



Subscription Television in Australia

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Major Differences Between the US and Australia

US is mature with profitable open broadcasters and subscription broadcasters.
Australian subscription TV is still developing, lacks scale and is loss-making

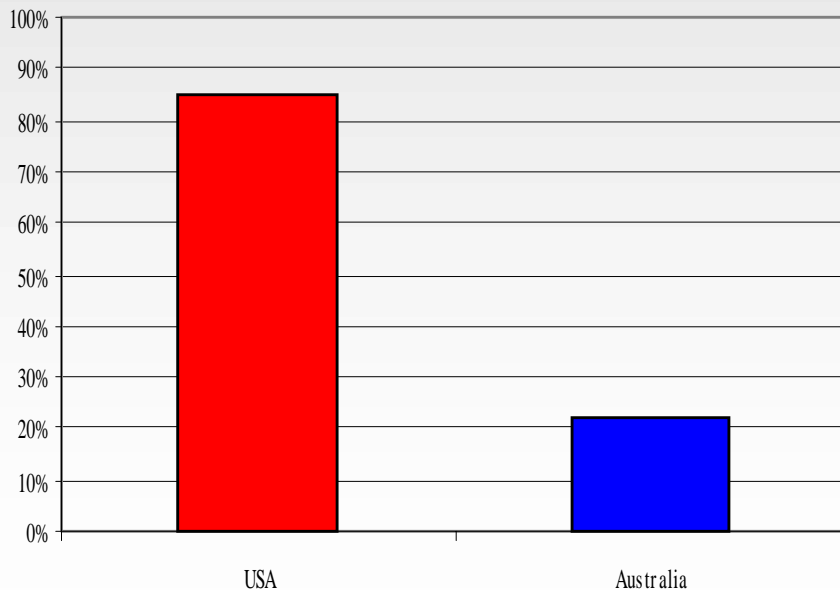
	USA	Australia
Population	287 million	20 million
Subscription Television Established	1940 (initially CATV)	1995
Lifecycle	Mature	Young
Financials	Lucrative	Unprofitable
Significant cable monopolies	Yes	No
Television Households	108 million	7 million
Households passed – cable	105.4 million	2.8 million
Basic Cable Subscribers	73.1 million	0.75 million
Total Subscribers (June 2001)	88.3 million	1.5 million
Level of vertical integration (using FCC methodology)	35%	20%
Penetration rates	82%	22%
Cable overbuild	1%	80% plus



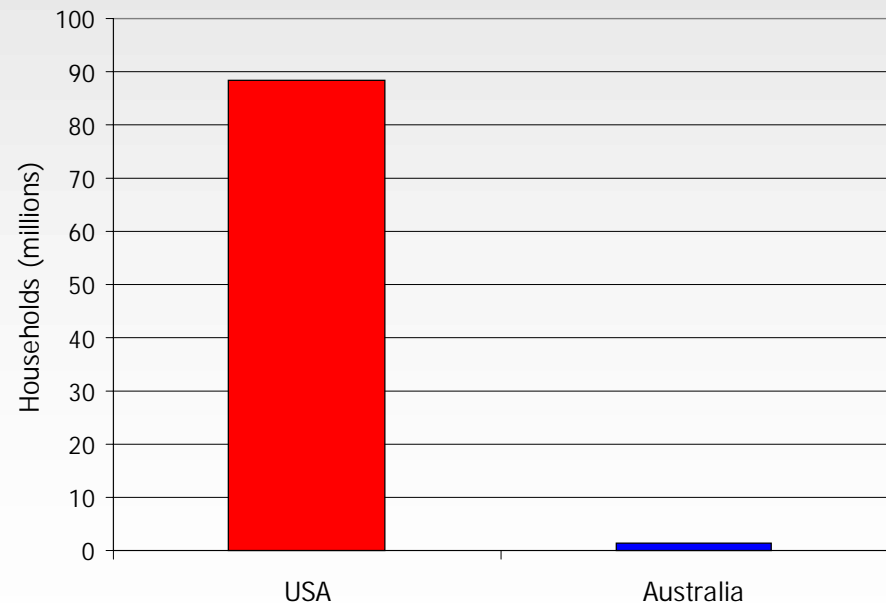
Australian Subscription TV Penetration and Number of Households is Much Lower than US

Australian subscription TV is not in the same league as the US

Subscription TV Penetration



Total Subscribers





US and Australian Subscription TV – Key Differences

- Cable operating for 50 years in US before exclusive content regulation
- Subscription television first licensed in Australia in 1994
- Subscription television is one of the most regulated start-up businesses in Australia
- Australia has the most extensive sports anti-siphoning regulation in the world. US has no anti-siphoning regulation.
- Australian subscription TV is unprofitable and unsustainable in its current form
 - ◆ US cable and satellite is connected to 82% of homes. Cable generates immense free cash:
 - ◆ US Cable industry revenue = US\$38 billion (A\$70b) per annum (2000)
 - ◆ US Cable industry EBITDA = US\$16.6 billion (A\$30b) per annum (2000)
 - ◆ Australian cable and satellite is connected to 22% of homes and generates large losses:
 - ◆ Australian total investment to date of A\$8 billion, without profit
 - ◆ FOXTEL operating business lost A\$100 million in 2002.
- FOXTEL and Austar operate both cable and satellite services



Open Broadcasters Dominate Australian TV

- Australian TV is dominated by open broadcasters controlling 87% of all TV viewing compared with 13% for subscription broadcasters
- Subscription television has 3% of national television advertising revenue
- Open broadcasting, print and radio remain the dominant voices in news and current affairs in Australia. Subscription TV provides diversity (7 news channels)
- Inequitable anti-siphoning rules covering 40 events have restricted the growth of subscription television in Australia. Of the hours of sport on the anti-siphoning list, 85% are never broadcast live by open broadcasters, and 75% are not open broadcast at all
- Open broadcasters often insist that content suppliers commit to 'holdback' periods (periods of exclusivity ranging from 3 months to 5 years) which deny subscription television providers access to that programming.



US controls the global flow of key content – and prices. Australia is a net importer of content

- US is the major global content supplier. Australia is mainly a content importer due to small scale
- Australian Government policy encouraged cable duplication. To differentiate, providers sought exclusive content – and now pay among the world's highest movie costs
 - ◆ Australian cable overbuild more than 80%. US cable overbuild around 1%
 - ◆ On launch cable services competed with national satellite and MDS service (Galaxy and its franchisees)
 - ◆ US has local cable franchises with geographic monopolies resulting in substantial market powers
 - ◆ Australia has no significant geographic cable monopolies, major overbuild, satellite competition and dominant open broadcasters (legislated commercial network oligopoly)
- ◆ **US subscription programming costs are 31-38c per \$1 of revenue**
- ◆ **FOXTEL programming costs are more than 65c per \$1 of revenue**
- ◆ **OPTUS programming costs are more than \$1 per \$1 of revenue**



Vertical Integration in the Australian Subscription TV Environment - Delivery Platforms

- Optus owns and operates a vertically integrated subscription TV and telephony business which provides cable modem and subscription TV services using its HFC
- Optus owns and operates the satellite used by FOXTEL and Austar for DTH satellite delivery. Optus proposes to offer FOXTEL television services as part of its retail telecommunications bundle
- FOXTEL is a retail subscription television creator and provider that proposes to expand to some wholesale
- FOXTEL is a pure television business - not a utility or telecommunications business
- Telstra owns and operates the HFC used by FOXTEL for cable delivery. Telstra uses this HFC to provide cable modem services and proposes to offer FOXTEL television services as part of its retail telecommunications bundle



Vertical Integration in the Australian Subscription TV Environment - Content

- Vertical integration in subscription TV content in Australia is a consequence of small scale and start-up factors
 - ◆ High content costs resulted from fierce start-up competition to secure and create premium content
 - ◆ Channel suppliers wanted to share channel start-up risks often requiring subscription platforms to take equity positions in the channels
 - ◆ Subscription platforms needed to create channels of their own to make them locally relevant
- Vertical integration within subscription TV content is not a significant issue in Australia
 - ◆ Unlike the US, Australia is a net importer of content, content is mostly licensed and not owned. All parties are free to bid for content licences on contract renewal.
 - ◆ Channels are the main acquirers of content
 - ◆ A major concern in the US is cable companies denying satellite companies access to content for areas outside the cable companies' reach (ie. hoarding). Hoarding does not occur in subscription television Australia (although common practice for open broadcasters).
- Subscription TV brings opinion and ownership diversity into a market dominated by the three commercial open broadcasters
 - ◆ The Sector carries more than 50 channels whose ownership is shared by more than 37 different Australian and international media companies



Vertical Integration in the Australian Subscription TV Environment - Content

- There are no significant cable monopolies in Australia and the level of vertical integration between subscription television providers and channel / program suppliers is low
 - ◆ Approximately 20% in Australia versus 53% in the US when the legislation was introduced and 35% by 2001
 - ◆ Optus and Telstra cable networks are more than 80% overbuilt.
 - ◆ The FCC's vertical integration rules have only been extended by 5 years, an acknowledgement that the decrease in vertical integration may not warrant extending the rules further
- Exclusivity has been critical to the development of subscription television because of the need to differentiate services in areas of duplicated infrastructure, and for subscription television to differentiate from other competitors.
 - ◆ Substantial countervailing powers exist
 - ◆ Competitors can bid against current licence holders on renewal for sports and movie rights
 - ◆ Movies and sports programmers exert countervailing power
 - ◆ Programming substitutability options successfully abound
- While at least some exclusivity, or uniqueness, is needed for differentiation and competition, exclusivity is reducing due to market forces. (eg. Proposed FOXTEL/ Optus content sharing agreement and FOX Footy Channel)



Interactive Television in the Australian Subscription TV Environment

- ITV in Australia is nascent
- Digital terrestrial television take-up has been slow and there has been no drive for interactivity from the open broadcasters
- Consumer interest in digital television will be significantly enhanced by subscription television
- ITV can be delivered over a range of delivery technologies
- Significant ITV development in Australia depends on cable digitisation which is not yet resolved
- Australia is likely to follow global trends in ITV services rather than lead them due to its small market size
- Content providers, open broadcasters and possible datacasters are likely to be strong competitors in the provision of ITV services



Bundling in the Australian Subscription TV Environment

- Optus bundles voice, internet and subscription television – the FOXTEL-Optus content sharing agreement would strengthen Optus
- Austar bundles (or co-brands) video, mobile telephony and internet services
- Other operators are building cable networks and developing bundling (eg TransACT)
- FOXTEL anticipates that future roll-out of cable will be by operators interested in high speed internet and subscription television will be an add-on
- FOXTEL does not bundle
- Telstra plans to bundle its telephony services with FOXTEL television



Conclusion

- **The US is substantially different to Australia in market structure, maturity and scale - regulatory approaches in the US are not always appropriate for Australia**
- Vertical integration in programming is much less in Australia than in the US and Australian market evidence shows there is reducing exclusivity and wide availability of premium content (eg FOX Footy Channel and proposed FOXTEL/ Optus content sharing agreement)
- However, some exclusivity remains critical for differentiation and competition
- ITV services in Australia are nascent. Australia lags behind many other developed countries with digitisation. FOXTEL plans to digitise. Open access issues are being addressed. A digital FOXTEL will also help the wider television industry achieve the scale required for meaningful ITV development in Australia.
- Bundling of voice and video services in Australia is likely to grow in importance. Sustainable subscription TV services are essential to enable sustainable bundling
- True convergence, as opposed to packaging or co-branding, is a long way off in the Australian market



Conclusion

Subscription Television in Australia

- The Australian subscription television sector has a vital role to play in developing consumer entertainment and information services, content opportunities, media diversity, digital television (ITV) and video/voice bundling.
- The US and other advanced television markets, while having different characteristics requiring different regulatory approaches, demonstrate the potential of subscription television and consumer demand for it
- However, the Australian subscription television sector is uniquely challenged by inappropriate regulation (eg anti-siphoning), high content costs (US movies), small scale, dominant open broadcasters – and unsustainable financial losses.
- This has led to the FOXTEL-Optus content sharing agreement. The agreement is essential to repair and make viable the subscription television sector in Australia.