collective wisdom®
SZABO ASSOCIATES, INC. VOLUME 25, ISSUE 4, DECEMBER 31, 2010

Dear Friends:

As the end of the first decade of the new millennium draws to a close, we anticipate the second with a great sense of optimism for the media industry. An important takeaway from the past few years is a renewed appreciation for the resilience of our dynamic industry, which has navigated through not only one of the worst economic downturns in recent history but also major technological changes that are occurring at a dizzying pace. What fun it will be to speculate about the innovations that the next decade has in store for us!

Szabo was pleased to sponsor lunch at the BCCA Media Credit Seminar on November 16th in New York City. We also had great fun at our annual Szabo holiday party here in Atlanta.

The coming year will be our 40th in business, and we would like to thank our many clients and friends for their continuing loyalty over these many years. All of us at Szabo wish you a wonderful holiday season and a very happy and prosperous 2011.

Robin

Robin Szabo, President
Szabo Associates, Inc.

Growing Pains …

Media Reinvent Themselves in the Digital Age

Reflecting on 2010 as the year comes to a close, media companies can raise a glass and celebrate. Upticks in business indicators hold promise for the future, and the darkest days of the recession are finally slipping into the past.

Much of the hope for renewed profitability depends on media's ability to develop viable alternative revenue streams in the evolving digital era. After a rough period of financial losses and competition with forces of technology, media companies must vigorously explore new delivery channels. Already some innovative strategies are emerging that could reinvigorate the marketplace for years to come.

A Perfect Storm.

The confluence of technological, societal, and economic factors that brought media to this turning point is unprecedented.

The rise of the Internet and advances in technology fundamentally and permanently changed the way society consumes information. We are now an "on-demand" society, able to retrieve content that is individually meaningful to us—when, how, and where we want it. People are no longer strictly loyal to one news organization. Rather, they "graze" instead, getting news and entertainment online and offline from a variety of platforms.

Advertisers and marketers have been quick to follow their customers, shifting their resources accordingly. Traditional media were slower to embrace the change, and after a few years of steadily declining advertising dollars and audiences, found themselves scrambling to catch up.

Then, in 2007, the economy crashed. The downturn hammered virtually every business sector across the country. The media industry suffered enormous losses. The future seemed bleak.

In the last half of 2010, however, most media sectors are seeing the beginnings of an upturn. Overall ad spending in broadcasting, cable, radio and some magazines is up 2.5 to 4 percent. Print newspaper is the only media segment posting continuously lower market share in ad revenue.

Television Rebounds Strongly.

The forecast for television is bright. Charlottesville, VA-based media researcher SNL Kagan projects total television station revenue (including online) will reach $25.4 billion by 2016, after bottoming out in 2009 at $17.3 billion, its lowest level since 1995. Online revenues are projected to increase to 7 percent in 2013 from 1 percent in 2006. The even-year phenomenon of political ad spending catapulted the recovery, with help from the return of automotive advertising and growing contributions of retransmission fees. SNL Kagan expects those fees to account for

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9 percent of a television station's overall revenue in three years, up from a 1 percent share in 2006.

Retransmission agreements are emerging as a promising revenue stream for broadcast television that could lower its dependence on advertising. A contentious issue, retransmission consent calls for cable and satellite operators to pay broadcast groups for the right to carry local television stations and their programming.

The recent settlement of an ugly fight between News Corporation's Fox Networks and Cablevision Systems may put broadcast groups in a prime position to fatten their pockets with increasingly large retransmission fees. The two companies argued over the financial terms of their retransmission consent agreement in New York. Fox won. Cablevision has to shell out nearly triple its transmission fees to Fox over the next five years. Cablevision will now pay 55 cents per subscriber in the first year, with the amount rising to $1 by the fifth year of the contract.

Television executives are also focusing on emerging opportunities in the interactive and technology realms. In fact, every segment of the media industry is exploring the vast potential of mobile delivery. The ubiquitous use of mobile devices represents an untapped frontier in digital marketing, which is projected to be a $5 billion mobile ad spend by 2015.

Radio Gets Boost from Digital.

Radio is bouncing back quickly after 2009's dismal returns. According to 2010 Q3 numbers, total advertising revenues were up about 6 percent to $12.7 billion. Local advertising revenue increased 3 percent to $2.97 billion in the third quarter, while national jumped 10 percent to $700 million. But the biggest boon came from online advertising revenues, which jumped 23 percent to $163 million.

Digital radio is gaining more and more traction in the radio arena. Clear Channel Radio recently introduced "iHeartRadio," a mobile app that offers users access to streaming audio from over 750 radio stations, websites and digital channels maintained by the media giant. Clear Channel partnered with Toyota to make iHeartRadio a standard factory-installed feature in vehicles beginning next year.

The radio industry is hoping to generate new revenue with mobile radio subscriptions. Trends in audience behavior suggest that people are more likely to pay for content they get on their cell phones than on their computers. Radio industry leaders are currently pushing for legislation that would require cell phone manufacturers to include AM/FM capabilities in their devices.

Cable Benefits from Multiple Revenue Streams.

The one media sector that didn't spiral downward financially in 2009 was cable. Subscriber numbers have been gradually dropping over time, but cable companies are compensating by upgrading the remaining subscribers to more expensive digital tiers, as well as adding broadband and phone subscribers. Cable networks' revenues depend on both advertising sales and fees-per-subscriber, and although advertising revenue was flat in 2009, subscriber numbers remained steady and profits actually rose 9 percent.

The cable industry's investment over the last few years in high-speed broadband networks provides a little extra security. Subscribers may "cut the cord" on traditional cable to get their video online, but are still likely to pay the cable company for Internet access to the video that streams to their televisions. Traditional cable customers would likely pay higher monthly fees to offset operators' retransmission contracts with broadcast networks. By 2019, cable could grow into a $55.1 billion industry, according to SNL Kagan predictions.

Print Media Seek Solid Ground.

After a couple of rocky years, magazines are now enjoying a modest increase in their advertising numbers. The third quarter of 2010 reported a 3.6 percent growth in ad pages across the sector, up .8 percent over last quarter, which was the first period showing an increase since late 2007. The increase skews toward lifestyle magazines, while newsweeklies continue their downward slide.

Print media still suffer, however. The first half of 2010 shows consistently declining ad revenue. According to the Newspaper Association of America (NAA), print advertising revenue dropped 28.6 percent in 2009 to $24.82 billion. Classified ads, once newspapers' bread and butter, plunged 70 percent between 2000-2009, from $19.6 billion to an estimated $6 billion. Though experts speculate that classified advertising will never again contribute as robustly to either print or online publications, it has recovered slightly in 2010 as normal buying patterns reemerge.

Numerous ideas for generating revenue are being batted around the industry, but none is quite as controversial as paywalls. Newspapers and magazines are testing online paywalls that require users to pay a subscription fee for access to their content. It's not a new idea; many newspapers, including the New York Times (NYT), have initiated—and later ended—a tryst with paywalls. (NYT recently announced it will take another stab at paywalls in 2011.) Many question its viability as a fruitful revenue stream, arguing that readers will not pay for news when they can get the same information free elsewhere on the Internet.

"Repurposing" of content is also proving to be a shot in the arm for print media. One successful model is *Real Simple* magazine, which has created profitable new revenue streams by supplementing its traditional hard-copy format with a sophisticated online presence. *Real Simple* repurposes magazine content for free, using its website to promote email-based newsletters, branded books and merchandise, event sponsorships, and radio and television programming.

Overcoming the Obstacles.

As with any major industry change, the challenges that interactive advertising poses to all parties involved are numerous and substantial. For media outlets' sales and finance departments, interactive advertising adds a new wrinkle to already complicated multimedia ad buys. Because all interactive advertising platforms are in their infancy, the industry has not yet established standardized performance and measurement guidelines. The current buying and selling process is inconsistent and confusing.

Many automated systems are not equipped to manage the complexities of today's multimedia campaigns. Outdated billing technology, unstable performance measurements, and unfamiliar terminology cause problems internally as well as with advertisers and agencies. Media outlets need new solutions to billing issues if they are going to maximize the potential revenue stream of interactive advertising.

"When the Boss told you to look into developing new revenue streams through Internet advertising, I don't think this is what he had in mind."

The growth of digital advertising has further complicated the legal battle over payment liability. Interactive agencies and advertisers are likely to adopt new standardized sequential liability practices advocated by the Interactive Advertising Bureau (IAB) and the American Association of Advertising Agencies (4A's). Pushing back to maintain joint and several liability puts media outlets in a precarious position, caught between their dual needs for advertising dollars and financial protection. If they cave to pressure from the interactive side, how can they hold the line for joint and several liability with traditional advertisers?

Mobile advertising, with its attendant layers of complexity, begs many questions for media regarding revenue streams. Who should be the main beneficiary of mobile advertising—the phone company or the content provider? Is the mobile device primarily another delivery system with retransmission fees in order? How should web impressions, click-throughs, and other direct response measures be counted and evaluated? As technology and "rich media" advertising—which expands in interactive content when users click on the initial ad—continue to evolve, how should the unique attributes of the mobile device be used to measure effectiveness? Although many sources of mobile advertising metrics—ad management companies, analytics groups, and trade associations—are entering the field, no industry consensus on measurement variables yet exists, let alone how they can be audited and verified.

Charging Forward.

Media credit and collection managers are facing new and complex challenges that begin

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with credit policy and end with collection procedures. Credit policy that was adequate for traditional advertisers must be adapted to accommodate new media and new revenue streams. New links in the chain of responsibility for ad creation, placement, and evaluation in the form of new media specialists and agencies add to the already complex issue of payment liability. Unfamiliar players are entering the field at a staggering rate, requiring an even higher degree of due diligence.

Conflicting payment liability positions also necessitate reevaluation of current terms and conditions. Media properties must decide whether to hold a consistent joint and several liability position with interactive advertisers or to concede to the sequential liability position recommended by the interactive trade and agency associations.

Finally, credit and collection managers need to actively stay abreast of developments within the interactive advertising community. Rapid-fire advancements are being made in all areas of this new technology, including metrics that will drive rates and billing systems.

In light of the new economic realities and the rapidly evolving interactive landscape, media are working hard to diversify product offerings and transform outdated business models. More and more companies are recognizing the enormous revenue potential in cross-leveraging their products across a variety of platforms. While some experiments will fail and others succeed, all will contribute to creating new opportunities for media properties to be dynamic and influential players in a digital world. ♦

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Media Collection Professionals,
3355 Lenox Rd., Suite 945, Atlanta, Georgia 30326
Tel: 404/266-2464, Fax: 404/266-2165
Web site: www.szabo.com
e-mail: info@szabo.com

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