

By Rory J. Altman

Will Over-The-Top Kill the Video Star?

It is impossible to escape intense discussion of “over-the-top” (OTT) video these days, as it has gone well beyond user-generated content on YouTube. If you believe the Hulu-hype, we are on the precipice of abandoning conventional video services from Comcast or AT&T and instead, we will simply watch Gossip Girl on our PCs. Surely, this medium that has attracted 149 million U.S. users and more than 14 billion downloads in March alone must threaten conventional video subscriptions and/or ARPU.

Here’s what we know: OTT video is neat and convenient. Using services like Joost, YouTube or Veoh, we can now watch TV shows when we forget to record a show on our DVR; we delete the recording, the DVR becomes full; others are using the TV; we’re away from home; or we want fringe or foreign content. People like that the flexibility and user interface resemble the Web. And, TV networks are cautiously placing their content on their own site as well as on joint venture sites like Hulu.

We also know that it’s possible to watch a great deal of TV on your PC and escape conventional video service entirely, as many young people are doing. For example, more than 40% of U.S. households under age 35 watch Internet video at least once a month, [according to research firm In-Stat](#). Within five years, the number of U.S. broadband households viewing Web-to-TV content will grow to 24 million, according to the research group.

In theory, OTT video also offers the potential for both consumers and artists to escape the producers and networks that “control” which TV concepts are produced and broadcast to our homes – the so-called democratization of TV. Although this disruption is one of the most interesting elements of OTT video, the music industry experience suggests that the TV networks will retain their funding, marketing, and monetization roles, even if they are somewhat diminished.

However, none of this excitement addresses two significant problems with OTT video:

#1: OTT video does not generate the same revenue for the network as conventional TV. Promising OTT video advertising models are just emerging and are already threatened by privacy alarmists. In conventional TV, 16 minutes of advertising plus cable programming fees generate about \$1,200 to the network for one hour of programming per thousand viewers. OTT video revenues range from \$150 up to \$300 per hour for best-in-class sites. Why should consumers care about advertising? If the OTT ad model never develops, the best network content will increasingly be restricted or removed from Hulu and other websites. Plenty of people are working on OTT advertising solutions to address the revenue gap, so this problem may be solved.

#2: OTT video provides a relatively poor picture quality on a tiny screen that sits only 30 inches away. For most people, OTT requires watching alone in a desk chair rather than lounging on a couch 10 feet from the TV with friends. (Try snuggling with your date in front of a laptop.) Now that a 40” flat panel HD set is available for \$600, and penetration surpasses 40% of households, picture quality matters. People are less satisfied with a sub-HD experience for many genres of long-form content.



To address these user experience shortcomings, the consumer electronics industry is racing to move OTT from the PC to the TV, by embedding browser and navigation capabilities directly in TVs and remote controls, in new set top boxes such as NetGear's Web-to-TV STB, or embedded in Blu-Ray players. In some cases, device manufacturers are creating a seamless service by integrating with OTT video services, e.g. Samsung-NetFlix. How are the cable companies, DBS operators, and telcos responding? AT&T and Verizon have launched reasonably good set top box-based user interfaces, but the cable companies still depend on clumsy legacy UIs that are one step above 1980s Atari. The terrestrial providers are expanding paid and free video-on-demand libraries. However, the quantity of content is still lacking—especially HD content—the cable navigation ranges from poor to awful, and the best of Web 2.0 is basically absent, such as friend referrals and recommendations. Overall, switched digital video and IPTV overlays offer the potential for terrestrial providers to expand content availability and flexibility, but we have yet to see real benefit.

OTT video will continue to be attractive to its core demographic of the young and mobile. However, conventional video providers must do more to enable content availability, location flexibility and more advanced UIs. They must also create even more value with targeted, set top box-inserted advertising. If service providers don't address these issues, the OTT video phenomenon will attract the mass market, eventually compromising the value of multichannel video service, which in turn will siphon ARPU and subscriptions. If OTT video captures too many eyeball-hours, service providers will be left with usage-based broadband pricing to monetize their networks, assuming this pricing model is not rejected by consumers or regulators.

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