Financial Analysis of Broadcast TV Programming

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Abstract

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With a landscape of vertically integrated media conglomerates and new distribution windows constantly emerging, a TV show can generate multiple revenue streams complicating the economics of television networks. The purpose of this study is to analyze the revenue sources that can be associated with a TV show and their impact on programming decisions. Through a combination of econometric models, statistical tests and financial analysis, the researcher studied the internal and external factors that influence the four main revenue streams of TV shows: advertising, syndication, home video and online platforms. In addition, the DVR and other time-shifting technologies were observed. The data analyzed suggested advertising rates are a function of ratings, total ad spending, TV gross ad revenue and GDP while syndication, home video and online downloads depend mainly on the genre of the show. The shows that consistently generated larger income across all windows were high rated comedies. The DVR appeared to have little to no influence in programming decisions, however new media technologies showed potential to change the way viewers experience television.

Chapter One : Introduction

We have witnessed fundamental changes in the media industry over the past couple of decades. Not only the technological revolution, but also the deregulation had a profound impact in the structure of media companies. The vertical integration of media companies has permitted them to have operations in every step of the television value chain. In the television industry, it is not uncommon to find that a show was produced, distributed, aired and syndicated by the same media conglomerate. This extended participation in all the stages of a TV show has funneled the diverse revenue streams into one final recipient: the media conglomerate. The consolidation of media industries has changed the way television business segments perform and interact with each other.

As a TV show moves across the different stages of the television value chain there are several revenue sources and costs that can be associated with it. First and foremost, a TV show is created to attract the biggest possible audience and, as a consequence, to be appealing to advertisers. Besides advertising, there are other alternative revenue streams to be considered. Even after the show has been cancelled it can continue to generate revenue in many forms, including syndication deals, DVD/Blu-ray sales and VOD among others. Likewise, the digital revolution is changing the way viewers watch television. Online streaming and subscription sites are providing new sources of income for the media conglomerates. Every revenue source also comes with its corresponding cost, creating a very complex money flow.

At the center of the value chain are the television networks where the programming decisions are made. The advertising revenue goes directly to the networks; however they are not the recipients of other cash inflows like syndication, online distribution and DVD sales. The money from alternative revenue sources flows to other segments of the media conglomerates mainly in-house production studios that hold the distribution rights of the TV

shows they produce. In this context, the shows programmers choose to air have long-term repercussions on the profits of their parent companies.

Traditionally, network executives made decisions mainly based on ratings, which are the best estimation of potential advertising revenue. However, with the current state of vertically integrated companies and new technologies in the mix, estimating the potential revenue throughout the lifespan of a TV show and beyond has turned into a very complicated task. Executives are now forced to consider not one, but several revenue streams as well as associated costs for every show they decide to put on or take off the air. Television is a business and as any business the main goal is to maximize profit, in order to achieve this objective managers must find the way to maximize revenue and minimize costs. In favor of maximizing profits at a corporate level, programmers need to perform a complex cost-benefit analysis of the potential revenue and costs associated to a TV show throughout the value chain. In addition, corporate managers need to find a way to incentivize network programmers to look beyond the immediate advertising revenue and consider the overall profit-generating potential of each TV show they decide to put on their schedule.

Statement of the Problem

Traditionally, network programmers focused on the immediate advertising revenue and perhaps gave some thought to the syndication revenue of the shows in their line-up. However, the television industry has suffered many changes over the past two decades. The emergence of new technologies and broadcasting outlets, paired with the vertical integration of media companies, has transformed the value chain of the television industry. Media conglomerates are complex structures that have integrated operations across the entire television value chain. Broadcast networks are a part of these conglomerates and they are privy to the advertising revenue. They are also the primary outlet for TV shows and the place where programming decisions are made. Subsequently those shows will move along the value chain generating income for other segments of the media conglomerates. The true

value of a TV show results from the aggregation of all the different revenue sources it may generate for several segments of a media conglomerate minus the corresponding costs. We will take into account that the cost component of the equation is a known measurable variable and therefore this study will focus on the analysis of the different revenue streams. The only way for programmers to maximize the overall profits of their media companies is to understand all these revenue streams and not focus solely on the advertising revenue. This study will study how vertical syndication could have an impact on the programming decisions at a network level and how these decisions later have an impact on the consolidated profit of their media conglomerates. Additionally, the study will discuss current practices and analyze how programmers could further improve the overall results of their media conglomerates.

Beyond advertising revenue, network programmers should look at alternative revenue streams that include: syndication, home video and new media. With the vertical integration of media conglomerates, many networks' parent companies are also owners of their prime-time TV shows and therefore they are the beneficiaries of the syndication revenue. Other important cash inflow during the past decade has been home video, which took a new life since the introduction of the DVD box set and continued with the inception of Blu-ray discs and VOD (Video On Demand). Finally, new media technology introduced alternative windows with the potential to generate revenue; nevertheless, it should also be taken into account that advances in technology have increased time shifting among viewers which has had negative repercussions on the advertising revenue. We will analyze the issues related to each of these revenue streams starting with the most traditional one: advertising.

Advertising revenue. We have mentioned that the revenue generating potential of a TV show goes beyond the advertising dollars; nevertheless, that does not mean advertising revenue should be disregarded. Advertising is the most immediate revenue stream and the

only one that goes directly to the broadcast network and is a main concern for network programmers.

Advertising revenue is directly tied to ratings, the shows with the highest ratings are the ones that generate higher advertising revenue. Therefore, the main concern for programmers is to select the shows that can maximize the number of viewers. If maximizing the broadcast network's profit was programmers' only concern, the analysis would end here. However, as we have mentioned, networks are only a small part of media conglomerates and to achieve optimal results the profits of all segments should be maximized. Having said that, advertising revenue is one of the major revenue sources and programmers simply cannot ignore it. A show that does not generate a sufficient amount of advertising revenue cannot survive on the schedule. Eastman and Ferguson (2009) assert that the inability to have a hit series eventually affects all other aspects of the business. Therefore the first step to achieve optimization is to maximize the advertising revenue of the lineup.

To achieve that goal, programmers make use of several scheduling tactics. In addition to audience size, programmers are also concerned with the demographic characteristics of the viewers. Most advertisers have their preferred target markets and programmers need to deliver the desired audiences. Moreover, the rise of cable has threatened the supremacy broadcast networks once had in the television market. Programmers need a deep understanding of the advertising industry in order to be able to effectively pick and schedule the shows that have the potential to generate the maximum amount advertising revenue.

Syndication revenue. The most traditional secondary window for a TV show is syndication. Syndication is the business practice by which a producer (content owner) sells the rights to retransmit a show in a determinate market for a period of time (Eastman & Ferguson, 2009).

Many shows that air on broadcast networks are in-house productions. This means their sister companies (part of the same media conglomerate) produce and own the show. In that event production houses are entitled to receive the syndication revenue. Hence, networks may not directly benefit from syndication but their conglomerates do. Network programmers are the ones who decide which shows to put on the air and, in order to sell on syndication; a show needs to premiere on a broadcast network first. In this context, the decisions of network programmers have an impact on the revenue of the production houses.

The conflict arises when advertising revenue is not directly correlated to syndication revenue. In this context it becomes difficult to determine which shows have the biggest revenue generating potential for the networks. Generally, high rated shows sell well on syndication, but this is not always the case. Occasionally shows that were hits during their broadcast runs have no afterlife in syndication and vice versa. Programmers determine which shows are put on the schedule and for how many seasons. The number of episodes is another key factor for the success of a TV show in the syndication market. In order to pick up shows with high syndication potential, programmers need to understand how the syndication market works and what type of shows sell better in syndication. Finally programmers need to balance advertising revenue versus syndication potential and select the shows that can maximize the revenue of both segments. If programmers are able to do that, they would be one step closer to reaching efficiency at a corporate level. However, the analysis does not end here; there are still other revenue sources to consider.

Home video market. To further complicate the analysis, advertising and syndication are not the only significant revenue sources of a TV show. Another important aftermarket revenue stream is home video. During the VHS area, television home video sales were not significant; however since the introduction of the DVD the situation has changed. Nowadays, home video is a considerable secondary window with high revenue generating potential.

In an analogous way to syndication, content owners (production houses) are the recipients of the home video sales revenue. Hence, when TV shows are owned by the same media conglomerate that puts them on the air, they can also benefit from the home video sales. In this sense, home video becomes a third revenue source associated to a TV show, complementing advertising and syndication.

Not every TV show performs well on the home video market, but the ones that do may generate big gains for the content owners. Home video sales potential is other variable programmers should take into account when making their programming decisions. Some shows may have low ratings, but big potential in the home video market. In this case, programmers need to determine up to what point they can sacrifice the advertising revenue in favor of future video sales potential.

Time shifting technology. Viewers now have the opportunity to watch TV shows at the time of their convenience. This phenomenon is referred to as 'time shifting'. The practice of time shifting has taken off due to the advances in video recording technologies such as the DVR as well as the increase in online streaming offerings.

Time shifting is a practice that may affect the revenue structure of the television shows that air on the networks. Time shifting has the potential to affect the advertising revenue because of two factors, delayed playback and advertisement avoidance. If viewers record TV shows on their DVRs for later playback, they will not be counted on the 'live' audience. Advertisers mostly look for 'live' viewers and they will usually not accept to factor in DVR playback in their negotiations with the networks. In addition, DVR has facilitated skipping commercials which is also detrimental to the networks' advertising revenue. On the other hand, online streaming is another way of time shifting, but in this case it is also an additional window for content owners. Content owners benefit from streaming their content online in the form of license fees and online advertising. Therefore, time shifting technology is a two blade sword, challenging existing windows on one hand and creating

new revenue sources on the other. Programmers need to take into account time shifting and decide how they can implement actions to take those effects into account. DVR may be a threat to advertisers, but it could also be an indicator of viewer's engagement. Online streaming produces a small percentage of the total revenue of the media conglomerates; however it is a segment with high potential of growth. Executives across the media conglomerates cannot ignore the impact of these technologies.

Media companies have become large companies that encompass many segments. The structure of today's media conglomerates is ideal for the creation of synergy within the company. Rather than operating as individual segments, broadcast networks should be regarded as an engine that can help generate profits for all the other business units. In order to achieve overall maximization of profits it is important for network programmers to understand the complete impact of their programming decisions on the bottom line of their parent companies. Starting with the advertising revenue, TV shows are products that generate revenue from many sources. The optimal lineup will feature the TV shows that can maximize the total revenue (including advertising, syndication, home video and new media) and minimize costs. In order to achieve that objective, programmers should have a clear understanding of the factors that determine each type of revenue mentioned above and the relationships between each other.

Background and Need

During the 1980s and 1990s, broadcast networks became part of giant international entertainment media companies as a response of declining ratings that pressured stockholders to sell their shares. Subsequently, the newly formed media conglomerates pressured the FCC (Federal Communications Commission) to relax some of the rules governing broadcasters. The FCC made some dramatic changes that favored broadcasters. The most notable changes included the relaxation of ownership regulations and the fin-syn rules. The FCC allowed networks to own television stations across the country, with the

potential to reach most of the population. Simultaneously, the FCC relaxed the financial interest rules (fin-syn) allowing media companies to own the programs they broadcasted. Therefore "the entire programming process, from production of programs (by owned studios) to distribution via the broadcast or cable network through owned stations and cable systems, to publicity from the units that promote everything, is controlled by the same enormous companies" (Eastman & Ferguson, 2009, p.124).

Consequently, business decisions made at the highest level of the parent corporations have an impact on all the subsidiaries, including the broadcast networks. On the other hand, programming decisions made at the network level also have the potential to impact the entire corporation's performance. This study will explore the impact of programming decisions on other business segments and overall performance of the media conglomerates.

The value of a TV show results from adding all the profits it can generate in the different stages of the television value chain; including: advertising during the network run, as well as aftermarket revenue streams like syndication, home video and online. Programmers jump start the chain by selecting the shows that will air on the networks. Later, those shows will produce income in the form of advertising, syndication, DVD/Blu-ray sales, VOD and online streaming. Each revenue stream has its characteristics that need to be understood in order to achieve an optimal result. Moreover, not all revenue sources are directly correlated and achieving optimization across segments could be harder than it looks. In this context, programmers and other media executives first need to understand the elements that influence each revenue stream, and secondly, they need to understand the relationship between revenue sources and what TV shows have the potential to generate the highest aggregated income for their conglomerates.

Advertising revenue. Broadcast television networks are an ad-supported business. In other words, their main source of revenue is advertising. Television networks' objective is to attract the largest number of eye-balls so advertisers can deliver their commercial messages. Maximizing the advertising revenue is the main concern of broadcast networks. To achieve this goal, the lineup needs to maximize audience size which is measured in the form of ratings. Furthermore, programmers should balance the advertising revenue of a show with the potential it has to generate other income in secondary windows.

The most common programming practices for commercial television are documented in the literature reviewed. Eastman and Ferguson (2009) explore in detail the aspects that impact programming decisions and ratings behavior. In their book *Media Programming*, they also include a comprehensive summary of the scheduling techniques programmers use with the objective to maximize rating points and outperform the competition. In addition to internal decisions and programming business practices, advertising revenue also depends on external factors. Trade publications and economic journals follow the evolution of the advertising market that, as any other industry, is linked to the general economic performance of the country. SNL Kagan tracks the total advertising spending as well as television's share for a period of over ten years. In addition to macroeconomic variables, television's advertising revenue has also been subject to other external influences that include the increased cable viewership and the use of the DVR ("Economics of TV…", 2007).

All the factors mentioned above have an impact on the total advertising revenue and on the advertising rates networks are able to charge. The direction and magnitude of this impact is explored on several industry articles and reports. Lotz (2007), among other authors talks about the concept of 'scarcity' of rating points. The decline of ratings creates scarcity of viewers driving the price per ad-spot up. This counterintuitive situation is one of

the reasons advertising revenue is still a major source of income even though broadcasters' ratings have been shrinking during the last decade.

The current programming and scheduling tactics used across the industry are the result of research and experience. However, the industry is evolving and programmers need to perform more complex analysis that factor in many new variables. Due to vertical integration, programmers need to include the potential revenue of shows on other windows like syndication, home video and online. Not much research has been done about programming decisions based on multiple revenue sources. This study will present a more comprehensive model that can systematize programming decisions in an era of vertically integrated media companies.

Syndication revenue. After the relaxation of the fin-syn rules, media conglomerates had the opportunity to benefit from the syndication revenue. Syndication can be a very significant revenue stream even after a show is off the air. The syndication revenue for a TV show can, in some cases, exceed the advertising revenue. However, not every show has the potential to be sold in syndication due to a number of factors including number of episodes, breadth of appeal and particular genre.

Syndication deals have been part of the television industry for a long time. Fletcher (2006) and Eastman and Ferguson (2009) provide a review of the syndication business including the main players and key points of a syndication contract. Furthermore, Oba and Chan-Olmsted (2006) analyze the impact that vertical integration within the industry has had in the U.S. syndication market. In alignment, SNL Kagan monitors the percentage of ownership networks have of their own schedule. In other words, it is analyzed whether network programmers favor shows that are owned by their sister production houses.

The syndication market has being evolving over the years. Among other changes, the once predominant buyers of syndicated content (local television stations) have ceded way to cable networks ("Media Trends", 2009) which are becoming the "shining spot for TV

distributors" (Myers, 2009a, p.1). In addition, syndication deals are starting to include digital rights and we have started to see the first direct-to-streaming syndication deals (Myers, 2011). With a rapidly changing industry, like television, new deals and negotiations happen every day. Trade publications follow the latest syndication deals. SNL Kagan summarizes the key syndication deals and their main characteristics in a series of data books and reports.

As with advertising, there has been a lot of interest in the syndication revenue; however, most of the research has been done on a stand-alone basis. The literature reviewed fails to address how the decisions made by network programmers may have an impact on the revenue that is later received for syndication. Another area that could be further explored is syndication potential by genre. Previous research mentions what type of shows are preferred in the syndication market; however the analysis is not extensive.

Home video market. For media conglomerates, another benefit of owning the programs they broadcast is receiving the revenue from home video sales. Television video sales revenue became a major source of income for content owners since the introduction of the DVD set box. The Blu-ray disc has been following the same path and Video On Demand has been thrown into the mix. To better understand the current dynamics of the home video market we first reviewed its evolution throughout the last couple of decades. An article by Kompare (2006) focuses on the historical context of the home video market and discusses the importance the DVD technology had on television. Additional work by Bianculli (2002), Hernandez (2003) and Brookey (2007) provides better insight on the factors that made the DVD so well received by consumers.

The latest developments in the home video market can be studied by the review of current articles on entertainment and technology journals. The market of physical formats has two main players: the new Blu-Ray disc and the established DVD. Blu-ray has three distinctive advantages over DVD: better image, sound and more special features ("Blu-ray vs. DVD). Although in decline, DVD is still the predominant format in the home video market

with much larger sales than Blu-ray and VOD combined (Digital Entertainment Group). Moving away from physical discs, some believe the future of home video relies on the digital space. Holden (2009) explores the potential transition to the digital world and to VOD services instead of physical discs. Through a series of interviews with industry insiders, Carr (2011) provides a different perspective. Even if he agrees the market will continue to gradually transition to VOD services, he presents the idea that physical formats, in the form of collectible items, will continue to have a place in the market.

From a financial point of view, historical revenue data can be found on databases like SNL Kagan ("The state of home…", 2009) and the Digital Entertainment Group. Statistical data can be easily found for the home video market as a whole; however there is no data that separates movies from television. The studios do not disaggregate the home video revenue in their financial documents either.

In later years, much of the researchers' attention has been devoted to new media technologies and studies of home video have been scarce. It is true that the television market is transitioning to the digital age and that the market is quickly becoming more interested in online streaming. Nevertheless, home video is still an important part of the overall revenue for media conglomerates. The literature reviewed also indicates physical formats will have a place in the television market. Therefore, understanding the segment and reviewing updated data is necessary for the present study. Furthermore, there has not been extensive research on what type of genre sells better in the home video market. It is a common notion that the so called 'cult hit' shows have incredible potential with merchandising sales, including DVDs and Blu-ray discs. However, there are no many formal studies that seek to find a link between ratings and home video sales or to explain other factors that determine the home video sales potential.

Time shifting technology. Time shifting makes reference to the practice of watching a TV show in a time different to its original telecast. Advances in technology have made this practice quite common amongst viewers. Currently the main time shifting tool is the DVR. This technology has brought advantages and disadvantages for media companies. In addition to DVR, consumers are also finding ways to time shift using the internet.

DVR technology has shifted control back to the viewers (Wilbur, 2008); however, this shift of control results in some negative side effects for the networks. Wilbur discusses how viewers are avoiding commercials making use of the DVR technology. Other authors provide a series of perspectives on the impact of the DVR. The general perception of advertisers is that the DVR is negatively impacting ratings. Nevertheless, Carter (2011) provides a new point of view, explaining how the DVR may be also giving some more obscure 'cult hit' shows a life-line. The positive implications of the DVR are mentioned in a series of other trade publications that will be reviewed.

As for the internet, SNL Kagan ("The State of Online…", 2011) provides the most comprehensive and up-to-date review of the internet video delivery services (over the top). The main concern of the over the top market is to find a delivery model that can successfully monetize online streaming. As of right now three different models prevail (ad-supported, subscription and paid), each of them with positive and negative implications from a financial point of view ("The State of Online…", 2011). In addition there is a lot of attention given to the most prominent online streaming video services including Hulu, Netflix and iTunes in journals and trade magazines. The services mentioned above are in constant evolution. A revision of current industry news provides insight on their latest developments.

The positive connotations of the DVR for some TV shows have recently been the focus of attention. Some TV shows present gains of over 60% when the ratings of an entire week are computed ("Live Plus Seven"). This situation may influence programmers' decisions when it comes to picking up shows. Advertisers do not respond to playback for

longer than three days, however, programmers are looking into seven day gains trying to determine the level of viewers' engagement. This engagement could be manifested as revenue in other windows. There is a gap in the research that links DVR playback with other revenue sources in the television chain and it is a common theme for our research. Perhaps Live plus seven ratings are of no use when negotiating with advertisers; however it could be valuable information to analyze the potential income on other windows. The same could be said for online revenue, where the different delivery models are still struggling to find their place in the market. Online revenue is one more window in the television value chain and its relationship with other segments of the business has not yet been fully explored.

In summary, a television show has the potential to generate revenue for their media companies in many windows. After the initial broadcast which generates revenue in the form of advertisement, a television show can be sold in syndication, home video and online video delivery services. There has been a lot of research conducted that explains the mechanics and variables of each window individually. However, there have not been many efforts to understand the relationship that exists between each other. It is a well known fact that programmers' decisions are influenced by their parent companies, yet there is no formal research that directly links programming decisions with financial income in later stages of the value chain. In order to understand the true value of a TV show from a product point of view it is not enough to understand the revenue streams on a stand-alone basis, the correlation between variables should be explored.

Purpose of the Study

The purpose of this study is to analyze the revenue sources that can be associated with a TV show in order to determine its overall financial value and help students and professionals in the field understand programmers' decision-making process.

Determining the actual value of a TV show is not as simple as looking at its advertising revenue anymore. There is a need for a valuation model that can systematize the

decision-making process in a comprehensive manner. Research has been conducted on the several revenue streams associated with a TV show, however previous research covers each revenue window on an individual basis and failed to explore the relationship between each other sufficiently in depth. In addition to a lack of cross-segment research in the field, there is also a scarcity of tools that combine financial analysis with media industry operations. The researcher explored the elements that influence programming decisions and constructed a valuation model with the findings. This model will be presented as a fictional case study (Appendix B) that could be used by students and professionals in the field to improve their understanding of the industry's current state.

Determining the value of a TV show is a task that involves a detailed quantitative and qualitative analysis of several variables that will be discussed in detail in future chapters. In order to narrow down the analysis, this study focused on a particular day part: prime-time and a specific genre of show: one-hour drama. The study included the analysis of TV shows that premiered during the past decade (2001-2010). Four revenue streams were analyzed: advertising, syndication, home video sales and online. Additionally, the impact of the DVR was taken into account. The researcher analyzed numerical data for each individual revenue source and cross-referenced the information to find links between the different segments. Finally the researcher summarized the findings in a fictional case study with a suggested solution. The case study can be found on Appendix B.

As a result of the study, it was expected to find the relative importance of each revenue stream. The expectation was to find that maximizing the advertising revenue is not enough to reach optimization at a corporate level and that the most efficient results are achieved when all the revenue sources are balanced to reach the maximum overall profit. Therefore it was expected to conclude that programmers need to pick shows that have the biggest revenue generating potential across all windows. Another goal of the study was to

build a comprehensive case study that would allow students to perform a complete financial valuation with realistic data that reflects the current state of the television industry.

Research Questions

- What are the micro and macro factors that affect the advertising revenue a TV show can generate?
- What are the variables that determine the success of a TV show in the syndication market and how much does it depend on its performance during the original broadcast?
- What types of shows have the biggest potential in the home video market and how did they perform during the original broadcast?
- What is the impact of DVR playback on the ranking of TV show and how can this affect programming decisions?
- How significant is the revenue a TV show can generate on online platforms?

Significance to the Field

This study has two main objectives: 1) expand the research in the field of television management and 2) provide a systematized model that can help improve and understand programmers' decision-making process. Most of the research conducted in the field of television has been from the communications and social sciences perspective. In the present study, the researcher will mainly take a financial approach. The end result will be the creation of a systematic valuation model that can be used to calculate the value of a TV show from a financial point of view. This analysis is of particular importance in a business context, since it can shed light on the way programmers approach their scheduling decisions in a heavily integrated industry. The findings of the study will be summarized in a fictional case (Appendix B) study which will help accomplish another objective: provide a tool that could be used by students and professionals in the field to comprehend the programming process and the television value chain. So far, the field of television management is lacking

didactic tools that can be used in the classroom as a way of analyzing the industry with a serious business approach. The fictional case study resulting from this research would make it possible for television/media management students to have a study tool similar to the ones used in business classes.

Definitions

- **Content owners:** For the purpose of this study this term refers to the production company of a TV show, therefore the terms “content owners”, “production studios” and “production houses” are used indistinctly.
- **FCC (Federal Communications Commission):** An independent agency of the United States Government that regulates electronic communication by radio, television, satellite and other means.
- **Fin-Syn rules (Financial Interest and Syndication rules):** Rules that enforced by the FCC that prohibited the establishment of in-house syndication arms and prevented networks from having an interest in the programs they broadcasted beyond the first-run.
- **Live Plus Seven:** Ratings that take into account DVR playback up to seven days after the original telecast**.**
- **Live Plus Three (C3):** Ratings that take into account DVR playback up to three days after the original telecast.
- **New Media:** Media vehicles that rely on digital technology for distribution and exhibition.
- **Off-network:** A syndicated show that originally aired on broadcast television.
- **Off-cable:** A syndicated show that originally aired on a cable channel.
- **O&O:** Local stations that are owned and operated by one of the major networks.
- **Over the top (OTT):** Delivery of video content via the internet.

- **Ratings:** Throughout this paper when we talk about ratings we are referring to the Nielsen ratings that can be defined as the number of viewers watching a TV show at a particular time divided by the total number of viewers that have a TV set in that market area.
- **Share:** Number of viewers watching a TV show at a particular time divided by the total number of viewers that are watching TV at that time in that market area.
- **Syndication:** The business transaction by which the content owners sell the rights to distribute the shows they produce.
- **Television Value chain:** The chain of activities that are involved in the creation, production and distribution of a TV show.
- **Valuation model:** A systematized tool that allows calculating the financial value of a product, in this case a television show.
- **Vertical Integration:** Expanding the operations in a way that multiple steps in the production and distribution of a product are controlled by one parent company.

Limitations

Like any other study, the present work has some limitations that need to be addressed. The first consideration to be taken into account is the fact that the researcher focused on the analysis of four revenue sources associated with a TV show: advertising, syndication, home video and online delivery. Those revenue streams are the most significant and account for most of the total revenue of a TV show, however, there are not all the revenue sources in existence. For instance, the revenue of other items like merchandising revenue is ignored. The impact of other minor revenue sources probably would not be significant, but it is still important to note that the four sources included in the research are not exhaustive.

The advertising revenue was considered to be associated to a particular TV show. It is true that ad-spots during a TV show are priced and sold based on its ratings' performance.

However, networks have the practice of packaging hit shows with least successful ones to sell to advertisers. This bundling component was not taken into account.

The main constraint of the study was the lack of detailed quantitative information. The financial information provided by the media conglomerates is consolidated and they do not disaggregate their accounts, online services like Hulu do not disclose financial details and some syndication deals are not made public. Therefore, some of the data used is based on estimates from industry professionals.

Finally, the study had the objective of modeling the decision-making process of programmers at a network level. It was not possible for the researcher to speak directly with industry insiders. As a consequence many assumptions were made in relation to the programming decisions that were made in the past. It is possible that some factors not taken into account by the researcher were in play when programmers made their decisions.

Ethical Considerations

The researcher took steps to ensure the accuracy of scientific knowledge and responsible manipulation of data and reporting of the results. Numerical data were obtained from trustworthy sources such as SNL Kagan, Deadline, Variety and Broadcasting & Cable among others. The data were not modified and results were reporting without omissions. In addition, the researcher respected the norms for quoting and paraphrasing material written by others and adhered to the limits of fair use in accordance to the APA manual and the copyright law.

Chapter Two : Review of the Literature

Television is a form of entertainment, but it is also a business like any other. As a consequence, every programming decision has the ultimate goal of maximizing revenue. The programming decisions made at a network level have an impact in the advertising revenue, but also on the aftermarket revenue windows for other business segments. To achieve optimization at a corporate level, all the revenue streams must be maximized. Programmers must find a way to accurately estimate the potential revenue of each television show in order to make informed decisions. Vertical integration of media companies has made this task somewhat more complicated. No longer is the advertising revenue the only source of income, but programmers also need to consider DVD sales, syndication and the impact of new media technologies. Each of these revenue streams brings an associated cost to be considered as well. The challenge is to build a valuation model that will allow the user to input the data of a particular TV show and estimate the potential revenue streams and costs all throughout the show's life and beyond. Many scholars have studied the diverse financial dimensions of TV making and the researcher compiled some of their most important findings.

The researcher assumes that the different costs associated with a TV show are known variables that can easily be computed by the media companies using their internal records. The difficulty, when studying TV shows profitability, is to understand the different revenue streams. The literature review will address four areas related to the financial performance of a TV show. The first section will address research related to the first and most traditional window: advertising revenue. The second section will focus on research studies about TV syndication. The third section will focus on the home video market. Finally, the fourth section will discuss research related to the impact of time shifting technology.

Advertising Revenue

Advertising dollars are traditionally the first and most important consideration for television programmers when building their schedules. “The overwhelmingly commercial US television industry relies on the sale of commercial time to support the production and distribution costs of nearly all the television content watched by the nation’s viewers” (Lotz, 2007, p.550). For this reason, it is impossible to start a discussion about broadcast television financials without understanding the advertising market.

The business model of broadcast television was built on the basis of advertising. Advertisers pay extraordinary sums of money to broadcasters, which in turn deliver viewers that are exposed to their commercial messages. On that account, programmers have one main goal: to schedule shows that attract the largest possible number of viewers. “The primary goal in programming advertiser-supported media is to maximize the size of an audience targeted by advertisers” (Eastman & Ferguson, 2009, p.3).

While it is true that the networks have seen their advertising dollars threatened in the last couple of years, selling ad spots is still a major concern for broadcasters. In Lotz’s words: “Understanding the means by which the US commercial system allocates the funding for creative production is necessary in order to evaluate subsequent components of the process” (2007, p.560).

The “currency” for the transactions between broadcast networks and advertisers, as Lotz (2007) explains, are cost-per-thousand (CPM). Cost-per-thousand (CPM) refers to the “Advertisers' cost-per-thousand viewers exposed to a commercial” (“Nielsen Media Research’s Glossary…”). In this context, advertising revenue is directly tied to ratings performance. The highest the ratings for a particular show, or the highest the price the network can charge for an ad spot. However, the advertising market is a little more complex and there are some other considerations that need to be taken into account in order to fully understand the process.

One of the first considerations to understand advertising revenue is understanding the difference between day parts. “Programmers strive to make their programming compatible with the day’s round of what most people do” (Eastman & Ferguson, 2009, p.13). CPMs vary across day parts since their demographics are very distinctive. Traditionally, the highest CPMs are seen in prime-time due to higher average ratings and the presence of desirable demographics. We will explore what makes a demographic desirable for advertisers later in this section. Talking about prime-time, Eastman and Ferguson write: “The 22 prime-time hours (…) constitute the center ring for the traditional networks, the arena in which their mettle is tested” (2009, p.128). The present study will focus on that particular day part. The importance of prime-time hours for the networks is undeniable, “while the rating difference between prime-time and non-prime-time periods may not be as large as it once was, prime-time is still the most heavily promoted and most talked about part of any schedule” (Eastman & Ferguson, 2009, p.128).

Prime-time may be the most important day part for broadcasters; however, the revenue potential has been significantly threatened by diminishing ratings. Writing about this phenomenon, Myers says: “Tough economic conditions and competition from cable networks and the Internet seem to have taken a toll on the broadcast networks' most valuable real estate: prime-time” (2008a, p.1). We will discuss some of the factors responsible for the decrease in broadcast ratings and the consequent contraction of advertising revenue next.

There was a time when broadcast networks were the undeniable leaders of the television advertising market, nevertheless; that is no longer the case. Cable networks have gained more terrain in the last couple of decades, as explained by Baine: “In 1990, the cable nets were generating just 18% of broadcast network revenue, but by 2000 that jumped to 60% when cable networks surpassed $10 billion in revenue for the first time”(2007, p.2). In fact, by 2008 cable billings exceeded broadcast billings for the first time (“TV billings…”,

2010). By 2010, cable billings represented 115% of broadcast networks' total advertising revenue ("TV billings…", 2010). In other words, broadcast networks had been the dominant force in the advertising revenue pie, until 2008 when the situation reversed and currently cable's share continues to grow as broadcast's shrinks.

In addition to the threat of cable, broadcasters had to face another menace in the form of DVR. Repurposing, online viewing and mobile devices are other considerations that may jeopardize traditional advertising. The factors mentioned above will be explored in later sections of this literature review. A final consideration is the general state of the economy, as a downturn in the economy limits the advertising budgets of major companies which, in turn, has a negative impact for commercial television networks. As the title of an article published in *The Economist* would suggest: "Ad-spending usually plunges when economic growth slows" ("Ad-spending usually…", 2008, p.1). In the same article it is explained that marketing expenses are generally the first to be cut when companies face financial difficulties.

The loss of viewers to cable channels combined with other threats, like the introduction of the DVR and the economic downturns have had an impact on the advertising revenue of the Big Four networks during the last couple of years. The networks started noticing a contraction of their advertising revenue around the year 2007. It was evident by then that the networks' cost per share point (Cost of one or a series of commercials divided by the share points of the show) was in a downfall. "ABC, CBS, FOX and NBC averaged a $16.7K cost per share point at the beginning of the 2005-06 season compared to a $15.8K mean for 2006-07" ("Economics of TV…", 2007, p.41). The descending trend continued for the next couple of years. The average ad spot price for the Big four networks (ABC, NBC, CBS and FOX) was $135K by 2008. In 2009 this average was only $117K (SNL Kagan).

As explained in an article in *The Economist*, 2008 was a relatively good year for advertising sales mainly because of the presidential election, the Olympics in Beijing and the

European Football championship ("Ad-spending usually…", 2008, p.1). On the other hand, 2009 was a difficult year for broadcast networks which were affected by the general economic downturn. The total advertising market suffered a drop in revenue of 15.6%. Broadcast networks were amongst the sectors more deeply affected, showing a revenue decrease of 22.4% while cable's revenue only fell by 4.2% ("Advertising Forecasts", 2010).

Even with the adverse conditions broadcasters had to face in the latest years, up until 2008 networks managed to remain profitable. The following passage appeared on a SNL Kagan report:

> Broadcast networks have been struggling for many years due to the rise of cable networks, which they have battled for both viewers and ad dollars. While broadcasters mainly rely on just one revenue stream (advertising), they have done surprisingly well over the past several years. The Big Four (ABC, CBS, FOX and NBC) have all generated positive cash flow in the past couple of years ("Media Trends", 2009, p.221).

However, the situation reversed on 2009. The Big Four's cash flow was significantly reduced. ABC had crossed over to negative cash flow by 2009. By 2010, all four networks, with the exception of CBS, had negative cash flows (SNL Kagan).

As mentioned, broadcast networks have steadily been losing audiences and experiencing difficulty with their cash flows over the past years. The logical conclusion would be that the CPMs and Gross Rating Points (a measure of the exposure to one or more commercials without regard to multiple exposures) of every network will also lose value. However, the opposite has occurred. Lotz describes this as:

> The introduction of new channels and viewer migration to them has decreased supply of gross rating points (GRPs) on broadcast networks. A decrease in broadcast supply of GRPs leads to an increase in demand and explains the increasing costs of advertising on broadcast networks despite their diminishing audiences (Lotz, 2007, p.564).

In fact, the correlation between CPM and rating points is negative and close to one, which suggests an inverse relationship between available audience and commercial spots' price. As in any other industry, the laws of supply and demand apply to the advertising

market. As reported by Myers (2010b), there was an increase of more than 8% in the average ad spot in 2010. The increase in 2010 was not a consequence of higher ratings; it was a result of higher CPMs. Broadcast networks continue to lose viewers, but in 2010 they were able to increase their prices. As viewers become scarcer, advertisers struggle to find mass audiences to deliver their commercial messages. Consequently, there is an excess of demand for eyeballs and networks are able to increase their average CPMs.

However, not even cable has been able to replace broadcast as the preferred mass media vehicle. “Despite viewers migrating away from broadcast networks over the past couple of decades, advertisers continue to look to them for drawing on the largest number of eyeballs” (“Economics of TV…”, 2007, p.42). Thus, broadcasters are able to charge higher CPMs than cable. To illustrate this point, the average CPM for broadcast networks in 2010 was $27.24 while cable’s average was only $5.41 (SNL Kagan). Basic cable is gaining terrain in the advertising market and they are billing considerable amounts, however their price per unit is only a small fraction of what broadcasters are able to charge.

We have discussed how cable has been stealing viewers from broadcast networks over the past few years, only to later conclude that broadcast channels are the biggest audience draws and are still the preferred vehicle for advertisers. To further examine this point, we take a look at the ratings of basic cable and broadcast networks. As a whole, cable currently has a better rating performance than broadcast. The aggregated rating of all basic cable networks is 42.1, while broadcast’s is merely 22.5 (SNL Kagan). From those numbers alone, one could conclude that the viewers are to be found on cable television and that advertisers should disregard broadcast networks. However, a closer look at the ratings would reveal that broadcast’s 22.5 rating results from adding the ratings of 11 networks (the big four amount to over 80% of that total rating); on the other hand cable’s impressive overall 42.1 rating is spread over 85 networks. Therefore, the reality is that the average

broadcast rating is 2.06 while the average cable channel only produces a 0.5 rating (SNL Kagan).

The Big Four networks combined have an average of 21 million viewers (SNL Kagan, 2010). In order to reach that number of viewers on basic cable we would need to aggregate the viewers of at least 19 of the top rated cable networks. The top rated cable networks are so diverse that they would never be able to reach a homogeneous audience, which brings us to our next point. Cable networks are usually targeted to a very specific niche market. For instance, the History Channel is very popular with male viewers while Lifetime has a predominantly female audience. Some networks pursue even smaller segments like the SyFy channel, The Golf Channel, The Food Network, etc. In other words, cable networks are great for targeting specific segments; however, if mass audience is what advertisers are looking for, broadcast is still the way to go.

The previous discussion is important to understand the general process of ad sales in broadcast television and how the economic conditions and other elements impact the advertising revenue. However, this study pretends to concentrate on the revenue potential of a TV show from the product point of view rather than the overall network strategy. So far, we have examined how networks sell advertising and how the market is responsive to general economic laws at the macro level (economic cycles) and micro level (demand and supply). We have also discussed the basic relationship between ratings and advertising revenue. We will continue this literature review with a closer look of the advertising revenue at the show level as opposed to the previous discussion on networks.

Programmers are conscious about the importance of having high rated shows in their lineups. Having a hit show can make or break an entire schedule and impact the main source of revenue: advertising. Because of the decrease in ratings the average ad spot by network is much cheaper than years ago. “The average ad spot price for the networks' debuting schedules was $127K [2010], up from $117K last year, but still down from the

$135K of 2008-09" (Myers, 2010b, p.1). The most expensive shows for advertisers during the season 2010-11 were *Sunday Night Football* and *American Idol*.

> The top-priced program debuting in the fall was NBC's "*Sunday Night Football*," which generated $415,000 per 30-second spot, a large jump from the $340,000 asking price during the 2009-10 season. "*American Idol*" tops as the highest-priced midseason replacement at $470,000, while the results show costs advertisers about $400,000 (Myers, 2010b, p.1).

Other major players of the 2010-11 season were: *Glee* (FOX), *Grey's Anatomy* (ABC) and *Two & Half Men* (CBS). Both *Grey's Anatomy* and *Two & Half Men* represent the most costly shows for their particular networks at $225K and $205K per ad spot respectively (Myers, 2010b, p.1). "Weblet CW trails considerably, with its most expensive show at $75K ("*Vampire Diaries*")" (Myers, 2010b, p.1). Table 2.1 summarizes the 10 top shows classified by Ad Spot price.

Table 2.1
Top Ten Shows of the 2010-11 Season Classified by Ad Spot Price

Rank	Show	Price per spot ($ 000)
1	American Idol	470
2	Sunday Night Football	415
3	American Idol (Results)	400
4	Glee	375
5	Glee	270
6	Family Guy	260
7	The Simpsons	250
8	Grey's Anatomy	225
9	House	225
10	The Office	215

Note. Source: SNL Kagan

Table 2.2
Top Ten Shows of the 2010-11 Season Classified by Ratings Performance

Rank	Show	Rating/Share
1	American Idol	8.8/24
2	Sunday Night Football	8.0/20
3	American Idol (Results)	7.7/22
4	The Voice	5.4/14
5	Modern Family	4.8/12
6	Dancing With the Stars	4.8/12
7	The Big Bang Theory	4.4/13
8	Grey's Anatomy	4.3/11
9	Survivor: Nicaragua	4.3/12
10	NCIS	4.1/11

Note. Source: Deadline

As expected the two priciest shows, *American Idol* and *Sunday Night Football*, are also the leaders in ratings. However, not every show in Table 2.1 is part of the top 10 shows based on highest ratings. Table 2.2 presents the 10 highest rated shows of the 2010-11 season. Aside from the first three spots the only other common show that appears in both tables is *Grey's Anatomy*. With the exception of *The Voice*, the rest of the highest rated shows were recurring shows. This begs the question then, why aren't all the highest rated shows amongst the most expensive ones? The answer to that question can include many considerations, but in summary we can say that it is not only about the size of the audience it is about the 'quality' of the audience. By quality we mean the demographic characteristics that make an audience particularly attractive to advertisers.

What constitutes and ideal audience has been a subject of discussion for programmers and advertisers for many years. Each advertiser tries to target the audience group that could be interested in their products. Nevertheless, there are certain groups that most advertisers seem to go after. In the 1970s advertisers mostly went after women 18-34 years old. The rationale was that "they were the most susceptible to advertising and controlled the economy" (Eastman & Ferguson, 2009, p.129). The most sought demographic

evolved to adults 18-49 in later years and was referred to as the 'ideal demographic' (Eastman & Ferguson, 2009). "At the broadcast network level, the programmers argue they know that targeting the ideal demographic group creates problems, but they have little choice because most advertisers demand this audience" (Eastman & Ferguson, 2009, p.130). Many disagree with advertiser's view of what constitutes the ideal demographic. Betsy Frank, executive president of research and planning for MTV believes that the "ideal viewer should be under 25" (Eastman & Ferguson, 2009, p.129), while "CBS argues the ideal should be higher, 25 to 54 years to be exact, and FOX argues that 18 to 34 urban men should be included"(Eastman & Ferguson, 2009, p.130).

As a matter of fact FOX has been having success charging higher CPMs than the other networks. For instance, in the 2009-10 season FOX had an average prime-time CPM of $28.22 while the other three only charged $17.08 on average. According to SNL Kagan's reports: "FOX's success at charging more than the other networks for its advertising on a share-point basis correlates directly to its ratings lead in the 18-49 demo for prime-time series" ("Economics of TV…", 2007, p.41). In fact out of the 10 most expensive shows (on an ad spot basis), as shown on Table 2.1, six of them air on FOX. Shows like *Family Guy* and *The Simps*ons are not included in the top ten highest rated shows; nevertheless, they are stronger in the adults 18-49 demographic. *Family Guy*, for instance, has won its timeslot in certain demographics like teens and persons 12-34. It also has reported higher ratings than *Desperate Housewives* for the adults 18-49 group (Rice, 2010). Consequently, advertising in these types of shows is more expensive.

Going back to the laws of supply and demand, in the television industry there is a very high demand for rating points in the adults 18-49 demographic. The supply in that segment seems to be insufficient and therefore there is a shortage of rating points. The laws of supply and demand tell us that an insufficient supply results in a price increase. FOX has been benefitting from this situation since it is able to offer advertisers the much coveted 18-

49 viewers. If other networks start airing shows that successfully appeal to that demographic the supply of rating points would increase correcting the shortage and pushing the price downwards. In this scenario, FOX would have to decrease their CPMs since now advertisers have other options for reaching the same target market.

It is also important to recognize that the price per spot for a particular show changes from season to season depending on its performance. Shows tend to lose viewers as they age and the prices of ad spots are also sensitive to the state of the advertising market. As an example, in 2007 "ABC's Sunday night *Brothers and Sisters* was the new show with the most expensive price tag, at $240K" ("Economics of TV…", 2007, p. 15). By the time *Brothers and Sisters* was ending its run (2010-2011 season) the price of a 30 second ad spot was merely $130K. A similar example is *Fringe* which premiered charging $300K for ad spot and only amounted to $120K by its third season.

A final consideration that affects a show's performance is "Audience Flow." Eastman and Ferguson explain "Aside from program's demographics, the networks look for audience flow from program to program. Each network hopes to capture and hold the largest possible adult audience, especially from 8 P.M. until 11 P.M [prime-time]" (2009, p.130). A show by itself may have excellent content and production values but its success depends on much more than that. Besides the preferences of the audience, a show's success is deeply linked to the time-slot it is given.

> Networks continue to try to produce flow by careful scheduling, such as placing programs with similar story lines one right after another, although the remote control and digital guides make flow-through difficult to achieve. Virtually all traditional scheduling strategies have been designed to maintain this flow (Eastman & Ferguson, 2009, p.130).

Some of the most popular scheduling strategies include: anchoring (begin the evening with an especially strong program), hammocking (schedule a weak show in between two strong ones) and counterprogramming (schedule a show that is completely different to what the competition offers in that time-slot) (Eastman & Ferguson, 2009). Programmers

use a number of other scheduling strategies, the exploration of which is out of the scope of this study.

Advertising is the main revenue stream for broadcast networks and it is dependent on their ability to produce audiences. Broadcast network ratings have been following a decreasing trend for the past two decades. Many factors are responsible for the drop in ratings, one of the most important ones being the migration of viewers to cable. Other considerations include the disadvantageous situation of the advertising industry as a consequence of the economic downturn and the introduction of DVR. The DVR had many implications for the television market (negative and positive). Its impact will be analyzed more carefully on a later section of this review.

In any way, "the drop in audience size has been compensated for by higher advertising rates and by adding more spots within programs" (Eastman & Ferguson, 2009, p. 125). If we examine the advertising revenue on a show by show basis, the price that can be charged by spot depends on the ratings performance. However, a show not only has to produce high overall ratings, the specific characteristics of the audience are also important. Advertisers are mostly interested in certain demographic groups; the most sought segment nowadays is adults 18-49. The shows with good performances in that demographic are the most likely to have higher prices per ad spot. Finally, programmers try to maximize ratings by achieving audience flow. Audience flow is obtained by applying a number of strategies at the time of creating a schedule. In summary, programmers try to attain audience flow in order to achieve high ratings in the demographic groups that advertisers seek and maximize their advertising revenue.

This concludes the review of the literature regarding advertising revenue. However, as we have discussed, maximizing the ad dollars is not enough in order to achieve optimal results at a corporate level. The next step is to analyze another major revenue source: syndication.

Syndication

This section of the literature review focuses on syndication. First, the researcher will explain and analyze the current state and projections for the future of the syndication market. Then the researcher will explore how vertical integration is changing the dynamics between production houses and networks and how interdependent relationships are emerging. Finally, the researcher will discuss the syndication potential for shows of different genres.

As we discussed in the previous section, when analyzing revenue sources, programmers have tendency to focus on the advertising revenue a show can generate. However, an important percentage of the revenue associated with a TV show comes after the original network run in the form of syndication deals. As stated in an SNL Kagan report:

> One key component to making money in TV programming is syndication. Networks try to get a stake in the shows they put on the air in order to help make the business model work. The end of fin-syn rules in 1995 made this possible. Prior to that, networks could not own a piece of the programming they aired in prime-time ("Economics of TV…", 2007, p.60).

Despite the attention given to ratings and advertising revenue, in reality broadcast networks operate with relatively small margins. For instance, the industry's average cash flow margin in 2010 was merely 3.12% (SNL Kagan "TV Network Industry Benchmarks"). O&O (Owned and Operated) stations generally have margins between 40% and 50% ("Economics of TV…", 2007, p.61). As this data suggests, broadcast networks are not the stars of their media conglomerates. "Although most of the largest broadcast networks generate a small profit margin when looked at on a standalone basis, their revenue pictures dramatically improve when sister networks and production houses are added into the equation" ("Economics of TV…", 2007, p.61). "In short, networks are no longer the economic powerhouses they once were but the profits for their parent companies keep growing" (Eastman & Ferguson, 2009, p.127). The parent companies' profits include revenue from

the, DVD sales, foreign, online and finally syndication which will be discussed in this section ("Economics of TV…", 2007, p.61).

In order to obtain considerable benefits from all the secondary windows mentioned above, TV shows still need to premiere on traditional television. It is not yet viable for a TV show to premiere directly online and enjoy the number of viewers and success a broadcast or cable show can generate. SNL Kagan analyst, Deana Myers stated that online programs are still in the "experimentation phase", with an audience and revenue that is not yet comparable to the "big broadcast and cable networks" (Yao, 2012) .There have been some initiatives for web based series like the WB's *Sorority Forever* and Lisa Kudrow's *Web Therapy*[1]. However, online series are more on an experimental phase and do not constitute direct competition for broadcast shows yet. The future of web based series may rest on online video services like Hulu and Netflix. Netflix announced that it will start offering originals; the first series scheduled to debut on 2012 is *Lilyhammer* (Ali, 2012). Hulu is also entering the original production territory with a more conservative approach. In 2011 Hulu started offering exclusive series partnering with filmmakers and entertainers like Martin Spurlock and Tracy Ullman. It is too soon to tell if these initiatives will turn into the future of television, it is certainly a possibility. We will discuss online platforms and their impact on the television industry in a later section of this review. Regardless of future trends, it is important to keep in mind that right now, even though there are many complementary sources of revenue, broadcast networks are still the vehicles that make any other cash inflows possible.

Briefly, syndication is "the practice of exclusive, market-by-market licensing rights to the presentation of television programs" (Oba & Chan-Olmsted, 2006, p.101). In other words the producer of a TV show sells the right to telecast their program for a determined period of time and number of plays per episode (Eastman & Ferguson, 2009). The customers for

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[1] *Web Therapy* premiered exclusively online and later moved to the cable network Showtime.

syndicated programs may include local television stations, cable channels or programming services like the National Broadcasting System (Fletcher, n.d.). Therefore, “syndication is the source of the ‘reruns’ often seen on network television and of much material seen on cable networks” (Fletcher, n.d., par.2).

Syndication is a key component of the television value chain. Oba and Chan-Olmsted explain the importance of syndication programs in the American television market: “Syndicators have become a significant player in the U.S. television media market, filling many time slots on independent stations and in non prime-time hours for network affiliates” (2006, p.101). Similarly Fletcher asserts that “the syndication of television programs is a fundamental financial component of television industries” (Fletcher, n.d., par.1).

The main focus of this study is prime-time TV shows that aired on broadcast television during the past decade (2000-2010). The prime-time shows are of utmost important for the syndication divisions of media conglomerates. According to Eastman & Ferguson “Prime-time programs are still the source of virtually all off-network syndication and, in consequence, remain the center of long-term profit potential” (Eastman & Ferguson, 2009, p.128). Within prime-time, the syndication potential for one-hour dramas has proven to be difficult. Not only less than 20% of all dramas are renewed past their second season, but also, the syndication market has historically favored comedies. Reality shows have it even rougher; their syndication potential is very low, especially for competition shows seeing that once the outcome is known they lose most of its appeal.

The classic syndication deal, as we mentioned before, is a simple transaction where the owner of the show receives a fee from the customer (local station or cable channel) and in exchange grants the rights to broadcast the show. However, syndication deals have evolved in complexity and currently there are many variants in the market. For example, several syndication deals now include ‘barter’ transactions.

> In barter syndication an advertiser purchases in advance all or some part of the advertising opportunities (commercial spots) in a syndicated program, no matter where the production is to be seen in any run. The advertiser benefits from the barter arrangement by insuring a friendly program environment for ads. The programmer--an independent station or a cable programmer--benefits because advertising slots are presold, assuring that the cost to acquire the program is at least partially covered. While this practice may reduce opportunities for the programmer to sell advertising time, the trade-off is considered a favorable one. The producer of the program also benefits because the prior purchase of advertising opportunities provides funds that may represent an important part of the production budget (Fletcher, 2006, par.10).

The downside of barter transactions is that they constitute an opportunity cost for buyers because they give up the future cash inflows from advertisement sales. Striking long-term barter syndication deals can prove to be unfavorable; since, in the event of positive market conditions the stations would be unable to benefit from high ad rates. Some syndication deals are cash only while others are purely barter, but also there are a number of hybrid deals. For example, in 2010 WarnerBros. Domestic TV Distribution reportedly struck a deal with TBS for the rights to the sit-com *The Big Bang Theory*. The show sold for around "$1.5 million per episode, plus one and a half minutes of barter advertising time in every run" (Littleton, 2010, p.1).

Another consideration when selling shows for syndication is the number of episodes. Traditionally, in order to be sold in syndication, a show needed to reach the magic number of episodes. The magic number refers to the minimum number of episodes a show should have to be effective for stripping (air daily Monday-Friday at the same time). *"All shows, regardless of number of episodes can be sold into syndication, but shows that can be stripped can command higher per-episode pricing"* (Seidman, 2011a, p.1). According to Eastman & Ferguson, 65 episodes of a show (three network seasons) are considered the minimum for stripping.

Seidman believes "the prevailing Hollywood mindset" is that the minimum number of episodes necessary for syndication is 88. "*The magic number for being able to strip a show*

in syndication used to be "100• but at least for the last few years it has been 88" (Seidman, 2011a, p.1). Citing a TV by the numbers analyst, Seidman gives the example of *Fringe*. While many were surprised by the renewal of the show (due to poor ratings), the analyst stated it would be rare for a series that was renewed for a third season not to get renewed for a fourth. In Seidman's words "no matter how lucrative or paltry a show's syndication prospects are, if it's within 22 episodes of 88 episodes, the studio will bend over backwards, including going very low on the licensing price to make it to 88 episodes" (2011a, p.1). Additionally, it would be important to note that while sit-coms are almost always stripped in syndication; many dramas (especially when sold to cable) are scheduled to air on weekends. In this case, the magic number could be much lower.

Furthermore,

> With more competition in the marketplace for hit shows, syndication deals are closing faster than was historically true. In the past couple of years, hit one-hour shows have been picked up earlier. *NCIS: Los Angeles* and *Hawaii Five-0* were both sold during their first broadcast net season and *The Mentalist* sold during its sophomore season. The old rule was that a series needed to have at least four seasons in order to sell well in syndication, but today the hits seem to be fewer and the buyers more numerous. Those factors have helped push up the buying on the hottest shows (Myers, 2011, p.2).

Customarily, shows that originally aired on broadcast networks (known as 'off-network' in the syndication market) were sold to local stations for their syndicated runs. Usually the stations that had the biggest demand for the syndicated programs were independent. However, the consolidation of the television market has reduced the number of truly independent stations. This situation combined with the lack of hit shows has negatively affected the demand of local stations for syndicated content. In the words of Myers, "Once, one of the hottest secondary windows for TV content was in station syndication, but that has cooled in recent years" (2010e, p.1). "One reason for the slowdown is likely the lack of megahit programming, as the broadcast networks have struggled to produce hit comedies in recent years and some of the drama successes have been with

episodic [shows with serialized storylines] productions such as *Lost* and *Grey's Anatomy*, which are more difficult to sell into syndication" (2009a, p.1).

In addition, local stations are also susceptible to the general economic conditions. The acquisition of syndicated shows is highly expensive which is driving local station programmers to seek less expensive sources to fill some of their day parts. According to an SNL Kagan report, local stations are turning to cheaper locally produced programs and they are also relying in long-form paid advertising (infomercials) ("Media Trends", 2009, p.224). The stations' demand for syndicated programs may no longer be what it once was, but that does not mean the segment should be entirely dismissed. As Oba and Chan Olmsted explain, if we examine the schedules of the local stations we will discover that they still air syndicated programs in many of their day parts. "In essence, to stay competitive with the affiliates of the more established networks (NBC, CBS, ABC and Fox), the minor affiliates and independent stations still very much rely on a healthy supply of syndicated programming products" (2006, p.101).

In spite of the contraction in the stations' demand, "the syndication market has enjoyed a couple of decades of growth thanks to strong sales to cable networks ("Media Trends", 2009, p.224). Before cable came into the scene in 1979, the total syndication revenue was $531 million. It was comprised primarily by affiliates' buys followed by independent stations. In the following decades, cable channels started acquiring syndicated programs helping the total revenue ascend to almost $19 billion by 2010. Out of the $19 billion in syndication revenue over $12 billion came from cable networks (68% of total revenue), while affiliate stations were only responsible for around $1.5 billion ("Syndication Deal Stats…", 2010). Ironically, off-network syndicated content has been one of the reasons cable networks were able to lure viewers away from broadcast.

The presence of cable in the syndication market results in many advantages for syndicators. Not only they have an important customer for their programming, but also they

have the opportunity to cut operating costs and increase prices. In the words of Eastman and Ferguson:

> Instead of sending a large sales force to call on three to eight stations in each of the 210 local markets to sell a program in syndication, that same program might be sold to a national cable network in a single deal. Sometimes the cable price exceeds what might be made in broadcast syndication. Also, sales staff salaries and travel expenses are saved. With more potential customers needing to fill 168 hours a week of airtime, cable syndication has become an extremely lucrative marketplace (2009, p.115).

Myers refers to cable networks as "the sunny side of the syndication business". She also projects the ascending trend of cable networks' demand for syndicated programs will continue during the next couple years (2010e, p.3). Another report indicates that "Despite a newer focus on original programming" it is expected that "cable networks will continue to be the sweet spot for syndicators in the next decade" ("Media Trends", 2009, p.224).

In addition to cable networks, internet streaming services are the new players entering the syndication market. "Off-network rights have recently become hot again. Stations not only have to contend with each other and cable networks for those rights, but also with new players in the mix" (Myers, 2010e, p.2). One of the most notorious recent syndication deals was the one announced by Netflix for the first run syndication of the AMC series *Mad Men*. According to Myers, Netflix reported that it would pay around $900,000 per episode for the exclusive streaming syndication rights of the show for seven seasons (2011, p.1). This deal marks the first time a show that aired on television is syndicated directly to a streaming service on the internet. *Mad Men* is a show that originally aired on a basic cable network. As of the writing of this thesis there had not been any similar deals for an off-network show.

Other syndication deals are including streaming rights as part of their contracts, but in a limited capacity. "In general, syndication pacts have limited streaming as part of the contract, instead focusing on the linear distribution side" (Myers, 2011, p.1). Myers also notes that deals for off-network shows are only recently including streaming rights since

distributors were concerned about limiting the exposure of their shows and in the past they were very reluctant to offer digital rights as part of their contracts or they demanded significantly more money for them (2011, p.1). An example of a contract that includes digital rights is *Hawaii Five-0*'s syndication deal. Myers reported that TNT acquired the show for around $2.3 million per episode. "The deal is said to include digital rights, so TNT will be allowed to stream episodes online" (2011, p.1).

During the last decade, the off network market was moving slowly. In 2006 Lifetime acquired the rights for the syndication of *Grey's Anatomy* for a reported price of 1.2 million per episode ("Media Trends", 2009). During the following couple of years there weren't any major off-network deals to report. Nevertheless, 2009 brought a couple large-scale deals including the early syndication pick up of *NCIS: Los Angeles* and *The Mentalist* for 2.5 million and 2.2 million per episode respectively. The *NCIS* deal tied with *The Sopranos* (an off-cable show) for the top cable network syndication deal of all time (Myers, 2009a, p.1).

The literature suggests that in the nearby future, the syndication market will be heavily supported by the cable channels which will continue to grow at a higher rate than the local stations. As discussed, cable channels have been making important deals for off-network shows; however, selling shows to cable does not prevent making deals with local stations as well. "To maximize revenue potential for network programs, a recent trend has been to sell off-network rights simultaneously to both traditional broadcast stations and cable networks" (Eastman & Ferguson, 2009, p.115). SNL Kagan expects that more deals will include barter "as content owners continue to use ad time in lieu of or in addition to cash for off-network product" ("Media Trends", 2009, p.224). "Barter has become a more important part of syndication deals as it shifts some of the risk to distributors and allows stations to control costs" (Myers, 2010e, p.1). However, as mentioned earlier in this thesis, it also prevents stations from benefiting of favorable advertising market conditions.

Writing about the future of the syndication market, Myers proposes that stations and networks will resist big increases in the syndication deals (2010e, p.3). “For one, new competitors such as Netflix and other online distribution venues could devalue the price paid on certain products” (Myers, 2010e, p.3). It is also noted that it is expected for the most popular shows to keep generating top dollar, however “mid- and low-tier shows will likely struggle to get big money from TV outlets” (Myers, 2010e, p.3). As an SNL Kagan report indicates, it is expected that the syndication market will continue its ascending trend, mostly driven by the increasing cable network spending (“Syndication Deal…”, 2010).

So far this review has discussed the mechanism of the syndication market, the type of deals available, the current state and future projections for the sector. Why should a broadcast network programmer be concerned about all of this? The answer is “vertical integration”

> With the strike down of Financial Interest and Syndication (Fin-Syn) Rules in 1995, broadcast networks established a new future in which they could also own the programming aired on their prime-time schedules. This paved the way for broadcasters to create in-house production and syndication facilities and/or merge with others to create vertically integrated companies (“Economics of TV…”, 2007, p.62).

Each of the big four networks’ parent companies has an in-house production studio and syndication arm. Therefore, networks may only benefit from the advertising revenue while their shows are airing; but, in case of in-house productions, their parent companies are the owners of the shows they air and the recipients of the syndication revenue as well as any other revenue from additional windows such as DVD sales, international distribution and digital rights. Speaking of this trend Oba and Chan-Olmsted wrote “media consolidations highlights an increasing phenomenon of vertically integrated units within large media firms that aim to maximize profits by utilizing the resources and products from their own upstream or downstream holdings” (2006, p.99).

Vertical integration creates a situation where programmers must take into consideration who owns the show they are contemplating to put on their schedules. As mentioned before, networks only generate a very small percentage of the total revenue of their conglomerates. Nevertheless, "Networks can help their parent companies reap the benefits of secondary revenue streams, however, by ordering their prime-time programming from their sister studios" (Myers, 2009c, p.1). "Ordering scripted series from in-house studios provides an opportunity to take advantage of syndication and home video sales for successful series" (Myers, 2009c, p.1). According to Eastman and Ferguson "enhancing the parent corporation's stock market value might outweigh the importance of higher ratings on a particular channel, and executives at the highest levels are generally focused on maximizing revenue to the parent corporation" (2009, p.27).

In summary, programmers need to perform a cost-benefit analysis in which they have to consider the potential revenue and costs and determine whether it will be more convenient to pick up a show owned by their parent company or to look outside for other sources of programming.

After talking to an industry insider, Eastman and Ferguson proposed a series of strategies for programmers to decide whether to air an in-house show or buy an external production. The strategies can be summarized as follows:

> If the show is strong but the time slot is weak, it should sell the show to others (…). If the time slot is strong but the owned show is weak, the network should buy better programs from others (…). If both the show and the time slot are weak, then the network should recycle its own library (…) (2009, p.27).

The historic data seem to suggest that the ownership of TV shows is an influential factor for the networks' programmers. For the 2010-11 season, Myers reported that on average 52.2% of the schedule was owned by the networks (Myers, 2010a). The CW constitutes the network with a higher ownership of the shows it airs (around 90% in the 2010-2011 season), due largely to both of its parent companies being in the business of

production, according to an SNL Kagan report. FOX follows The CW with 75% of ownership of its schedule during the same season. “NBC owns the smallest percentage at 31.8 %” (Myers, 2010a, p.1). Finally CBS and ABC reported an average of 57% and 48% of ownership for the 2010-11 season (Myers, 2010a, p.1). Ordering in-house productions could benefit the revenue of the networks’ media conglomerates; nevertheless, “the downside of ordering in-house, aside from possibly limiting creativity, is that the studio also bears the losses on shows that are canceled early” (Myers, 2009c, p.1).

To conclude, this section examines the potential for syndication of TV shows based on their genre. Three basic genres are addressed in this research: One-hour drama, comedy and reality. In the last couple of seasons, broadcast networks’ prime-time lineups have been filled mostly with dramas (39 dramas vs. 20 comedies and 15 game/reality shows for the 2010-2011 season) (Myers, 2010a). Regardless of the prevailing trend in programming prime-time “syndication has not historically been a strong revenue generator for one-hours” (“Economics of TV…”, 2007, p.8). One hour dramas tend to be less popular in syndication than sitcoms because dramas are usually more serialized.

Throughout the 1990’s all of the top syndication deals, with the exception of *Murder She Wrote*, were sit-coms (“Economics of TV…”, 2007, p.8). In addition “The odds are quite long that a show will even reach a syndicatable level in terms of total episodes [89 episodes according to the study]” (Myers, 2008b, p.1). In the latest decade only an approximate of 9% of the dramas on the schedule reached the syndicatable level of episodes (Myers, 2008b, p.1). Among the top syndication deals of all times are the sit-coms *Seinfeld* and *The Cosby Show* which sold for $3.3 million and $4.4 million per episode respectively. *Seinfeld* is particularly notorious because it actually generated a higher license fee ($4.1 million per episode) in its second syndication cycle. However, networks have been unable to generate hit comedies in the past few years. The highest syndication deal for a sit-com in 2011 was *The Big Bang Theory* which sold for $1.5 million per episode.

Despite the historical unfavorable odds for dramas, the syndication of one-hours has been picking up since the mid 90's, when Turner bought *ER* for $800,000 per episode. "Today, top one-hours often exceed $1 million per episode in cable network syndication" ("Economics of TV…", 2007, p.8). Once again, we stress the importance of cable networks as buyers of syndicated programs. "One-hours generally sell to cable networks during the syndication window. Generally, only the top one-hours will also get a weekend station syndicated run" ("Economics of TV…", 2007, p.80). Nevertheless, some stations buy syndicated dramas to play during the weekends ("Economics of TV…", 2007).

Understanding the syndicated potential of a TV show is now a factor that network programmers should take into account. Vertical integration has made syndication a part of the TV show value chain, even at the network level since the syndication revenue highly benefits their sister companies. Programmers should consider the long-term revenue generating potential of the shows they pick up. Syndication is a big part of the aftermarket revenue and in this context the syndication market is no longer a separate entity from broadcast networks' programming teams; rather, it should be a very present concern. The following section of this review will explore another aftermarket revenue window: home video.

Home Video Market

As mentioned before, "Traditional windowing [for TV product] was simply the broadcast network period followed by syndication several years later. Today, a far more complex model has emerged, including cable network repurposing, DVD and now video on demand" ("Economics of TV…", 2007, p.59). We have discussed how network programmers should look into potential syndication revenue of the shows they decide to air, as it is a source of income for their parent companies. In the same way, programmers should take into consideration DVD sales and other forms of home video. In this section, we will discuss

the impact of the DVD on the television industry as well as other video technologies that are becoming the successors of the DVD in the home video market.

According to Kompare, the way viewers consumed television has changed with the introduction of home video in the mid-1970s (2006). “Home video enables people to use their sets to create or access programming on their own terms rather than stay locked to the fare and schedule dictated by the broadcasting industry” (Kompare, 2006, p.336). Kompare also notes that in the early days, home video functioned as an extension of the film industry but it was not necessarily attached to the television industry (2006). “Television’s primary goal is selling potential audiences to advertisers, not selling products to consumers.” For that reason, home video releases of television series were not as widespread (Kompare, 2006, p.337).

Nevertheless, content owners slowly started to offer select series on VHS since the early 1980s. However, television home video distribution did not take off until the DVD was introduced in 1997. The DVD was the video technology that “allowed studios to cheaply produce and distribute high quality versions of their product” (“Economics of TV…”, 2007, p.59). Some authors go as far as to refer to the DVD as the “media product” that “reinvented the home video market” (Brookey, 2007, p.207). Scholars seem to agree on the importance DVD technology had for the home video industry as a whole, but we want to highlight the impact it had on television. In the words of Kompare:

> DVD technology (…) has been especially critical (…) not only for the film industry but even more so for television. With much higher resolution sound and image, random access capability, a smaller size, and most significant, a larger storage capacity, the DVD has rejuvenated the home video industry and has finally enabled television to achieve what film had by the mid-1980s, namely, a viable direct-to-consumer market for its programming (2006, p.337).

Kompare also notes that the success of DVD in the television industry is highly attributable to the introduction of the season long DVD box set. “The DVD box set in particular, as introduced with Fox’s first set of *The X-Files* in 2000, has reconceived television

series as collectible objects, fostering a new commodity relationship between television and its viewers" (2006, p.335). According to an executive quoted by Hernandez, "Once the studios hit on the entire season concept, it [television DVD] really took off" (2003, p.1). After the first box sets were introduced, they quickly became the standard adopted by all distributors (Kompare, 2006). Kompare maintains that the DVD box set was the culmination of many factors including the "exponential growth of the DVD market; the unique properties and distinction of the technology itself; and the successful creation and exploitation of cult audiences" (2006, p.343). The box, not only made possible to acquire an entire season with one purchase, another important characteristic was its compact presentation. A full season of a show could be fitted in a small square box, which was impossible in the times of VHS (Kompare, 2006).

The success of the DVD box set changed the dynamics of television consumption. Kompare theorizes that in the pre-DVD model "media users (i.e., viewers) are irrelevant" and they are "represented only by the statistical fictions of ratings and demographic data." The viewers have a passive role of consuming whatever shows and advertising the programmers have chosen to air. On the other hand, consumers hand-pick the DVDs (or other type of video discs) they want to buy. They possess an active role in choosing the shows they value enough to purchase (Kompare, 2006, p.339-340). The DVD was the technology that launched the success of television shows in the home video market. In later years, other video technologies entered the market and were able to profit from the TV shows' demand that the DVD had already generated. The evolution of the home video market is summarized below.

Following the path of Betamax, mini-discs and laser discs; the VHS format was forced to officially retire from the home video market in 2006. The demise of VHS was attributable to the introduction of the DVD. "After a fruitful career, VHS tapes started to retire from center stage in 2003 when DVDs became more popular for the first time"

(Garret, 2006, p.1). For a while, DVD was the predominant player in the home video industry. However, in recent years "consumers have stopped buying DVDs at the pace they once did" ("The state of home…", 2009, p.2). Unlike VHS, DVD has not yet disappeared due to the introduction of new video technologies; however it has been forced to share the market with the new players. Blu-ray is the new generation high-def disc (developed by Sony) that entered the market as a successor of the DVD. The format was launched with an initial release of six Sony movie titles and one from MGM in 2006 ("Sony rearranges…", 2006). Initially, Blu-ray faced competition from another high-def format HD-DVD (manufactured by Toshiba), however the format was discontinued in 2008 (Williams, 2008) and currently Blu-ray is the only high definition disc[2] in the industry. In addition to the physical disc formats, VOD (Video on Demand) is gaining popularity within the home video market, taking away some of the market share from Blu-ray and DVD.

For the networks, the successful performance of television DVDs came at a time when they were experiencing financial hardship due to diminishing ratings and scarce syndication deals (Mcclintock, 2005). "Media industries have required increasing amounts of revenue from extant products to survive and as media users have favored media that provides flexibility and choice" (Kompare, 2006, p.344). Accordingly, executives were quick to recognize the importance of the home video market for their consolidated bottom lines. After realizing the sales potential of DVDs, studios made efforts to release as many of their shows on DVD as the market allowed. Now the release of TV shows on DVD and to some extent on Blu-ray is regarded almost as a mandatory step.

With the success of television shows' video releases, studios found an additional revenue stream, much needed to help their overall profits. However, concerns about hurting other segments of their conglomerates were arisen. Nonetheless, video releases do not seem to affect revenue of other segments. There have been many concerns about hurting

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[2] Blu-ray has a maximum resolution of 1080p while the DVD is limited to 480p

the syndication cycle by releasing TV shows on DVD or Blu-ray; in any event, there is no evidence so far that video releases hurt the success of a particular show in syndication re-runs. Kompare writes about Fox's concerns regarding the release of the first season DVD box set of *Buffy The Vampire Slayer*. Executives feared the DVD release could interfere with the syndication debut; however, *Buffy* "performed well in cable and local syndication and has sold extensively on DVD" (Kompare, 2006, p.352).

In fact, many believe that the release of TV series on home video helps the promotion of the show. Nowadays studios do not wait until a show is over to release it to home video. On occasion shows are released on video even before they are sold on syndication (Kompare, 2006, p.351). Many studios release previous seasons on DVD and Blu-ray as a way of promoting the new upcoming season scheduled to premiere on broadcast. For example *Grey's Anatomy* season 7 DVD was released on September 13th, 2011 in preparation for the season 8 premiere on September 22nd of the same year. It is now common practice to tie in the DVD release with the new season's of promotional campaign. "This practice is only feasible in an era when massive, horizontally and vertically integrated corporations control the media as they can take advantage of the synergistic opportunities offered by new technologies, new business practices, and new audience habits" (Kompare, 2006, p.351).

As mentioned, the success of television home video started with the introduction of DVD technology which was the predominant format during the past decade. Bianculli summarized the success of DVD in the following passage:

> DVD has been an early success because it's the perfect marriage of the medium and technology: Fans can watch their favorite series in a high-quality format, access their favorite scenes more easily than before and enjoy extra footage, all in a compact form (2002, p.1).

The Blu-ray disc, which is the direct successor of the DVD, maintains all these characteristics plus improved image quality, better audio and other special features such us

pop-up menus, “picture-in-picture video commentary and the ability to download new content right from your Blu-ray player” (“Blu-ray vs. DVD”, para. 5).

One of the most obvious advantages of digital discs is the ability fans have to watch their favorite TV shows at any time of their convenience. “Programs can now be accessed completely at the whim of the viewer, without waiting for a rerun airing or searching through commercial breaks” (Kompare, 2006, p.352). Furthermore, the viewing experience is even better on DVD, where the viewer can also enjoy “supplemental material that rounds out the viewing experiences" (Hernandez, 2003, p.1).

Supplemental materials usually include deleted scenes, interviews with cast and crew, behind the scenes documentaries, audio commentaries, photo galleries, etc. According to Kompare “These extras add filters of meaning to the original episodes” and promote the idea that the TV box set is superior to the original broadcast version (2006, p.349). It has been proven that consumers highly value the inclusion of extra features on DVDs. Disney Studio’s home video distribution division conducted a survey about DVD consumption and found that 63% of the respondents “considered extra features as an incentive to purchase DVDs” (Brookey, 2007, p.201).

The pricing of digital discs was another factor that differentiated them from VHS. According to Kompare, the DVD industry was launched with a model that promoted sales over rentals (2006). The price for buying a DVD was not much higher than renting it, which incentivized sales (Kompare, 2006). This was particularly true for film DVDs which have a very low price around $10-$20. However, television shows’ DVDs have higher retail prices. Season box sets have a price that ranges from $40 to $60. Cable shows like *Mad Men* or *The Tudors* have shorter seasons; hence the price of their box sets is usually closer to $40 or less (Amazon.com). Broadcast dramas generally have more episodes per season (17-24) and consequently their DVDs have higher prices. With shorter running times than dramas, comedies usually have a price between $15 and $30. Reality shows also have much lower

prices ($10-$20) than the average drama (Amazon.com). Blu-ray discs are more expensive than DVDs. The price for a movie is around $25 ("Blu-Ray vs. DVD"). TV series on Blu-ray are usually between 15-20% more expensive than their DVD counterparts (Amazon.com).

Online retailers, like Amazon, offer discounts of 20% to 40% in DVD and Blu-ray boxes. Regardless, the purchase of a season long box is still a big investment for consumers, compared to buying a single disc movie, especially when a viewer wants to own an entire series (Kompare, 2006). "However, it has apparently been a cost worth bearing for those interested in acquiring the definitive edition of their favorite television series" (Kompare, 2006, p.350-51). People are willing to 'invest' in videos of their favorite shows, in this sense; the season long box sets become collectible items. It is not only about watching on their own terms and enjoying the extra features, it is about viewers wanting to own an item that has intrinsic value for them.

For the better part of the last decade DVD was the king format in the home video market. However, the market has evolved and DVD sales are decreasing as Blu-ray increases its market share. According to the Digital Entertainment Group, by year 2010, 90 million households had at least one DVD player, 70% of those households had more than one. In the same year, DVD sales generated $14 billion, down from $15.8 billion in 2009 (Graser, 2011, p.2). Blu-Ray sales amounted to $1.8 billion, a reported climb of 68% compared to the previous year (Digital Entertainment Group). Video On Demand (VOD) also had $1.8 billion in revenue, an increase of 20.8% from the previous year (Graser, 2011, p.2).

Even though DVD sales are still bigger than any other format, it is clear that the DVD market has begun a descending trend. "Consumers have stopped buying DVDs at the pace they once did. New rental services are attracting more new customers, the economic recession grinds on and quality VOD services are on the rise" (Holden, 2009b, p.2). Holden (2011) proposes that consumers are moving away from buying discs and to new media options like video on demand and streaming which will be discussed in a later section of this

literature review. Even DVD rental outlets have ceased to exist; the only current options for renting DVDs are RedBox kiosques and online services like Netflix and Blockbuster (which was forced to close all its brick and mortar outlets). However, in 2011 Netflix decided to separate their DVD and streaming segments. In a letter to the members Netflix's CEO Reed Hastings stated that, "DVD by mail may not last forever, but we want it to last as long as possible" (Hastings, 2011, p.2).

Some argue that the sole purpose of digital video discs was to prepare the market for a transition to the digital space. However, it is likely that a complete transition to digital consumption will not occur as quickly as some may think. "We expect consumers will take a little longer to shift their home libraries to the digital space, as there are still issues with picture quality, storage, device interoperability and download speeds that will take longer to resolve" ("Media Trends", 2009, p.253). Moreover, talking about DVDs, Brookey explains "many (…) consumers may be resistant to the idea that they have invested in a collection of obsolete media, particularly when that collection is relatively new" (2007, p.206). That concept can explain the reluctance to switch across physical formats (from DVD to Blu-ray), or from physical formats to the digital space (streaming). Studies seem to support the idea that consumers are hesitant to abandon physical formats just yet. According to a consumer survey conducted in March 2011 as part of the NPD group's Entertainment trends in America, the majority of consumers are "unwilling or unable to transition from physical to digital" (Massoud, 2011, p.1).

In addition to consumer's tendency to treat DVDs and Blu-ray discs as collectible items, there is another factor that has been slowing down the offerings of digital content. Studios are reluctant to make all of their content available online for fear of losing control over their properties (Brookey, 2007). Also, online video services face other issues related to digital license agreements that we will explore in the following section of this literature review. For these reasons, there is still some content that can only be found in physical

formats and not available for streaming. In general, TV has a bigger online presence than movies. Television has such a significant presence online that even services like Netflix are reporting more TV streaming than movies. In a recent article, Ted Sarantos (Netflix's chief content officer) declares that "50 percent and sometimes 60 percent of viewing is TV episodes now" (Dredge, 2011, p.1). It is easier to find TV shows online than current feature films. Most broadcast shows are available for free on sites like Hulu or the networks' own websites. Older episodes of broadcast shows can usually be found online ready to be streamed for a small fee. However, piracy is a present concern in the minds of studio executives, and as a result there is certain reluctance to reach digital distribution agreements for online streaming. Likewise, many long-term distribution contracts were signed before VOD or internet were a common concern and they don't include provisions for digital distribution.

The biggest question probably is whether or not streaming content will end up killing consumer's desire to purchase physical copies of their favorite TV shows. As an illustration, Carr explores the following question: "Are Amazon's streaming offerings cannibalizing its DVD and Blu-ray sales?" (2011, p.1). The answer, according to Amazon's spokesperson Cat Griffin is "No." Griffin states that "consumers want both" (streaming and DVDs). He explains that although, streaming is very popular right now, they are "still seeing a lot of interest in physical DVDs" (Carr, 2011, p.1). "Russ Crupnick, NPD's [National Purchase Diary] entertainment industry analyst, admitted that while digital content will increase in popularity and become a staple in more homes, physical media is safe for now" (Massoud, 2011, p.1). While it may be true that consumers now have a number of alternatives for catching up with past TV shows like streaming and VOD, using services like Hulu and Netflix; physical discs (DVD, Blu-Ray) provide the avid consumer with the option of owning a copy of their favorite shows. This characteristic is not present with streaming services and therefore

the need for consumers to 'collect' items will probably ensure the survival of physical disc formats.

Streaming and VOD are gaining terrain while the discs are fighting to maintain their presence in the market; DVD may be past its peak, however it still represents the biggest percentage of the home video market and therefore should still be taken into account. Blu-ray is outpacing the growth of VOD, Adams states, "Physical media continues to capture the lion's share of the home video entertainment market, which is why studios are so focused on successfully transitioning from DVD to Blu-ray" (Adams, 2011, p.1). Nevertheless, the transition from DVD to Blu-ray will not happen overnight. Blu-ray presents many advantages over DVD, however it also has some disadvantages. Mainly higher cost and lower number of titles released. As a consequence, it is likely that DVD and Blu-ray will co-exist for a period of time, before the transition is complete.

Regardless of the prevailing format, it all comes back to vertically integrated companies. It is in this context that network programmers should consider the home video sales potential of the shows they are deciding to air. "Rather than only function as draws for advertisers over broadcast or cable channels, television programs are now seen as multi-faceted properties that can spark several complimentary revenue streams" (Kompare, 2006, p.353). Now, vertically integrated companies have several revenue streams to supplement the traditional advertising dollars. We have explained the importance of the syndication market and now we are throwing home video revenue into the mix. Home video sales are an important revenue stream for the studios. Programmers need to keep in mind how this aftermarket revenue stream impacts their parent companies' bottom line. Broadcast networks are only a small part of their media conglomerates. Their net income is important, but it only represents a fraction of the consolidated profit of their respective conglomerates. The overall profit is a sum of the net income of all the separate business segments including syndication and home video sales. In order to maximize their profits, media conglomerates

need to achieve a corporate culture that promotes synergies across business units. Broadcast networks should choose to air the shows that could achieve the highest aggregated revenue across multiple business segments. This means, the shows that could reach the highest overall revenue including advertising, syndication, DVD sales, online distribution, and other sources.

Now we will briefly explore what types of shows fair better in the home video market. We have discussed how procedurals sell better than serialized shows in syndication; nevertheless, that may not be the case in the home video market. In fact it seems to be the opposite. Some of the best selling television DVDs of the last couple of years include: *True Blood*, *Lost*, *Heroes, Grey's Anatomy*, *24*, *Dexter* and *Smallville* (Seidman, 2010). All the shows mentioned above are serialized dramas. In addition to the DVD market favoring serialized shows, top selling lists seem to lack comedies. The only comedies that consistently appeared in best selling DVDs lists were *Family Guy*, *Southpark* and *The Office*. Reality shows, are persistently absent from the top selling DVD lists.

Vice president of PBS consumer products notes that the titles that sell best on DVD "are the titles that people want to watch again and again. They really want to own them, much like you would want to play, again and again, a favorite CD" (Bianculli, 2002, p.2). Another executive asserts, "You need to think about big events or hitting passionate groups," some shows that have broader appeal while they air on network television may not be adequate to sell on DVD. Peter Chernin gives the example of *Judging Amy*: "We couldn't sell it on DVD if we paid people to take it because it appeals to a broader group" (Mcclintock, 2005, p.2). In other words "distributors prioritized programs with particularly solid—if not necessarily "mass"—followings—the so-called cult audiences (in industry-speak) who had proven to be loyal consumers of licensed merchandise in the past" (Kompare, 2006, p.349). Therefore, shows that probably did not have the highest ratings but had cult-following audiences may be the most appropriate to launch on DVD (or other form

of home video). Studios ideally want to target fans that are highly invested with their favorite shows, sometimes; the highest rated shows do not achieve the highest levels of investment. The so-called 'cult hits' are usually more obscure shows with lower ratings but obsessively loyal fans.

The analysis of TV shows' revenue potential grows in complexity. Some shows, like *American Idol* have dominant ratings, but they would never sell well in syndication or DVD since they lose their value once the outcome is known. Other shows like *The Mentalist* were very profitable in the syndication market, while heavily serialized shows like *Lost* had a hard time reaching syndication deals. However, when we talk about the home video market, particularly DVD sales, we find out consumers clearly prefer to spend their money on serialized dramas. The question is what type of shows programmers should put on their schedules in order to maximize the long run profits of their parent companies? What type of analysis should they make? Those are the questions that this study pretends to answer.

The Impact of Time-shifting Technology

A couple of decades ago the only way to watch a TV show was to catch the live broadcast on an actual TV set. That situation has changed over the years due to technological advances that have transferred the power from programmers to viewers. A phenomenon referred to as "time shifting" emerged. Time shifting has existed for many years now, first with VCRs and now with the latest video recording technology, DVR. Additionally, in recent years, viewers have found another way to time shift; namely, watching TV shows on their computers at any time they desire. The internet has become a comprehensive secondary window where viewers can now access the programs they want to see on their own terms.

Many concerns have been raised since the introduction of these technologies. The majority of these concerns relate to the threat they pose to the live audience and consequently to the advertising revenue. On the other side, distributing shows online has

also provided the studios with an additional revenue stream. “For content owners, releasing product in different windows is a long tradition that has helped maximize revenues. New technologies have afforded the opportunity to enhance or add a new window to the mix” (“Economics of TV…”, 2007, p.59).

In this section, the researcher examines the impact of time-shifting technologies on broadcast prime-time shows and how they could negatively affect traditional revenue. The researcher will also discuss their potential for generating new revenue sources and other positive consequences they may entail.

DVR. The first technology we will discuss is the Digital Video Recorder also known as the DVR. The DVR, as its name suggests, is a device that allows to record video in a digital format. Viewers can easily program their DVRs to record their favorite shows for later viewing at their own convenience. “The fundamental effect of DVR proliferation is a shift in control, from television networks and advertisers, to viewers” (Wilbur, 2008, p.143). Besides the ability to record and playback TV shows, the DVR has another feature that deeply concerns network executives. With the DVR, viewers have the ability to easily skip commercials. If viewers start skipping commercials, advertisers will not have an incentive to buy highly expensive spots on TV shows.

The current debate circles around the true impact the DVR has on viewership. According to a study conducted by Pearson and Barwise in 2008, DVR users skipped around 68% of the commercial ads when they watched recorded programming (Wilbur, 2008, p.144). However, not every household in America has a DVR. The latest data indicate 40.8 million homes in the U.S. have a DVR which represents a penetration of 47% (Olgeirson, 2011). DVR penetration has been slowing down during the past few years. The current growth trends seem to suggest the industry has reached a stationary level. It is likely that the penetration level will remain around or below 50% in the short to midterm future.

When discussing the advertising business model, this research suggested how declining ratings have in fact elevated the price of the ad-spots. The introduction of DVRs is at least partially responsible for the decreasing "live" audience of telecasts. Wilbur explains the consequences of declining ratings for advertisers:

> The principal negative consequence of DVR proliferation is the increasing scarcity of viewer attention. Scarcity drives up the price of advertising exposures, not just in television, but across media, as advertisers shift money away from rising television ad prices (Wilbur, 2008, p.145).

Trying to remain positive, an industry executive notes that: "DVRs are not hurting her business," DVR penetration is below 50% "and the average household has 3 to 4 TVs and only one is connected to a DVR" (Di Grazia, 2010, p.1). Regardless, as Wilbur explains, DVR proliferation is bound to "make advertising exposures more scarce and costly" and also to have an impact in networks' interactions with one another and their negotiation process with advertisers" (2008, p.146).

Since the introduction of the DVR, a conflict between networks and advertisers has emerged. Advertisers maintain that ratings including DVR viewership are not the same as 'Live' ratings, because DVR viewers usually skip the commercials. Networks, on the other hand believe DVR ratings should be taken into account when negotiating CPMs. Advertisers would like to negotiate based on 'Live' ratings and networks push for the inclusion of DVR playback. They have reached a middle ground and the current agreement is to use "live + 3" ratings (also known as C3 in the industry). This means that advertisers pay networks based on the number of viewers watching the commercials in their shows during the first three days after the original broadcast (Carter, 2011, p.1).

In addition to skipping commercials, there is another problem associated with DVR playback. "Aaron Cohen, the chief negotiating officer for the ad-buying firm Horizon Media, said advertisers would have little or no interest in looking at data beyond three days" (Carter, 2011, p.2). The reason of advertisers' reluctance to go farther than three days is

simple. As Cohen explains in Carter's article "Advertisers like retailers and restaurants, anything with near-term openings, are looking for one- to three-day campaigns" (Carter, 2011, p.2). For that reason, it is very unlikely that advertisers would agree to take into account DVR playback for more than three days; however network executives are monitoring playback up to seven days with other purposes in mind. "Networks are monitoring how shows do over a full week after they are broadcast to gauge the depth of audience interest and loyalty" (Carter, 2011, p.1). Carter also explains that although networks "are not pressing the issue, they would eventually like to persuade advertisers to take more notice, as well" (Carter, 2011, p.1).

Some of the literature reviewed suggests that the DVR may not be as damaging as advertisers claim. "Much of the hype about DVRs stems from their facilitation of advertising avoidance. What is often ignored, however, is that viewers have long avoided advertisements" (Wilbur, 2008, p.143). Wilbur goes on to explain the many ways viewers have avoided commercials for many years. Viewers "change channels with remote controls ("zapping"), divert their attention to companions or other media ("multitasking"), leave the room ("physical zapping"), mute or turn off the television, or fast-forward through commercials in recorded programming ("zipping")" [not necessarily with a DVR] (Wilbur, 2008, p.143).

Unlike zapping or multitasking, where viewers are completely removed from the commercials, zipping as done with a DVR may still convey the advertiser's message. According to Wilbur (2008), zipped ads have the potential of being at least partially effective due to heightened attention when they are fast forwarding and latent effects that make an impression on the viewer at an unconscious level. It seems likely that, as Wilbur explains, DVR proliferation will shift advertising avoidance from other forms to zipping (2008). With the use of DVR, skipping commercials will probably be more common; however, zipping may actually be the least damaging form of advertising avoidance as viewers still have eyes on

the screen. Furthermore we should remember that more than half of the TV households do not have a DVR and will not be zipping through any commercials.

Notwithstanding, for the households that do have a DVR, advertisers could find good use for the information it can provide. The DVR can provide important information about viewers' behavior and how to improve advertisement delivery. The DVR "can help advertisers to craft more relevant and engaging messages; rotate creatives to prevent wear-out; measure and account for ad avoidance when buying media and vehicles; and improve ROI measurements" (Wilbur, 2008, p.147). Moreover, according to Wilbur, the DVR has the potential for addressable advertisement (targeted ads using geographic and demographic data). Even though advertisers do not hide their disapproval of DVR technology it may actually be a useful instrument for them in the future.

The impact of the DVR on advertisement delivery may not be entirely clear at the moment; however it is safe to say that this technology has affected the negotiation process between broadcast networks and advertisers. The current consensus is to use C3 ratings, but neither party seems to be satisfied with that agreement. Also, "DVR use will likely accelerate current trends toward "unskippable" advertising such as product placement, branded entertainment, and program sponsorship" (Wilbur, 2008, p.145). Manifestations of that trend are evident in the current prime-time season, with product placement getting more frequent and less subtle every day. How much viewers can take before they switch to commercial free television is yet to be seen.

This examination has focused on how the DVR poses a threat to advertisers and the consequences for networks' advertising revenue, but if we take a look at the impact of the DVR from a different perspective, this technology may have been the salvation of certain shows that would have never made it past their first season in a pre-DVR world. In Carter's words, "The digital video recorder was supposed to lay waste to network television. Instead the playback device is offering some shows a lifeline" (2011, p.1). Advertisers may not

accept any ratings data beyond 'Live + 3' (C3), however, that does not mean programmers do not take DVR playback into account. The impact of DVR playback on the total number of viewers is, in some cases, so substantial that it is impossible to ignore it. **"**Programmers now factor in ratings a full week after a show's scheduled appearance" (Carter, 2011, p.1). Some shows report gains of over 40% on 'Live + 7' ratings (compared to 'Live' ratings) in the key demographic of Adults 18-49 ("Live Plus Seven", 2011).

This review of the literature has discussed advertisers' views on 'Live+7' ratings; notwithstanding, network executives have a completely different perspective on the subject. In a *New York Times* article, Alan Wurtzel (NBC president for research) expresses his opinion regarding DVR playback data: "You'd be foolish not to look at the DVR performance as a measure of the potential a program has (…) You have to recalibrate everything: what's a hit; what's a marginal show; what's a failure" (Carter, 2011, p.2). Other executives quoted in the article include David F. Poltrack, chief research officer for CBS and Kevin Reilly, top programmer at FOX. Poltrack asserted that they take into account live plus seven ratings data. Reilly referred to the early renewal of Fox's prime-time show *Fringe* for the 2011-2012 season where DVR playback played an important role: "With a show that has a passionate loyal following like *Fringe*, playback numbers are especially meaningful" (Carter, 2011, p.3).

Speaking of FOX, the network gained the most viewers from DVR playback this season, according to an article posted on TV by the numbers (Gorman, 2011). **"**FOX added an average of 3 million viewers from DVR viewing within the first seven days of the live telecast, with originals – more than CBS (2.9m) and ABC (2.0m), and nearly twice as much as NBC gained on average (1.6m)" (Gorman, 2011, p.1). The TV show that presented the biggest gain after a week of DVR during the 2010-11 season was FOX's *Fringe* with a 40.9% gain on Adults 18-49 and 34% gain on total viewers ("Live Plus Seven", 2011). Fringe was selected for early renewal on March. Carter noted that if the show had been renewed based

merely on Live ratings the chief programmer would have been considered "borderline delusional" (2011, p.1).

> *Fringe* manages only about a 1.7 rating (about 2.24 million viewers) among the 18- to 49-year-olds (…) That number walks right up to the cancellation line. But the tally jumps to a 2.5 rating (about 3.3 million viewers) by the time a week's worth of recorded playback is included, a number that qualifies as satisfactory for most current television dramas — and robust for any show on a Friday (Carter, 2011, p.1).

It makes sense that a science fiction cult hit like *Fringe*, which airs on a Friday night, would have high levels of DVR recording. However, other types of shows also present big 'Live + 7' gains. Family dramas like *Parenthood* or *Brothers and Sisters* and procedurals such as *House* or *Hawaii Five-0* are also among the top ten DVR gainers of the past season ("Live Plus Seven", 2011). Top DVR gainers vary week by week and there is not a clear preference for comedies or dramas. Reality shows are rarely among the top DVRed programs, perhaps because viewers prefer to watch them live.

Industry executives also attribute the success of some serialized long-form dramas to the DVR. Vincent Bruzzese, president of the Worldwide Motion Picture Group says "People allow themselves to become more invested in these shows [serialized dramas] because they are not worried about missing an episode, they can always watch them later online or on their DVR" (Di Grazia, 2010, p.1). Without the DVR, heavily serialized shows like *Lost*, *Prison Break* or *24* may not had been able to exist, and the audience would have missed out on some of the most compelling storylines out there.

As the reader can see DVR is a technology that has had a multifaceted impact on the television industry. On one hand it has threatened advertisers with its capability to skip commercials; however it has also provided them with the opportunity to better understand their audience. From other point of view, DVR has allowed many shows that would not have been able to succeed otherwise to get renewed. Creative-wise, DVR could be one of the best innovations of the latest years. Its true impact is not completely understood yet, and it is

very likely that the industry will continue to evolve its dynamics to factor in DVR playback in the future.

Internet. Alongside the DVR, online streaming has provided viewers with yet another way to time shift. The advances in internet delivery and speed now permit downloading and streaming video content effortlessly. Missing the original telecast does not mean the viewers have to miss an episode. Even if they do not have a DVR, they have the opportunity to watch TV shows online. The industry dynamics have been altered by the introduction of the internet. "Internet or over-the-top (OTT) distribution of television programming and movies has rapidly altered the way industry players address the space" ("The State of Online…", 2011, p.6).

The media conglomerates are still struggling to find a business model that can maximize the profits in the online world. "Both old and new players in the industry have been seeking ways to make money. The older companies mainly have protection in mind, and have looked to protect other windows, including home video, syndication and affiliate license fees" ("The State of Online…", 2011, p.6). As several online models emerge, revenues are still fairly low. As of right now, programmers regard online video more like a supplemental marketing tool and not a profit center. Nevertheless, "the business model will need to change in such a way that content owner and distributor online revenues can match or surpass their licensing fees from multichannel providers and other media" ("The State of Online…", 2011, p.9).

Online video is a minimal portion of the revenue pie for media companies; all the same, according to many industry insiders it is where the audience is heading and it is indubitably a trend worth analyzing. This study will present the current online models and the most popular sites, we will discuss the revenue making potential for the networks and we will analyze the impact of online video delivery on other business segments of media companies.

As an SNL Kagan report states, **"**online video has quickly emerged as both a business threat and an opportunity for players in traditional and emerging video distribution" ("The State of Online…", 2011, p.6). Since the proliferation of online video, media players have been looking for ways to gain substantial revenues from the internet. "In the struggle to monetize Internet video, a plethora of models have been tested, but few have ultimately proven to be winners" (Myers, 2010c, p.1). Some of the most successful online video delivery models include Hulu, iTunes and Netflix; however, as Myers explains, "none has definitively helped boost the overall revenues of content distributors" (2010c, p.1). Networks have not found the way to successfully monetize internet video delivery yet, but even though revenues are small, "the networks need to capture a new generation that simply views TV differently than previous generations" ("Advertising Forecasts", 2010, p.31). Therefore, "broadcast nets have been fairly progressive in offering many of their shows online (via platforms such as iTunes, Hulu and their own websites) and via on-demand services" ("Advertising Forecasts", 2010, p.31).

SNL Kagan divides online video delivery services in three main categories: paid, subscription and free (ad-supported) ("The State of Online…", 2011). We will briefly explore each of them.

Paid services. There are a number of paid video services in the market offering movies, however, not all of them offer television shows. Presently, the only two services that have a substantial catalogue of TV shows are iTunes and Amazon Instant Video ("The State of Online…", 2011). Another smaller player in the sector is CinemaNow that, despite the name, has an offering of 215 television titles (CinemaNow). CinemaNow has a much smaller catalogue than iTunes or Amazon, but they have current shows (cable and broadcast) and current seasons with a price of $ 1.99.

The undisputable leader of the paid video services market is iTunes as Apple's iTunes has the largest catalogue of TV episodes (69,000). In addition, "Apple's iTunes

remains one of the preferred Web video platforms for a number of TV networks" (Castaneda, 2008, p.2). In an effort to replicate the success in the monetization of the music industry, iTunes entered the online video market at an early stage with the objective of building a revenue model to supplement advertising (Castaneda, 2008).

The first network to jump into the iTunes delivery model was ABC when its parent company, Walt Disney, agreed to launch their prime-time shows on the platform during the fall of 2005 ("Economics of TV…", 2007). "Apple has had a successful run at selling TV episodes on iTunes" (Myers, 2010c, p.1). The iTunes store now includes episodes from several shows airing on ABC, NBC, FOX, CBS, The CW and others. In 2010, iTunes began offering TV rentals for just 99 cents; however TV rentals were discontinued in August 2011 since customers showed preference for buying over renting (Mitchel, 2011). Between 2005 and 2010 iTunes sold 450 million TV episodes (Myers, 2010c). According to Myers, "the split between content owners and Apple is roughly 70% to studios and 30% to Apple". Therefore, over the course of five years iTunes has generated around $ 627 million for studios, a hardly dismissible sum (Myers, 2010c, p.1).

Amazon has two different online video services. A subscription service, that will be discussed later and a paid service denominated Amazon Instant Video. "Amazon Instant Video paid view offering is one of the most popular and widely available digital movie and TV rental services available" ("The State of Online…", 2011, p.11). Amazon's offerings are close to iTunes with 2,300 TV shows and 62,000 episodes ("The State of Online…", 2011), it is certainly one of the major players in the paid sector and iTunes biggest competition.

Subscription services. The second online video delivery model is based on subscriptions as opposed to pay-per-item. "The three most popular subscription OTT video services are Netflix, Amazon Prime Instant Video and Hulu Plus" ("The State of Online…", 2011, p.10). Netflix is the current leader in the segment, followed by Hulu Plus, Amazon

Prime Instant Video (not to be confused with Amazon Instant Video paid service) was just launched in 2011 and it is in its initial stages ("The State of Online…", 2011).

Netflix was launched in 1998 as a mail to order DVD service. Almost 10 years later, in 2007, it started offering streaming video on its website "giving its subscribers unprecedented access to a video library at no additional cost to them" (Holden, 2010, p.1). In 2010, the streaming library transitioned from being an added feature to an entirely independent new service. "The company announced Nov. 22 that it now offers a streaming-only plan for $7.99 a month" (Holden, 2010, p.1). In 2011, Netflix separated their offerings into DVD only and streaming only making it more costly to rent DVDs and keeping the streaming service price intact. Netflix considered the possibility to create a separate business unit for the DVD rental service rebranding it with a different name; however, the massive negative response of the market forced them to keep both services (streaming and DVD rentals) under the Netflix umbrella. Netflix's management declared their intention to preserve the DVD by mail business as long as possible; however, "the company has also been spending more money to acquire content for streaming than it will on DVDs and Blu-ray Discs in 2010" (Holden, 2010, p.1). Amongst all the subscription based services, Netflix has the largest library of movies and television. The television catalogue includes 750 shows and 23,500 episodes. However, the TV episodes available do not include newer shows or current seasons ("The State of Online…, 2011).

Setting the DVD rental service apart, "the problem for Netflix is that its business is going to change completely. Rather than buying discs wholesale and turning a profit rather quickly, Netflix will be in the business of licensing content — a much more expensive proposition" (Holden, 2009a, p.1). In fact, Netflix has already begun experiencing content acquisition related issues. Netflix used to feature past seasons of Showtime's series, but the cable network has removed all of its TV shows from the service ("The State of Online…", 2011). Same thing happened more recently with Starz, which chose not to renew their

streaming deal. On the broadcast side, things seem to be going better for Netflix. In late 2010, Netflix signed a streaming deal with ABC offering, “content from ABC, ABC Family and Disney Channel, some airing within 15 days of the original telecast” (“The State of Online…”, 2011, p.9). On the cable side, AMC has several deals in place with Netflix for the streaming rights to some of their most popular shows including: *Mad Men*, *Breaking Bad* and *The Walking Dead* (Goetz, 2011). Broadcast shows can also be found on Netflix, but they usually feature older seasons that have already been released on DVD.

The future of Netflix depends on how successful the company is in striking deals with content owners. For the service to survive as a streaming service, the content of the streaming library has to dramatically improve and they must be able to maintain the titles of their library for a certain amount of time. Customers have already reacted negatively to the recent changes (and so has the stock market), but the company claims it was a move necessary to ensure their long-term strategic vision. As more users stream TV shows on Netflix, the platform has to worry about acquiring television content as well as films. How popular the platform will be for TV fans in the future remains to be seen. For content owners, Netflix future plans may result in less DVD sales and more licensing fees for online streaming. If this is the case, the net result will probably be more money for the studios.

Next to Netflix, the other big player breaking into the subscription arena is Hulu Plus, the paid subscription version of Hulu. In the same way to Netflix, Hulu Plus is priced at $ 7.99 per month. Hulu Plus has less TV titles than Netflix in its library: only 450 shows and 16,000 episodes. However if we include the free library of Hulu, the number of episodes would surpass Netflix’s. Moreover Hulu Plus “offers the biggest collection of first-run TV shows often allowing viewing the day after they air” (“The State of Online…”, 2011, p.11). Hulu Plus is associated with television as opposed to Netflix that is usually identified with films. Television fans are more likely to find current content on Hulu Plus than Netflix. Another important thing to note about Hulu Plus is that it has provided the opportunity for a

dual revenue model. Free Hulu is supported by advertisements while Hulu Plus is subscription based. The hybrid model was launched because the company claimed they needed “two revenue streams in order to survive long-term” (Myers, 2010d, p.1). With Netflix price increase upsetting many users; it could be the opportunity for Hulu Plus to gain some terrain.

The final subscription service we will discuss is Amazon Prime Instant Video. Unlike Amazon’s instant video, ‘Prime instant video’ is a subscription service. Amazon Prime has an annual subscription of $79 (equivalent to $6.58 per month). The streaming video service was introduced recently as an added value for the already existing Prime membership, for which the main feature is free two day delivery on most products sold on the website. The service features 500 TV shows but only 4,000 episodes (“The State of Online…”, 2011). In addition most TV shows available are fairly outdated. “The service does not yet have the deals in place with studios and networks to get fresher content” (“The State of Online…”, 2011, p.11). The service will very likely increase its offerings in the future, but not to the level of Netflix or Hulu since Amazon’s prime main attribute is not the streaming library.

Ad supported services. Ad supported services provide free streaming video to the public and they include advertisements. Hulu dominates this segment of the market. Hulu was created in 2007 as a joint venture of three media conglomerates: NBCUniversal, Walt Disney and News Corp. It was “designed as a marketing tool and a means to capture online advertising revenues” (“The State of Online…”, 2011, p.6). The site provides access to most shows on NBC, ABC and FOX the day after they premiere (although some networks like FOX are delaying that window). Towards the end of 2011, Hulu started streaming all The CW shows, previously unavailable, with a delay of 8 days after the original telecast. The site does not have content from CBS but they do provide outside links for most of their shows. Hulu also has an easy to use webpage that allows the user to build a queue and receive e-mail alerts. In 2011, the site integrated its content with social media sites like facebook, giving

one more added feature to their platform. Commercials are much shorter than TV ads; however they are becoming longer and more frequent than they were during the first years of ad supported streaming video. Hulu has a steady offering of free current shows; the only disadvantage is that episodes are posted for short periods of time (usually around 30 days). Nevertheless, Hulu has the biggest compilation of current shows with most studios supplying content and aggressive marketing campaigns (Holden, 2009a). With the introduction of Hulu Plus, the company as a whole will enjoy a dual revenue stream model.

On top of Hulu, the major networks usually have their own website where they stream full episodes that feature ads. Some examples include ABC.com, NBC.com, FOX.com, CWtv.tv and CBS.com. The former does not post its videos on Hulu; hence its website is the only place where you can stream their latest episodes for free. The advantage of Hulu over the individual network sites is that you can find TV shows from almost all networks in one site and it includes features that make it easy to keep track of what shows and what episodes the user is watching.

This research has reviewed the different online platforms where networks are posting their content; in the meantime, “Multichannel service providers are working to fill consumer demand for increased online options and combat the competitive threat of over-the-top video with their own initiatives, which largely fall under the TV Everywhere label” (“The State of Online…”, 2011, p.6). With TV everywhere, multichannel operators mainly pretend to satisfy their customer’s demand for flexible viewing options (“The State of Online…”, 2011). For other OTT services, TV everywhere means increased competition. For content owners it means another outlet that would be paying them for streaming rights. “These companies [Online video service providers] will face a great many issues in getting video content to consumers. The one thing they all share is that they are at the mercy of the studios.” (Holden, 2009a, p.1)

Consumers have made it clear that they want television shows to be available online; however, **"**studios continue to be wary of the online video market. In large part, their fear is rooted in the idea that it will eat away at their existing business" ("The State of Online…", 2011, p.9). As it usually happens with the introduction of new distribution windows, content owners become apprehensive of them hurting ratings and therefore advertising and syndication revenue. It has been speculated that after ABC launched its prime-time series on iTunes, some were negatively impacted. According to an SNL Kagan report, *Lost* suffered a ratings decline during its third season, right after the show was made available for downloads on iTunes ("Economics of TV…", 2007, p.60). Nevertheless, it is hard to say if the decrease in ratings was actually attributable to the content made available on iTunes; the show had a mid season break and it was up against *American Idol*, both of those reasons seem more likely to be responsible for the ratings downturn ("Economics of TV…", 2007).

Touching on the same subject, Joanne Burns, executive vice president for marketing, research and new media at Fox Television, explains that the majority of TV viewing remains live, with only 1.7% of all viewing being on the internet. In addition, she says, "there is little overlap between TV and streaming viewers" (Di Grazia, 2010, p.1). Moreover, as Vincent Bruzzese notes, "video increases show pickup by allowing viewers to catch up on past episodes" and it also promotes sampling new TV shows to potentially increase the live audience (Di Grazia, 2010, p.1). "However, at the end of the day, it comes down to money. If the networks are not getting paid for their content, they will have little incentive to distribute it online" (Di Grazia, 2010, p.2).

Content owners profit from online distribution in two different ways: license fees (streaming rights) and advertising revenue. Companies like Netflix are heavily investing to enter the digital world and many other companies will soon follow. Consequently, there will be many digital distribution deals struck between online video service providers and the

studios in the coming years. As of right now, content owners appear to have the upper hand. They have the content and without it platforms like Netflix simply cannot exist. Online platforms are beginning to fight back with the introduction of original content; however, content owners could simply decide to cut the middle man and find direct to consumer outlets. Out of both scenarios the former certainly seems more feasible and it is very likely that studios will maintain their bargaining power in the future.

Currently, "digital still delivers a fraction of what other windows generate" (Myers, 2010c, p.2). However, content owners are striking larger and more frequent digital rights contracts and licensing online content could become a very important cash in flow for the studios, enough to replace other decaying windows like DVD sales. Online advertising revenue is still very small when compared with television's share. For 2010, online advertising represented around 5.2% of total advertising revenue for the networks (Flynn, 2010, p.1). However, the segment is growing rapidly. "The Internet remains the most promising media sector in terms of advertising growth, given the increasing popularity of the Web as a primary source for entertainment and the adjustments made by traditional media conglomerates that seek to capture shifting audiences" (Castaneda, 2010, p.1). Furthermore, "Online video is projected to be the fastest-growing ad format online" (Castaneda, 2010, p.2).

Online advertising still has lower profits than television seeing that, "TV ads still beat online video ads in terms of reach" (Kee, 2009, p.1). In the past, it was a given, advertising online was cheaper; however "video sites like Hulu and TV.com are finally starting to deliver ad rates that are greater than what the networks would get for their shows on air" (Kee, 2009, p.1). According to Bloomberg, running an ad during The Simpsons on Hulu has a CPM of $60, while the same ad on TV costs around $20-$40. "The reason people are paying such a high premium for these ads on the Internet is they do have a captive audience" (Kee, 2009, p.1). For all of these reasons, online video advertising shows great promise for the future.

From the advertiser's point of view, online video provides many new opportunities as well. "The internet's interactivity and wealth of product information make it the best means of generating short-term sales" ("Ad-spending usually…", 2008, p.2). Also, "the internet has brought greater accountability to advertising. Marketing chiefs can now prove that a click on an online ad produces a sale" ("Ad-spending usually…", 2008, p.1). In other words, online video ads can be very effective for advertisers, they are usually cheaper than broadcast television ads, they can be targeted and their effectiveness can be measured by click through ratios. "Advertisers also have an unprecedented opportunity to capitalize on their investment as the Internet offers more ways to target a specific audience. Some studies further suggest that, for people watching a TV program, ads are more engaging online than seen on a traditional set." (Castaneda, 2008, p.1)

Online revenue may still be small when compared with other segments of the media conglomerates. Regardless, "it is essential for networks and studios to provide a legitimate way for consumers to access their content online, whether through paid downloads, subscription, rentals or ad-supported" (Di Grazia, 2010, p.2). Consumers are quickly transitioning to the digital world and studios cannot ignore the advance of technology. As Holden explains, "There are many unanswered questions in this transitional phase of home entertainment" (2009a, p.2), the key one probably been what delivery model works best. Myers summarizes the state of the market:

> The success story of the moment is paid models, which have generated the largest pool of monies for professional content producers. Ad-supported models have also shown great promise. Paid models have generated more revenue in the online video market, to the tune of $2.3 billion in 2010, versus $1.5 billion for advertising. However, we expect the growth of TV Everywhere models will help boost advertising for online video as more content owners allow distribution of their product in authenticated services (2010d, p.1).

Regardless of what model will prevail and what platforms will succeed, internet has become a part of the everyday life of the average consumer. Content owners cannot avoid

making their shows available in the online world. They should embrace the digital revolution as one more way to make money with their content.

Summary

Like any other product, TV shows have revenues and costs associated with them. The costs are somewhat controlled variables with relative ease in measurement. The different revenue windows on the other hand, are complicated and depend on many factors therefore. Without disregarding the corresponding costs, we focused our analysis on the revenue side of the equation.

This research began with the analysis of the advertising revenue. Commercial television is heavily influenced by ratings which determine the price per spot that can be charged for each show. Programmers have developed scheduling techniques to maximize ratings. In addition, other external factors such as the economic conditions and the performance of cable have an impact on the overall advertising revenue. Although a main concern for programmers, advertising is only the first item in the revenue chain. Following the broadcast premiere, shows are often sold in syndication. With the relaxation of fin-syn rules, networks are allowed to own part of their TV series and benefit from syndication. Another important revenue source is home video. The industry of home video took off with the advent of DVD. Because of vertical integration, networks are also benefiting from DVD sales. Finally, networks had to adapt to the ever-changing markets and enter the digital age. This study focused mainly on two items that fall under the 'time shifting technology' category: DVR and online streaming. Both technologies had positive and negative consequences for broadcasters. One thing is certain, digital alternatives are here and industry players need to figure out a way to take advantage of them.

The studies reviewed in this research do a thorough job of analyzing the particular areas they cover; however, there is a lack of research that explores the relationships between areas and how decisions made at a network level can impact other business

segments of the media conglomerates. Additionally the researcher has not found a single study that summarizes all the cash inflows and outflows of a TV series from a financial perspective. The objective of this study, therefore, is to compile the data in one single model that will try to systematize and replicate the thought process of executives across the industry when evaluating financial viability of a TV show. The findings will later be summarized in a fictional case study that can be used as a tool by industry professionals and students in the field. The case can be found on Appendix B.

Chapter Three : Methods

Within a landscape of vertically integrated media conglomerates and new distribution windows constantly emerging, a TV show can generate multiple revenue streams. For a long time, networks measured the success of a TV show as a simple reflection of the ad revenue. However, other revenue sources can be of equal or more importance than advertising revenue and among these revenue sources are syndication, home video sales and digital distribution. As part of larger media companies programmers need to take into consideration many more factors when determining which shows are successful, redefining success as the aggregation of all the revenue they can generate across windows during their entire lifespan.

The following research questions were addressed in this study:

- What are the micro and macro factors that affect the advertising revenue a TV show can generate?
- What are the variables that determine the success of a TV show in the syndication market and how much does it depend on its performance during the original broadcast?
- What types of shows have the biggest potential in the home video market and how did they perform during the original broadcast?
- What is the impact of DVR playback on the ranking of TV show and how can this affect programming decisions?
- How significant is the revenue a TV show can generate from online platforms?

This study was based on quantitative analysis of secondary data obtained from databases and trade publications. The analysis was divided in five parts corresponding to each research question. The first step was to collect data related to advertising revenue and the factors that may have an influence on it. The data were analyzed using an econometric model based on the Ordinary Least Squares (OLS) method. Secondly, the researcher

collected data of reported syndication deals. The data were transcribed and categorize with the goal of inferring common characteristics among the highest earning shows in the syndication market. In an analogous manner, the researcher monitored the top selling DVDs and Blu-rays to identify the aspects that ensure success in the home video sector. Next, the researcher collected data regarding DVR playback in order to compare Live and Live + 7 ratings and infer how they may influence programming decisions. Finally, the researcher reviewed industry publications to study the potential of online platforms as a form of distributing TV content.

Sample

Below, the researcher describes the samples for each section of the analysis and explains how they were selected from the broader population.

Advertising Revenue Analysis. The sampling procedure used by the researcher was purposive sampling. This section analyzes the advertising revenue of broadcasting networks. The researcher worked with industry averages for broadcasters that are ad supported, public/educational broadcasters such as PBS were excluded from the sample. The networks included in the sample are the 'Big Four': ABC, CBS, NBC and FOX; the 'small three': The CW, ION and MyNetwork TV and finally the Hispanic networks: Univision, Telemundo, Telefutura, Azteca Americana and Estrella TV. The researcher included data going as far back as 1994. The reason to take into account older data was to expand the number of observations to obtain more reliable results in the econometric model.

Syndication Revenue Analysis. For this section, the sample was selected using purposive and convenience sampling. The researcher selected a sample from the TV shows of the 2006-07 schedule. The networks included were: ABC, CBS, NBC, FOX and The CW. The 2006-07 season was selected because all the shows that aired that year, would have reached a syndicatable level of episodes by now (provided that they were not cancelled). First, the researcher tabulated the entire 2006-07 schedule and then the shows that had enough

episodes for syndication were selected. Out of all the shows with the minimum number of episodes, the researcher analyzed the ones that had reported syndication deals. The resulting sample included 37 shows that aired during the 2006-07 season. To date, all the shows included in the sample have reached 80 episodes or more, with the exception of *Heroes* which only had 79 episodes. The shows included in the sample were 9 comedies, 23 dramas and 5 reality shows. Other genres such as sports and news were excluded from the sample. Both in-house and externally produced shows were included.

Home Video Revenue Analysis. The sampling procedure used by the researcher was purposive sampling. Out of all the TV series available on home video, the shows that were included in the sample were the top selling DVDs and Blu-ray discs. To select the sample the researcher monitored the 'Best Sellers' lists on Amazon.com for a period of four weeks from January 2, 2012 to January 29,2012. The final sample comprised the top 20 DVDs and top 5 Blu-ray discs for the period mentioned above. All the shows that were available on DVD or Blu-ray had equal opportunity to be included in the sample.

DVR Playback and Programming Decisions. The sampling procedure used in this section was purposive sampling. The researcher used as a sample the shows that aired on broadcast television during the 2010-11 season. That particular season was selected because renewal/cancellation decisions had already been made for and the researcher was able to cross-reference said decisions with DVR playback data. The genres included were drama, comedy and reality. News/magazine and sports were excluded. The networks included were ABC, NBC, CBS, FOX and The CW.

Online Revenue Analysis. The sampling procedure used by the researcher for this section was convenience sampling. The focus of the analysis for this section was TV shows that have some sort of digital distribution deal in place. However, not all online platforms reveal the financial details of their negotiations with content owners. In this context, the researcher was able to analyze Netflix deals for streaming content from 2010 to present. At

the same time, the researcher used purposive sampling to monitor the top downloaded TV shows on iTunes and Amazon Instant Video with the objective to infer which shows are the most popular on paid services. All shows that are available for download had the possibility of being included in the sample. Finally, to analyze the evolution of online ad revenue, the researcher analyzed the historic revenue of a sample that included all the national broadcasters from 2006 to 2010.

Measurement Instruments

The researcher worked entirely with secondary data that were already collected and available for further processing. Below we detailed the main sources of information:

- ***SNL Kagan database:*** The researcher used historic data collected on a regular basis by this database including: CPM, ratings, total advertising spending (all media) and gross broadcast advertising revenue. In addition the researcher used the complete 2006-07 schedule published in one of the company's data books. A spreadsheet detailing Netflix's historical content deals was also provided by this service as well as several articles on digital distribution deals. Financial metrics published by SNL Kagan are estimates of the SNL Kagan team, with portions based off of the Nielsen company data.
- ***Trade Publications:*** Trade Publications were reviewed extensively by the researcher to obtain details about syndication deals and digital distribution agreements. The main publications consulted were the SNL Kagan news archive as well as Broadcasting & Cable, Variety, The Hollywood Reporter and Deadline. The publications mentioned above are reliable sources of information written by professionals in the industry. In order to ensure the accuracy of the information, the researcher cross referenced at least two different sources for most reported syndication and digital distribution deals.

- ***TVbythenumbers (Zap2it.com):*** The researcher obtained the Live + SD and Live + 7 ratings for the 2010-11 season from the archive of this site. Additionally, the researcher used the Bubble Watch and the Renew/Cancel Index to determine the status of the shows analyzed. The website uses information provided by Nielsen.
- ***Internet Movie Data Base (IMDB.com):*** The researcher used this database to determine the number of episodes of the shows analyzed. The IMDB is a cooperative database; however contributions must be approved by the site's staff before they are posted ensuring accuracy. The site is continuously updated.
- ***Amazon and iTunes:*** The researcher built the top selling DVDs and Blu-ray discs and top downloads lists using information from online video providers. Amazon keeps a list of Best Selling DVD's, Blu-rays and Amazon Instant downloads while iTunes has a list of top TV downloads. Amazon is one of the most popular DVD and Blu-ray retailers; therefore the best sellers list is a valid indicator of the market's trends. The lists are based on consumer purchases and are updated hourly. In the same way, iTunes and Amazon Instant Video are the biggest platforms for electronic downloads.
- ***World Bank****:* The researcher used macroeconomic data from the World Bank website including GDP (Gross Domestic Product) and CPI (Consumer Price Index).

Data Collection

Advertising Revenue. The data for this section were collected from online databases. The researcher collected historical data for the following variables: Broadcast CPM, 24 hour average broadcast ratings, total advertising spending, gross broadcast advertising revenue, cable CPM and GDP. The number of observations included in the sample was 17 corresponding to the time period from 1994-2010. Once the researcher finished collecting the data, the observations were organized in a chronological table. To eliminate the effects of inflation the variables, with the exception of the ratings, were converted to constant prices using the CPI with base year 2000.

Syndication Revenue. The complete 2006-07 broadcast schedule was obtained from the SNL Kagan database. The schedule was tabulated in a spreadsheet. The researcher classified the shows by genre, network and production company. In addition, the researcher collected information on number of episodes that aired before December 2011.The shows that had fewer than 80 episodes were eliminated from the sample. For the remaining shows (56 shows), the researcher included the following additional data: 2006-07 average share, price per ad spot and number of spots per hour. The researcher then reviewed reported syndication deals. Out of the 56 shows that had 80 episodes or more, the researcher found reported syndication deals for 37 of them. The rest of the shows did not have syndications deals in place or their details were not made public, therefore they were not included in the sample.

Home Video Revenue. The data collection process for this section took place over a period of four weeks from January 2nd, 2012 to January 29th, 2012. The researcher checked the Best Sellers list on Amazon.com every day during that period and transcribed the top 20 DVDs and top 5 Blu-ray discs to a spreadsheet. The researcher then assigned a reverse score to each title (the top selling DVD had a score of 20 and the top selling Blu-ray had a score of 5). At the completion of the observation period the researcher added the scores of the titles and built a consolidated table. In addition, the researcher gathered information on the release date and average ratings for the top selling shows.

DVR Playback and Programming Decisions. The researcher worked with the complete list of Live + 7 ratings for the 2010-11 season obtained from TV by the numbers. The data were summarized on a spreadsheet where the Live + 7 ratings were compared to the Live + SD ratings for the adults 18-49 demographic.

Online Revenue. The researcher tabulated the historic data of the online advertising revenue and total advertising revenue for broadcast stations from a period that extended from 2006 to 2011. These figures corresponded to estimates of the SNL Kagan database. To

determine the license fee potential revenue the researcher studied Netflix historical data. First the total content acquisition expenses were analyzed from 2007 to 2010. Finally, the researcher analyzed the paid download model and monitored the top downloaded shows on iTunes and Amazon Instant video following the same procedure as for the top selling DVDs and Blu-rays. The collection process to determine the top 20 downloads took place over four weeks from January 9th, 2012 to February 5th, 2012. The resulting top 20 table was complete with information about ratings, status of the show, genre and network where they air.

Data Analysis

Advertising Revenue Analysis. To analyze the behavior of the television advertising rates and the internal and external factors that have an influence on it, the researcher performed a multiple regression analysis using the Ordinary Least Squares (OLS) method. The collected data were analyzed with Eviews software. The input consisted of the following variables:

Dependent Variable

- Y: Broadcast CPM [USD constant prices base year 2000]

Independent Variables

- X1: Broadcast 24 hour average ratings
- X2: Total advertising spending (all media) [USD constant prices base year 2000]
- X3: Gross broadcast advertising revenue [USD constant prices base year 2000]
- X4: Real GDP growth [% base year 2000]
- X5: Cable CPM [USD constant prices base year 2000]

The researcher collected data for a time period that extended from 1994 to 2010 (17 observations). However, the variables were not stationary, which is one of the requisites to use the OLS method. In order to work with stationary variables, the researcher used the first difference of the variables.

After the first difference of the variables was calculated, the number of observations of the model was reduced to 16. To confirm the stationarity of the variables the researcher implemented the Augmented Dickey-Fuller (ADF) Unit Root Test. Once the stationarity was guaranteed, the researcher performed the multiple regression of the depended variable "Y" with respect to the independent variables "X1", "X2"," X3", "X4", "X5" and a constant "C". Individual samples t-tests were conducted to test the significance of the estimated partial regression coefficients. In addition, the researcher conducted a joint F-test to ensure the overall significance of the coefficients. A correlation coefficient R2 was also calculated to determine what percentage of the dependent variable variation is explained by the regressors of the model. Next, the researcher performed an autocorrelation Durbin Watson test, the heteroscedasticity White test and the Normalcy-Jack-Berra test to guarantee that the OLS assumptions of Homoscedasticidy and normal distribution of the error were met. Finally the researcher built a correlation matrix and calculated the Variance Inflation Factor (VIF) of each regressor to determine possible multicolinearity issues.

Syndication Revenue Analysis. The collected data were transcribed and organized in an excel spreadsheet that included: name of the show, genre, number of episodes, network, ownership (in-house, external production), network ad revenue per episode, 2006-07 average share and syndication revenue per episode. The researcher calculated the correlation between syndication revenue and the following variables: network ad revenue, number of episodes and share with the objective to find if they are significantly correlated. In addition, using dynamic tables, the researcher observed the influence of the genre and ownership on the syndication revenue. Finally, the researcher created an abbreviated cash flow for selected TV shows of each genre to compare the advertising revenue per year and the total syndication revenue.

Home Video Revenue Analysis. The collected data were organized on two excel tables. The first table included the top 20 best selling DVD titles, the genre of the show, release date and ratings. The second table had the same elements for the top 5 best selling Blu-ray discs. The researcher observed the release date information to determine if novelty has an influence on sales. Also, the researcher observed the genre and network of the shows in the top selling. Finally the researcher compared the relative placement of the shows on the home video market with their ratings performance during the original broadcast.

DVR Playback and Programming Decisions. Using the 2010-11 season data, the Live + SD ratings were compared with the Live + 7 ratings to determine the audience increase due to DVR playback. The researcher ranked the shows by relative increase in ratings and observed the characteristics of the shows that presented the biggest gains. Following this, the researcher compared the top 10 shows ranked by Live + SD ratings and the top 10 shows ranked by Live + 7 ratings to see if DVR playback has a significant impact on the ranking of the shows. The same comparison was performed for the 10 lowest rated shows. Finally, the shows were classified by network and genre. The researcher observed the renewal/cancellation decisions of each network to infer if DVR ratings may have had an impact.

Online Revenue Analysis. As was explained in the literature review, content owners benefit from online platforms via advertising revenue and/or license fees. License fees can be obtained by selling streaming rights to subscription services such as Netflix, but also via paid downloads on platforms like iTunes. The researcher first examined the online advertising revenue and created a time series that compared the online advertising revenue with the total advertising revenue of broadcast stations for a period of six years (2006-11). The researcher calculated the relationship between online advertising revenue and total advertising revenue and observed the trend. Next, the researcher took a look at the financial information of Netflix. The researcher built a comparative table of Netflix investments on

the DVD library and streaming library observing and comparing their trends. In addition, the researcher analyzed selected streaming deals that included television content. Finally, the researcher looked at the paid download model of iTunes and built a top downloaded shows chart following the same procedure that was used for the home video section.

Chapter Four : Results

In this chapter we will present the results of the data analyzed according to the methodology described on Chapter Three. As mentioned, the analysis was divided in five sections, each one corresponding to one of the research questions: Advertising revenue analysis, syndication revenue analysis, home video revenue analysis, DVR playback and online revenue analysis.

Advertising Revenue Analysis

The researcher performed an Ordinary Least Squares (OLS) multiple regression using the first difference of the following variables:

- Y: Broadcast CPM [constant 2000 USD][3]
- X1: Broadcast 24 hour average ratings
- X2: Total advertising spending [constant 2000 million USD]
- X3: Gross broadcast advertising revenue [constant 2000 million USD]
- X4: Real Gross Domestic Product (GDP) growth [% base 2000]
- X5: Cable CPM [constant 2000 USD]

n: 16 observations (1995 – 2010)

Unit Root Test. The variables included in the model need to be stationary (without a trend) to be able to use the OLS method. The researcher performed an Augmented Dickey Fuller (ADF) test on the independent variables to ensure they were stationary.

Ho: The variable has a unit root (it is not stationary)

Variable	ADF probability
X1	0.37%
X2	1.22%
X3	0.01%
X4	0.16%
X5	0.05%

Note. For the Ho to be accepted at $p<0.05$, the ADF probability should be bigger than 5%

[3] To avoid the effects of inflation, variables Y, X2, X3 and X5 were converted to constant prices using the CPI with base year 2000

As we can see the null hypothesis of the test is rejected for all variables indicating they are in fact stationary.

Multiple Regression. The researcher performed a multiple regression of: Y=f(X1, X2, X3, X4, X5). The resulting equation was:

$$Y = 0.69 - 0.73*X1 - 5e\text{-}005*X2 + 0.00053*X3 + 26.36*X4 + 0.16*X5$$

The correlation coefficient (R2) of the regression was: 69%. Before proceeding any further, the researcher performed individual and joint independent sample tests.

F-test (Joint independence sample test).

Ho: There is no significant difference in the CPMs (Y) as a result of combined changes in the independent variables(X1, X2, X3, X4 and X5).

F-statistic	Prob.(F-statistic)
4.39	2.25%

Note. For the Ho to be accepted at p< 0.05 the prob. (F-statistic) should be bigger than 5%

The Null hypothesis of the F-test is rejected; therefore the estimated coefficients jointly explain the variations of the dependent variable.

t-test (Individual independence sample test).

Ho: There is no significant difference in the CPM (Y) as a result of changes in the independent variable Xi

Variable	t-Statistic	Prob.
X1	-1.91	8.53%
X2	-2.59	2.69%
X3	2.20	5.25%
X4	3.56	0.52%
X5	0.24	81.82%

Note. For the Ho to be accepted at p<0.1, the prob. Should be bigger than 10%

The t-test null hypothesis is rejected for all the coefficients except X5, which means that X5 does not explain the variations of the dependent variable and should be removed from the model.

Revised multiple regression. The X5 variable was taken out of the model and the researcher performed the multiple regression as follows: Y=f(X1, X2, X3, X4). The revised regression equation is:

$$Y = 0.71 - 0.68*X1 - 4.83e\text{-}005*X2 + 0.00054*X3 + 26.61*X4$$

Table 4.1
Revised Multiple Regression Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.705355	0.150949	4.67	0.07%
X1	-0.684870	0.320954	-2.13	5.62%
X2	-4.83E-05	1.71E-05	-2.83	1.64%
X3	0.000544	0.000226	2.41	3.46%
X4	26.61427	7.009858	3.80	0.30%
R-squared	68.52%	F-statistic		5.98
Adjusted R-squared	57.07%	Prob(F-statistic)		0.83%

Note. C=Constant. R-Squared (R2) Correlation coefficient. Adjusted R-Squared=modified correlation coefficient adjusted for the number of regressors.

As we can see in Table 4.1, the null hypothesis of the F test is rejected as well as the t-test hypothesis for all the coefficients. The correlation coefficient is relatively high (68.5%). We can infer that the estimated coefficients included in the model explain 68% of the changes in the dependent variable.

To guarantee that the model follows all the OLS assumptions and that the calculated equation is valid, the researcher performed a series of tests. These tests ensure that the variables do not present multicolinearity or autocorrelation and that the error has a normal homoscedastic distribution.

Normalcy Jack-Berra (JB) test.

Ho: The error presents a normal distribution

JB= 61%

The null hypothesis is accepted; hence the normalcy assumption is met.

Heteroscedasticity White Test.

Ho: The error is homoscedastic

White heteroscedasticity test			
Obs*R-squared	8.94	Probability	34.76%

Note. For the Ho to be accepted at p<0.05, the probability should be bigger than 5%

The null hypothesis is accepted, which indicates the model meets the homoscedasticidy assumption.

Autocorrelation Durbin Watson test

Durbin-Watson stat	1.81

The Durbin Watson Stat is close to 2; this indicates that the model does not present autocorrelation.

Multicolinearity. Finally, the researcher checked the variables for multicolinearity. The first step was to build a correlations matrix:

	X1	X2	X3	X4
X1	-	-0.174	0.063	0.211
X2	-0.174	-	0.777	0.485
X3	0.063	0.777	-	0.504
X4	0.211	0.485	0.504	-

As we can see, X3 (total ad spending) and X2 (gross broadcast advertising revenue) are highly correlated (77%). This situation was expected since the gross broadcast advertising revenue is part of the total ad spending. However, those variables do not present a perfect correlation and even on occasion they move on opposite directions.

According to Gujarati ("Basic Econometrics", 2004), there is a serious problem of multicolinearity when the correlation between two variables is larger than 80%. In this case, the correlation is slightly below that level. To guarantee the multicolinearity was not severe, the researcher performed a second test for multicolinearity using Variance Inflation Factors (VIF).

Variable	VIF
X1	1.25
X2	3.11
X3	2.86
X4	1.51

Conservatively speaking if the VIF of a coefficient is larger than 5, there is a serious problem of multicolinearity. The calculated VIFs are all below this level. The researcher concluded that while there is some multicolinearity present in the model, it is not serious and decided to keep the four coefficients in the model.

The hypothesis tests performed above guarantee that all the assumptions of the OLS model are met. For that reason, the equation resulting from the multiple regression can be used to explain the model.

$$Y = 0.71 - 0.68*X1 - 4.83e\text{-}005*X2 + 0.00054*X3 + 26.61*X4$$

The equation indicates that Broadcast CPM levels vary as a consequence of changes in the broadcast ratings, total ad spending, gross broadcast ad revenue and GDP. The estimated coefficients also show that the Broadcast CPM level is directly correlated to the gross broadcast ad revenue and the GDP and inversely correlated to the ratings and the total ad spending. In addition, the correlation coefficient (R2) reveals that around 68.5% of the variations in the broadcast CPMs can be explained by the variables of the model, therefore the remaining 31.5% of the variation is caused by factors outside the model. These results will be further discussed in Chapter Five.

Syndication Revenue Analysis

The second part of the analysis focuses on syndication revenue. Using the table of syndication deals for the 2006-07 season that can be found in the appendix (Table A1), the researcher calculated the correlation between the syndication revenue and other relevant variables. The variables analyzed were: Advertising revenue, number of episodes and share points.

Table 4.2
Syndication Revenue Correlation Matrix

		1
1	Syndication fee	
2	Ad revenue	0.0962
3	No. of episodes	0.2283
4	Share	0.3298

From Table 4.2 we can see there is no significant relationship between the syndication fee and any of the variables analyzed. These results indicate that the syndication revenue is not correlated to the performance of a show during the original broadcast. Also, a larger number of episodes (beyond the minimum number necessary for syndication) do not generate higher syndication fees per episode. Moreover, the researcher did not find any definitive pattern between the ownership of the show and the syndication revenue. In other words the syndication revenue did not depend on whether the shows were produced by the same company that aired them.

One factor that seems to have a decisive influence over the syndication revenue is the genre of the show. The syndication market has a high demand for half hour comedies. The genre that follows comedies in popularity is procedural dramas bought mostly by cable channels. Serialized dramas struggle to sell in syndication, and are usually acquired by niche cable networks. As we see in Table 4.3, even less popular comedies like *30 Rock* performed better in the syndication market than hit serialized dramas like *Lost*.

Table 4.3
30 Rock/Lost Syndication Revenue Comparison

Show	Genre	No. episodes	Network	Syndication per episode ($ 000)	2006-07 Share
30 Rock	Comedy	104	NBC	800	8.0
Lost	Drama	115	ABC	200	15.0

Note. Source: SNL Kagan

Reality shows have the lowest demand in the syndication market. *Fear Factor* struck the most successful syndication deal for a reality show to date. The show was sold for $280 thousand per episode, a very low syndication fee compared to other genres. Most reality shows, however are sold for much less if anything at all. For instance the ratings hit *Survivor* barely made any money in the syndication market as shown on Table 4.4.

Table 4.4
Advertising and Syndication Revenue Comparison

Measure	Survivor	The Office	Grey's Anatomy	CSI
Ad Revenue per episode	3,781	1,957	5,814	4,636
Average License Fee per episode	1,654	882	1489	2322
Profit from advertising per episode	2,127	1,075	4,325	2,314
Syndication fee per episode	65	2,400	1,200	1,600
Syndication/advertising	3.06%	*223%*	28%	69%

Note. Each episode of Survivor, Grey's Anatomy and CSI has 19 ad spots. Episodes of The Office have 10 spots. All numbers are expressed in thousand of $, except for the %. Source SNL Kagan

The syndication fee per episode of *Survivor* represented only 3.06% of what the show generated with advertising during the original broadcast. In contrast, syndication revenue for half-hour comedies exceeds the money made from advertising as we can see in Table 4.4.

Dramas do not perform as badly as reality shows, but they do not generate the high revenue of comedies either. The data revealed that even popular serialized dramas like

Grey's Anatomy have a hard time producing syndication revenue comparable to what they earned with advertising. This situation is illustrated in Table 4.4.

From Table 4.4 we can observe, procedural dramas fair better, but still below the remarkable performance of comedies:

Clearly the definitive factor in the syndication arena is the genre of the show. None of the other variables analyzed appears to have considerable influence during syndication agreements; even ratings are a secondary concern. Regardless of the ratings a show generates during the original broadcast, syndication market favors half-hour comedies (even the less popular ones). However, while other genres are less desirable in the syndication market, this may not be the case in other windows.

Home Video Revenue Analysis

In this section, the researcher observed the best selling TV titles in the home video market. The researcher compiled lists of the top 5 Blu-ray discs (Table 4.5) and top 20 DVDs (Table 4.6) according to the methodology described on Chapter Three.

Table 4.5
Amazon's Top 20 Bestselling DVDs

DVD Rank	Show	Release date	Rating A18-49 Live + SD	Genre
1	Masterpiece Classic: Downton Abbey S2	02/07/12	2.7	Drama
2	Masterpiece Classic: Downton Abbey S1	01/01/11	2.7	Drama
3	Justified S2	01/03/12	0.9	Drama
4	The Big Bang Theory S4	09/13/11	4.0	Comedy
5	Boardwalk Empire S1	01/10/12	1.3	Drama
6	The Big Bang Theory S1	09/02/08	4.0	Comedy
7	Archer S2	12/27/11	0.6	Comedy
8	The Big Bang Theory S2	09/15/09	4.0	Comedy
9	The Big Bang Theory S3	09/14/10	4.0	Comedy
10	Justified S1	01/18/11	0.9	Drama
11	Dexter S5	08/16/11	1.0	Drama
12	Modern Family S2	09/20/11	4.5	Comedy
13	Smallville S10	11/29/11	1.1	Drama
14	Game of Thrones S1	03/06/12	1.4	Drama
15	One Tree Hill S8	12/20/11	0.9	Drama

Table4.5 (continued)

DVD Rank	Show	Release date	Rating A18-49 Live + SD	Genre
16	Merlin S3	01/17/12	0.5	Drama
17	The Walking Dead S1	03/08/11	3.5	Drama
18	Homeland S1	N/A	0.7	Drama
18	The Borgias S1	12/27/11	0.2	Drama
19	Sherlock S1	11/09/10	N/A	Drama
20	Shameless S1	12/27/11	0.7	Drama

Note. For the broadcast shows (except PBS) the ratings correspond to the average of the 2010-11 season. For cable shows and PBS, ratings are the latest available as to January 2012. The letter "S" followed by a number indicates the corresponding season of the DVD box. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. N/A= information not available. Source: Amazon.com

In the previous section of this chapter, we discussed how the genre of a show is a determining factor in the syndication market. The same applies to the home video market only that in this sector drama is the predominant genre, furthermore serialized drama. As it can be observed in Table 4.5, there are only three comedies: *Modern Family, Archer* and *The Big Bang Theory* (four different seasons). On the other hand there are 15 dramas (there is a tie in position 18), most of them heavily serialized. *Justified* and *Smallville* have procedural storylines to some extent, however they have predominant serialized arcs per season. The rest of the dramas are without a doubt serialized.

Another common trend of the shows in Table 4.5 is that most of them air on cable. Two of the comedies, *Modern Family* and *The Big Bang Theory,* are broadcast shows airing on ABC and CBS respectively. However on the drama side, broadcast networks are underrepresented. Ten out of the 15 dramas included in the table air on cable and the remaining five air on PBS and The CW; a public broadcaster and a low rated national broadcast network. None of the dramas of the Big Four made it to the best selling lists. We can also see that the comedies are amongst the top rated shows; however, the dramas have relatively low ratings in comparison with the exception of *The Walking Dead.*

The novelty factor definitely plays a role. Most of the shows, with the exception of older seasons of *The Big Bang Theory* and *Sherlock,* were released during 2011 and 2012.

Nevertheless, many other titles such as *Law & Order, The Simpsons, Jersey Shore* and *The Game* were also released one or two months prior to the measuring period of this study and never made it to the top selling lists. This indicates that novelty, while important, is not the only determinant factor. The same trends seem to apply to the Blu-ray discs as it can be observed in Table 4.6.

Table 4.6
Amazon's Top 5 Bestselling Blu-ray Discs

	Show	Release date	Rating A 18-49 Live + SD	Genre
1	Masterpiece Classic: Downton Abbey S2	02/07/12	2.7	Drama
2	Justified S2	01/03/12	0.9	Drama
3	Boardwalk Empire S1	01/10/12	1.3	Drama
4	Game of Thrones S1	03/06/12	1.4	Drama
5	Archer S2	12/27/11	0.6	Drama

Note. Ratings correspond to the last available data as to January 2012. The letter "S" followed by a number indicates the corresponding season of the DVD box. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. Source: Amazon.com

The entire list of Table 4.6 is comprised of dramas except for *Archer*. There is only one broadcast show (*Downton Abbey* on PBS) and all the shows on the list are serialized.

DVR Playback and Programming Decisions

In this section, the researcher observed the 2010-11 broadcast season to determine the influence of the DVR in viewing habits and programming decisions. Table 4.7 summarizes the 25 shows with the largest gain in ratings when DVR playback for an entire week was included.

Table 4.7
DVR Effect on Ratings

Show	A18-49 Live+SD rating	Ratings increase after 7 days DVR playback	Genre
Fringe	1.6	56%	Drama
Chase	0.6	50%	Drama
Good Guys	0.7	43%	Drama
The Event	1.7	41%	Drama
Supernatural	1	40%	Drama
Outlaw	0.5	40%	Drama

Table 4.7 (continued)

Show	A18-49 Live+SD rating	Ratings increase after 7 days DVR playback	Genre
Modern Family	4.5	38%	Comedy
Hawaii Five-0	2.9	38%	Drama
Parenthood	2.1	38%	Drama
Friday Night Lights	0.8	38%	Drama
Happy Endings	1.4	36%	Comedy
The Vampire Diaries	1.4	36%	Drama
The Office	3.7	35%	Comedy
Grey's Anatomy	4.1	34%	Drama
The Mentalist	2.9	34%	Drama
House	3.6	33%	Drama
Private Practice	2.7	33%	Drama
Blue Bloods	1.8	33%	Drama
90210	0.9	33%	Drama
Gossip Girl	0.9	33%	Drama
The Good Wife	2.2	32%	Drama
V	1.9	32%	Drama
Lie To Me	1.9	32%	Drama
Law And Order:SVU	2.6	31%	Drama
America's Next Top Model	1.3	31%	Reality

Note. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback.
Source: TV by the numbers

First, the researcher observed the list to determine which genres are more likely to be recorded for later playback. Table 4.7 includes 21 dramas, three comedies and only one reality show. The data suggest viewers are more inclined to record dramas; however, contrary to what it may be expected there is no clear preference for serialized dramas over procedurals.

The next topic of concern was whether or not the DVR ratings could have an impact on programming decisions. To determine how much the DVR can affect the rankings of shows, the researcher compared the top 10 shows classified by Live + SD ratings with the top 10 shows classified by Live+7 ratings for the 2010-11 season.

Table 4.8
Top 10 Rated shows Classified by Live + SD and Live +7 Ratings

	Top 10 rated shows A18-49 Live + SD			Top 10 rated shows A18-49 Live + 7		
Rank	Show	Live + SD Rating	7 day DVR gain (%)	Show	Live + 7 Rating	7 day DVR gain (%)
1	American Idol (Wed)	8	11%	American Idol (Wed)	8.9	11%
2	American Idol (Thu)	6.9	12%	American Idol (Thu)	7.7	12%
3	The Voice	4.9	18%	Modern Family	6.2	38%
4	Modern Family	4.5	38%	The Voice	5.8	18%
5	Two and a Half Men	4.5	20%	Glee	5.6	27%
6	Dancing with the Stars	4.5	7%	Grey's Anatomy	5.5	34%
7	Glee	4.4	27%	Two and a Half Men	5.4	20%
8	Grey's Anatomy	4.1	34%	The Big Bang Theory	5.1	28%
9	The Big Bang Theory	4	28%	The Office	5	35%
10	NCIS	4	23%	NCIS	4.9	23%

Note. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. Live + 7 ratings include one week of DVR playback. Source TV by the numbers

As we can the lists in Table 4.8 are virtually equal. There is only one show that differs from one table to another. In the top 10 Live + SD list, *Dancing With the Stars* is included while *The Office* appears in top 10 Live + 7 list, mainly due to the 35% of DVR playback gain. Although there is a minor alteration to the shows' rankings, it is safe to say that DVR playback does not completely alter the order of the top rated shows. The researcher repeated the process for the lowest rated shows where no significant differences were observed either, confirming that the DVR does not have a profound effect on the ranking of the shows.

In addition, the researcher observed each network's renewal/cancellation decisions to determine if DVR playback may have played a role. Upon observing the statistics of all networks, most results were straight forward. The lowest rated shows (Live + SD) of each genre were cancelled and the top rated shows were renewed. CBS and FOX had a couple of examples where shows with lower Live + SD ratings, but higher Live + 7 ratings were renewed. Those examples are presented in Table 4.9.

Table 4.9
Renewal/Cancellation Decisions at CBS and FOX

Shows	Status after 2010-11 Season	A18-49 Live+SD (rating	A18-49 Live+7 (rating)	Ratings increase after 7 days DVR playback
		CBS		
The Defenders	CANCELLED	1.9	2.3	21%
Blue Bloods	RENEWED	1.8	2.4	33%
		FOX		
Lie To Me	CANCELLED	1.9	2.5	32%
The Chicago Code	CANCELLED	1.9	2.4	26%
Human Target	CANCELLED	1.8	2.3	28%
Fringe	RENEWED	1.6	2.5	56%

Note. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. Live + 7 ratings include one week of DVR playback. Source TV by the numbers

The CBS drama *Blue Bloods* was renewed over *The Defenders* even though the former had higher Live + SD ratings. When DVR playback was included *Blue Bloods* had higher Live + 7 ratings than *The Defenders.* Also to be taken into account, *Blue bloods* aired on Friday nights which is considered one of the hardest nights to program and lower ratings are expected. Over at FOX, *Fringe* was renewed while three other higher rated shows (*Lie to Me, The Chicago Code* and *Human Target)* were cancelled. *Fringe's* ratings dramatically improved when DVR playback for an entire week was included. It could be argued that the DVR played an important part in the decision to renew *Fringe*; however other considerations are in order. *Fringe,* as *Blue Bloods,* aired on Friday nights. In addition, *Fringe* was on its third season and it is very likely that the production studio (Warner) granted many concessions to FOX in order to get a fourth season and reach enough episodes for syndication.

Programming executives have expressed on many occasions that they pay attention to DVR ratings (at least internally); nevertheless, the data analyzed reveals that the DVR has little to no influence on programming decisions.

Online Revenue Analysis

In this final section, the researcher studied the potential of online windows as another alternative source of revenue. As was previously mentioned, content owners may benefit from online advertising revenue as well as the more substantial license fees paid by video delivery platforms. Therefore the analysis was subdivided in three parts: advertising revenue, revenue from license fees and paid downloads.

Online Advertising Revenue. So far, online advertising revenue has been insignificant when compared with traditional advertising revenue as it can be seen in Table 4.10.

Table 4.10
Broadcast Stations Advertising Revenue

Revenue	2006	2007	2008	2009	2010	2011
Traditional ad revenue	23,575	21,576	21,062	16,337	18,672	18,030
Online ad revenue	587	776	904	949	1,087	1,233
Online/Traditional	2%	4%	4%	6%	6%	7%

Note. All numbers are expressed in $mil., except for the %. Source SNL Kagan

Online ad revenue does not even amount to 10% of total advertising revenue for television stations. Nevertheless the data presented in this section shows a clear ascending trend that is bound to be intensified in the future. Online advertising revenue may only be a small part of the total advertising income at the moment; but, as this percentage grows, media companies will need to pay more attention to it. The implications are further discussed on Chapter Five.

License Fees. The second form of online revenue for content owners comes from license fees. Video platforms pay content owners for the exclusive or non-exclusive rights to stream their TV shows. As it was stated in the literature review the predominant subscription platforms in the market are Netflix, Amazon Prime and Hulu Plus.

To understand the scale of the content agreements between video platforms and content owners, the researcher analyzed Netflix's operating summary. Figure 4.1 illustrates the company's content acquisition expenses from 2006-10.

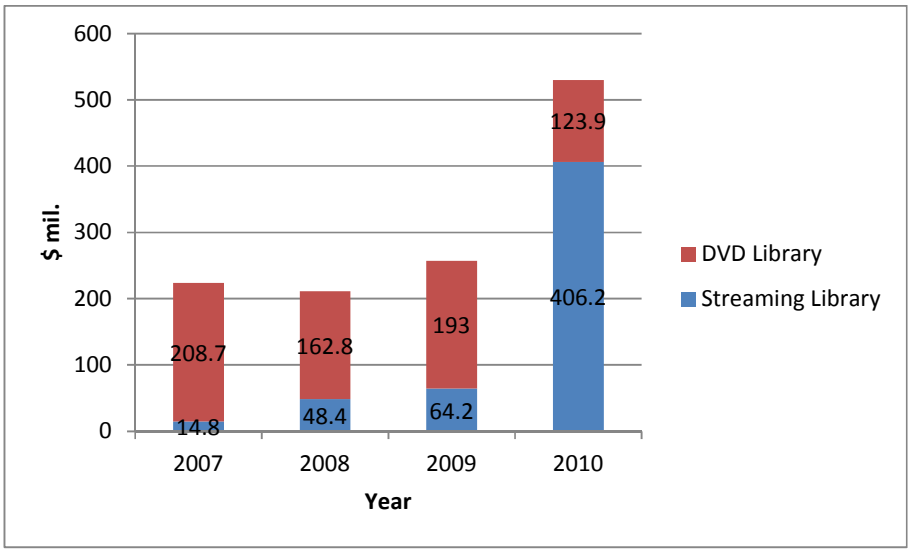

Figure 4.1
Netflix content acquisition expenses. Source SNL Kagan

Two trends are evident by observing Figure 4.1. First, content acquisition expenses have doubled from 2009 to 2010. Second, the company is reducing investments for the DVD library in favor of acquiring more streaming content. In 2010 the company spent more than $406 million on streaming content. This number includes movies as well as television shows. Netflix may be more identified with movies, however as it was reported earlier this year 60% of Netflix streaming corresponds to TV shows.

Streaming content agreements are usually not negotiated on a show by show basis. Most deals are negotiated in bundles. In Table 4.11 we present some selected examples of Netflix deals for streaming television content over the past couple of years:

Table 4.11
Selected Netflix deals

Date of the deal	Distributor	Shows	Terms	Total $ 000,000
12/08/10	ABC/ABC Family/Disney Channel	Grey's Anatomy, Brothers & Sisters, Ugly Betty, Lost	$175 mil./year for a period of 1 Year	175
02/21/11	CBS	Medium, Flashpoint, The Twilight Zone, Star Trek, Family Ties, Twin Peaks, Cheers and Frasier.	100 mil./year for a period of 2 years	200
03/18/11	Media Rights Capital	House of Cards (original)	$3.84 mil./episode for 26 episodes over 2 years	100
04/05/11	LionsGate	Mad Men	$ 1 mil./episode for 91 episodes over 5 years	91
10/03/11	Rubican TV AS	Lilyhammer (original)	$ 1 mil./episode for 16 episodes over 2 years	16
10/13/11	CW	Ringer, Hart of Dixie, One Tree Hill	$ 250 mil./ year for a period of 4 years	1000
11/18/11	Twentieth Century Fox TV/Imagine TV	Arrested Development (new)	$ 3.2 mil./episode for 10 episodes over 1 year	32

Note. Source SNL Kagan

As we can see, Netflix will pay between $1 to $3 million per episode for original content (*House of Cards*, new episodes of *Arrested Development* and *Lilyhammer*); and around $1 million per episode for the exclusive first run syndication of *Mad Men*. The other deals mentioned above include bundles of shows (old and new) and it is hard to determine the revenue each show can generate. For instance; the agreement with The CW included around 700 hours of TV content and each show was valued between $150,000 and $700,000 per episode depending on the popularity (Di Grazia, 2011).

Unfortunately, other subscription platforms like Hulu Plus and Amazon Prime do not disclose financial information. Regardless, the researcher was able to observe that online distribution is a very profitable window. Even a show that is already airing in regular

syndication can generate over half a million dollars per episode via online platforms. Shows that are syndicated directly to online windows can aspire to even higher amounts. This situation may change the fate of certain type of shows that were not successful in traditional syndication windows as it will be discussed on Chapter Five.

Paid Downloads. Finally, online windows can also generate revenue via paid downloads in services such as iTunes and Amazon Instant Video. Table 4.12 shows an estimate of the revenue from iTunes downloads for the year 2010.

Table 4.12
Estimated iTunes Revenue Split for 2010

Total TV downloads	Total revenue	Content owner revenue
450,000,000	*$ 895,500,000*	$ 626,850,000

Note. Average price per download = $1.99. Content owner split 70%.
Source SNL Kagan

From Table 4.12 we can see that even though the price per download is very low, with a large volume of downloads the total revenue can be quite significant. Content owners can expect their shows to generate significant revenue depending on their popularity. To observe which shows are the most popular, the researcher compiled a table of top iTunes and Amazon Instant Video downloads (Table 4.13 and Table 4.14):

Table 4.13
Top Amazon Instant Video TV Downloads

Rank	Show	A 18-49 Live +SD	Genre	Status	Network
1	Downton Abbey	2.7	Drama	Airing	PBS
2	The Vampire Diaries	1.4	Drama	Airing	CW
3	The Real Housewives of Atlanta	2.1	Reality	Airing	Bravo
4	Top Chef	0.9	Reality	Airing	Bravo
5	Fringe	1.6	Drama	Airing	FOX
6	Justified	0.9	Drama	Airing	FX
7	The Walking Dead	3.5	Drama	Hiatus	AMC
8	White Collar	1.1	Drama	Airing	USA
9	Once Upon a Time[a]	3.5	Drama	Airing	ABC
10	The Big Bang Theory	4.0	Comedy	Airing	CBS

Table 4.13 (continued)

Rank	Show	A 18-49 Live +SD	Genre	Status	Network
11	Archer	0.6	Comedy	Airing	FX
12	Gossip Girl	0.9	Drama	Airing	CW
13	Glee	4.4	Comedy	Airing	FOX
14	The Good Wife	2.2	Drama	Airing	CBS
15	Leverage	0.8	Drama	Airing	TNT
16	Supernatural	1.0	Drama	Airing	CW
16	Castle	2.7	Drama	Airing	ABC
17	House	3.6	Drama	Airing	FOX
18	Grey's Anatomy	4.1	Drama	Airing	ABC
19	Grimm[a]	1.8	Drama	Airing	NBC
20	Pan Am[a]	1.2	Drama	Airing	ABC
20	The Secret Circle[a]	0.7	Drama	Airing	CW

Note. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. Ratings for broadcast (except PBS) recurring shows correspond to the 2010-11 season average. Ratings for new shows, cable shows and PBS correspond to the latest rating data as to February 5th, 2012. Source: Amazon.com and TV by the numbers.
[a] New shows (premiered in the 2011-12 season)

Table 4.14
Top iTunes TV Downloads

Rank	Show	A 18-49 Live +SD	Genre	Status	Network
1	Downton Abbey	2.7	Drama	Airing	PBS
2	Kourtney & Kim Take New York	2.6	Reality	Airing	E!
3	The Real Housewives of Atlanta	2.1	Reality	Airing	Bravo
4	Gossip Girl	0.9	Drama	Airing	CW
5	Pan Am [a]	1.2	Drama	Airing	ABC
6	Alcatraz [a]	2.8	Drama	Airing	FOX
7	Once Upon a Time [a]	3.5	Drama	Airing	ABC
8	The Vampire Diaries	1.4	Drama	Airing	CW
9	Glee	4.4	Comedy	Airing	FOX
10	Grey's Anatomy	4.1	Drama	Airing	ABC
11	Jersey Shore	3.2	Reality	Airing	MTV
12	Modern Family	4.5	Comedy	Airing	ABC
13	Hart of Dixie	0.6	Drama	Airing	CW
14	The Good Wife	2.2	Drama	Airing	CBS
15	Family Guy	3.6	Comedy	Airing	FOX
15	Pretty Little Liars	0.9	Drama	Airing	ABC Family
16	White Collar	1.1	Drama	Airing	USA
17	90210	0.9	Drama	Airing	CW
18	The Big Bang Theory	4.0	Comedy	Airing	CBS
19	The Real Housewives of Beverly Hills	1.4	Reality	Airing	Bravo

Table 4.14 (continued)

20	30 Rock	2.3	Comedy	Airing	NBC
20	Fringe	1.6	Drama	Airing	FOX
20	Revenge [a]	2.5	Drama	Airing	ABC

Note. A18-49= adults 18-49 years old. Live + SD= Live ratings + same day playback. Ratings for broadcast (except PBS) recurring shows correspond to the 2010-11 season average. Ratings for new shows, cable shows and PBS correspond to the latest rating data as to February 5th, 2012. Source: iTunes and TV by the numbers.
[a] New shows (premiered in the 2011-12 season).

Table 4.13 and 4.14 are very similar with at least 60% of the titles appearing on both. The first evident trend is that users download shows that are airing at that moment. The only exception is *The Walking Dead* which was on hiatus during the measuring period. Similarly to the home video market, dramas seem to be more popular in the paid download segment. Most of the titles in Table 4.13 and 4.14 are dramas, with a few comedies thrown into the mix. Nevertheless, a unique characteristic of online downloads is that for the first time in this analysis the reality genre makes an appearance in the top ranks.

Unlike in the home video market, broadcast networks seem to be better represented in the paid download sector. Around 70% of the titles in Table 4.13 and 4.14 air on broadcast networks. ABC, The CW and FOX have the most titles with CBS, NBC and PBS falling behind. Regarding the ratings, most shows that are on the top download lists have above average performance (with the exception of The CW shows). The shows that air on cable networks have lower ratings; however they are among the best performers of their respective channels.

The results presented in this chapter take us closer to understand the economic performance of TV shows across several windows. As we were able to see, TV shows have different performances in each window. With the analysis of advertising revenue, the researcher took a numerical approach to the much discussed subject. In addition, other revenue windows were explored. We were able to understand why comedies are so coveted in the syndication market, while dramas are the most popular genre in the home video

segment. Also, the analysis suggested that the DVR is not a determining factor for programming decisions. Finally we were able to observe the increasing potential of online platforms as revenue generating windows. The implications of these findings will be discussed further in the following chapter of this study.

Chapter Five : Discussion

The landscape of media has changed radically in the last couple of decades. Television shows have become commodities that can be traded across many platforms. Advertising is one type of revenue TV shows can generate, however they can also be profitable in the syndication market, home video and more recently online video platforms. In order to keep up with these developments, industry professionals need to adjust the way they determine which shows have the biggest potential.

Certain shows are considered hits during their original broadcast. Hit shows generate high advertising revenue; however, they may not have the same success in other windows. Maximizing the advertising revenue is no longer enough to maximize the overall result of vertically integrated companies. Other revenue windows such as syndication, home video and online distribution have the potential to match or exceed the revenue generated by advertising. Consequently, maximizing the revenue of television companies depends on identifying what shows can be successful in each window and which shows can achieve the maximum overall performance. This analysis will bring us one step closer to understanding how to maximize profit across windows in media conglomerates.

The advertising revenue analysis of this study had the objective of finding internal and external economic variables that influence the broadcast CPM rates. The econometric model revealed that there is no significant relationship between the average broadcast CPM rates and average cable CPMs. However, the results indicated that broadcast CPMs are partially determined by the following variables: ratings, total advertising spending, gross broadcast advertising revenue and GDP. The correlation coefficient is 0.68, which suggests that 68% of the variation on broadcast CPMs can be attributed to the variables included in the model. The results of the econometric analysis are summarized in the following equation:

Broadcast CPM= 0.71 - 0.68*Ratings - 4.83e-005*Total Ad Spending + 0.00054*Gross Broadcast Ad revenue + 26.61*GDP[4]

This equation shows that broadcast CPMs are directly correlated to the broadcast ad revenue and GDP. Also, the model indicates that broadcast CPMs are negatively correlated to the broadcast ratings. Total ad spending is also negatively correlated to the broadcast CPMs.

It was expected that CPMs would be directly correlated to the gross ad revenue. When demand for advertising spots is high, networks are able to increase their price (CPMs). More indirectly, variations in the GDP also have an impact on CPMs. When there is an economic downturn, many companies tend to cut their marketing budget which results in less demand for TV advertising and networks are forced to lower their CPMs.

Supporting what was reviewed in the literature research, ratings and CPMs move on opposite directions. As rating points become scarcer, there is a shortage of audience supply which drives the price of each rating point higher. The negative coefficient in the equation supports this hypothesis.

Finally, there is a negative correlation between broadcast CPMs and total ad spending. In the time period of the sample (1994-2010), especially in the last couple of years, the advertising market has changed because of the introduction of new media windows. Before the introduction of the internet, advertisers divided their marketing budgets between traditional windows. Nowadays, advertisers have the option of spending online instead of paying for more TV spots. Online advertising presents many advantages: it is less expensive, it can be easily measured and it has great potential for targeted ads. Many advertisers are cutting down their TV spending in favor of online ads and as a consequence,

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[4] Total advertising spending and Gross broadcast ad revenue are expressed in constant 2000 million USD, Real GDP is expressed as % growth with base year 2000. Broadcast CPM is expressed in constant 2000 USD

even if total ad spending increases, TV spending may decrease pushing the CPM prices down.

Besides advertising, syndication is another highly profitable window. In some cases, syndication can even exceed the advertising revenue. The analysis revealed that syndication revenue is not correlated to the advertising revenue. Moreover, the ratings during the original broadcast do not have a direct impact on the syndication fee per episode. The number of episodes is an important factor; shows that have less than 80 episodes are very rarely sold for syndication. Notwithstanding, once the shows have reached a syndicatable level, additional episodes do not mean additional syndication fees per episode. The researcher also failed to find a relationship between the ownership of the shows and the syndication revenue.

According to the analysis, the only element that had a clear influence over the syndication fees was the genre. Half-hour sitcoms had the highest syndication fees of the sample and their total syndicated revenue, in most cases, nearly duplicated the advertising revenue. Following comedies, procedural dramas also had moderate success in the syndication market (although the syndication revenue was usually lower than the advertising revenue). Serialized dramas, regardless of their popularity, usually struggle to reach profitable syndication deals. Even if they are sold in syndication, usually the fee per episode is lower than what they used to generate with advertising. Finally, the worst performing genre in syndication was reality.

The results evidently indicate that the syndication market favors comedies. In this context, networks are under a lot of pressure to produce hit comedies. However, very few of the comedies that are premiered each year become hits. Therefore, the question for programmers is whether it is better to keep mediocre comedies on the schedule with the hopes of profiting in the syndication market, or if they should favor other genres that have immediate advertising revenue but no significant after life. In this context, the extreme

genres are sitcoms and reality shows, with procedural and serialized dramas falling somewhere in between. Determining the optimal mix of shows requires a detailed analysis of the revenue across windows. A financial analysis of that scale requires information that is not entirely available to the public. Nonetheless, what the researcher was able to confirm in this study was that the most successful shows in the syndication market are not always the ones that bring more advertising dollars. To further complicate the picture, the following sections of the analysis will also reveal that the shows that perform well on syndication do not necessarily perform well on other windows like home video and online video delivery.

The sample analyzed revealed that serialized dramas are the preferred genre in the home video market. Only very popular comedies are in the top seller lists. On the other hand, there are several more obscure dramas that are among the bestselling titles. Also, cable dramas perform much better in the home video market than their broadcast counterparts. The only broadcast dramas in the top selling lists belonged to PBS and The CW and not to any of The Big Four.

The syndication market has a big demand for half hour comedies because they are easy to program: they strip well on weekdays and people enjoy watching lighthearted entertainment during the day. Serialized dramas, on the other hand, require a certain amount of engagement by the viewer and must be shown in sequence. Missing an episode can harm the viewing experience and for this reason they are traditionally not very desirable in the syndication market. In the home video market the exact opposite occurs. The analysis indicates that dramas, more specifically serialized dramas, generate a level of engagement in viewers that is stronger than the one generated by comedies. This situation is reflected in the stronger DVD and Blu-ray disc sales for serialized dramas.

It could also be argued that many of the top selling home video titles fall under the category of cult hits. Serialized dramas generally fit the description of cult hits, especially the fantasy/sci-fi shows such as *Smallville, Game of Thrones* and *The Walking Dead.* On the

other hand *The Big Bang Theory* is popular among a broad audience; however some of its fans are highly devoted much like the fans of the cult hits mentioned before. Period dramas like *Boardwalk Empire, Downton Abbey* and *The Borgias* also enjoy a cult following and are very popular in the home video market.

In this context it makes perfect sense that the top selling home video lists are dominated by cable shows. Cable shows are narrowly targeted, bolder and more complex than broadcast shows. As a consequence, cable shows can easily become cult-hits. The Big Four are the complete opposite: they air shows that can attract the largest possible audiences. Smaller broadcast channels like The CW are more targeted to a specific niche, probably the reason why many of its shows are also popular in the home video market.

These cult-hits (with the exception of the comedies) are not rating stars and do not perform well in syndication, but they dominate the home video market. Once again there is the question of balancing revenue streams. Is it worth developing and producing cult hit shows? Is it worth sacrificing advertising revenue in favor of home video sales? It depends on how big the potential home video revenue is and exactly how much ad revenue needs to be sacrificed. It could also be argued that most of these cult hit shows are only sustainable when they air on cable or public broadcasters that do not depend on advertising revenue. Proving the validity of the previous statement goes beyond the scope of this study.

Advertising and the subsequent syndication and home video were the traditional windows that generated revenue for TV shows. New media technologies have added complexity to the value chain. In addition to traditional measurement of ratings, the introduction of the DVR has provided yet another data set. There is a lot of speculation on the importance of Live + 7 ratings. Network executives claim they consider DVR ratings, while advertisers deem them irrelevant. Through analysis of DVR playback data, the researcher observed the impact of the DVR on programming decisions.

After comparing the Live + SD and the Live + 7 ratings, the researcher was able to observe that there is no direct link between DVR ratings and programming decisions. First, the ranking of the shows was not significantly altered by including DVR ratings data. In other words, the top rated Live + SD shows also had the highest Live + 7 ratings. In addition, except for some isolated examples, there was not enough evidence to indicate programmers take into account Live + 7 ratings when making their renewal/cancellation decisions.

Advertisers are only concerned with the live audience and have little interest in Live + 7 ratings. Shows that present big DVR audience gains can hardly claim more viewers are exposed to the commercials since most people skip ads during playback. What DVR ratings could indicate is the level of engagement viewers have with a particular show. This level of engagement may not generate advertising dollars, however it could translate to higher revenue on other windows like the home video market and online video downloads. Nevertheless, until there is a clear link between the DVR ratings and potential revenue on other windows, DVR ratings alone will not be enough to save underperforming shows.

In addition to the DVR, online windows have also had an impact on the television industry. Over the past few years, online video platforms have increased their investments on streaming content. Platforms like Netflix negotiate bundle agreements with distributors for the rights to stream episodes of old and current TV shows. A current show can cost between $150 and $700 thousand per episode. In addition to streaming re-runs a new model has emerged: first-run-direct-to-streaming syndication. The first deal of this kind was *Mad Men* which was sold to Netflix for an estimated $1 million per episode. Furthermore, original content that premieres online can cost $1-$3 million per episode.

Besides subscription platforms like Netflix, online windows also generate revenue via paid downloads. Apple's iTunes is one of the most important players in the paid download market. Content owners receive roughly 70% of the revenue totaling over $6 million per year. Popular shows (from all genres but mainly drama) are usually among the

top downloaded shows. Some of the most downloaded shows also include lower rated cable shows (*Archer)*, sci-fi shows *(Fringe)*, imported shows *(Downton Abbey)* and shows popular among younger viewers (*The Vampire Diaries, Gossip Girl).*

In previous sections we have discussed how traditional windows have experienced inconsistent revenue. Advertising is often volatile and moves in cycles along with the rest of the economy, syndication can prove to be difficult for some type of shows and home video formats are slowly decreasing in popularity. However, everything indicates that online platforms are growing and will increase license fee revenue for content owners in the near future. It is very likely that diminishing returns in some of the traditional windows could be upset by the profit potential of online platforms.

Online video platforms are taking measures to become more independent from content owners, introducing original series among their offerings. As original streaming content gains popularity, the profitability of content owners may be threatened. Nevertheless, it is unlikely that online original content could exceed the popularity of broadcast shows. It is more feasible that online shows will slowly build a fan-base and potentially become cult-hits.

Limitations

Because of limitations in the data availability, the researcher used only 17 observations (reduced to 16 observations after taking the first difference) to build the econometric model. Econometric models are much more reliable when they are built using larger samples (20 or more observations). The limited number of observations could have produced inaccurate results or overstated some of the correlations. In addition, the multicolinearity present in the model was ignored since it did not reach the necessary level to be considered “serious”. However, the fact that there was multicolinearity present in the model could have also distorted or overstated some of the results.

The top selling DVDs and top selling Blu-ray discs lists were built based on an observation that took place over a month. Since the measurement period was short, it is possible that some titles were ignored and some of the conclusions drawn were not completely accurate. In a similar way, top downloaded lists were built over an observation period of a month. Top downloads usually include shows that are airing at the moment. Given that the observation was limited to a month, many shows that only air on other seasons (summer cable shows e.g.) did not have the opportunity to appear in the top downloaded lists. As a consequence some features of the top downloaded shows could have been overlooked by the researcher.

The initial objective of this study was to build a financial valuation model of a TV show that included the different sources of revenue and costs. The researcher was able to infer which genres are better performers in each window; however, it was not possible to quantify the performance of the shows in all windows since financial details of home video sales and online distribution deals were not available.

Recommendations for Future Research

For researchers that want to build a similar econometric model of the TV advertising market, it would be recommended to work with a larger number of observations. It would also be advisable to work with one day part (primetime e.g.) and more specific demographic groups (adults 18-49 instead of households).

In order to achieve a better understanding of the top performing shows in the home video market and paid download platforms it would be advisable to extend the measuring period. Instead of monitoring the top lists for a month, researchers could repeat the process four or three times a year, during sweep months for example.

Finally, this study would be more comprehensive if financial data from all windows was available for each TV show. If more financial information could be obtained, future researchers could build a historical cash flow and even perform a discounted cash flow

analysis comparing and contrasting shows from different genres to observe which one generates the higher net present value.

Conclusions

Regardless of the limitations, the present study has shed light into some of the many issues that surround the current state of the television industry. The major findings are summarized below:

The advertising industry will not be transformed overnight

While it is true that the advertising industry has experienced several changes over the past few years, it is unlikely that the prevailing model will disappear. A lot has been written about the main threats to broadcasters' advertising revenue, including: cable channels, online platforms and the DVR. Cable channels have gained importance in the past few years; nevertheless they will always be more targeted outlets that seek to attract niche markets unlike broadcasters that appeal to a broader audience. Broadcasters compensated the decrease in viewership by increasing their CPMs which has prevented the advertising revenue from falling to far. This analysis revealed that there is no direct link between cable's CPMs and broadcasters CPMs. The data suggested that broadcast CPMs are a function of other variables, mainly the general state of the economy and overall ratings. Online advertising has also been up for debate as a substitute for traditional TV advertising. Online ads are on the rise and the data analyzed indicates that some companies may be moving some of their advertising budget to the internet. However, at the moment, online advertising is still a very small part of the advertisers' budget. It is possible that this window will gain more importance in the future, but it will not happen overnight. Meanwhile, advertisers will continue to spend large amounts of money on television spots. Finally, the study indicated that the DVR has very little influence in the state of television. No evidence was found to support the claim that DVR ratings play a part in programming decisions. In

other words, programmers still focus primarily on live ratings which are the preferred currency in dealing with advertisers.

The most successful genre

This study analyzed several distribution windows with an eye on which shows perform better in each of them. It was revealed that the performance of shows is not consistent across windows. Success during the original broadcast depends entirely on ratings. Hit shows can emerge from any genre, the latest examples include: reality shows (*American Idol),* comedies (*The Big Bang Theory)* and Dramas (*Grey's Anatomy).* It was also evident that the syndication market favors comedies, while serialized dramas perform better in the home video market. Likewise, online windows favor dramas, but also young skewing shows, foreign imports and hit comedies.

In this sense, it is hard to determine which genre is the most profitable. If content owners were to select one type of show to have in their line-ups it would have to be a hit comedy. A comedy that has high ratings will obviously generate high advertising revenue. Additionally, in the syndication market, comedies are coveted regardless of ratings. Hit comedies can generate the highest syndication fees recorded (even in the second run syndication). Home video does not favor comedies in general; however, hit sitcoms (*The Big Bang Theory, Modern Family)* appear in the top selling lists. Finally hit comedies are also among the most downloaded shows on platforms like iTunes. Comedies with lower ratings were not as lucky, and none of the other genres were among the top performers in all windows. Hit comedies are not easy to come by, but one true hit has the potential to generate more money across windows than any other genre.

Online windows may change how future generations experience TV

As mentioned, online advertising is still far from reaching the level of traditional TV advertising. However, stealing away ad dollars from broadcasters is not the only way online video platforms are threatening to change the television industry.

The most prominent video platforms are starting to offer original content. This strategy is more about attracting subscribers than competing directly with the major networks. Original series may gradually gain popularity and perhaps even become hits in the future. But probably their most important contribution will be to offer an alternative to the linear experience of TV. On February 2012, Netflix premiered its first original series *Lilyhammer.* The entire first season, consisting of eight episodes, was posted on the same day. Instead of waiting a week for new episodes users had the option of watching the entire first season on one day. This type of delivery is consistent with the streaming video culture, where users are accustomed to watch many episodes in a row. As they become more common, these distribution strategies may have a profound impact on how future generations experience television.

Simultaneous episode releases may also be the way to go for certain genres that traditionally did not perform well in syndication. Direct to streaming syndication for serialized shows could be the ideal window as they would not be bound by linear programming and their cult following could enjoy several episodes in one sitting. Other genres that are enjoying popularity in the streaming services are young skewing shows and foreign series. Young viewers may be the most open to online platforms. They are not limited by pre-conceptions of linear TV and they are much more willing to consume television in new ways. Many of the streaming websites have been acquiring content that appeals to young viewers like shows from The CW and ABC Family. Another trend of online streaming is foreign imports. Popular shows include *Downton Abbey, Dr. Who, Sherlock* and *Merlin;* all of them originally aired on broadcast or cable networks. However, the amount of foreign shows that air in the U.S. is limited. Perhaps online platforms could become first-run windows for certain foreign shows. This was the case for *Endgame,* the Canadian import exclusively available to American viewers on Hulu.

The television industry is clearly evolving. A big part of this change is attributable to new media technologies. However, the introduction of online platforms and other new media technologies does not mean the death of traditional television. Rather, they complement traditional TV viewing providing a rounder experience and additional potential for profit. For the viewers, the plethora of distribution outlets gives them the opportunity of a richer and more diverse TV experience. From a financial point of view, the economic analysis has grown in complexity. One thing is certain; media professionals can no longer ignore the impact of alternative distribution windows and new technologies. The way in which TV shows are distributed is no longer set in stone. In the future, different shows may reach their maximum potential through different combinations of distribution outlets. Shows with broad appeal could continue to premiere on broadcast TV while potential cult hits could go directly to streaming services. The possibilities are endless as new generations begin to conceive TV under an entirely different light.

As a companion tool, the researcher included a fictional case study that summarizes the findings of this thesis. The case study can be found on Appendix B.

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Appendix A: Syndication Revenue

Table A1
Syndication Revenue for the 2006-07 Lineup

Show	Genre	# Episodes	etwork	Ownership	Network Ad revenue per episode 2006-07 ($ 000)	Syndication per episode ($ 000)	2006-2007 Share
The Office [a]	Comedy	150	NBC	I	1,980	2,400	8
Two and a Half Men [a]	Comedy	191	CBS	E	2,565	2,250	15
How I Met Your Mother[a]	Comedy	150	CBS	E	1,663	2,150	9
Family Guy [a]	Comedy	187	FOX	I	1,280	2,000	7
Law & Order: Criminal Intent	Drama	195	NBC	I	2,790	1,925	11
CSI: NY	Drama	173	CBS	I	3,420	1,900	17
CSI: Crime Scene Investigation	Drama	261	CBS	I	6,650	1,600	22
House	Drama	176	FOX	E	4,480	1,400	14
Law & Order: SVU [b]	Drama	283	NBC	I	3,600	1,300	15
CSI: Miami	Drama	226	CBS	I	5,035	1,225	19
Grey's Anatomy [b]	Drama	157	ABC	I	6,650	1,200	18
Criminal Minds [a]	Drama	148	CBS	I	2,660	825	13
30 Rock	Comedy	104	NBC	I	1,575	800	8
Crossing Jordan	Drama	117	NBC	I	1,440	800	11
ER	Drama	331	NBC	E	4,950	800	14
NCIS	Drama	199	CBS	I	2,565	750	15
Ghost Whisperer	Drama	107	CBS	I	1,995	700	12
My name is Earl	Comedy	96	NBC	E	1,890	600	9
Desperate Housewives	Drama	170	ABC	I	7,600	500	19
Gilmore Girls	Drama	154	CW	I	1,472	500	5
Everybody Hates Chris	Comedy	88	CW	I	680	450	4
Bones	Drama	134	FOX	I	2,080	450	8
Las Vegas	Drama	106	NBC	E	1,800	450	10
Smallville	Drama	217	CW	I	1,360	400	5
The New Adventures of Old Christine	Comedy	88	CBS	E	1,948	350	12
Heroes	Drama	79	NBC	I	3,060	300	10
Fear Factor	Reality	149	NBC	I	N/A	280	N/A
24	Drama	195	FOX	I	N/A	250	N/A

Table A1 (continued)

Wife Swap	Reality	123	ABC	I	1,805	250	9
Ugly Betty	Comedy	85	ABC	I	1,919	200	7
Lost	Drama	115	ABC	I	6,175	200	15
The O.C.	Drama	92	FOX	E	2,000	200	4
Boston Legal	Drama	101	ABC	E	2,660	175	11
One Tree Hill	Drama	175	CW	I	1,120	175	3
Cops [b]	Reality	153	FOX	I	1,008	100	7
America's next top model	Reality	213	CW	I	2,160	75	5
Survivor	Reality	357	CBS	I	5,605	65	16

Note. I= Owned by the same company that airs it. E=owned by a company different than the one that airs it. Source: SNL Kagan

[a] Syndication fee includes cable syndication and local syndication. [b] The show is available on local syndication but the local fee is not included in the total

Appendix B: Fictional Case Study

Modeling the Current State of TV

Background. It is the middle of February and John Scott, the chief programmer officer of UBC (one of the major television networks in his country), is pressured to make a programming decision by the end of the month. He needs to select a show that will replace a cancelled drama in the Tuesday 9:00 PM slot. After careful consideration he has narrowed down his choices to three shows:

- ***Triple Threat:*** A new reality show where contestants are asked to participate in singing, dancing and acting competition rounds. The winner of all rounds receives the "Triple threat" title.
- ***Single Talk:*** An hour long comedy about a single mom that has to balance her unconventional family life and her job as a TV personality.[5]
- ***G-Men:*** A cult following sci-fi show where two brothers that work for the FBI hunt vampires in a small town of Georgia during the prohibition era.

Single Talk and *G-Men* are currently on UBC's schedule, but unless they are picked for the Tuesday night spot they will be cancelled. John Scott is torn between these three shows. *Triple Threat* has great potential to become a hit. It is expected to produce at list a 4.0 rating ***(See Exhibit 1)***. However, the show is not owned by the company and aside from the advertising revenue, it would not produce any other income. On the contrary, *Single Talk* and *G-Men* are owned by UBC's parent company. Therefore, UBC has the rights for syndication, home video and online distribution of these two shows. *Single Talk* is currently airing its fifth season and will have a total of 110 episodes. *G-Men* is in its third year, coming up to 66 episodes by the end of the current season. The show has the potential to be sold in syndication, but not unless it gets a fourth season and totals 88 episodes. *Single Talk* is not as popular as other sitcoms but is has a steady audience. *G-Men* has been struggling with

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[5] For simplicity we are considering an hour-long comedy instead of two half-hour sitcoms.

ratings, however it has a very loyal following and performs extremely well in the home video market and paid downloads.

John Scott also needs to consider the costs of each alternative ***(See Exhibit 2).*** The production team of *G-Men* is very interested in getting a fourth season order and they have lowered their license fee for next year. On the other hand, after 5 years, the actors, producers and writers of *Single Talk* are renegotiating their contracts. Therefore the license fee for next year is expected to have a considerable increase. Finally, as most reality shows, *Triple Threat* has a lower license fee than any of the other shows.

The competition. UBC is one of four major television networks in the country. Currently it is ranked # 2 on overall ratings; however it is ranked # 4 on Tuesday nights. The other three networks: ABS, CBC and NBS have a mix of successful shows on Tuesdays, but they have started to show signs of aging and UBC wants to cease the opportunity. UBC programs only two hours of primetime per night, starting at 8 PM. On the 8 PM slot on Tuesday nights, UBC has scheduled *Cipher* one of its highest rated procedural shows about a computer genius that works with the CIA. The show is very popular and will provide a solid lead in. Now, John Scott needs to decide which show will follow *Cipher* on Tuesday nights.

In the same time-slot (Tuesday 9 PM), ABS and CBC air comedies. CBC's comedies are among the highest rated shows in the entire line-up. ABS's comedies are not as popular. NBS on the other hand has a reality show about extreme sports.

Syndication prospects. Since *Triple Threat* is not owned by UBC, they would not receive any of the syndication money. John Scott is not concerned about that since he knows reality shows cannot be sold at much profit in the syndication market. Once it finishes its fifth season, *Single Talk* will have 110 episodes, if they order a sixth season; this number will increase to 134. UBC has already pre-negotiated the syndication of the show for $800 thousand per episode. The first-run syndication agreement will be paid over two years with monthly amortizations starting the year after the next ***(See Exhibit 3).*** They also estimate

that the second cycle can generate at least 70% of the first cycle's revenue paid over two years. The amortization of the second cycle will start right after the first cycle is paid.

Currently, *G-Men* does not have enough episodes to be sold in syndication. An additional 22 episodes order will allow UBC to sell the show. The company estimates that the show could generate around $300 thousand per episode paid over two years starting the year after the show's last episode airs. Unfortunately, if UBC cancels the show after only three seasons, there will not be any syndication deal.

Home video projections. As content owners of *G-Men* and *Single Talk,* UBC would also benefit for the DVD and Blu-ray disc sales. Previous seasons of *Single Talk* have been released on DVD and Blu-ray, but they have not performed well. On the other hand, *G-Men* has constantly appeared in the top selling home video lists. If any of these shows is picked for one more season, their DVD and Blu-ray would be available the following year. Based on past seasons performance in the home video market, the UBC team was able to estimate the potential home video sales ***(See Exhibit 4).***

Online potential. In the past, UBC has sold many of their shows to the streaming service Quickflix. They have expressed interest in acquiring both *G-Men* and *Single Talk* ***(See Exhibit 5).*** Quickflix would start streaming episodes of the shows the year after the next and make a single payment for the total at that point. Quickflix believes that *G-Men* has many cult followers that are likely to subscribe to their service; for that reason they are willing to pay more for this show than for *Single Talk,* regardless of the ratings.

In addition, the new episodes of either show would be available for paid downloads at Nile Instant Video the day after the original airing. Each episode could be downloaded for $1.99, the content owner receives 70% of that income. UBC estimated the total number of downloads each show could generate during the next year if they were picked **up** ***(See Exhibit 5).***

The advertising industry. The advertising industry is recuperating after an underperforming year, consequence of the general economic downturn. However, the prospects for the following year are positive and it is estimated there will an increase in TV ad spots demand. John Scott has consulted with the network's sales department and they are positive spots for the Tuesday 9 PM slot can be sold at a rate of $27 per thousand viewers (27 CPM).

The company's options. With all this information, John Scott needs to pick one of the three shows to air on Tuesday nights at 9 PM. In addition to improving the ratings performance of Tuesday nights and maximizing the advertising revenue, John Scott also needs to consider the revenue of other divisions of UBC (syndication, home video, etc.).

Additional considerations.

- In addition to traditional advertising UBC can also profit from online advertising (around 6% of regular advertising) for any of the three shows.
- UBC would not have the digital distribution rights of *Triple Threat.* Therefore they wouldn't benefit from the paid downloads.
- The total adult 18-49 viewers are 130,000,000
- All syndication deals will be cash only (no barter)
- There are 19 ad spots per episode of any given show
- UBC's weighted cost of capital (WACC) is 10%

Exhibits

Exhibit 1. *Estimated Ratings in the 9 PM Time-slot*

Show	Live A18-49 rating	Live + 7 rating
Triple Threat	4.0	4.2
Single Talk	2.5	2.9
G-Men	1.6	2.6

Note. A18-49= adults 18-49 years old. Live + 7 ratings include one week of DVR playback.

Exhibit 2. *Production Costs*

Show	License fee per episode ($000)	No. of episodes next season
Triple Threat	700	22
Single Talk	1500	22
G-Men	1250	22

Exhibit 3. *Syndication Prospects*

Show	First-run Syndication fee per episode ($000)	Second-run syndication fee per episode ($000)
Triple Threat	-	-
Single Talk	800	560
G-Men	300	-

Exhibit 4. *Home Video Market Predictions*

Shows	Year 2	Year 3	Year 4	Year 5
	Units			
Single Talk S6	250,000	125,000	62,500	31,250
G-Men S4	700,000	420,000	252,000	151,200
	Revenue per unit ($) [a]			
Single Talk S6	15			
G-Men S4	20			

Note. The letter "S" followed by a number indicates the corresponding season of the DVD box.
[a] Profit for UBC after discounting manufacturing and distribution expenses.

Exhibit 5. *Online Predictions*

Streaming deal with Quickflix

Show	Fee per episode ($ 000)
Single Talk	300
G-Men	400

Nile Instant Video Predictions

Show	No. of downloads ($ 000,000)	Price per download ($)
Triple Threat	40	1.99
Single Talk	6	1.99
G-Men	10	1.99

Teaching note

Modeling the Current State of TV

Case Synopsis. John Scott is the chief programmer officer of UBC, one of four major television networks in his country. The other three dominant networks are ABS, CBC and NBS. Currently UBC is ranked #2 overall ratings but it has a weak spot in its line-up on Tuesdays at 9:00 PM. John Scott needs to select a show to schedule on that time-slot following their hit procedural Cipher, which airs Tuesdays at 8:00 PM. John has narrowed down his alternatives to three possible shows: a reality competition *Triple Threat,* comedy *Single Talk* and sci-fi cult hit *G-Men.*

Each show has advantages and disadvantages: *Triple Threat* has the potential to become a rating hit, but since it is not owned by UBC it will not produce any money in the aftermarkets. *Single Talk* does not have solid ratings or DVD/Blu-ray sales and it has become very costly; however it could be sold at a very high price in the syndication market. Finally *G-Men* has very low ratings but it performs extremely well in the home video market and it has generated interest from online platforms. This last show has potential in the syndication market, however it only has 66 episodes and unless it gets picked up for another season it is unlikely it will get a syndication deal. On the cost side, the cheapest show is *Triple Threat* while *Single Talk* has recently became very expensive to produce. The production team of *G-Men* is willing to cut the license fee, provided they get another season.

John needs to carefully examine the alternatives he has, balance the revenue vs. costs of each option and select the show that will benefit his company the most.

Course Usage. The case was designed to be used by students from the following majors: television management, media management, arts and entertainment management and other related subjects. The case is adequate for graduate or upper undergraduate students. Students should have prior understanding of the structure of the television industry and the business model of television networks. Students should also be aware of

the basics of media programming and have taken at least an introductory course in finance and accounting.

The case will allow media students to perform a formal business analysis in their field and to combine their media knowledge with the skills obtained in their business classes. Used in conjunction with additional readings, the case could also be suitable for business students who wish to learn about the television industry.

Learning Objectives. The objective of the case is to illustrate the complexities of the television industry and the difficult decisions network programmers need to make. The case should help students to develop a systematic approach to decision-making. While solving the case, students will have the opportunity to analyze and discuss the main revenue sources and costs of a TV show. In addition, the information provided will enable students to refine their financial analysis skills.

Suggested Readings. The case was written taking into account basic TV programming techniques detailed in:

- Eastman, Susan T., & Ferguson, Douglas A. "Media Programming Strategies and Practices". This book details the most common programming techniques and it also touches the syndication market economics.

In addition, the following SNL Kagan publications provide background information related to the case:

- "Economics of TV programming and syndication" (2007). This data book has information about advertising rates, syndication deals and license fees.
- "The State of Online Video Delivery" (2011). This is a comprehensive overview of the current options for online video delivery.

Regarding the concepts of financial valuation needed to solve the case, the following book provides the necessary background:

- Ross, Stephen A., Westerfield Randolph W. & Jordan Bradford D. "Fundamentals of Corporate Finance". This book explains the basics of building a cash flow, cost of capital and calculating net present value (NPV).

Possible Assignment Questions. The following assignment questions intend to direct students to perform a systematic financial analysis and to make a distinction between maximizing advertising revenue and maximizing overall profit. Additionally, they leave room for other considerations such as counterprogramming the competition, brand image, current trends, etc.

- *What should John Scott do if he was only concerned with maximizing the revenue of the network?*
- *What should John Scott do if he wanted to maximize the overall revenue of UBC and all its divisions?*
- *Which course of action would you recommend?*

Teaching Questions and Class Discussion Plan. A suggested way for using the case is to start with a class discussion and then divide the students in groups so they can work building the cash flow.

The class discussion should address the following topics:

1. The advantages and disadvantages of each alternative. Formulate hypothesis of which option is the best and why.
2. Identify the four revenue sources associated with each TV show.
3. Identify the marginal costs, marginal revenue and opportunity costs.
4. Other qualitative considerations such as branding of the network, current state of television, marketing opportunities, offerings of the competition, etc.

Suggested Solution

There are four main revenue streams: Advertising, syndication, home video and online video delivery. Advertising can be further divided in traditional and online. Online

video delivery can also be divided in two subsections: streaming and paid downloads. For the purpose of this analysis the costs are the license fees of producing in house or acquiring the show from an external producer.

A suggested approach is to use marginal analysis meaning that only additional benefits and costs of picking a new season of each show should be included in the cash flow. The rest of the benefits and costs are irrelevant for the analysis. Students should build a cash flow detailing revenues and costs for each show for a minimum of 5 years.

Triple Threat is not owned by UBC, therefore the only revenue source is advertising and the cost is the license fee. In the same way, advertising revenue and costs can be computed for *Single Talk* and *G-Men.* Since *Single Talk* and *G-Men* are owned by UBC they also generate money from syndication, home video and online. Home video, streaming and paid downloads can be calculated according to the information provided in the exhibits. The only difference between these two shows is the treatment of the syndication revenue. *Single Talk* would receive the syndication revenue of the 5 previous seasons regardless of getting a new season order. Therefore, the marginal revenue would only include the syndication fees of the potential new season. On the other hand *G-Men* would not be sold in syndication unless it gets one more season. In this sense, the marginal revenue includes the money of all three previous seasons and the new one.

Once the revenues and costs are tabulated, the yearly profits for each show can be computed. Finally, the Net Present Value can be calculated using the given WACC. The calculations of the suggested solution are presented in Table B1.

Table B1
Suggested Solution to the Fictional Case Study

Revenue/Cost	Year 1	Year 2	Year 3	Year 4	Year 5
		TRIPLE THREAT			
Ad. Revenue [a]	58,687,200				
Online advertising	3,521,232				
Costs	15,400,000				
Net Profit	46,808,432				
NPV	46,808,432				
		SINGLE TALK			
Ad. Revenue [a]	36,679,500				
Syndication [b]		8,800,000	8,800,000	6,160,000	6,160,000
Home Video		3,750,000	1,875,000	937,500	468,750
Online advertising	2,200,770				
Streaming		6,600,000			
Paid downloads	8,358,000				
Costs	33,000,000				
Net Profit	14,238,270	19,150,000	10,675,000	7,097,500	6,628,750
NPV	45,754,234				
		G-MEN			
Ad. Revenue [a]	23,474,880				
Syndication [c]		13,200,000	13,200,000		
Home Video		14,000,000	8,400,000	5,040,000	3,024,000
Online advertising	1,408,493				
Streaming		8,800,000			
Paid downloads	13,930,000				
Costs	27,500,000				
Net Profit	11,313,373	36,000,000	21,600,000	5,040,000	3,024,000
NPV	61,585,404				

Note. NPV= Net Present Value.
[a] Advertising revenue = (Rating * Total Viewers/1000)*CPM*# episodes* # spots per episode. [b] Since UBC would receive the syndication fee for the 110 episodes of the 5 previous seasons even if the show is cancelled, we only included the syndication revenue for the additional 22 episodes of S6. [c] If UBC cancels the show, all the syndication money would be lost. Therefore we included the syndication revenue for the 66 episodes + 22 for the new season.

What should John Scott do if he was only concerned with maximizing the revenue of the network? *He would pick up the reality show Triple Threat since it would produce the highest advertising revenue for the network.*

What should John Scott do if he wanted to maximize the overall revenue of UBC and all its divisions? *He would renew G-Men, cancel Single Talk and pass on Triple Threat. Single Talk has the potential to produce almost as much money as Triple Threat if we take into account all revenue sources; however, the show has already 110 episodes and it has become costly to produce. The additional 22 episodes order will not add enough value to justify keeping it on the schedule. On the other hand, G-Men has the potential to produce high revenue in alternative windows, revenue that could be lost if one more season is not ordered.*

Which course of action do you recommend? *It depends on UBC's overall strategy. If the company promotes the maximization of profit across all business units in the long-term, G-Men should be renewed. If the company is more concerned with immediate profit, it should probably pick Triple Threat. There are several other qualitative considerations such as branding, competition, marketing strategy, state of the market, etc. In summary, there is not an absolute answer, but the financial analysis provides a guideline to select the course of action that is more in line with the company's overall strategy.*