

# Research Notes

2Q 2010

Actionable Research on the Broadband, Media & Entertainment Industries

## One Bad Apple

**O**n June 22, 2010, Apple announced that it had sold its three millionth iPad just 80 days after the product was introduced in the US. This represents a far faster launch than that of the iPhone, which took 74 days to reach one million iPhones sold. The iPhone has certainly picked up steam over the past three years. In the most recent quarter

alone, Apple reported that 8.75 million iPhones were sold worldwide, as well as 10.89 million iPods.

Apple's recent success with the iPod, iPhone, and iPad is undeniable, but even Apple has its blemishes. One is Apple TV.

On March 21, 2007, Apple proudly announced that "Apple TV is Now Shipping."

The press release stated that "Apple TV is like a DVD

player for the Internet age – providing an easy and fun way to play all your favorite iTunes content from your PC or Mac on your widescreen TV." About ten months later, on January 15, 2008, Apple announced a price reduction for Apple TV to \$229, along with new software that provided the ability to rent movies directly from a widescreen TV. Apple CEO Steve Jobs is quoted in the press release saying,

*"With the new Apple TV and iTunes Movie Rentals, movie lovers can rent DVD-quality or stunning HD movies from their couch with just a click of a button... No more driving to the video store or waiting for DVDs to arrive in the mail."* **Clearly, Jobs and Apple believed that Apple TV was a viable product, but in the more than 1,000 days since Apple TV was introduced, there has been no triumphant announcement of the one millionth Apple TV sold** (that I can find) similar to the iPad or iPhone.

In the three years since the launch of Apple TV, the product has gone from "a DVD player for the Internet age" to a self-described "hobby" for Steve Jobs and Apple. Speaking at a recent conference, Jobs said, *"The problem with innovation in the television market is the go-to market strategy. The television industry fundamentally has a subsidized business model that gives everybody a set-top box for free, or for \$10 a month, and that pretty much squashes any opportunity for innovation, because no one is willing to buy a set-top box... A lot of people have tried. They've all failed."*

**While it may be a convenient excuse to spin the blame for the lack of success of Apple TV on cable, satellite and Telco TV providers, the business models of the multi-channel video industry were firmly in place when Apple enthusiastically designed and**

### In this issue:

- One Bad Apple
- 1.7 Million Added Multi-Channel Video Services Over the Past Year
- 1.4 Million Added Broadband in the 1<sup>st</sup> Quarter of 2010
- U.S. Broadband Subscribers are Satisfied with Their Service
- Industry by the Numbers

**launched the product.** Now that Apple TV has floundered, Jobs says, *“The only way that’s ever gonna change is if you can really go back to square one and tear up that set-top box and redesign it from scratch with a consistent UI across all these different functions and get it to the consumer in a way that they are willing to pay for it, and right now there is no way to do that... That’s the problem with the TV market... it’s not a problem with technology, it’s not a problem of vision, it’s a fundamental go-to market problem.”*

### Did you know?

94% of U.S. households with annual household incomes > \$50,000 are online at home – compared to 52% with annual incomes < \$30,000

Help with this “market problem” and the ability to start from scratch may come from all places, the Federal Communications Commission’s National Broadband Plan (NBP). While it is a stretch to ascertain how this actually fits into a significant part of a plan for the future of high-speed Internet

*Right now, most people still turn to the Internet for video content distinct from television. Online video remains dominated by short-form content like YouTube videos, says Bruce Leichtman, the president of Leichtman Research Group. Data suggest that people see online viewing as a supplement -- not a substitute -- for traditional TV-watching, Leichtman says.*

- **Smart Money**  
May 13, 2010

in the US, Recommendation 4.12 of the National Broadband Plan states: *“The FCC should initiate a proceeding to ensure that all multichannel video programming distributors (MVPDs) install a gateway device or equivalent functionality in all new subscriber homes and in all homes requiring replacement set-top boxes, starting on or before Dec. 31, 2012.”*

**Is it truly necessary to regulate the overhaul of multi-channel video providers’ set-top boxes under the auspices of improving broadband in America?**

The core of the justification for this recommendation is because *“retail set-top boxes have been competing on an uneven playing field.”* The NBP notes that, *“Without the ability to integrate Internet video with traditional TV viewing, Internet video devices like Apple TV and Roku have struggled to gain a foothold in U.S. homes.”* This statement is related to footnote 113, which states that *“estimated share of US households with Apple TV or Roku is 1%. Letter from Bruce Leichtman, President, Leichtman Research Group (LRG).”*

While the data are from me, the interpretation is not mine at all. From my perspective, the data demonstrate the lack of market demand for these types of stand-alone devices. **I do not believe that the struggle for Apple TV and others to gain a foothold in US households is due to a roadblock in integrating Internet video with traditional TV viewing. Rather,**

**Apple TV lacks a unique selling proposition that takes consumers from awareness to interest and purchase.**

(This is a classic Marketing 101 example of a failed product rollout.)

While the consumer market is not demanding a fundamental redesign of multi-channel video providers' set-top devices, **if the cost of the NBP's Recommendation 4.12 is to be paid for by consumers, it will fall disproportionately on the shoulders of those who can least afford it.** A recent nationwide LRG study found that individuals in households with annual incomes under \$30,000 were three times more likely to have moved in the past year than those in households with annual incomes over \$75,000. These movers will be among the new subscriber homes "requiring replacement set-top boxes" whether they want them or not.

Apple (along with Roku, TiVo, and other stand-alone device manufacturers) knew, or should have known, exactly what they were getting into when they entered the market. The same is true for Google, which is now attempting to enter the business. Other companies, like Netflix, have successfully built and enhanced their video business with the same "roadblocks" in place. Netflix's "watch instantly" feature essentially established what Jobs described that Apple TV would do in the aforementioned 2008 press release.

**Did you know?**

Households with incomes < \$30,000 account for 41% of non-subscribers to multi-channel video services

The success of Apple's iPod, iPhone, and now iPad, demonstrates that consumers will purchase products and services that meet their needs. Apple TV remains Steve Jobs' hobby because consumers have not seen the value in the product given other alternatives.

**1.7 Million Added Multi-Channel Video Services Over the Past Year**

Leichtman Research Group, Inc. (LRG) found that the largest cable, satellite, and Telco TV providers in the US acquired over 1.7 million net additional multi-channel video subscribers over the past year. While the top ten cable companies cumulatively lost about 1.4 million cable TV subscribers in the year-long period through the end of the first quarter of 2010, these losses were more than offset

by a gain of 1.33 million satellite TV subscribers (from DirecTV and Dish Network), and 1.78 million subscribers to Telco TV services (from Verizon FiOS and AT&T U-verse). In the first quarter of 2010 alone, the multi-channel video industry as a whole added about 580,000 subscribers.

New consumer research from LRG complements these figures:

- In areas where cable TV is available, 89% of households with a TV set subscribe to some form of multi-channel video service – an all-time high

- In areas where cable TV is available, 66% of multi-channel video subscribers get cable – compared to 79% in 2004
- The mean annual household income of multi-channel video subscribers (where cable is available) is 59% higher than that of non-subscribers
- Just 1% of current non-subscribers to a TV service do not subscribe because they can watch all that they want on the Internet or in other ways. None of these non-subscribers reported dropping a video service in the past year
- 11% of satellite TV subscribers, 9% of cable TV subscribers, and 5% of Telco TV subscribers are likely to switch from their current provider in the next six months – figures that are similar to previous surveys
- Less than 1% of cable subscribers who are likely to switch mention getting all the programs they want on the Internet or in other ways as a reason for potentially switching

These findings are based on a telephone survey of 1,600 randomly selected households throughout the United States, and are part of a new LRG study, *Cable, DBS, & Telcos: Competing for Customers*.

The number of US households subscribing to some form of multi-channel video service is at an all-time high. Multi-channel video industry gains will likely be slower in the coming year than they were in the past year, due to the saturated market, coupled with tepid new housing growth, and a slowdown in the rollout of Telco TV

In the last year, the nation's largest TV providers added more than 1.7 million new video customers, suggesting that cord cutting is not a trend, according to fresh research from Leichtman Research Group ...

The research firm analyzed official data from cable, satellite and telephone companies and found that *while the nation's ten largest cable operators lost more than 1.4 million video customers during the last year, satellite operators and telcos added more than 3 million new customers for an overall net gain.*

- [ABCNews.com](http://ABCNews.com)  
June 23, 2010

services. Consumers' decisions to disconnect from multi-channel video services to only watch video from other sources are unlikely to have a substantial impact on the market in the near-term.

## 1.4 Million Add Broadband in the First Quarter of 2010

Leichtman Research Group, Inc. found that the nineteen largest cable and telephone providers in the US – representing about 93% of the market – acquired over 1.4 million net additional high-speed Internet subscribers in the first quarter of 2010. These top broadband providers now account for over 73 million subscribers -- with cable

companies having 40.2 million broadband subscribers, and telephone companies having nearly 32.9 million subscribers.

*With or without governmental help, more Americans continue to add high-speed Internet service.*

*Leichtman Research Group Inc. found that the 19 largest cable and phone providers in the U.S. -- which together represent about 93 percent of the market -- added more than 1.4 million net additional broadband subscribers in the first quarter of 2010.*

**- The Capital Times**  
May 13, 2010

Other broadband findings for the quarter include:

- The top cable companies added over 915,000 subscribers, representing 65% of the net broadband additions for the quarter versus the top telephone companies
- Overall, broadband additions in 1Q 2010 amounted to 86% of those in 1Q 2009 -- with cable having 108% as many additions as a year ago, and Telcos 63% as many additions as a year ago
- The top cable broadband providers have a 55% share of the overall market, with a 7.3 million subscriber advantage over the top telephone

### Did you know?

Major US broadband providers added nearly 39 million subscribers over the past five years

companies – compared to 6.4 million a year ago

Net broadband additions in 1Q 2010 were over 500,000 more than in 4Q 2009, and the most since the first quarter of 2009. Cable providers had a particularly strong quarter. With more than 900,000 net broadband additions, the top cable companies combined to have their best quarter since 1Q 2008.

## U.S. Broadband Subscribers are Satisfied with Their Service

New consumer research from Leichtman Research Group, Inc. (LRG) finds that 71% of US broadband Internet subscribers are very satisfied with their current Internet service at home (rating satisfaction on 8-10 on a 10-point scale), while just 3% are not satisfied (rating satisfaction 1-3).

In addition, while 77% of broadband subscribers do not know the download speed of their Internet service at home, they are generally pleased with the speed of their Internet connection. Overall, 66% of broadband subscribers rate the speed of their connection 8-10, and 6% rate it 1-3.

These findings are based on a telephone survey of 1,600 randomly selected households from throughout the United States and are part of a new LRG study, *Broadband Access & Services in the Home 2010*. This is LRG's eighth annual study of this topic.

Other related findings include:

- At the time of the survey, over 70% of US households subscribed to a broadband service – compared to 20% in 2004
- 26% of broadband subscribers are very interested in receiving faster Internet access at home than they currently receive (rating interest 8-10 on a 10-point scale), while 44% are not very interested (rating interest 1-3)
- 17% of broadband subscribers say that there is not another high-speed Internet provider in their area. In urban and suburban areas, 11% of broadband subscribers say that there is not another high-speed Internet provider in their area – compared to 34% of subscribers in rural areas
- Of all Internet subscribers, 3% say that broadband is not available in their area. In rural areas, 8% of online households say that broadband is not available in their area – compared to 1% in urban and suburban areas

- Overall, 1.4% of all households are interested in getting broadband, but say that it is not available in their area
- Less than 1% of all households are interested in getting broadband, but cite cost as a reason for not currently subscribing to broadband.

*More than 70 percent of U.S. broadband customers are happy with their overall service, ranking it between 8 and 10 on a 10-point scale, according to Leichtman Research Group. A mere 3 percent scored their service with a 3 or less on the recently conducted survey, while just 26 percent said they're "very interested" in receiving faster speeds at home. In other words, big, bold fiber efforts, such as Verizon's FiOS, aren't yet supported by consumer demand.*

**- Business Week**  
June 22, 2010

In just the past six years about half all US households have begun subscribing to a broadband Internet service. During this period of rapid growth, consumers have remained very satisfied with their broadband service at home.

## Industry by the Numbers – (as of the end of 1Q 2010)

### Top 10 Cable MSOs in the U.S.

	Passings	Subscribers	Availability	Penetration	Net Adds in 1Q 2010	Net Adds in 1Q 2009
Basic Cable	116,900,000	55,520,000		47.5%	(155,000)	(35,000)
Digital Cable*		41,180,000		74.2%	785,000	600,000
Broadband Internet**	115,700,000	39,880,000	99%	34.5%	925,000	850,000
Telephone***	107,500,000	20,235,000	96%	18.8%	570,000	735,000

Sources: The Companies and Leichtman Research Group, Inc.

Totals include LRG estimates and pro forma results from system sales and acquisitions.

\* Digital penetration of Basic subscribers; among the top MSOs, digital cable is now available to essentially 100% of basic subscribers

\*\* Internet data does not include RCN

\*\*\* Telephone data does not include Bright House Networks

### Telco Video

	Subscribers	Net Adds in 1Q 2010	Net Adds in 1Q 2009
Verizon FiOS	3,029,000	168,000	299,000
AT&T U-verse	2,296,000	231,000	284,000
<b>Total</b>	<b>5,325,000</b>	<b>399,000</b>	<b>583,000</b>

Sources: The Companies and Leichtman Research Group, Inc.

### DBS

	Subscribers	Net Adds in 1Q 2010	Gross Adds in 1Q 2010	Subscriber Acquisition Cost*	Average Revenue Per Sub/Month**
DIRECTV	18,660,000	100,000	925,000	\$768	\$85.47
Dish Network	14,337,000	237,000	833,000	\$741	\$71.18
<b>Total DBS</b>	<b>32,997,000</b>	<b>337,000</b>	<b>1,758,000</b>		

Sources: The Companies and Leichtman Research Group, Inc.

\* Includes leased equipment and unreturned box costs

\*\* Includes revenue from commercial accounts and other non-consumer spending

## Top Broadband Internet Providers in the U.S.

Broadband Internet Provider	Subscribers at the end of 1Q 2010	Net Adds in 1Q 2010
<b>Cable</b>		
Comcast	16,329,000	399,000
Time Warner	9,510,000	221,000
Cox*	4,250,000	50,000
Charter	3,166,000	103,700
Cablevision	2,610,000	42,000
Mediacom	804,000	26,000
Insight	516,300	14,800
Cable One	405,311	12,479
RCN	315,000	3,000
Other Major Private Companies**	2,289,000	55,000
<b>Total Top Cable</b>	<b>40,194,611</b>	<b>926,979</b>
<b>Telephone Companies</b>		
AT&T	16,044,000	225,000
Verizon	9,310,000	90,000
Qwest^	2,852,000	40,000
CenturyLink	2,306,000	70,000
Windstream	1,167,900	35,800
Frontier	644,060	8,113
FairPoint*	295,000	0
Cincinnati Bell	247,600	3,600
<b>Total Top Phone</b>	<b>32,866,560</b>	<b>502,513</b>
<b>Total Broadband</b>	<b>71,061,171</b>	<b>1,429,492</b>

Sources: The Companies and Leichtman Research Group, Inc.

\* LRG estimate

\*\* Includes LRG estimates for Bright House Networks and Suddenlink

^ Qwest now excludes business and wholesale market customers from broadband subscriber totals

Totals reflect pro forma results from system sales and acquisitions

Company subscriber counts do not include wireless broadband service

Company subscriber counts may not represent solely residential households

## U.S. Residential Telephone Lines – Gains and Losses

	1Q 2009	2Q 2009	3Q 2009	4Q 2009	1Q 2010
Telco Net Adds*	(1,753,000)	(1,772,000)	(1,872,000)	(1,520,000)	(1,367,000)
Cable Net Adds	735,000	525,000	625,000	530,000	570,000

Sources: The Companies and Leichtman Research Group, Inc.

\* Retail residential phone lines include both primary and additional lines, but do not include wholesale lines  
Includes LRG estimates and some results adjusted from prior reports



# LRG

Leichtman Research Group

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**Leichtman Research Group, Inc.**

3 Ellison Lane

Durham, NH 03824

(603) 397-5400

(603) 397-5410 (Fax)

[www.LeichtmanResearch.com](http://www.LeichtmanResearch.com)

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