre show. They may represent a very fast growth opportunity if new minimum purchase thresholds can be introduced into the market through the use of pre-paid vouchers offering much lower purchase commitments than the current packages; for example through shorter timescales or reduced numbers of channels. With the CHKVIEW pre-paid service, the overheads incurred per activation and deactivation are so low that such consumers can be profitably serviced even if they activate (& deactivate) their set-top boxes multiple times in a single month.

#### c) Offer Premium Events at High Volumes

*“IVR lines and call-centre operators would struggle to cope with thousands of incoming transactions per second immediately prior to a premium event”*

Some Operators are already able to offer pay per view events because they possess a return path channel or the ability to pre-load some form of tokens onto a set-top box. Without these tools, Operators may currently find it impractical to enable mass-market impulse pay per view offerings. This is due to the cost and capacity challenges of the more "manual" methods, where consumers activate a short-term event package via an IVR line or even an actual call-centre operator. The total cost of a call-centre transaction is typically between \$2 and \$7, depending on the territory of location, which rules out the possibility of offering short-term events at low enough prices to attract major transaction volumes. On the other hand, if pricing could be lowered sufficiently to attract high volumes, IVR lines and call-centre operators would struggle to cope with thousands of incoming transactions per second immediately prior to a premium event.

The CHKVIEW service is designed to handle vast volumes of transactions at ultra-high speed. If consumers buy pre-paid vouchers at retail outlets and keep them at home next to the TV, they can send pre-paid voucher codes to the CHKVIEW system on impulse at any time via a variety of familiar and user-friendly channels: SMS text messaging, online webpage, email or instant message service. These codes can be received and processed extremely quickly in high volumes and the CHKVIEW system will interface directly with the Conditional Access (CA) system at the Operator to entitle the correct content to each consumer and to lock it again at the appropriate time. If desired, a batch file upload can then be performed at a later stage to the Operator's Subscriber Management System (SMS) to update the long term historical record of each consumer's purchases. Business rules can also be applied within CHKVIEW, for example only allowing activations of premium events to viewers whose basic subscriptions are already up to date.

#### d) Offer Pure Pre-Paid Packages to New Consumers

*“Consumers who do not have sufficient disposable income to be able to afford a full monthly package are willing to pay premium rates for equivalent services in exchange for flexibility”*

In certain markets, a large number of consumers do not have sufficient disposable income to be able to afford a full monthly package and/or to make an ongoing commitment to the payments. The experience of the mobile phone industry suggests that this market segment is willing to pay premium rates for equivalent services in exchange for flexibility. It further suggests that this segment might be significantly larger than that currently served by the Pay TV industry through its traditional post-paid contract subscription model, where the stable revenues collected currently justify a complex and costly set of billing and administration systems running behind the scenes at the Operator.

Serving these new market segments profitably might prove difficult with traditional business models, but CHKVIEW offers flexible pre-paid solutions, where new business offers can be created to suit any market requirement. Channels or events of any time duration can be offered, comprising single or multiple-use activations, as well as points-based or multi-play offerings. Low cost automated activation and deactivation of any such package is effected via direct interface with the Operator's existing CA and/or SMS to ensure that all consumers can be profitably serviced.

The use of this outsourced service ensures that costs are only incurred for a viewer when a package is activated, ensuring that actual costs are always proportional to actual revenues. To complete this new flexible cost model and remove financial risk, Operators also need to investigate paying content fees per active pre-paid viewer. The CHKVIEW service supports this approach by providing detailed real-time measurements and reports on the activations of any package or event, and this information can also be made available to content providers as authorised by the Operator.

*“CHKVIEW offers flexible pre-paid solutions, where actual costs are always proportional to actual revenues”*

**Appendix A: Newly Emerging Entertainment and Technology Providers**

**Appendix B: Mobile Industry Case Studies and Experience**

**Appendix C: Further Practical Details of Pre-Paid Models**

If you would like to read these Appendices, they are included in the online copy of this white paper available at [www.chkview.com](http://www.chkview.com)

## More about the CHKVIEW Pre-Paid Service

CHKVIEW offers a rapid, low risk and profitable entry into these new mass markets. This secure and comprehensive outsourced payment service supports a fully flexible range of new pre-paid business models for digital TV, IPTV and mobile environments.

Flexible consumer commitments require flexible costs. With CHKVIEW, Operators incur no new capital costs or internal overheads and simply pay a minimal cost per activation sold via the outsourced CHKVIEW service. The service can be implemented immediately without any significant system changes from the Operator, allowing large numbers of new consumers to be reached quickly.

The solution includes both electronic vouchers and a unique range of secure physical scratch voucher formats to suit any package offering and sales channel. Consumers simply purchase a voucher and submit the voucher code to the CHKVIEW service. This can be done online, via SMS text message from their mobile phone, via email or via instant messaging. CHKVIEW integrates seamlessly with the CA system or SMS at the Operator to effect the immediate activation of the consumer's chosen content package on his chosen device.

CHKVIEW also includes a host of special features to help operators grow revenue from pre-paid viewers, including targeted and up-to-date marketing messages returned to them at the time of activation. Instant-win competitions and loyalty reward features can also be used within CHKVIEW to generate additional viewer excitement around new service offerings. Operators can monitor activation rates in real-time on a digital dashboard to generate market intelligence on viewer behaviours and patterns, drive up advertising revenues and assist with content fee management.

# APPENDICES

## Appendix A: Newly Emerging Entertainment and Technology Providers

Higher-end consumers of Pay-TV services, especially those with ready access to advanced technologies, are also targeted by a wide range of other entertainment and technology providers. For example, an Operator in the USA now offers immediate VOD over IP access to a vast library of current and past TV and movie content for \$1 per month. What's the "catch"? In order to be able to access this content effectively, consumers will certainly also need to upgrade to the Operator's highest speed uncapped internet service at a \$20 monthly premium to the cost of the standard service which might previously have been perfectly adequate for most other purposes. In short, this Operator has switched the business model from selling content to selling bandwidth. Tripleplay offering from Telco-providers, advertising supported on-line offerings from Hulu.com and Over-The-Top services are further examples of this trend.

## Appendix B: Mobile Industry Case Studies and Experience

### Removing Barriers to Entry

Pre-paid offerings removed the immediate barriers to entry of creditworthiness and access to formal banking services. Innovative ways were also found to overcome the barrier of the substantial upfront cost of handsets and SIM cards, which would otherwise have excluded lower income earners. Wealthier, post-paid contract customers were encouraged to continually upgrade their handsets to the latest models, providing a steady stream of second-hand handsets given away or sold to lower end consumers. Manufacturers were encouraged to produce simple, low cost handsets to be sold into these lower income markets segments at a target price point of around \$30. Marketing campaigns at peak gift-giving periods such as Christmas encouraged people to club together for one-off gift buying of handsets for relatives or friends. Finally, the mobile Operators chose to subsidise the SIM cards upfront with a view to recovering the cost from usage over time. In many markets they are sold for as little as one sixth of the actual cost price to the Operators. In all cases, the basic logic has been that once a person has managed to obtain a handset and SIM card they have immediately become a potential consumer of the Operator's services, whether on a regular or an occasional basis.

### Increasing ARPUs

Once the new pre-paid consumers were active, substantial revenues and increased ARPUs were then made by mobile network Operators from selling data bandwidth and content such as ringtones, pictures, skins and games. All of these services were made widely and flexibly available to all manner of consumers by means of pre-paid vouchers. In many cases, hybrid subscription and pre-paid business models were also offered; where a monthly subscription covered a basic minimum monthly level of phone calls and SMS text messages but all further services over and above these in a given month were then purchased by means of pre-paid vouchers.

### Micro-pre-Paid: Expanding Even Further into the Mass Market

Initial pre-paid offerings targeted the middle of the economic pyramid by offering pre-paid scratch and e-vouchers at price points of between about \$30 and about \$5. As this market segment began to saturate, especially in developing economies, mobile network Operators began to consider how to move even further towards the bottom of the pyramid. The following case studies describe how this was achieved in the case of 3 mobile network Operators, each in a different developing economy:

#### Case Study 1

In the first case study, the Operator had noticed that a substantial number of their subscribers remained active at a minimum level required to maintain a phone number and receive calls but would go for 2 or 3 months at a time without purchasing even a single recharge. It soon became clear that the immediate affordability of a single recharge transaction was more of a problem than the affordability of the actual services themselves, since these consumers would happily use a public pay-phone to make a short call at a higher rate per minute than the mobile network charged simply to avoid having to spend the minimum voucher price to recharge their mobile. The key to understanding this behaviour was the short economic planning horizon of these consumers, who typically earn and spend their money within a single day or a few days at a time. The Operator then noticed that the consumer product companies like Unilever and Colgate already served this market very effectively by using an Every Day Low Pricing (EDLP) strategy where products like shampoo, washing powder and aspirin are sold in tiny sachets or tear-off strips sufficient only for today's immediate use. Simply put, these consumers could not afford to spend today's entire budget on a single commodity, whether a large box containing a month's supply of washing powder or a voucher providing a week's supply of mobile phone airtime.

The Operator thus commissioned the development of a special low cost mini-recharge voucher and launched it with a face value of 20% of the previous minimum level. The response was immediate, with the turnover of the entire network increasing by a staggering 35% in only 6 weeks, and then continuing to grow steadily from there. Analysis showed that a large part of this immediate growth came from the immediate and sustained re-activation of the previously dormant SIM cards. Indeed, consumers who previously spent nothing per month when faced with the previous minimum purchase threshold would often now buy 8 or 10 vouchers a month, spending up to twice the previous minimum recharge price.

## Case Study 2

In the second case study, an Operator likewise launched new packs of mini-vouchers each with a face value of 25% of the previous minimum purchase threshold and grew 37% in 10 months. This Operator served a highly competitive market and analysis showed it had grown primarily by taking on consumers churning from the 3 competing Operators, who did not offer the same level of daily recharge affordability.

## Case study 3

In the third case study, an Operator reduced their minimum purchase threshold to 33% of its previous level and grew by a massive 55% in 8 months. This Operator had a total monopoly in its market and was found to have caused both the re-activation of previously dormant SIM cards and a substantial actual increase in the size of the national cellular phone market.

## Broadening Distribution

In all of these 3 cases, it was also interesting to note that the introduction of the new low-value vouchers took account of the reluctance of the normal formal distribution chain to handle such low value transactions by bundling them into 10-voucher packs. The process of breaking these down into single mini-vouchers for sale to end consumers was then carried out by informal traders, who appeared virtually overnight in each of these markets to purchase bulk packs from formal retailers and re-sell them. The appearance of this new level in the distribution chain was unplanned and occurred spontaneously in each case.

## Appendix C: Further Practical Details of Pre-Paid Models

### Set-top Boxes and Smart Cards

Consideration must be given to the need to cover the upfront cost of the set-top box and smartcard for flexible pre-paid consumers, since all future revenues will thereafter be uncertain. Following the example of the mobile phone industry, Operators could offer very basic low cost set-top boxes, encourage the resale / hand-down of used set-top boxes from high-end subscribers who upgrade their boxes (wherever security / encryption considerations allow this) and also offer special gift-orientated or seasonal promotions. Smartcards may need to be subsidised or offered at as close to cost price as possible with a view to recovering margins on expected viewer usage. Again, the simple logic is that once a person has managed to obtain a set-top box and a smartcard they have immediately become an additional potential consumer of the Operator's services, whether on a regular or an occasional basis.

### Interfaces with Subscriber Management System (SMS) and Conditional Access System (CA)

It is not always necessary to employ a traditional SMS to cover the new pre-paid consumers, since the CHKVIEW service can interface directly with the Operator's CA system to activate and deactivate the consumers' chosen packages and provides full transaction audit trails and extensive real-time reporting and lookup capabilities online. This can serve to further reduce capital and/or running costs for the Operator. However, the CHKVIEW service can also be alternatively or additionally configured to interface with an existing SMS and to activate and deactivate packages via the SMS and/or to upload batch files to it. An example of appropriate use of a dual CHKVIEW interface with both the CA and the SMS is discussed in the main text under "c) Offer Premium Events at High Volumes".

### Voucher Options

The CHKVIEW service offers many different kinds of scratch voucher products as PIN carriers to suit various product packages and retail environments; as well as electronic PIN delivery methods.

Physical vouchers range from scratch labels on a folded leaflet (which allow for a lot of information regarding new services) all the way to strings of very small tear-off strips each carrying a scratch panel and suitable for simple products like a single sports event or movie. Such products can then be sold in strings of 5, 10 or more at a time and kept at home by the viewer for impulse pay per view purchases. (Brand-ID has extensive experience in the selection of suitable scratch voucher products dependant on the details of their intended use, and will be happy to discuss with and advise customers as required).

It is also possible to use any available virtual PIN distribution channel. For example, in many countries mobile network PINs are printed out on till-slips by point of sale terminals in retail outlets or printed on slips at ATMs. Secure files of CHKVIEW PINs can be supplied to any of these virtual distributors, in addition to supplying CHKVIEW PINs in the form of scratch vouchers.