



## Cable / Pay-TV: Market Weight Relative to the DB Index

The alarm bells around the maturation of the Pay-TV industry have been going off for years. Despite clear headwinds that have undoubtedly had negative impacts on cash generation, management throughout the industry has done well in not only weathering the storm, but positioning their respective companies for the future. For the wired cable companies, the natural business pivot has been focusing on generating a higher mix of revenue from broadband and venturing into commercial, which just so happens to have a materially better margin and cash flow profile than the historical linear TV business. For DBS, the challenge of reinventing itself has been much more difficult considering it doesn't have an HSD offering into the household. While DTV got acquired and integrated into a large platform at AT&T that has inevitably helped its relevance and extended its lifespan, both DTV and DISH saw the writing on the wall early and instead of trying to exclusively protect its legacy subscriber base, which is a given, they created two of the industry's best OTT products.

In addition to fighting top-line difficulties, margins have also been under pressure as content and programming costs have been increasing at high-single digit / low-double digit rates for the better part of a decade. The response from operators has varied, but recent approaches can all be filed as incrementally emboldened compared to even just five years ago prior to the Pay-TV market cracking. Certain operators have resorted to going dark on channels during negotiations. Others have completely eliminated certain programming altogether and substituted with more attractively priced alternatives. Then there are those providers like WaveDivision who simply pass the cost of programming through to customers. The integration of OTT products into the platform is more prevalent and actually lowers churn as the complementary features and all-in-one place for access produces a more seamless, enjoyable experience particularly via a cross-catalog guide. While the OTT marketplace has gained market share and inspired certain demographics to cut the cord and will continue to do so over time, we believe the worries over linear TV trends are a bit too draconian. For example, in its 3Q17 Video Trends Report, TiVo points out that the number of respondents in its survey that have cut cable within the previous 12 months declined for the first quarter since 3Q16. It could just be an outlier, but after trending up 3% y/y for the past year, it could also present a data point that supports the notion that the biggest wave of cord cutting are the first movers, which is now entering its own maturity stage. Should that trend continue declining, that presents an even longer tail for linear TV which we believe would help the DBS business most given they're more levered to that segment.

*The reports of the death of linear video will prove to be – as Mark Twain would have said – greatly exaggerated. We still expect declines, but we see linear video decreasing at a moderate rate with some carriers such as DISH and ATT offsetting some of these losses with lower-ARPU OTT video adds – partially lessening the blow.*

*In terms of cord shaving/cutting, last quarter we actually saw the trend of cord cutting decline for the first time in recent history. It is too early to call this a sustainable trend, though it might be able to offer some support to the notion that the raging concerns over linear video might prove overdone. The bigger worry for us remains content pricing, which continues to increase at a pace that seems impossible to offset in the video business.*