Television

Topics for Today

- How do Networks Create Value
- The Relation Between the Studio and Television

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What is a Network?

A Network is a Distributor

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What Is a Network?

- A Network Is a Distributor
  - It Buys Programs From Producers
  - It Supplies These Programs in Bulk to Affiliates
  - It Sells Advertising Time in Bulk

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Economic Issue

- How do Firms Deal with Each Other
  - Market Sales
  - Contract
  - Joint Ownership
- Which is Best Depends on Circumstances

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How Does Network Create Value?

- Reduce Transactions Costs
  - Deliver a National Audience in One Purchase for Advertisers
  - Deliver National Coverage of Shows in One Sale for Program Producers
  - Deliver a Portfolio of Programs in One Deal for Affiliates
- Creates Additional Value by Setting Optimal Schedule of Programs

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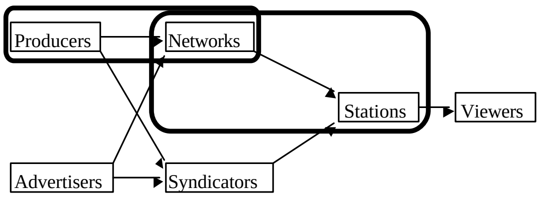
Who Are the Players in the TV Market?



The Advertising Market

- Network TV is less than 10% of total advertising
- Substitutes for Network Advertising
  - Spot market
  - Barter syndication
  - Cable, superstation
  - Radio
  - Other media
- Not as big a buy, but can be targeted
  - Less duplication with national TV buys

How Does a Buy Work?

- May sponsor entire program
  - Common in 1950's, less common now
- Norm is buy of participations
  - Up front market sells 70%– 80%
  - Rest in pick-up market
- Webs use unsold time for
  - Public service
  - Self promotion

Competition in this market

- Number of stations has no effect on price of time sold in a particular area
  - Indicates competition
    - Either from other stations or other media
  - National and spot market buys appear to be close substitutes

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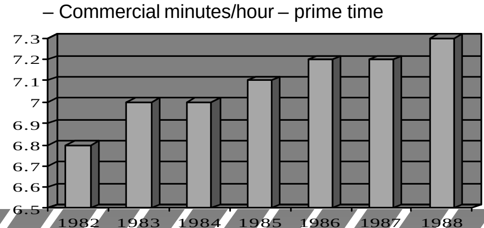
Commercial Minutes

- Limits appear not to work
  - NAB code violates unconstitutional
  - Commercial minutes/hour – prime time



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How Do Networks Deal With Affiliates?

- In General They Pay Affiliates to Carry Programs, But This Is Changing
  - Networks Require Clearance
  - But, who Gets Value NFL Creates at Local Affiliates?
- Networks Cannot Force Affiliates to Carry Programming
  - Cannot Require Exclusivity in Contracts
  - Cannot Withhold High Rated Program to Induce Affiliate to Carry Low Rated Program
  - Networks Cannot "Fine-tune" Compensation to Affiliates

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Effect of Contract Limitations

- Depends on Who Has Bargaining Power
  - Are There More Stations in Area Then Networks, or *Vice Versa*
- Creates a Free-rider Problem
  - Network Programming Is, on Average, More Profitable
  - But Only If Sufficient Coverage
  - What If Each Station Carried ONLY Those Programs That Make More Money for It Than Syndicated Programming?
    - Everyone's Costs Go up
- Solve Problem by Owning All Stations

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What About Dealing With Producers?

- Key Here Is Financial Interest Restrictions which will be covered later

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TV and Studios

- Consider the Relation Between TV and Movies in the Early 1950's
  - 4 Networks
    - None Related to Movie Studios
    - 2 Related to Hardware Makers
      - NBC
      - DuMont
- Consider the Situation Today
  - 6 Over the Air Webs
    - 4 Related to Movie Studios
    - None Related to Hardware
  - Not Counting Cable Web Such As TNT

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Why the Change?

- Initial Stage in Many New Technologies Has Hardware Makers Fostering Content Development
  - – Motion Picture Patents Trust
  - – Edison Makes Movies
  - – NBC, RCA are Set up by AT&T, GE
- This Happened in TV, but Now Control Has Shifted to Content Providers

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Vertical Integration

- When Does It Make Sense to Bring Two Stages of a Vertical Process Under Joint Ownership?
- If Each Side Must Make Relationship Specific Investments That the Other Can Exploit
- If Ex-post Settling up Is a Problem
- If It Is Difficult to Determine Contribution of Each Side to Joint Enterprise

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Initially Link Content With Hardware

- Color Programming by NBC Is the TV Version of Visicalc
- Also Gives Content Providers a Role in Setting Technical Standards So Their Costs/Benefits Are Reflected in Final Decision
- This Can Have Interesting Effects
  - – Use of FM for Sound Part of TV
  - – Choice of Standard for Color TV

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Movies Fight TV Early on

- This Almost Always Happens
  - Records and Radio
  - Movies and Live Theatre
- Change in Movie Content to Fight TV
  - Switch to Wide Aspect
  - More Color Movies
  - More Location Shooting
  - Jack Warner and the Search for 3D Movies
- Recent Movies Kept off Network
- Movies and TV Are *Competitors*

Then Movies Complement TV

- Shared Factors of Production
  - Actors
  - Stars
  - Soundstages
- Some Studios Produce TV Shows Themselves
- TV Buys Film Libraries
- TV Used to Advertise Movies
  - Remember Increase in P&A Costs
- Indeed, Now Some Content Changes to Fit Video Aspect Ratio

But Why *Joint* Ownership?

- We Are Talking About Intellectual Property
- Much of the Benefits From Both Movies and Television Lies If Follow-up Products
  - Sequel
  - Spin-off
  - TV Show From Movie
  - Movie From TV Show, Etc.
- In Order for Initial Investment to Be Optimal Downstream Revenue Sources Must Be Taken Into Account
  - This Is Automatic With Joint Ownership

Example: Buying Sequel Rights

- Take a Simple Hypothetical (or Not So Hypothetical) Deal Where We Agree to Buy, Sight Unseen, the Sequel Rights to a Studios Slate of Movies for a Fixed Amount Up-front
  - Must Do It Before Production Starts, Else Studio Knows More Than Us
- Will This Affect What the Studio Does?
  - Marketing
  - Content--maybe They Kill-off Rambo

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