

Weekend Media Blast: A Crisis is a Terrible Thing to Waste

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By: Craig Moffett

Addressable advertising on cable has been two years away from reality for, oh... about ten years.

At first blush, it's hard to imagine that *now* is finally the right time. After all, launching a new interactive, addressable, singing and dancing, all-things-to-all-advertisers, bells and whistles new advertising capability in the midst of the worst ad market in a generation would seem spectacularly bad timing. But, to paraphrase Rahm Emanuel... a crisis is a terrible thing to waste.

There's no mistaking that we're in the midst of an ad crisis. Cyclically, local ad spending is in free fall. Key local advertising segments – especially car dealers and retailers – have gone into hibernation, or worse, bankruptcy. Even with a boost from political ad dollars in 2008, Fourth Quarter advertising revenues at Comcast were down 5% from year ago levels. Without political spending, advertising would have dropped by 20%. Secularly, television advertising of *all* sorts is losing ground to the Internet. Web based advertising offers richer measurability and a more tangible ROI.

Against this hostile backdrop comes *Project Canoe*, the codename for the cable industry's first – and long overdue – coordinated attempt to make addressable advertising a reality. Canoe Ventures LLC is a joint venture of Comcast, Charter, Cox, Time Warner Cable, Cablevision, and Bright House Networks.

Dictionary.com defines "canoe" (*kuh-noo*) as "a small, primitive light boat," "traditionally formed of light framework covered with bark...or formed from a dug-out or burned-out log." Cable, behold your future.

That definition might have added "*painfully slow... and eerily silent.*" Since the Canoe initiative was announced to great fanfare in September 2007, not much has happened, at least above the waterline of visibility. For investors, the notion of addressable advertising has quietly receded back into obscurity, encumbered by the real world politics of competing priorities, constrained capacity on cable systems, and a bewilderingly complex ecosystem of agencies and advertisers. We wrote our first in-depth piece about addressable advertising almost five *years* ago... and we were hardly the first. White papers on the topic go back ten years before *that*. To re-read our 2004 report today (*available on request*), you'd hardly notice that five years had passed. Then, like now, addressable advertising seemed "right around the corner." Key elements of the technology were already largely ready. Indeed, the same companies that looked so promising then – like Visible World, OpenTV, and INVIDI – are the same companies that... well, still look *promising* now.

That so little progress has been made is a tragedy of lost opportunity.

But that's not to say there hasn't been *any* progress. Investors will get a long overdue peek at developments on the addressability front at next week's NCTA *National Cable Show* in Washington, DC., where addressable advertising is almost sure to be a central theme. Canoe CEO David Verklin, the former CEO of Aegis Media Americas who was named to the project in June of last year will be everywhere at the Show, including appearing as a panelist for "*Economics of a New Advertising Era*," a General Session panel I will be moderating on Thursday, April 2nd. (The panel will also feature Comcast's Steve Burke, Discovery's David Zaslav, Time Warner Cable's Landel Hobbs, and Turner Broadcasting's David Levy).

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It's helpful to revisit briefly the tantalizing prize at the end of the rainbow. Addressable advertising combines the broad reach of television with the targeting capability of the Internet. Targeted ads can be sent to individual set top boxes based on a nearly infinite array of household level demographic data. Addressability offers the prospect of a diaper manufacturer sending its ads only to families with young children, or a pet food seller sending its ads only to homes with dogs. American Express could send an acquisition ad only to households who don't have a card, a stimulation ad to households who already have a card, and a loyalty ad to its best Platinum Card holders.

The pay-off for cable is higher CPMs (Cost per Thousand). As John Wanamaker famously opined a century ago "*I know that half of my ad dollars are wasted... I just don't know which half.*" Addressability improves that batting average by reducing waste (say, those families without young children for the diaper advertiser) while simultaneously improving relevance, and therefore, presumably, engagement.

Eventually, addressable advertising will break down the distinction between local and national ad inventory. Indeed, it will *need* to. Cable operators don't have enough ad inventory to transform the industry alone. "Local avails," which are granted to cable MSOs by the national cable networks, account for only about 10-20% of cable network inventory. The rest is "national." Cable operators alone can provide the requisite "addressing" technology. Cable programmers on the other hand, can provide the inventory and entrée to the national advertisers. It would seem a perfect match.

The problem, of course, is that all this takes time. Before addressability takes hold, MSOs need to be able to offer a nationally interconnected platform in order to offer advertisers greater reach (the Canoe moniker was chosen to connote the need for all operators to paddle together). Advertisers and agencies, too, need time to adjust. And crafting a partnership between cable MSOs and national programmers raises the knotty problem of how they will divide the spoils (but let's face it, in a world of falling ad dollars, that's a prince's problem). After a decade of waiting for addressable advertising investors are impatient.

As is so often the case, Cablevision hasn't waited for the rest of the industry to figure it all out... they dove in and got started. And for a dose of instant gratification, Cablevision offers a tantalizing model. Cablevision has recently completed a 100,000-home addressability trial in Brooklyn that used addressability not to sell higher priced ads, but instead to sell more cable services. And it worked.

Using technology from *Visible World*, a New York-based addressable advertising firm, Cablevision spent a year targeting ads for *their own services* to their own subscribers. Video-only subscribers saw ads to upgrade to voice and high speed data services. Video subscribers who already had high speed data customers saw ads promoting Cablevision iO voice service. Triple play customers saw ads promoting Cablevision's iO Rewards retention program. According to David Kline, President and COO of Cablevision's Rainbow Advertising Sales, the test showed a "double-digit" lift in sales in areas that received the addressable ads versus areas that did not.

On a footprint-wide scale, that kind of uplift could mean thousands of incremental RGUs... and a quick and immediate return on deploying addressable advertising technology without even having to actually *sell* a single addressable ad.

Ironically, at a time when ad sell-out rates are low due to the recession, this kind of self-promotion enhancement is even more valuable... simply because there's so much advertising inventory to use up with these kinds of promotional spots. Cable operators typically use unsold ad avails to promote their own services like video on demand or high speed data. Much better would be to promote *children's* VOD offerings to families with children, or Turbo High Speed Data to inveterate gamers.

Cablevision and Visible World are moving beyond their initial trial to actually selling ads. They have expanded their addressable footprint to 500,000 households across Brooklyn, the Bronx, and Newark and Hudson County, New Jersey, and offering insertion of thirty networks through agencies that represent the vast majority of ad buying in the U.S., including Starcom USA, GroupM, and Universal McCann. Tracey Scheppach, Senior Vice President and Video Innovation Director at Starcom said advertisers have expressed interest in target groups as small as 8,000 homes.

Demographic data is provided by credit scoring/consumer data provider Experian, which also provides "arm's length" data matching capabilities to ensure that subscriber privacy is protected. Cablevision offers advertisers the ability to target customers based on income, family size, geography... or any other criterion available through Experian, or through a match against the advertiser's own customer list. Cablevision hasn't named the advertisers (saying only that they are major national brands ranging from entertainment to technology), but they apparently had no trouble finding advertisers who were eager for the chance to participate.

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For their initial roll-out, Cablevision is selling only an entire avail (that is, they are not allowing an advertiser to purchase *only* subscribers who have young children, for example). In a recent interview, Kline indicated that the advertisers participating in the new addressability program (it is no longer a "trial") are paying a "significant premium" to prevailing CPMs. Cablevision ultimately expects to bring addressability to all of its 2.8 million digital TV subscribers.

There's more. Cablevision is already offering sponsored VOD "showcases" to advertisers like Walt Disney resorts, allowing customers to drill down on resorts, and click to speak to an agent; exactly the kind of measurability and ROI that makes the Internet so enticing to advertisers. According to Kline, 23% of click-thru's resulted in a confirmed booking. VOD advertising is another target initiative for Canoe. Kline emphasizes that Cablevision "*fully supports Canoe,*" but, he concedes, "*we're running ahead of them right now.*"

Verklin and Canoe have been paying attention. In a conversation earlier this year, Verklin indicated that the Cablevision model of using addressability to target ads promoting cable's *own* services first is a great place to start, and offers to pay for deployment quickly, providing quick and high returns. A second early priority is monetizing set-top box census data itself – that is, a potentially huge census of what tens of millions of people are *actually* watching (rather than a statistical prediction of what people *might* based on a handful samples, as ratings data is compiled today).

Like selling cable services on unsold avails, set top census data could provide a quick win for Canoe, and buy time for the "big show" that is full addressability.

Meanwhile, Cablevision's initiative marks the first time that addressability technology has definitively been proven scalable, not just in a trial, but in a full scale rollout

There are no excuses left.

Quote of the Week

"#7: Consider cutting the cord: Many families and small businesses are discovering that the best way to cut overall telecommunications spending is to eliminate their landline phone and use wireless for their communications needs at home and on the go."

– "Top Ten Ways to Help Get the Most Value From Your Wireless Service," Verizon press release dated March 27, 2009

Current Company Views & Weekly News

U.S. Media Conglomerates (Nathanson, Borst & Nowak)

DIS	M: Tough studio comps in FY08 and waning momentum at Parks and ABC
NWS	M: Near-term earnings risk from exposure to structurally-weak and cyclically-affected markets
TWX	M: Content stub now fairly valued, cable stake valued at market levels
VIA	O: Superior brands transcend distribution shifts; estimate appear achievable
CBS	U: Concerns about local advertising exposure and dividend sustainability

Pure-Play Cable Networks (Nathanson, Borst, & Nowak)

DISCA	M: Affiliate fee exposure and international story give it relative stability during times of advertising contraction
SNI	M: Higher advertising exposure makes company a more pro-cyclical play, but optionally on higher affiliate fees provides some upside

Global Advertising Agencies (Nathanson, Borst, & Nowak)

OMC	M: Best mix of assets and should post the highest long-term growth rates
IPG	M: Less diversified asset mix leads to slower growth and higher risk
WPP.LN	O: Attractive asset mix and best-in-class cost management

U.S. Cable, Satellite & Telecom (Moffett, Possavino, Del Deo & Pan)

CMCSA	O: Our preferred pick. Compelling value, terrible sentiment
CVC	O: Low capital intensity yields compelling FCF valuation, notwithstanding competitive challenges from high FiOS overlap.
DISH	M: Weak operating results fully priced into stock. Eroding DBS industry trends and outstanding litigation remain significant risks.
DTV	M: Operating at high level but catalysts well-known; Valuations now neutral
TWC	O: Advantaged technology and cost structure; strong defensive characteristics.
T	M: Defensive characteristics may be overstated; Growth and margin expectations appear too high; Dividend yield remains attractive.
VZ	U: Similar to AT&T but weaker ROIC and richer valuation
S	M: No clear path to turn-around, nor clear catalysts for bankruptcy

U.S. Internet (Lindsay, Byrd & Sam)

AMZN	M: A strained consumer will lead to more moderate growth in 2009
EBAY	M: Unlikely to see benefits of management's actions in near future due to the very tough macro-environment
GOOG	O: Revenues from new initiatives (GMail, Apps, YouTube) drive continued growth
IACI	M: Still four separate business lines; modest growth compared to peers
YHOO	M: Right Media and Panama are pluses, but loss of DSL subs will hurt
BIDU	O: Market leader in China's high growth paid search sector with sustainable competitive advantages
SOHU	O: Number two web portal in China with sustainable online brand advertising business and leading online games

This Week's Reports (available on Firstcall or bernsteinresearch.com)

- U.S. Media: Cable Networks - Simplicity In A Complicated World; Initiating on Discovery and Scripps Networks 3/23
- Quick Take - DirecTV (DTV): Is the NFL Sunday Ticket Really Still Exclusive? U.S. Wireless '09: A Recipe for Disaster? [Conference Call Transcript] 3/24
- IAC: Check-Up Of Vital Signs Shows First Quarter Performance In Line With Diminished Expectations 3/25
- Time Warner Cable (TWC): Meetings with CFO... Is a Regular Dividend in the Cards by 2010? 3/27

This Week's Rating / Price Target Changes

- DISCA/DISCB/DISCK: Initiated coverage with a \$16.50 Target Price
- SNI: Initiated coverage with a \$25 Target Price
- IACI: Lowered EPS estimates from \$.100 to \$0.58 for 2009E and from \$1.20 to \$0.78 for 2010E
- TWC: Lowered EPS estimates from \$2.90 to \$2.84 for 2009E and from \$3.63 to \$3.57 for 2010E

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Next Week's Calendar

- 3/31/09, 11am ET: U.S. Internet Conference Call: How Are eBay and Amazon Weathering the Downturn?: A Q&A Session With Three Power Sellers

Risks

Risks to media, cable and satellite companies globally include execution, economic and technological. Any economic weakness will hurt the advertising market and these consumer cyclicals. Technological changes will transfer value in to, from and between companies.

Valuation Exhibit 1: U.S. Telecom, Cable & Satellite Valuation Summary (Moffett, Possavino, Del Deo & Pan)

Ticker	SCB Rating	3/26/2009 Price	Target Price	YTD Performance	Prem. (Disc.)	YTD Rel. Perf.	Shs Out.	Mkt Cap (\$ MM)	EV/2008E EBITDA			
									Current Consol	Target Consol	Current Cable/DBS	Target Cable/DBS
CMCSA	O	\$14.55	\$24.00	-14%	65%	-14%	2,061	29,988	5.2x	5.6x	4.2x	5.5x
CVC	O	\$14.13	\$31.00	-16%	119%	-16%	242	3,419	8.0x	10.2x	4.4x	7.0x
TWC	O	\$27.80	\$39.00	0%	40%	0%	352	9,786	4.6x	5.5x	3.9x	5.5x
DISH	M	\$12.12	\$14.00	9%	16%	9%	460	5,576	2.8x	2.1x	2.8x	2.1x
DTV	M	\$23.59	\$23.00	3%	-3%	3%	1,017	23,991	5.3x	6.3x	5.2x	5.4x

Ticker	SCB Rating	3/26/2009 Price	Target Price	YTD Performance	Prem. (Disc.)	YTD Rel. Perf.	Shs Out.	Mkt Cap (\$ MM)	EV/2008E EBITDA		P/FE (2009E)	
									Current Consol	Target Consol	Current Consol	Target Consol
S	M	\$3.91	\$2.00	114%	-49%	114%	2,790	10,909	5.8x	5.9x	-26.8x	-13.7x
T	M	\$26.35	\$27.00	-5%	2%	-8%	5,893	155,281	5.1x	4.7x	13.0x	13.4x
VZ	U	\$30.54	\$27.00	-1%	-12%	-10%	2,841	86,764	4.8x	3.9x	12.9x	11.4x

Valuation Exhibit 2: U.S. Media Conglomerates & Global Advertising Agencies (Nathanson, Borst & Nowak)

3/26/2009	Rating	Target Price	Current Price	Mkt Cap	EPS 2010E	PE 2010E	Rel. PE 2010E	2010E FCF Yield
US Media Conglomerates								
Disney	M	\$24.00	\$19.06	\$35,920	\$1.97	9.7x	90%	11.5%
News Corp.	M	\$8.50	\$7.03	\$18,372	\$0.90	7.8x	73%	19.9%
Time Warner	M	\$10.50	\$8.85	\$32,055	\$0.97	9.1x	85%	14.4%
Viacom	O	\$21.00	\$18.30	\$11,126	\$2.46	7.4x	69%	14.7%
CBS Corp.	U	\$5.00	\$4.71	\$3,155	\$0.88	5.4x	50%	32.5%
Pure-Play Cable Networks								
Scripps Networks Interactive	M	\$25.00	\$23.20	\$3,826	\$1.82	12.8x	119%	9.3%
Discovery Communications	M	\$16.50	\$16.52	\$4,647	\$1.42	11.6x	109%	10.2%
Global Advertising Agencies								
Omnicom	M	\$28.00	\$24.96	\$7,721	\$2.68	9.3x	87%	10.6%
Interpublic	M	\$4.00	\$4.50	\$2,376	\$0.44	10.2x	96%	12.9%
WPP (U.K.)	O	£5.00	£3.85	£4,837	£0.55	7.0x	65%	13.6%
S&P 500 Index			833		\$77.78	10.7x		

Note: News Corp. is FY ended 06/30; Disney is FY ended 09/30; others are CY ended.

Source: Bernstein Estimates and Analysis, First Call

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Valuation Exhibit 3: U.S. Internet (Lindsay, Byrd & Sam)

Company	Rating	3/26/2009 Price	YTD Rel. Performance	Market Cap (\$M)	Target Price	Upside	2009E EPS	2009E P/E
Amazon.com	M	\$73.69	43.7%	31,613	\$60.00	-18.6%	\$2.00	36.8x
eBay	M	\$13.10	-6.2%	16,807	\$15.50	18.3%	\$1.57	8.3x
Google	O	\$353.29	14.8%	111,993	\$400.00	13.2%	\$24.44	14.5x
IAC/InterActiveCorp	M	\$15.86	0.8%	2,212	\$15.00	-5.4%	\$0.58	27.3x
Yahoo!	M	\$13.35	9.4%	18,610	\$13.00	-2.6%	\$0.33	40.5x
Baidu	O	\$186.35	42.7%	6,485	\$170.00	-8.8%	\$6.66	28.0x
Sohu	O	\$42.40	-10.4%	1,611	\$80.00	88.7%	\$4.65	9.1x

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12-Month Rating History as of 03/26/2009**Ticker Rating Changes**

AMZN	M (RC) 12/19/08	O (RC) 08/27/07	
CBS	U (RC) 01/26/09	M (IC) 01/04/06	
CBS/A	U (RC) 01/26/09	M (IC) 01/04/06	
CMCSA	O (IC) 05/29/03		
CVC	O (RC) 03/06/07		
DIS	M (IC) 03/01/05		
DISCA			
DISCB			
DISCK			
DISH	M (RC) 10/10/08	U (RC) 08/20/08	M (RC) 01/04/08
DTV	M (RC) 04/24/08	O (RC) 02/01/08	
EBAY	M (RC) 12/19/08	O (IC) 06/21/07	
GOOG	O (IC) 06/21/07		
IACI	M (IC) 06/21/07		
IPG	M (IC) 03/30/04		
NWS	M (RC) 04/14/08	O (IC) 03/01/05	
NWSA	M (RC) 04/14/08	O (IC) 03/01/05	
OMC	M (RC) 07/07/08	O (IC) 03/30/04	
S	M (IC) 10/17/07		
SNI			
T	M (RC) 01/05/09	O (RC) 06/25/08	M (IC) 10/17/07

TWC O (IC) 03/13/07
TWX M (RC) 02/10/09 O (RC) 12/01/08 M (RC) 09/03/08 O (RC) 09/25/06
VIA O (RC) 01/12/06
VIA/B O (RC) 01/12/06
VZ U (RC) 01/05/09 M (IC) 10/17/07
WPP.LN O (IC) 03/30/04
YHOO M (IC) 06/21/07

Rating Guide: O - Outperform, M - Market-Perform, U - Underperform, N - Not Rated
Rating Actions: IC - Initiated Coverage, DC - Dropped Coverage, RC - Rating Change

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