Global Consumer Trends

Streaming is the future of media

- Streaming market boom expected to continue
- Increased SVOD services will likely boost adoption
- Covid-19 a catalyst for SVOD, less so for music or games

Digitalization of consumption, one of the trends our Global Consumer Trends strategy focuses on, is still profoundly transforming the media and entertainment industry. Among the structural winners of this trend are streaming platforms. These have enjoyed strong success over the past few years, and their prospects remain bright despite the dire economic consequences of the Covid-19 crisis. But there is a caveat: commercial success often comes at a hefty price when producing the necessary exclusive content.

The market

After years of stellar growth, the streaming boom is expected to continue in the coming years – mainly due to a surge in global demand for video streaming. According to Digital TV Research, global online TV episode and movie revenues could double between 2019 and 2025, from USD 83 to 167 billion.[1] Around USD 16 billion will be added this year.

The total online TV market consists of various segments – the main one being subscription-based video on demand (SVOD), offered by players such as Netflix, Disney+, or Amazon Prime Video. Digital TV Research expects global SVOD revenues to double over the next few years, and climb by USD 50 billion between 2019 and 2025, to a total of USD 98 billion.

Article
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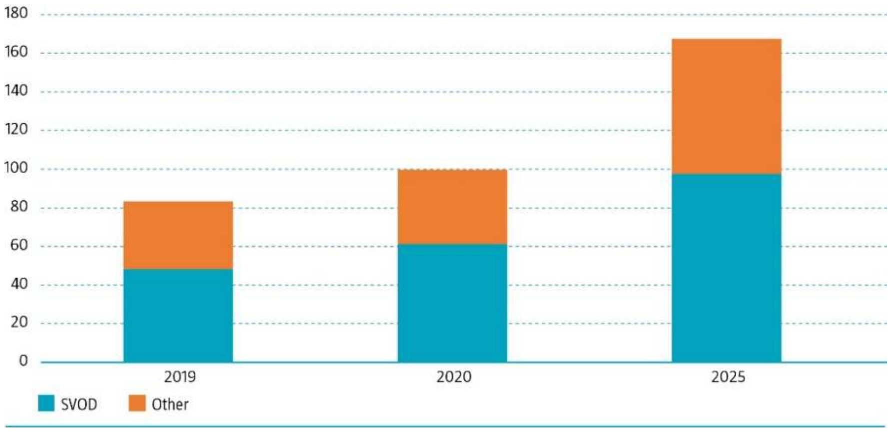
[1] Source: Digital TV Research, Global OTT TV and Video Forecasts, May 2020.

The streaming market, also called the OTT (over-the-top) market, refers to all types of media services and content offered to customers directly online, bypassing traditional cable, broadcast, and satellite television networks and platforms. It therefore includes not only increasingly popular SVOD services, but also music streaming and video games services.

Figure 1 | Global online TV episode and movie revenues in USD billion



Source: Digital TV Research. May 2020.

One of the main growth drivers behind OTT service demand is convenience. Customers can easily subscribe and cancel online, and content is available all the time. Subscribers can watch what they want, where they want and when they want, using the device they want. This has become increasingly important to customers, particularly for younger generations.

Another important factor driving demand, particularly for SVOD, is cost. OTT providers charge their clients relatively low monthly fees, compared to cable networks and more traditional distribution channels, such as DVDs or movie theater tickets. This is important, especially given the relatively high content quality, typically offered by these platforms nowadays.

Over the years, the main SVOD platforms have made considerable efforts to offer a very wide, and often exclusive, selection of trending films, series and documentaries. In order to standout from competition, these platforms have had to move into the production business. Netflix[2] was the first platform to pursue this strategy when it launched "House of Cards" back in 2013.

Since then, SVOD platforms have been following the same strategy: producing exclusive content for their subscribers. Premium content that used to first be distributed through movie theatres or via traditional TV channels, is now increasingly being made directly available on these platforms. Lockdown measures against Covid-19 ensured most consumers stayed home, further accelerating this shift.

For recorded music, the advent of streaming has revived a once rapidly collapsing music market. Music consumption, which used to revolve around the sale of records, CD and DVDs, started declining quickly with the arrival of the internet. This was mainly because revenues from downloads could not compensate for the nosedive physical recordings had taken.

But after years of contraction, the music market started growing again in 2015, due to the success of platforms such as Spotify or Apple Music. It is now close to the levels of 2002-2003. In 2019, streaming accounted for 56% – USD 11.1 out of 20.8 billion total – of the total recorded music market worldwide.[3]

In addition to video and music, the concept of streaming is increasingly catching up in other areas as well. Subscription-based online gaming, where players signup to access a selection of video games from their computer, smartphone or tablet, is a case in point. However, this segment is still in its infancy and remains dependent on technological improvements, as it requires a very fast internet connection.

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[3] Source: International federation of phonographic industries (IFPI), 'Global Music Report – The industry in 2019', May 2020.

The players

In the OTT market, two major types of players emerge: SVOD providers and music streaming platforms. These services are usually offered by pure players, such as Netflix and Spotify, or by tech giants that include Apple, Amazon and Google. Other types of players include media groups, telecom companies and diversified consumer electronics conglomerates, such as AT&T and Sony.

SVOD

The SVOD segment is by far the most relevant for investors, given its size. It is dominated by a small group of very large US-based players, including Netflix, Amazon Prime Video, Hulu and Disney+. These giants compete against each other and against a myriad of smaller players, usually backed by either movie studios, local internet providers or TV networks.

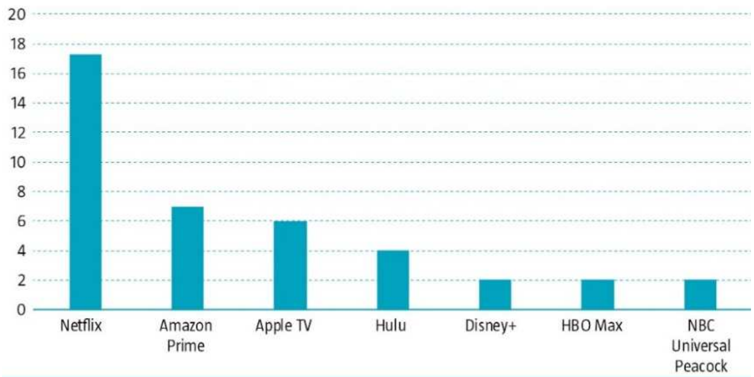
In the early 2010s, pioneers of SVOD, such as Netflix, enjoyed relatively good relations with established movie studios and TV networks. These sometimes struggling incumbent players initially thought that using these new platforms for their catalogues would be an opportunity to make high-margin additional revenue. This made Netflix's initial expansion all the easier.

But as SVOD viewing grew and clients cancelled their cable subscriptions, studios and TV networks started to rethink their strategy. They pulled their content from these platforms, which they increasingly saw as direct competitors.[4] In reaction to all these developments, Netflix and other platforms started to shift away from distributing licensed content and started producing their own exclusive films and series.

Some studios and cable networks also decided to launch their own SVOD services. A platform would give them direct access to end customers, which would enable them to collect key information on who watches what, when, how and on what type of device. It would also allow them to receive feedback from clients. Without such a direct link, studios would not get much further than knowing how many viewers they had had, at best.

However, only very few studios have managed to gain traction against Netflix, so far. Disney, with its popular Disney+ and Hulu offerings, is more an outlier than a norm. Other players are still struggling to gain enough scale to make up for the high productions costs associated with the exclusive and differentiating content that is needed to attract subscribers.

Figure 2 | The sinews of streaming wars: estimated content spend for 2020



Source: Robeco, BMO Capital Markets via Tubefilter, January 2020.

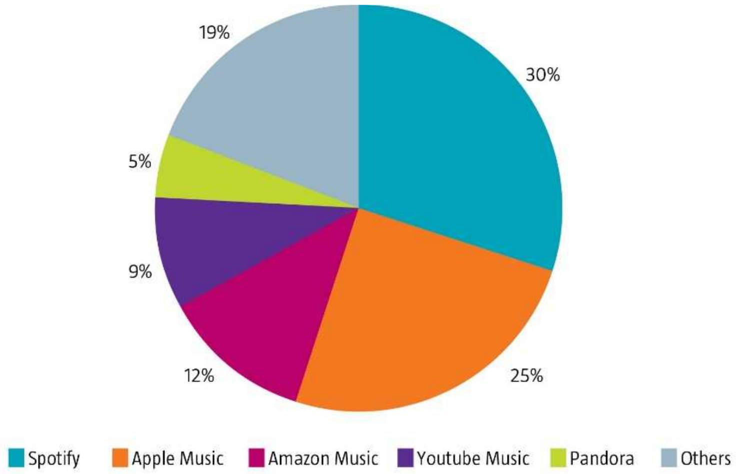
Another outlier in the SVOD market is Amazon's Prime Video. This service is usually given away for free with subscriptions to Amazon's Prime offering, and therefore essentially remains a customer acquisition tool for the retail giant. Yet, this strategy has enabled Prime Video's subscription base to grow massively, despite an arguably lower-quality content library than Netflix or Disney+.

[4] For instance, market data firm, Ampere Analysis, expects US pay TV penetration to drop below 60% in 2020, down from close to 80% in 2015.

Music streaming
The music streaming market shares similarities with SVOD as it is also dominated by a handful of very large global players, including Amazon Music, Apple Music or Spotify in western countries, and local giants, Tencent Music or NetEase Cloud Music, in China. However, the business model is very different from SVOD, as it is essentially based on royalty fees.

Streaming platforms do not offer exclusive in-house produced content. Instead, they act as the middleman between artists or record labels and listeners, and pay royalties each time a song, a piece of music or an audio book is played. In this sense, music streaming platforms have much lower fixed costs, but also much less exclusive content they can leverage on.

Figure 3 | Global music streaming revenue by brand in Q1 2020



Source: Counterpoint research, July 2020.

All players give access to approximately 35 to 40 million songs and most newly-produced content, meaning there are few opportunities to standout. This is why Spotify has recently been investing in exclusive podcasts as a way to differentiate their services. In May, the firm announced Joe Rogan's very successful show, 'The Joe Rogan Experience', would become a Spotify-exclusive.

Another important difference with SVOD is that, while the film and series production landscape remains very fragmented, the music industry is virtually under the thumb of three record labels: Universal Music, Sony Music and Warner Music. These firms have managed to keep their grip on the industry despite dire circumstances and have little incentive to favor one platform over others.

Video games
Although important technical challenges remain, in particular in relation to broadband speed, video games are currently one of the most promising areas for streaming. In recent years, a number of key players have actually taken important steps to get a head start, in an attempt to revitalize a generally slowing growth pace for the global video games business.

These players include companies such as Alphabet and its Google Stadia service, Microsoft and its xCloud project, Apple with Apple Arcade, and Sony with its PS Now service. More recently, Chinese tech giants, such as Tencent and NetEase, have followed suit and have launched their own online gaming service in China.

Video game streaming – sometimes referred to as cloud-based gaming – follows SVOD in that its business models are also based on exclusivity. Competing platforms either distribute their own games – often initially developed for console playing – or, in the specific case of Google, sign exclusivity deals with game developers.

So far, these platforms have been relatively slow to take off, in part due to technical issues. However, many experts see streaming as the main growth driver for the video game sector in the near future, in particular as 5G networks will be rolled out.

Recent developments

After years of virtual complete supremacy for Netflix, this SVOD pioneer has seen competition intensify in recent years, in particular as Hulu and Amazon Prime Video strengthened their positions. This was reinforced by the launch of Disney+, in November 2019, fueling concerns over a potential price war for market share. So far, however, these fears have not materialized.

The different services offered appear to be clearly differentiated, with Disney+ geared toward youngers audiences, for example. Many customers have actually subscribed to several SVOD services simultaneously. Over the last quarter of 2019 and the first quarter of 2020, all major SVOD platforms have seen their subscription base grow, helped by the Covid-19 pandemic (see Box 1).

Box 1: SVOD adoption boosted by the Covid-19 pandemic

Video streaming platforms have been among the biggest winners of the lockdown measures taken worldwide to slow the expansion of the Covid-19 pandemic. For instance, Netflix added 15,8 million paid memberships in the first quarter of 2020 as opposed to the 8.8 and 9.6 million paid membership additions in the fourth and third quarters of 2019, respectively.

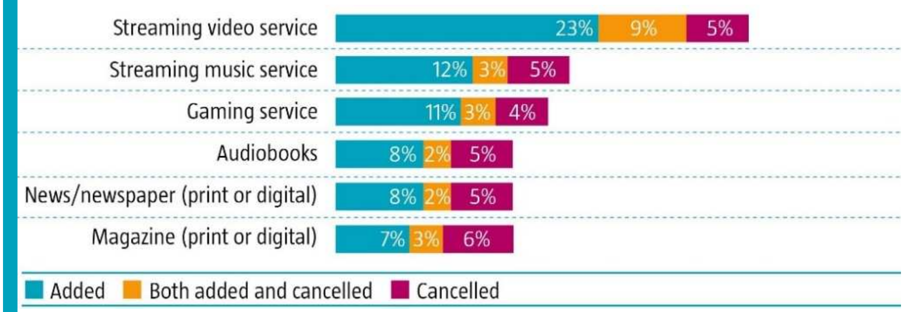
Other SVOD platforms also saw strong increases in new subscriptions during the first quarter of 2020. Disney+, for example, added 8 million subscribers over this period, reaching a total 33.5 million at the end of March. Disney services, ESPN and Hulu, also saw sharp increases in terms of new subscribers.

Growth is expected to return to normal rates in the coming quarters. Yet, these figures bode well for overall SVOD adoption relative to more traditional TV viewing. In fact, the first quarter of 2020 saw almost two million subscriptions wiped off the top seven pay TV providers in the US, according to market data firm, Ampere Analysis. That is 1.2 million more than in the same period of 2019.

Yet, such enviable numbers do not come without challenges for SVOD platforms. Such growth also encompasses a pressing need for ever more exclusive content to keep new subscribers satiated, in a context marked by numerous production shutdowns – due to sanitary measures taken to fight the pandemic – and a likely less captive audience as lockdown measures ease.

While the impact of Covid-19 has been strongly positive for SVOD demand, the consequences have been less clear-cut for other segments, as figure 3 shows. It provides a glimpse of the impact the Covid-19 pandemic has had on media subscription additions and cancellations in the US, based on a survey carried out by Deloitte in May 2020.

Figure 4 | Changes made to paid subscriptions since the Covid-19 pandemic began



Source: Deloitte Insights, June 2020.

Subscription additions clearly dominated video streaming services, but the outcome was more mixed for music and video game streaming. This is consistent with the numbers reported by industry leader, Spotify, who saw a 31% increase of the number of premium users year on year, in the first quarter of 2020. That is roughly the– still enviable – pace seen in previous quarters.

In fact, increased services from SVOD platforms may well turn out to be a long-term positive factor for the whole sector, luring a growing number of viewers away from traditional pay TV subscriptions.

Competition has also been intensifying among music streaming platforms, as they sought to stand out from rivals. Spotify's Joe Rogan signup is the most recent twist in a series of deals that have seen Spotify spending hundreds of millions of US dollars to buy podcast production companies, such as The Ringer, Gimlet Media, Anchor and Parcast, or to sign exclusive podcast deals with DC Comics and Kim Kardashian West.

Conclusion

The streaming boom seen over the past decade is far from over, as viewers continue to shift from analog media, such as television or radio, towards video and music streaming alternatives. While competition is expected to remain fierce and the race for the best exclusive content is likely to continue, current trends suggest there is room for multiple dominant platforms, provided they can differentiate their offering.

So far, the Covid-19 crisis has been a catalyst for online video adoption, as captive viewers accelerated their move towards these platforms. Cord-cutting has increased, indicating that these customers are unlikely to return to their traditional viewing habits anytime soon. The positive flywheel effect from a larger user base, leading to higher monthly subscription income and enabling platforms to add more exclusive content, is also very much intact.

A similar development is happening in the music industry. Streaming has not only stemmed the decline in music consumption, but consumers are paying for music again, as the ease of use and vast libraries are providing value in excess of the usually low monthly fees charged. Streaming platforms are expanding their offering beyond music adding all kinds of other audio content, including podcasts and audiobooks, to lure an even wider audience.

For video game streaming, the outcome is less clear-cut, for now. We remain in the early stages of cloud-based gaming and latency issues still tend to affect user experience for multi-player games, for instance. Yet broadband speed is expected to continue to improve in the coming years. It is therefore likely just a matter of time before video game streaming can really take off.

Overall, the long-term prospects remain bright for the streaming industry, despite the dire economic consequences of the Covid-19 crisis. The future of media is certainly streaming.

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