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# PAY TV: STRUGGLE FOR RELEVANCE

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VALUE PARTNERS

**Pay TV:**
**Struggle for relevance**

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Pay TV operators struggle to differentiate themselves in a harsh and competitive environment. Small and medium-sized operators are overwhelmed as they try to keep up with the special offers of big players and all of the market has to come to terms with the rising cost of premium content.

# EXECUTIVE SUMMARY

The Pay TV business model is challenged by new technologies and business models emerging in content delivery. In the largest Pay TV market, the USA, despite a mature market and slowly diminishing subscriber base, consolidation is driving growth for larger players. DirecTV, a US satellite Pay TV company is a success story, due to its continued success in gaining a larger share of the market.

The key challenge to existing Pay TV business models comes from subscription video on demand (SVoD) services. SVoD key drivers are demographics, content, media habits, technology, and customer behaviour.

Young and prosperous demographics are more likely to adopt SVoD. SVoD specializes mostly in TV shows and movies, which make up almost half of the viewing time. Media habits are evolving, as streamed content, connected TV technology and binge watching come together to create a new experience in media consumption. Increasing broadband penetration and the ubiquity of mobile devices are the main technological drivers that support SVoD business. The last but most important driver is the higher customer satisfaction and convenience factor that shapes customer behaviour as evidenced by net promoter scores that are three times those of pay TV.

The Turkish Pay TV market is marked by modest penetration levels and a levelled-off subscription base that is typical of a mature market. Turkish pay TV does not attain its expected potential due to free key content, macro factors, content infringement and football losing its appeal.

Looking forward, Pay TV operators can employ a dual infrastructure model, engage in partnerships, provide over-the-top content services or outsource the services. Regardless of the strategy employed, Pay TV operators must adapt to changes to stay relevant, or ideally innovate their businesses to lead the change.

# INTRODUCTION

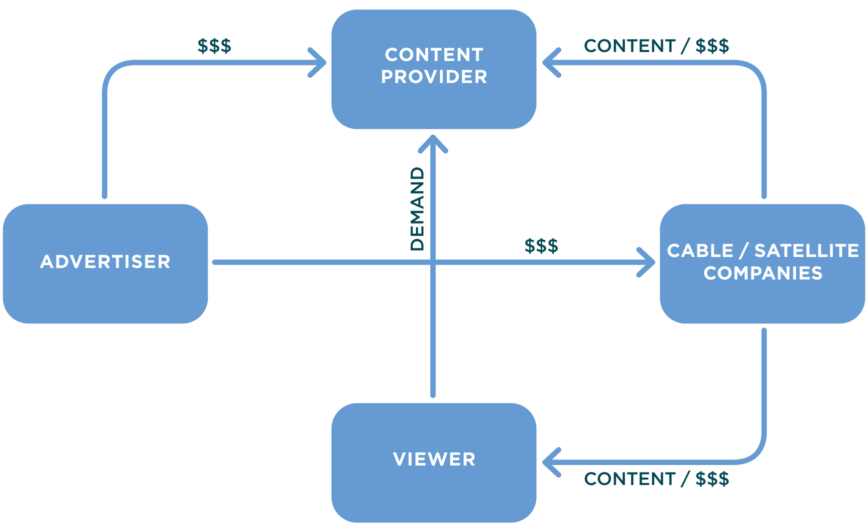
Pay TV, also known as premium or subscription TV, may be defined as television broadcasting paid for by the end user. Typically, viewers who wish to avail the services of the Pay TV operator make monthly payments for their subscription to a particular channel or group of channels. These channels are typically not available without the subscription, although public channels are usually included in the delivered content package. Pay TV historically began with satellite broadcasting, and further developed with the proliferation of cable infrastructure in urban areas.

For simplicity, the television business may be divided into two parts: production and delivery. Traditionally, content creation, production and aggregation is handled by content providers. Pay TV providers deliver the content to viewers, and provide them with services and goods that revolve around this.

The core difference between production and delivery is that Pay TV service providers are focused on the front end of the content business. In other words, they own the relationship with the customer base to which they serve the content. Thus Pay TV operators have two main revenue streams; advertisement revenues and subscription fees. They also charge sub-fees for any additional services and devices they provide in order to support main revenue streams.

Content providers, on the other hand, have a product that they "were" not interested in selling directly to the viewer. They relied on advertisement revenues until ESPN discovered a new revenue stream in 1987 to boost its struggling financial streams, namely affiliate fees.

**EXHIBIT 1**
**Pay TV business structure**



# PAY TV MARKET IN US

The United States is the most prominent Pay TV market, accounting for more than a third of global pay TV revenues in 2016. The first subscription cable TV emerged in 1949 and with the advent of satellite services, the market enjoyed growth until 2010. As Exhibit 2 demonstrates, the rate of decline in Pay TV subscriber growth has been following a steady pattern. The market has been shrinking in terms of the number of subscribers at an increasing pace since the beginning of 2013. This phenomenon may be attributable to longer contract terms put in place in to consolidate customer base in Pay TV.

Today, different business models and players with different backgrounds abound in the market. Cable operators like Comcast and Charter, phone companies like AT&T and Verizon, satellite companies like DISH provide Pay TV service to over 94 million households in US.

In the US Pay TV market, the limited subscriber growth also reflects the penetration levels. As evidenced by Exhibit 3 (next page), penetration is in steady decline in the US market. Over the period Q1 2014 to Q3 2016, the penetration level receded by 3% in absolute terms. The decline in penetration levels may be attributable to SVoD.

**EXHIBIT 2**
**Pay TV subscriber growth in US**

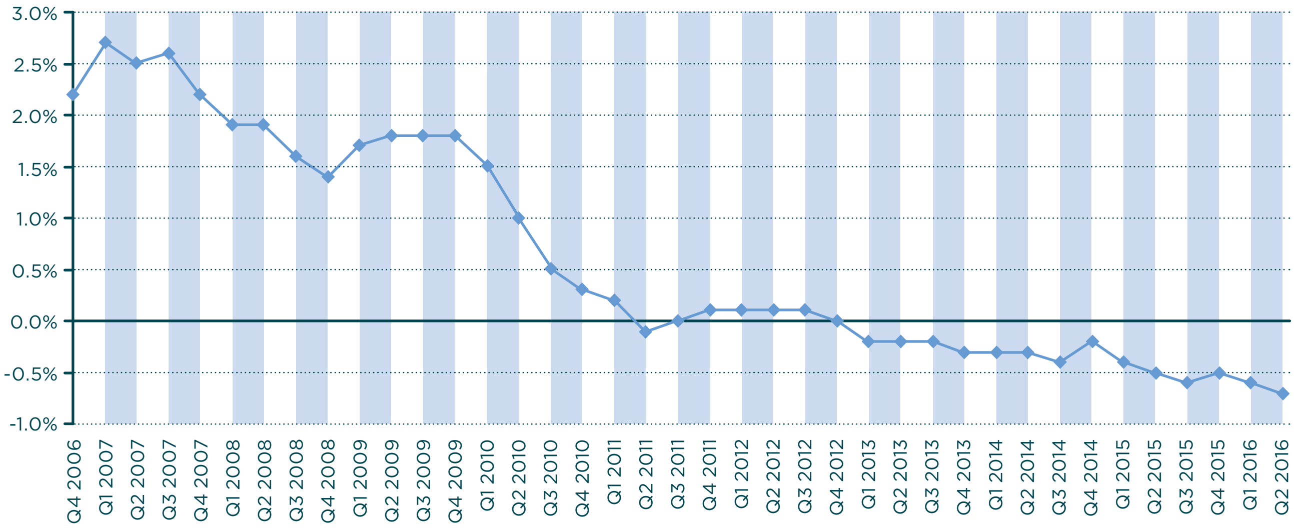


**EXHIBIT 3**
**Penetration and change in penetration in bps in US**

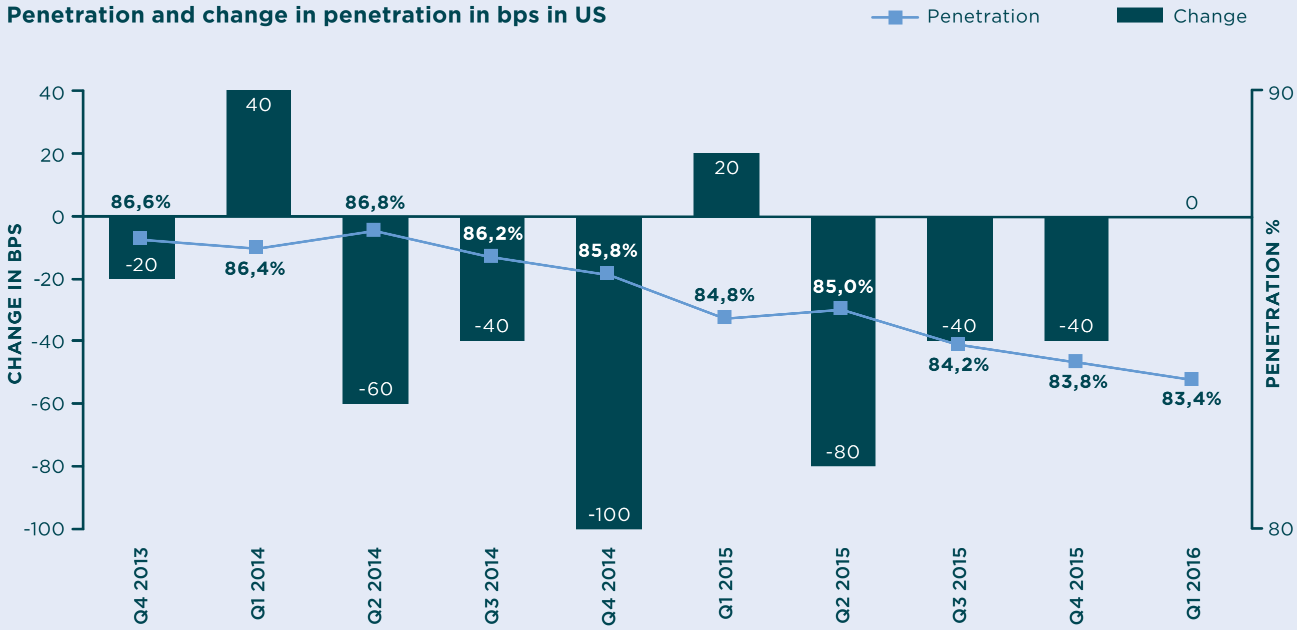



**EXHIBIT 4**
**Quarterly Pay TV subscriber change in US**

| PAY-TV PROVIDERS | 2015 SUBSCRIBERS AT THE END OF 4Q | 2016 SUBSCRIBERS AT THE END OF 1Q | 2016 NET ADDS IN 1Q |
|---|---|---|---|
| **CABLE COMPANIES COMCAST** | | | |
| Comcast | 22.347.000 | 22.400.000 | 53.000 |
| Time Warner Cable | 11.035.000 | 11.056.000 | 21.000 |
| Charter | 4.430.000 | 4.445.000 | 15.000 |
| Cablevision | 2.594.000 | 2.579.000 | -15.000 |
| Suddenlink | 1.093.000 | 1.085.000 | -8.000 |
| Mediacom | 855.000 | 853.000 | -2.000 |
| Cable One | 364.150 | 350.579 | -13.571 |
| Other major private companies* | 6.345.000 | 6.345.000 | 0 |
| **Total Top Cable** | **49.063.150** | **49.113.579** | **50.429** |
| **SATELLITE TV COMPANIES (DBS)** | | | |
| DirecTV | 19.784.000 | 20.112.000 | 328.000 |
| DISH^ | 13.897.000 | 13.874.000 | -23.000 |
| **Total DBS** | **33.681.000** | **33.986.000** | **305.000** |
| **PHONE COMPANIES** | | | |
| Verizon FiOS | 5.827.000 | 5.863.000 | 36.000 |
| AT&T U-verse | 5.640.000 | 5.260.000 | -380.000 |
| **Total Top Phone** | **11.467.000** | **11.123.000** | **-344.000** |
| **Total Top Pay-TV Providers** | **94.211.150** | **94.222.579** | **11.429** |

| PAY-TV PROVIDERS | 2015 SUBSCRIBERS AT THE END OF 2Q | 2016 NET ADDS IN 2Q |
|---|---|---|
| **CABLE COMPANIES COMCAST** | | |
| Comcast | 22.396.000 | -4.000 |
| Charter | 17.312.000 | -143.000 |
| Altice | 3.639.000 | -25.000 |
| Mediacom | 842.000 | -11.000 |
| Cable One | 338.974 | -11.602 |
| Other major private companies* | 4.330.000 | -30.000 |
| **Total Top Cable** | **48.857.974** | **-224.602** |
| **SATELLITE TV COMPANIES (DBS)** | | |
| DirecTV | 20.454.000 | 342.000 |
| DISH^ | 13.593.000 | -281.000 |
| **Total DBS** | **34.047.000** | **61.000** |
| **PHONE COMPANIES** | | |
| Verizon FiOS | 4.637.000 | -41.000 |
| AT&T U-verse | 4.869.000 | -391.000 |
| Frontier | 1.340.000 | -70.000 |
| **Total Top Phone** | **10.846.000** | **-502.000** |
| **Total Top Pay-TV Providers** | **93.750.974** | **-665.602** |

The subscriber figures of top Pay TV providers must be analysed to understand the trend of Pay TV market in depth. The preceding figures show that the Pay TV market is shrinking at an increasing pace, and company data show that the market is consolidating. Larger cable companies such as Comcast, Time Warner and Charter gained ground in the first quarter of 2016, while smaller players lost ground. Satellite TV Companies show a similar trend for the same period, with DirecTV gaining ground and the relatively smaller Dish subscriber base declining in modest terms. A similar trend is also valid for phone companies: AT&T U-verse lost many subscribers in the same period, both absolutely and in percentage terms. It can be inferred that AT&T follows a voluntary attrition strategy to phase out U-verse after its acquisition of DirecTV.

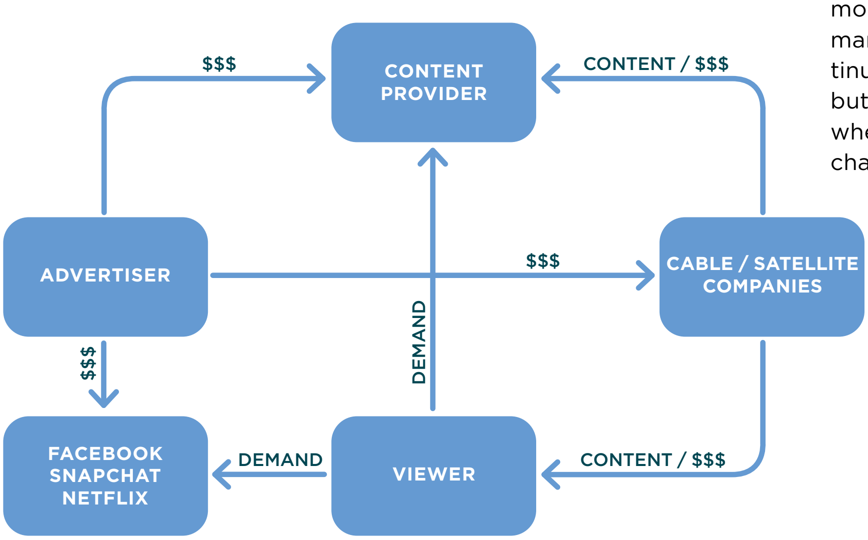
The second quarter of 2016 shows us that while experiencing overall decline in subscriptions, Pay TV is consistently successful in its consolidation cycle: DirecTV.

Second only to Comcast in terms of subscriber base, DirecTV has continued success in consolidating the market with its services. The second quarter also marks the changing landscape in Phone Company play in pay TV: on April 1 2016, Verizon services in California, Florida and Texas moved to the Frontier network.

US Pay TV operators face declining advertisement revenues with the advent of SVoD and social media. Viewer demand for content is split between Pay TV, user-created content and SVoD. In parallel with the shift in consumer demand for different channels, the advertising budget is split further to accommodate the new channels for media consumption. Social media offer more flexibility and potential to get the advertisers' message across to a more specific group of people and allows the customization of the proposal.

Due to the digital nature and feedback mechanisms, advertisements on internet are easier to quantify for returns than other media. Initial trend of overemphasis on social media advertising for early adopters has receded, but such new channels are utilized in balance with more traditional channels by marketing managers. Pay TV companies will continue to receive advertising revenues, but should consider premium packages, where there is no advertisement in paid channels and user interface.

**EXHIBIT 5**
**Pay TV new structure**



# SUBSCRIPTION VIDEO ON DEMAND: A DISRUPTIVE TREND ENABLED BY TECHNOLOGY

Subscription video on demand, SVoD, is a service business model where viewers are charged a monthly subscription fee to gain access to programmes. Viewers are able to watch TV series and block-buster movies without programming. The offer enables access to any content, made available through the system, at will by the consumer.

SVoD service providers have grown rapidly in markets where broadband connection is almost ubiquitous. The three biggest SVoD services increased their US subscriber base by 440% in five-year period, increasing from 24.4 million to 107.7 million between 2010 and 2015. The average YoY growth of 88% observed in this period cannot be met in 2016 and onwards as high penetration level makes it impossible to grow at these levels.

Today SVoD penetration has reached 50% in US TV households, equal to the penetration of DVR. Room to grow for SVoD is limited by broadband penetration; almost 2 out of 10 US TV households still do not have access to broadband. SVoD can grow a further 60% whereby it is constrained by current broadband penetration.

It is crucial to analyse key drivers of growth in SVoD subscribers in order to understand fully if SVoD services are a real threat for the Pay TV business.

Key drivers of growth in SVoD subscriptions are:

- Demographics
- Content
- Media habits
- Technology
- Customer Behaviour

**EXHIBIT 6**
**Three SVoD service provider subscriber change in five years, 2010-2015**

| | | SUBSCRIBERS (2015) | GROWTH (SINCE 2010) |
|---|---|---|---|
| NETFLIX | NETFLIX | 44.7M | **+24.6M** |
| AMAZON | amazon | 54.0M | **+50.0M** |
| HULU | hulu | 9.0M | **+8.7M** |

**Demographics: young and rich more likely to adopt early**

Understanding demographic drivers is a must to decipher the market shifts between pay TV and SVoD. Demographics stratify the market to support intuitive hypotheses. Exhibit 7 demonstrates SVoD homes are younger; almost 50% of SVoD subscribers are under 45, whilst for Pay TV households (TV HH) the rate is 36%. Households with children are more likely to select SVoD: 45% of SVoD homes have children compared to 35% for TV HH. This fact comes naturally, as convenience of serving content on demand helps families to have more freedom with regard to their schedules. The children can have their favourite show during their allotted TV time, and the parents can catch their favourite show after the chores. The elderly group (65+) is two times more likely to have Pay TV than SVoD.

Habits can explain the difference, as well as fear of change, and difficulty of interfacing with some SVoD alternatives compared to a familiar remote control (which is replicated in IPTV experience). Daily TV watching habits are seen in some 60% of those under 30, while the figure is over 80% for those over 60, globally. Given these facts, we must conclude that younger demographics are watching less TV and are more likely to pick SVoD over Pay TV when they do.

US SVoD houses tend to have higher income levels. Median income for SVoD houses is around $75k compared to $50k for TV HH. As a result, SVoD houses have above-average ownership across all devices. SVoD has expensive infrastructure requirements and as such urbanized and wealthy parts of the world are able to avail themselves of such services. SVoD users, with their higher average incomes, are also more likely to own devices that enable SVoD services as seen on Exhibit 9 (next page).

**EXHIBIT 7**
**Age distribution for Pay TV and SVoD**

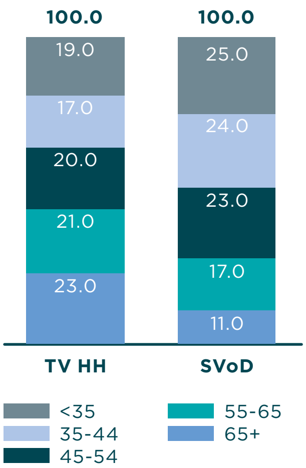



**EXHIBIT 8**
**Income distribution**

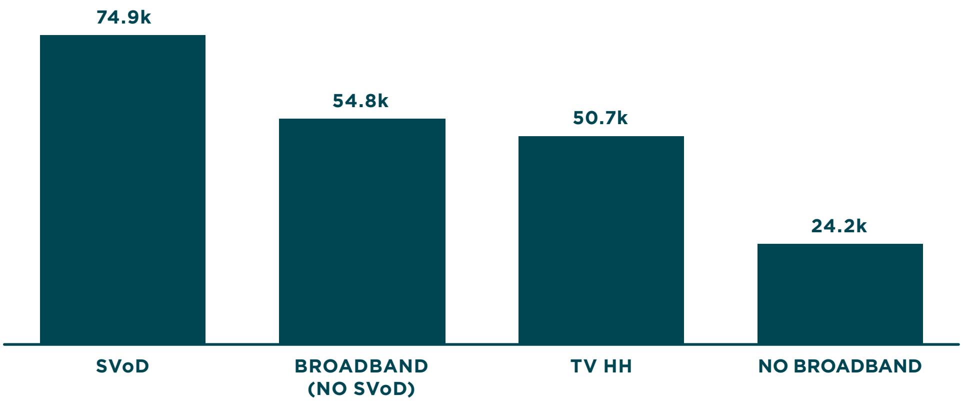


**EXHIBIT 9**
**Device ownership, % of households**

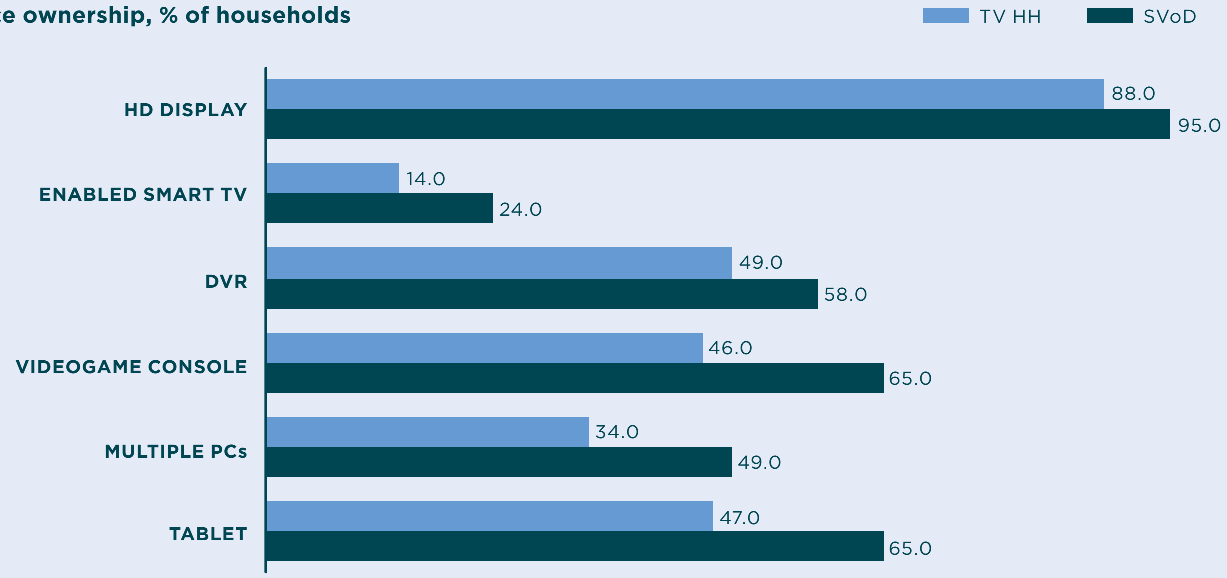



**EXHIBIT 10**
**Content consumption, weekly hours spent**

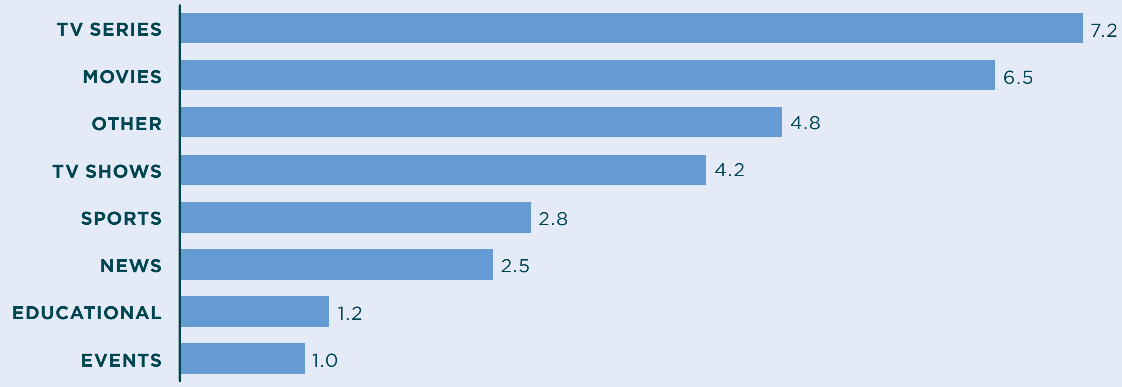
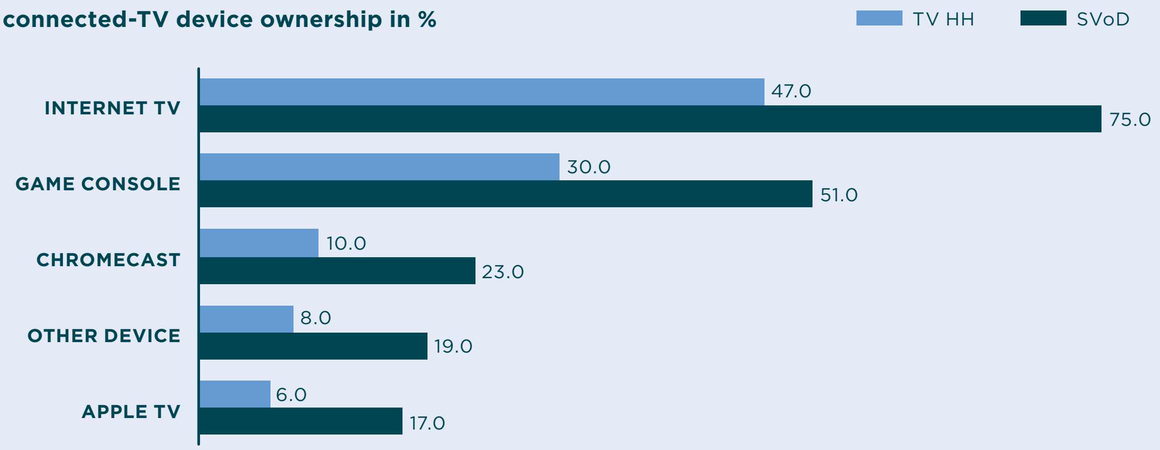



**EXHIBIT 11**
**Household connected-TV device ownership in %**



## Content: Drama drives the business

The amount of time spent watching TV presents a declining trend, but some content – namely TV series and movies – is able to buck this trend by increasing its share through new distribution methods. In 2014, average hours spent watching TV totalled almost 34 hours per week, but in 2016 this figure dropped to 31.5 hours per week. Viewers still spend 7.15 hours for TV series and 6.5 hours for movies every week, which is almost half of total viewing time. The key challenge to Pay TV comes from streamed content.

## Media habits: Fragmented viewing time

Since 2010, significant shifts in TV watching habits around the world have been observed. In the second half of 2015, the percentage of people who watch Pay TV every day has receded to 52% from 75%. Streamed media on the other hand grew to 59% from 30% in the same period.

Since 2011, the time spent on streamed TV series and movies has more than doubled, from 2.9 to 6.0 hours per week. The increase in streamed TV series during 2011-2016 is very significant at 121%. The increase in streamed movies for this period is 90%. One driver behind this growth is the fact that SVoD technology enables binge viewing, the consumption of relevant media in fast succession (e.g. watching two episodes of a TV series in one sitting, or watching a movie and its sequel in one sitting). In 2015, 60% of SVoD users reported binge-watch habits, compared to 47% for non-SVoD.

Since 2012, binge watching has become more mainstream and content that especially caters to this type of viewing has emerged. This prevailing trend has shifted the cultural understanding of watching TV in long blocks at a time, and made its way into social life as a conversation piece which has altered the overall standing of TV in our societies.

**EXHIBIT 12**
**Daily viewing in %**

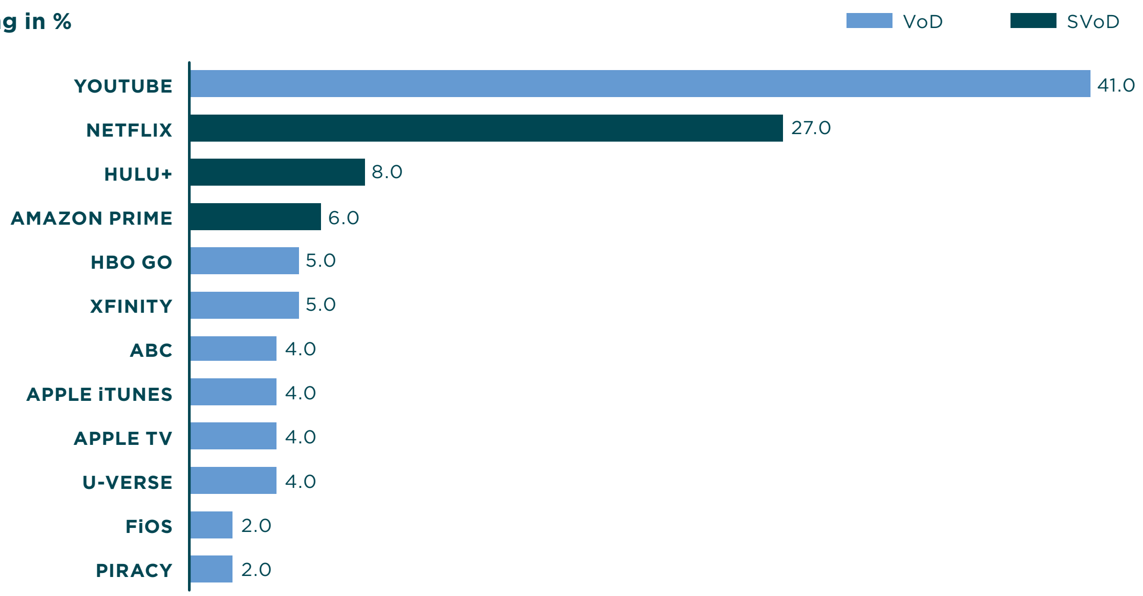
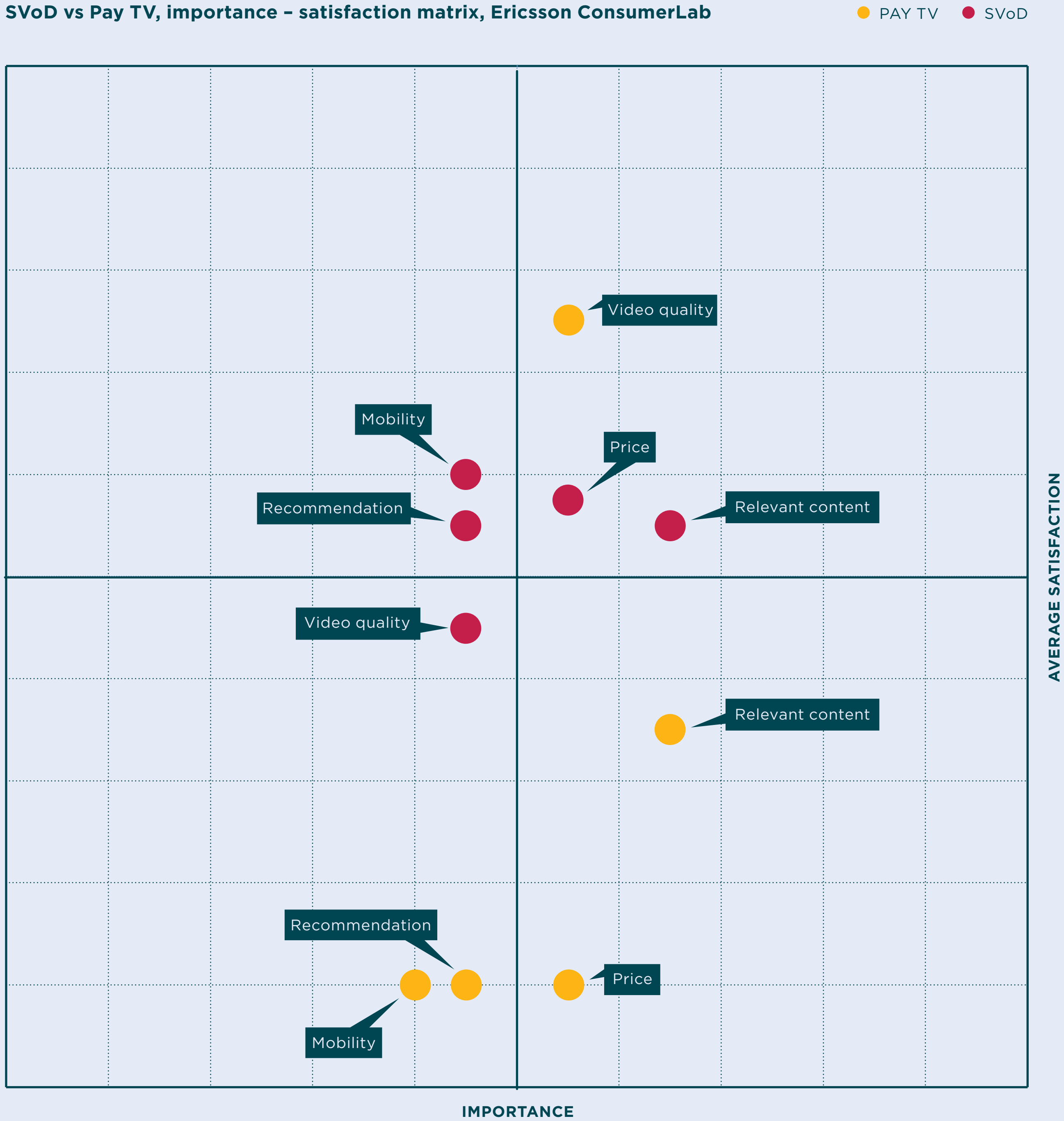


**EXHIBIT 13**

**SVoD vs Pay TV, importance – satisfaction matrix, Ericsson ConsumerLab**



Technological enablers of SVoD are not limited to broadband, as these changing habits may also be associated with the new connected TVs. Connected TVs are TV screens enhanced with an on-board computer and a light operating system that enables the TV to connect to the internet. Over 80% of SVoD users have connected TVs in their homes and over-the-top content providers such as YouTube usually come preloaded as an app on the TV. Even if the TV is not a connected TV, other devices such as game consoles, Chromecast and Apple TV etc. can quickly transform the screen by enabling online streaming.

When it comes to daily viewing between SVoD and alternative VoD services of other Pay TV companies, SVoD clearly stands out between the others. YouTube continues to dominate the list for daily views. The list then follows with SVoD players and Pay TV operators. One out of every three customers think that user-generated content is one of the most interesting contents available. It is worth to note that SVoD services are paid-for services, unlike YouTube.

## Technology: feeding into new media habits

Technological advances enable content to be mobile and empowers users to pick up where they left off at their convenience. With broadband access proliferation and ever larger screens on popular smartphones, SVoD has its share on smartphone screens. 33% of the content watched on smartphones are user-generated content. Streamed media has a share of 16% where Pay TV only has 9% share which is equal to the share of live news.

Smartphones and tablets are not ready to replace other screens. Viewers spend an average of 200 minutes per week on YouTube from their smartphones which is 20% less than the average time they spend on Netflix. From their tablets, they spend an average of 270 minutes per week which is less than half the average time on Netflix.

## Customer behaviour: Cord-cutters, cord-shavers and cord-nevers

Cord-cutters, cord-nevers and cord-shavers are terms for the three different consumer behaviour patterns observed with the advent of SVoD services. Cord-cutters are, as the name suggests, those who cancel their subscriptions with Pay TV operators. Cord-nevers are those who never had a subscription with a Pay TV operator. Cord-shavers are people who reduce their cable package. These segments show different tendencies towards SVoD and Pay TV plays.

SVoD is cheaper than Pay TV for the consumer. Today, the average cable bill in US is more than $90 excluding additional fees and devices.

With additional fees and devices, the average cable bill reaches $125 per month, which is an astronomic figure compared to subscription fees of SVoD providers of around $10 per month. On average, a person only watches 17 channels from the whole bundle where SVoD providers offer their subscriber unlimited access. Cord-nevers are an important market for SVoD as this group takes up the value proposition and creates the market growth otherwise untapped by Pay TV.

Cord-shavers keep the Pay TV contract, but choose a service level that matches their consumption: their screen time is split between pay TV and SVoD.

The motive behind SVoD adoption is not based primarily on price. According to the customer survey presented in Exhibit 14, 56% of people prefer to watch TV in line with their own schedules, and 52% of them think it is much more convenient. Only 29% of people indicated it is cheaper than any other Pay TV services. The convenience of fitting TV habits into one's own schedule trumps any perceived advantage over other decision factors.

Cord-cutters and cord-shavers are thought to be mainly motivated by the convenience factor.

The net promoter score (NPS) of SVoD is higher as a result of higher customer satisfaction. Consumers address their lifestyle problems around entertainment habits with the SVoD services and are happier with their choice. 36% NPS of SVoD is more than three times TV HH (38% NPS, see Exhibit 15).

**EXHIBIT 14**
**Survey results: Why SVoD?**

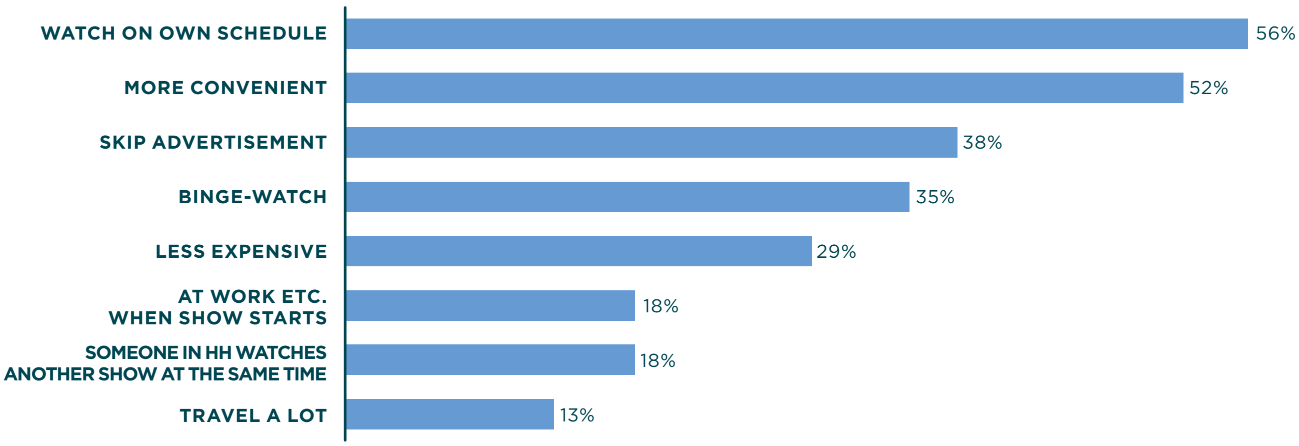
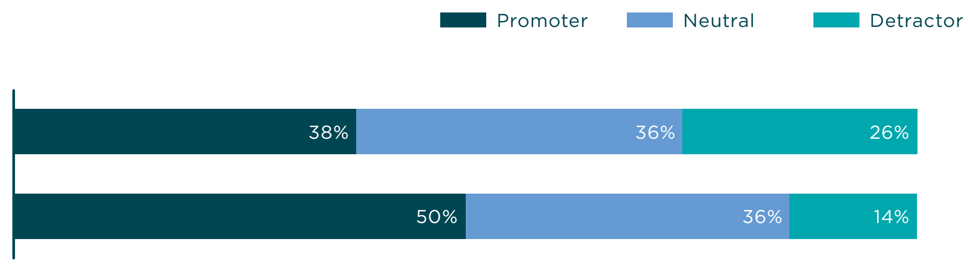



**EXHIBIT 15**
**Net promoter score, %**



# PAY TELEVISION IN TURKEY

Turkey is the youngest country in Europe, with a population of 78.7 million people. In 2016, Pay TV penetration in Turkey has grown to 25.7%. Over the period between 1980 and 2015, the average number of people per household has decreased sharply from 6.5 to 3.7. The number of households in Turkey has grown faster than the population. The Pay TV market is expected to benefit from this decline in the number of people per household, as the country continues to grow and the young populace ages. The average Turkish household size of 3.7 is still high compared to the average of 3.1 in Spain, 3.0 in Greece, 2.5 in Russia and Romania, 2.3 in France and 2.2 in the UK.

Pay TV penetration in Turkey still lags significantly behind its peers. Currently, average penetration in Western Europe is 60%.

Turkish households experienced a shift in viewing habits from satellite to IPTV in 2014-2016. In 2014, 71.5% of Turkish Pay TV households had satellite TV, 22.5% of them had cable TV and 6.0% them had IPTV. In 2016, satellite TV declined to 66.6%, losing 4.9%, while IPTV reached 11.6% with a gain of 5.7%. However, the main IPTV operator, Tivibu has adopted satellite TV on top of IPTV in 2016. The move made by Tivibu signifies that satellite TV is still relevant for the industry.

**EXHIBIT 16**
**Pay TV penetration for Turkey, TURKSTAT**

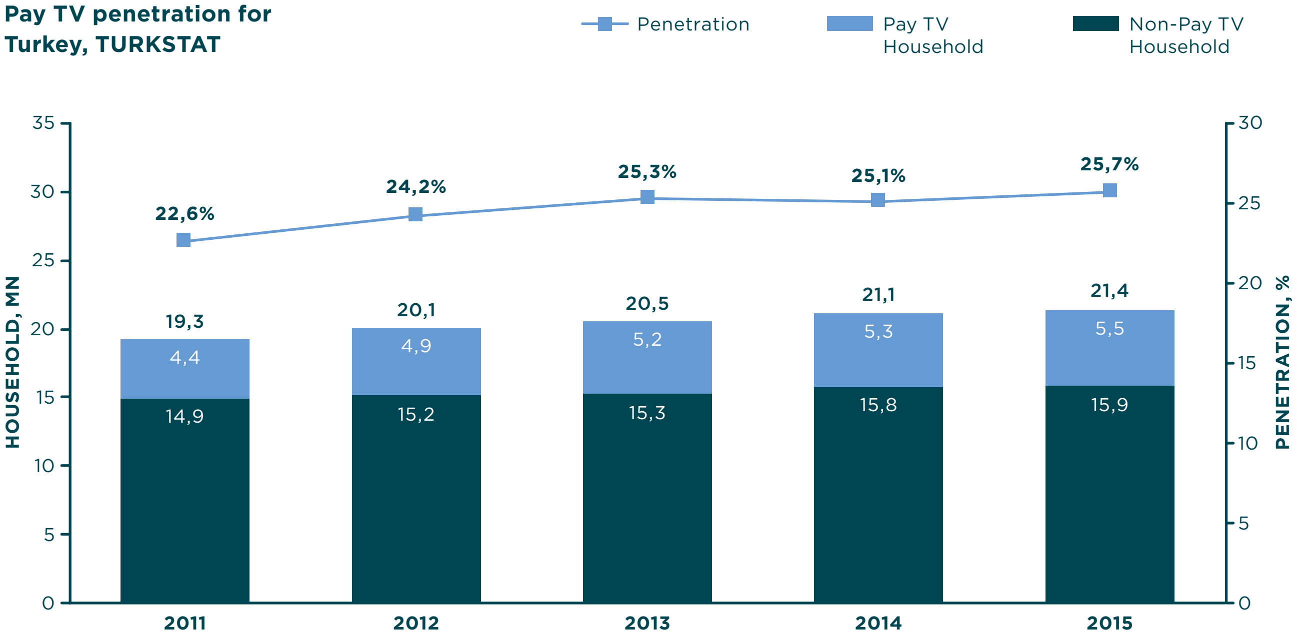


**EXHIBIT 17**
**Pay TV penetration for selected countries, Analysis Mason**

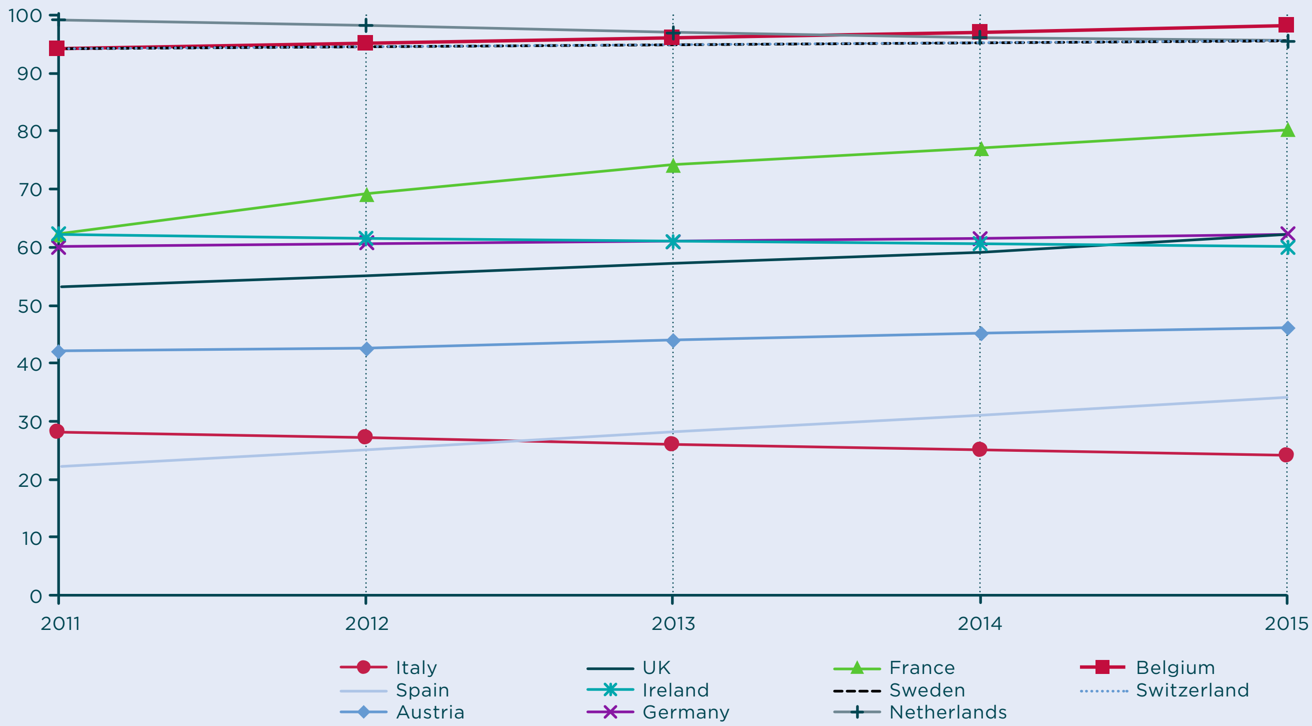



**EXHIBIT 18**
**Pay TV household by Pay TV provider service in Turkey**

| PAY-TV PROVIDERS | 2014 SUBSCRIBERS AT THE END OF 1Q | 2015 SUBSCRIBERS AT THE END OF 1Q | 2016 SUBSCRIBERS AT THE END OF 1Q | 2014-2016 NET ADDS | 2015-2016 CAGR, % | 2014-2016 CAGR, % |
|---|---|---|---|---|---|---|
| **CABLE COMPANIES** | | | | | | |
| Teledunya | 603.038 | 725.386 | 835.016 | 231.978 | 15,1% | 17,7% |
| Other | 563.230 | 445.073 | 328.025 | -235.205 | -26,3% | -23,7% |
| **Total Top Cable** | **1.166.268** | **1.170.459** | **1.163.041** | **-3.227** | **-0,6%** | **-0,1%** |
| **SATELLITE TV COMPANIES (DBS)** | | | | | | |
| Digiturk | 2.861.141 | 2.916.435 | 2.787.024 | -74.117 | -4,4% | -1,3% |
| D-Smart | 1.032.710 | 1.046.903 | 931.608 | -101.102 | -11,0% | -5,0% |
| Filbox | 0 | 4.880 | 28.765 | 28.765 | 489,4% | N/A |
| Tivibu | 0 | 0 | 116.387 | 116.387 | N/A | N/A |
| **Total DBS** | **3.893.851** | **3.968.218** | **3.863.784** | **-30.067** | **-2,6%** | **-0,4%** |
| **PHONE COMPANIES** | | | | | | |
| Turkcell TV | 0 | 98.476 | 268.110 | 268.110 | 172,3% | N/A |
| Tivibu | 308.315 | 281.483 | 350.674 | 42.359 | 24,6% | 6,6% |
| **Total Phone** | **308.315** | **379.959** | **618.784** | **310.469** | **62,9%** | **41,7%** |
| **Total Top Pay-TV Providers** | **5.368.434** | **5.518.636** | **5.645.609** | **277.175** | **2,3%** | **2,5%** |

Another way of interpreting this move is that the shift to IPTV in the Turkish market will be limited due to the modest coverage of broadband networks in the country. Over the two-year period, the number of cable subscribers stayed flat. Growth in Teledunya's subscriber base may be explained with its transition from analogue broadcasting to digital broadcasting.
Analog broadcasting services are expected to be terminated by mid-2017.

The Turkish Pay TV market will be challenged by the following factors in near future:

- Macro factors
- Key content is free
- Football's declining appeal
- Content infringement

### Macro factors that thwart growth

The Turkish Pay TV market is faced with opportunities and challenges as a result of the increasingly bipolar landscape with regard to disposable income distribution. As of 2015, Turkey had the sixth highest discretionary spending in Western Europe, with Istanbul being a major hub of commercial activity and high consumption. Due to income inequality with a S80/S20 ratio of 7.4; companies selling both mass products and premium products will have opportunities for growth.

Differentiation with customized offerings for the market can transform the outlook for the Turkish Pay TV operators in decades to come. The last decile takes almost 30% of total disposable income. Cost-effective food and communication products may be targeted at the first decile while luxury travel, premium services and educational services may be targeted at the last decile. Affordability analysis indicates that real market potential is around 8.4 million households. Among quintiles, minimum growth of disposable income since 2010 is 9.4%. If growth in disposable income per household continues in the following years, both overall market size and penetration might benefit from this growth.

Pay TV expenditure is evaluated as a "recreation and culture service (RCS)" which is classified under recreation and culture expenditure (RCE). Among 34 benchmark countries in Europe, Turkey is second to last with a 22.1% RCS / RCE ratio. The only benchmark country below Turkey is the Netherlands, which compensates its last place with a high Pay TV expenditure / RCS ratio. Compared to 15.4% RCS / RCE ratio in 2008, an improvement in the RCS / RCE ratio of Turkey is expected in the future.
This expectation is based on disposable income quintiles comparison for Turkey and the rest of Europe: Turkey ranks last for the first four quintiles and the fifth quintile ranks in the middle of European countries.

**EXHIBIT 19**
**Total disposable income shares by decile in Turkey**

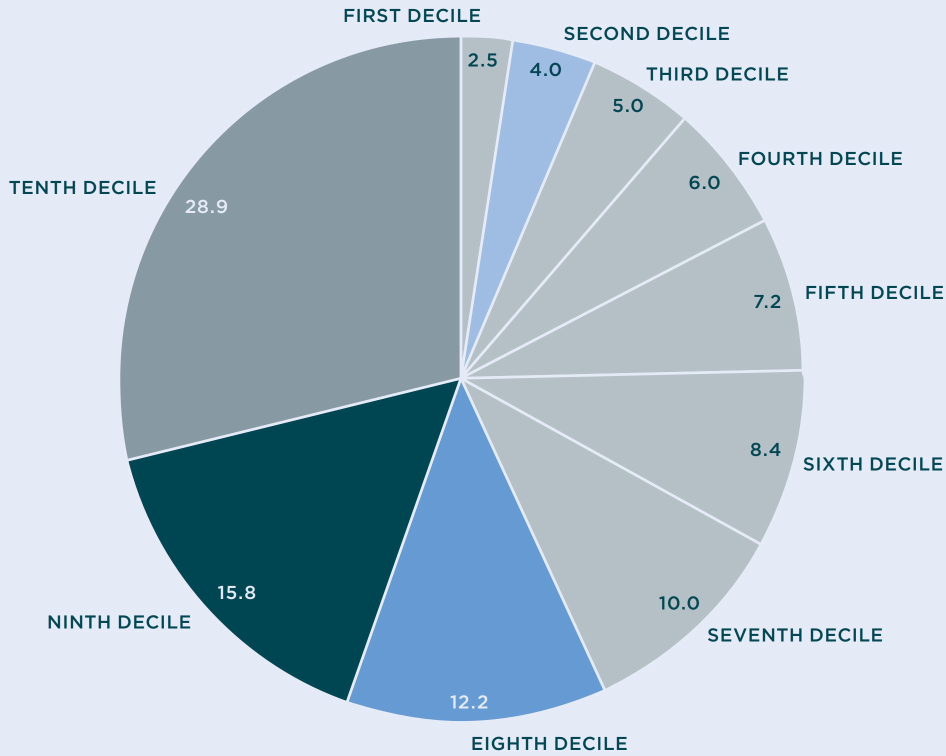
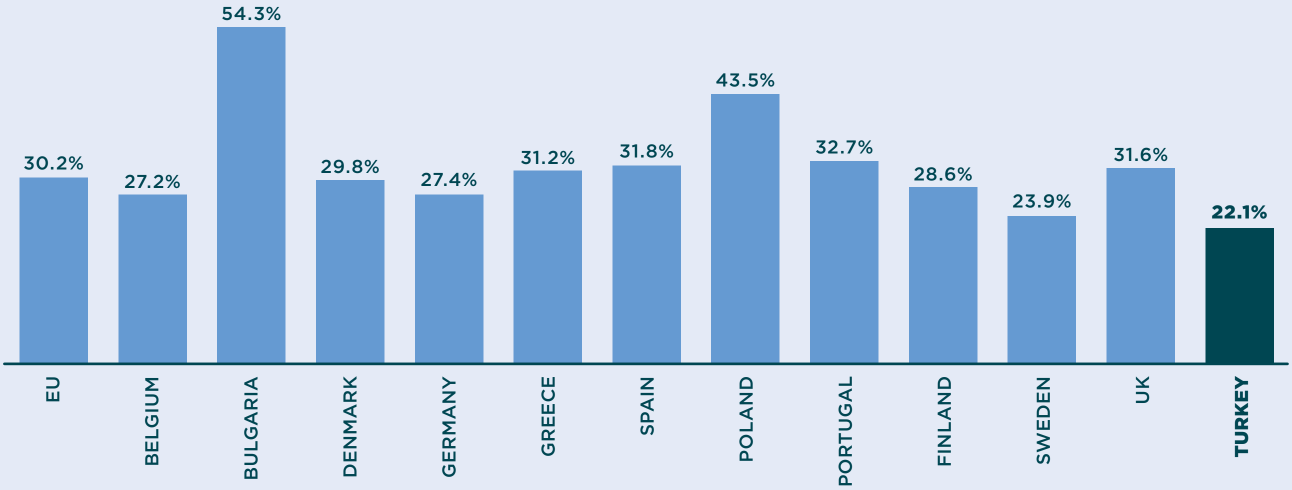



**EXHIBIT 20**
**Recreation and culture services expenditure in overall recreation and culture expenditure**



## Key content is free

The top 10 broadcasters' prime time shows analysis clearly demonstrates that domestic TV series are the most popular programme type in Turkey. According to Figure 20, 62.6% of total time has been spent by viewers on domestic TV series. Viewers spent more time on re-runs or summaries of TV series than on movies or entertainment shows.

In Turkey, the competitive environment for TV series is intense. Only one third of TV series launched gets a green light for the production of additional seasons. The competitive nature of the market for TV series arguably increases the quality of the TV series. Keeping the audiences attracted to longer series while creating a loyal fan base, comes with increased financial stakes for producers. Scenarios are either based on well-known novels / historical characters or are copied from popular international TV shows.

The scenarios are supported with famous actors and advertisements. Casting costs are higher than before and expected to increase more as popular TV show stars are in high demand. In the near future, it would not be surprising to see a significant increase in the share of entertainment shows considering their low production cost compared to TV series. This expected shift towards entertainment shows is unlikely to affect pay TV subscriptions positively as like TV series, entertainment shows are also widely accessible without any payments or subscriptions.

**EXHIBIT 21**
**Total time spent by program type during prime time**

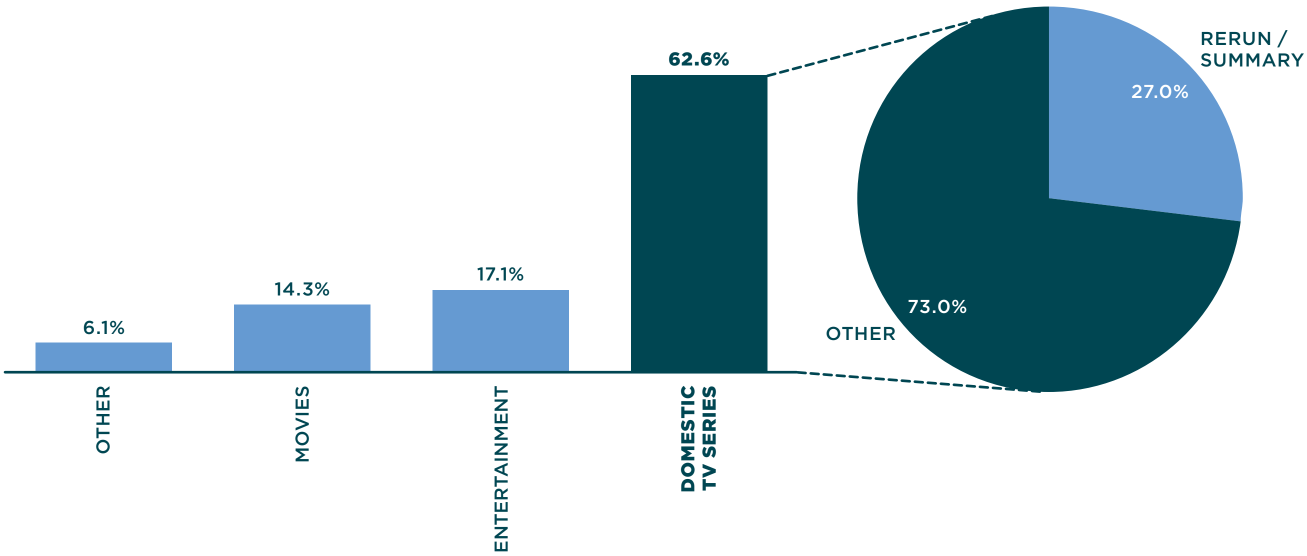


**EXHIBIT 22**
**Amount paid for broadcasting rights of Turkish League per year, excl. VAT (mn US $)**

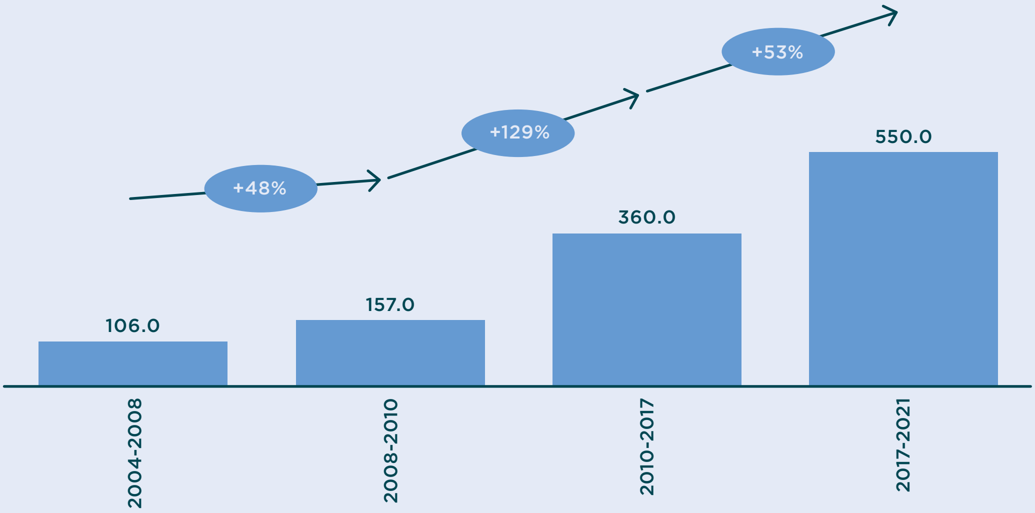
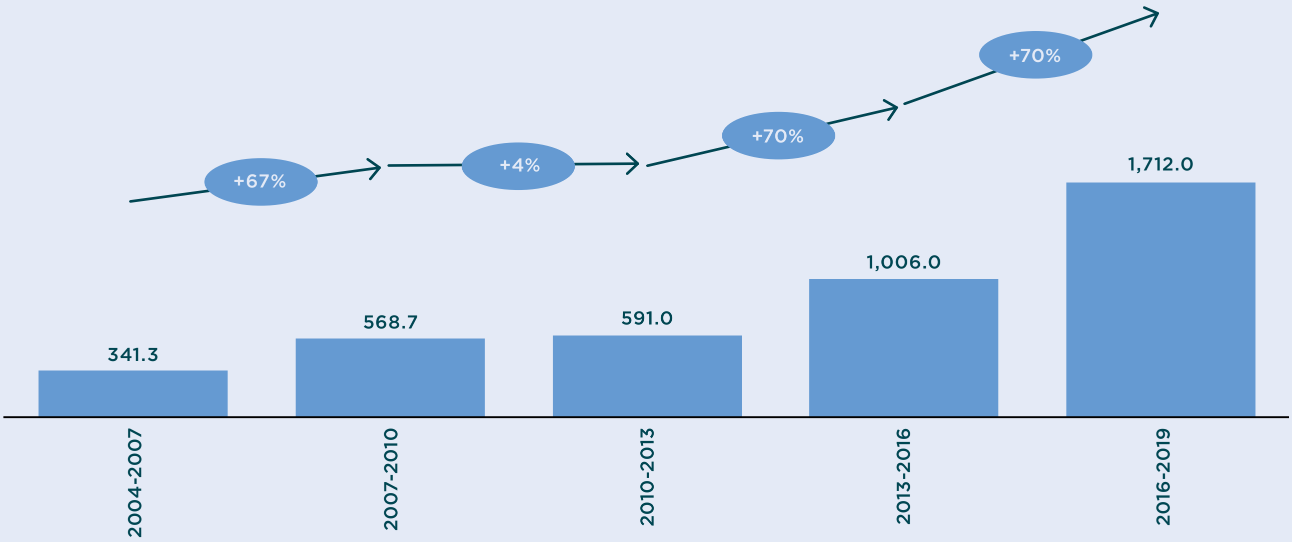



**EXHIBIT 23**
**Amount paid for broadcasting rights of Premier League per year (mn £)**



# FOOTBALL PUSHING THE LIMITS

## Crushing broadcasting rights fees

Broadcasting rights payments constitute 45% of revenues of Turkish League teams. It is the sixth largest football league in Europe, and share of broadcasting rights are slightly lower than Premier League (49%) and Serie A (51%) and considerably higher than La Liga (37%), Bundesliga (25%) and Ligue 1 (34%). Broadcasting revenues constitute a major part of funding, especially for leagues popular across borders, where content is marketable in many parts of the world. The Turkish League is arguably more reliant on broadcasting fees, despite its limited audience compared to the top five largest leagues in Europe.

Broadcasting rights payments are increasing rapidly due to global trends and the depreciation of TRY against USD. Since last tender ('08-'09), football broadcasting rights have increased by 129% in USD terms.

This increase is exacerbated by the increasing FX rates that influence the contracts. Broadcasting rights in Turkey are appointed in a tender that takes place every four years with exceptions. The previous contract awarded to Digiturk lasted until the 2013-2014 season. However, it was extended for three additional seasons. Due to the appreciation of USD against TRY, Digiturk's contractual position is further encumbered. Digiturk carries or otherwise manages a foreign exchange risk. Global trend for broadcasting rights fee increase is also evident for the Premier League as shown in Figure 22. Similarly, between 2013-2014 / 2016-2017, Bundesliga earned 2.51 billion Euros in broadcasting rights. With the last tender, the sum paid to Bundesliga has been increased by 85%.

**EXHIBIT 24**
**Stadium attendance of population (15-64) per 100 football games, %**

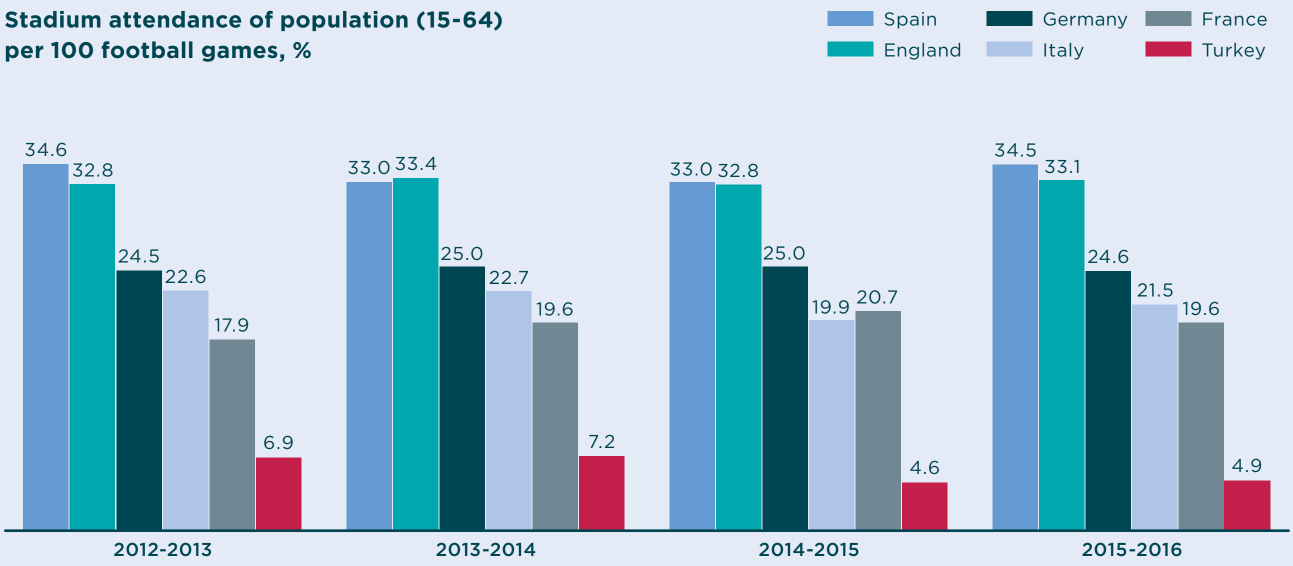
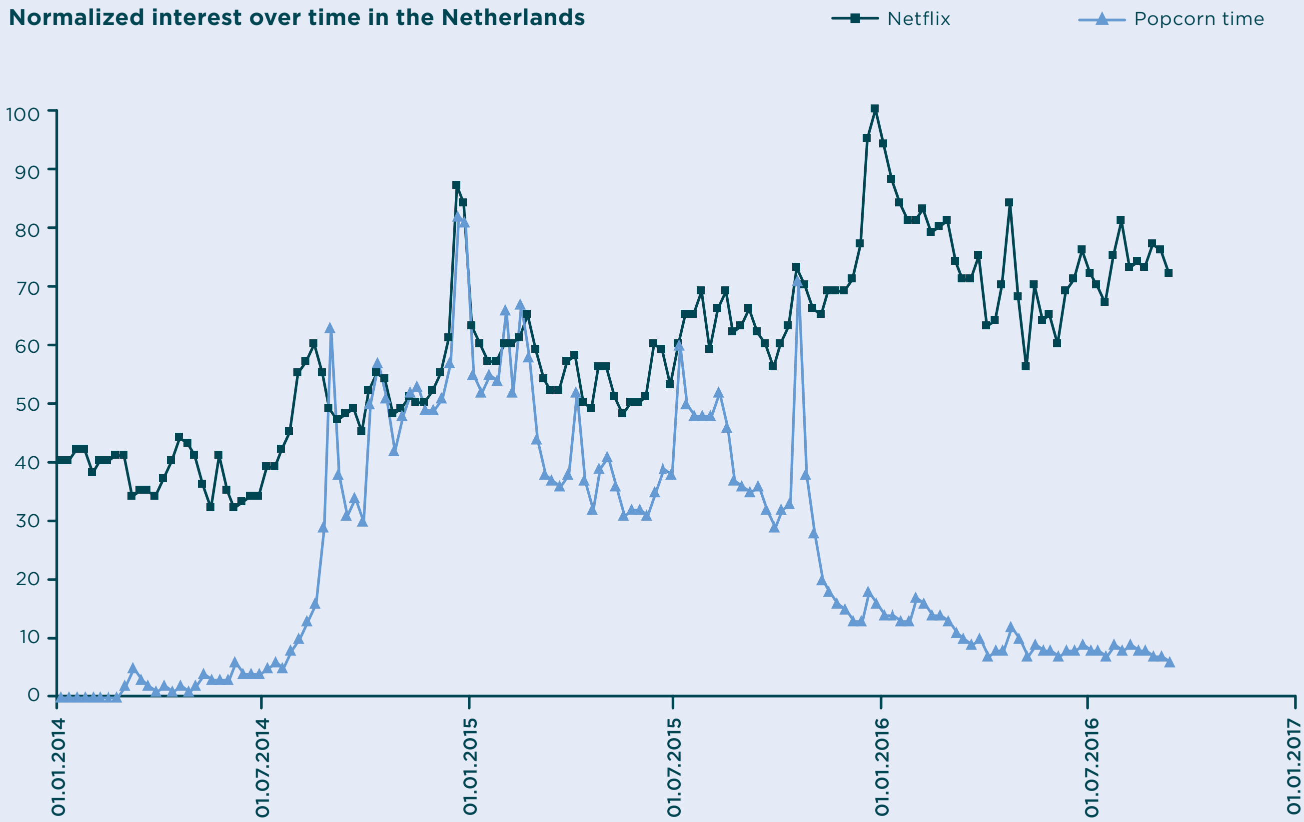



**EXHIBIT 25**
**Normalized interest over time in the Netherlands**



### Is football losing its appeal?

People are losing interest for football in Turkey due to the match-fixing scandal that broke out at the end of the 2010-2011 season. Globally, football has been shaken by a series of match-fixing scandals. Especially in Europe and Asia, online football betting has been pointed to as the main reason behind these scandals. Italian football still bears the scars of "calciopoli": Juventus was relegated to the second division and lost some of its major stars. Italian football players themselves also left the Serie A right after the scandal. Absence of fair play has caused fans to abandon the sport, major players to leave their teams and made it harder for clubs to replace the talent. It takes a league some time to recuperate fully from such a low point, if ever.

Turkish football is further challenged by regulatory pressures from the authority: In 2014 the Turkish government introduced a new e-ticket system including the implementation of a fan identity card called the "Passolig" card, to prevent violence at football matches. While it can be argued that people did not go to stadiums due to new fan identity cards and the e-tickets, the pay TV operator Digiturk did not enjoy any substantial increase in subscriber base to offset the decline in stadium viewers. Indeed, Digiturk's subscription growth has been negative since the first quarter of 2015. Over the past four-year period, Turkish stadium viewers have declined whilst other prominent leagues have remained flat.

### Content infringement is the imminent barrier

In line with other emerging markets in the world, low incomes and relatively high prices for media goods are the main reasons driving content infringement in Turkey. Thanks to insufficient intellectual property laws, Turks are enjoying "free" content available online.

According to a Ministry of Culture and Tourism survey, only 11% of Turkish people refuse to watch pirate movies or series. It is estimated that software piracy in Turkey is around 62%, music piracy goes up to 65%, and video piracy is around 45%.

With the introduction of cheap solutions on the market, piracy rates are decreasing steadily. After the introduction of Netflix, interest for "Popcorn time", a streaming application allowing users to watch torrent video files without downloading them, decreased over time. Similar evidence exists for Spotify for music piracy and Steam for game piracy.

# STRATEGIES FOR PAY TV OPERATORS TO STAY RELEVANT

## Reaching a wider customer base via dual infrastructure

One strategy to reach a wider customer base is to provide services on different platforms. IPTV providers need to make huge infrastructure investments to reach more households. Satellite services might be used to solve both problems. Incorporating satellite into IPTV play retrospectively, allows the pay TV operator to reach a larger customer base in a shorter period. Further, the client base can be switched over to IPTV when the infrastructure becomes available. It would be easier for the operator to build on existing relationships.

TP is a Pay TV provider in Poland. After launching its IPTV service in 2006, the net addition was only 43,000 subscribers in a year. In 2008, they launched their satellite service. The number of subscribers at the end of 2009 was more than 350,000 and about 70% of the base comprised of satellite subscribers.

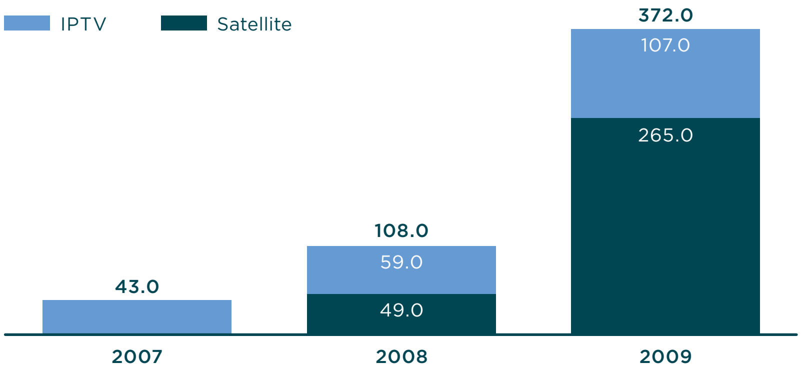
Cannibalism between different infrastructures is a non-issue, as long as the customer stays with the operator and the movement is aligned with strategy. It is important to note that according to AT&T, significant subscriber loss of their IPTV service is not a cause for concern since they are focusing on the growth of their satellite services. DirecTV gained slightly under 700,000 subscribers which compensates for subscriber loss of IPTV offerings.

## Partnerships

Partnerships between satellite companies and telco or cable operators is an alternative to the dual infrastructure model in reaching out to a wider customer base. Telco and cable companies face challenges during the development of infrastructure. The most challenging aspect is usually geographical, as accessing remote areas is costly and time-consuming. Telco and cable companies might offer specials bundles to customers by making partnership deals with satellite companies. Such deals and bundles offer a fast and cost-effective way to reach a larger base.

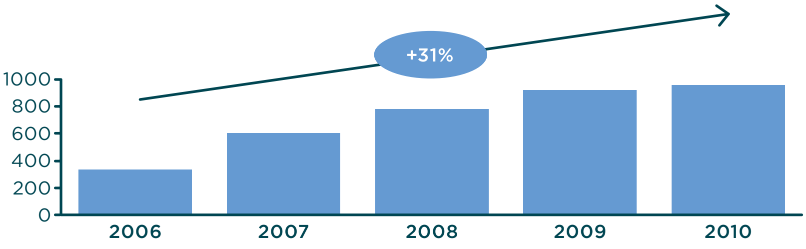
Success in this partnership model is demonstrated by Qwest, a telco operator. Qwest provided a local service in 14 US states, phased its IPTV service in new select locations and partnered with DirecTV in order to offer special bundles at those locations. After the launch, which took place during late 2006, Qwest almost doubled its customer base within a year.

**EXHIBIT 26**
**Subscriber change of TP, thousands**



Beyond partnerships, mergers and acquisitions are also common to take advantage of synergies. It is worth noting, for instance, that Qwest has been acquired by CenturyLink. All benefits aside, Qwest continued offering bundled satellite services using CenturyLink's DishNetwork. AT&T's acquisition of DirecTV has made it the world's largest pay TV operator, and unlocked many synergies with bundling and customer retention. AT&T will leverage solid subscriber base of DirecTV by offering broadband internet to more homes and businesses.

**EXHIBIT 27**
**Subscriber base of Qwest, thousands**




## Outsourcing

Open Broadband TV means basic subscription is not tied to just one provider of television content. Instead, subscribers have many different providers to choose from and can select and combine the TV channels and packages that they want in the set top box (STB). Content is aggregated from various sources and it includes free to air (FTA), niche and premium content. Then all subscribers need is a basic subscription. On top of this subscription, consumers are able to add any further package they wish to order.

Serverado provides an open IPTV platform in Switzerland. The Swedish Post and Telecom Authority view this service as providing choice for those stuck into a specific provider, especially housing association residents.

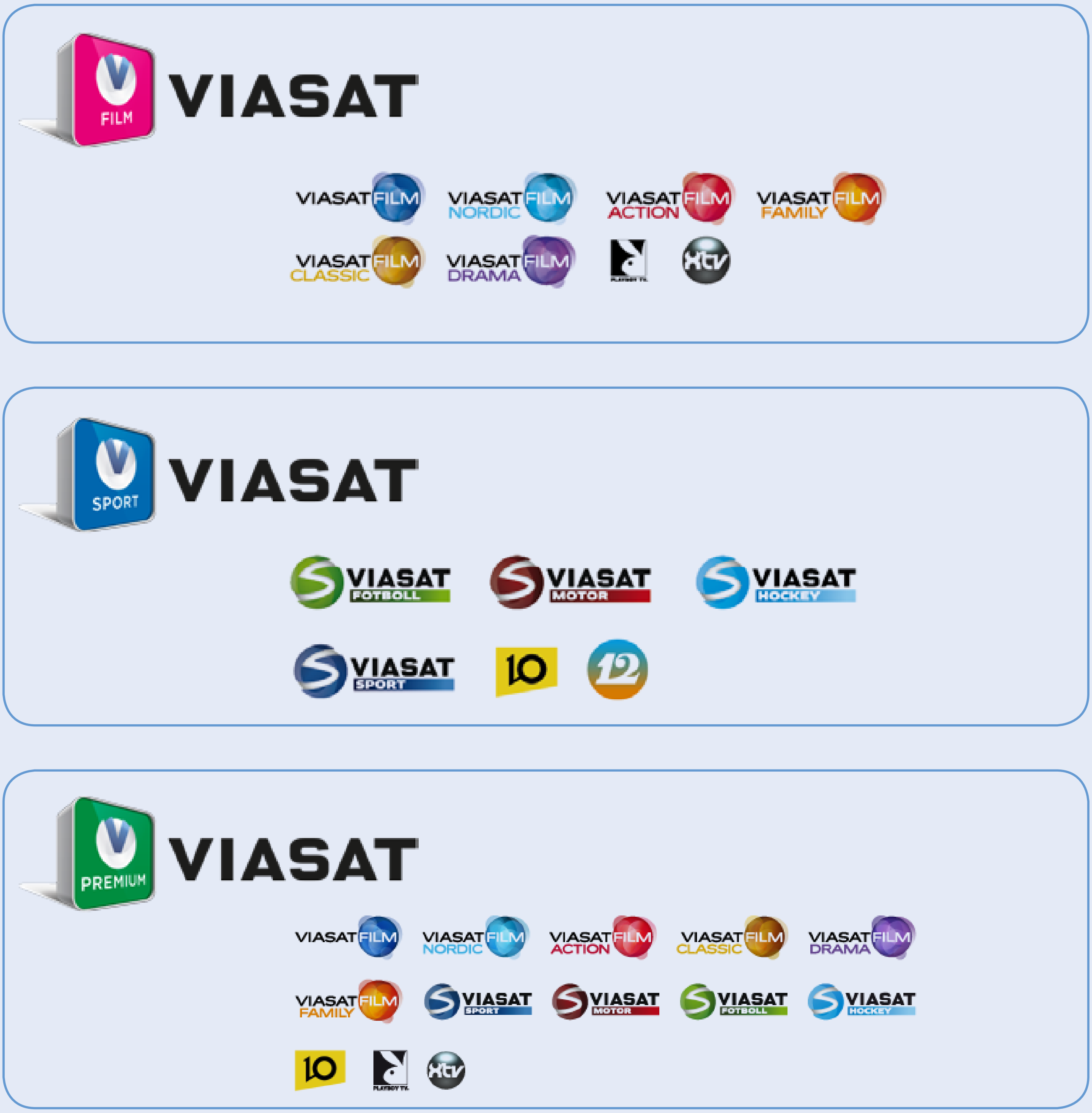
## Over-the-top

Households having a fixed broadband subscription but not Pay TV services may be targeted with over-the-top (OTT) services. Different models already exist in the different markets. Danish YouSee offers Web TV free service for its broadband subscribers and on a paid-for basis for non-subscribers. Telecom Italia even went one step further and combined OTT-offerings with value-added STB called Cubovision. FTA content may be accessed via satellite. Web TV and VoD services may be accessed via broadband. It may be used with any broadband connection. The device itself has its own memory to record personal content and to enable users to watch it later, and is expandable with universal serial bus (USB) functionality.

AT&T has been steadily moving its U-verse TV customers over to the DirecTV platform. Later this year, AT&T plans to launch DirecTV Now, DirecTV Mobile and DirecTV Preview. DirecTV Now lets customers access the service over any Internet connection, DirecTV Mobile is a service for the customers who want to consume premium video on a mobile device. DirecTV Preview, on the other hand, will offer "some" millennial-focused video programming and aims to get users to upgrade to a premium package.

OTT services are not direct alternatives for SVoD services. Instead, they mostly aim to supplement the provider's existing products or subscribers' existing devices / habits. Since OTT services are not tied to a STB, the potential for sharing passwords with non-paying customers should be evaluated carefully depending on the market conditions.

**EXHIBIT 28**
**Selected offers from Serverado website**



# CONCLUSION

The Pay TV business model based on providing premium content is destined to be phased out due to challenges from new technologies and emerging business models. Consolidation in mature markets drives growth for successful players with economies of scale.

To face the challenge from subscription video on demand (SVoD) services, Pay TV operators should factor in the reasons generating SVoD growth into their new strategies. Losing in young and rich demographics is not sustainable. Changes in media habits that evolved with streamed content, connected TV technology and binge watching is unlikely to reverse or stay as a niche. Physical challenges before the rise of new models – primarily reliance on expensive broadband infrastructure – is buying much-needed time for Pay TV operators to adapt to the new landscape. Customer satisfaction and high level of service is becoming more important with the shifts in consumer behaviour.

The Turkish Pay TV market is showing a mature market trend despite its potential to grow. Turkey might not experience the SVoD bloom to the extent of the US market since Turkish content providers are challenged with free key content, macro factors, content infringement and loss of value proposition in sports.

Operators must understand the new trends and address substitute services with cost-effective solutions. Strategies should focus on creating substantial long-term value that can address market challenges and compete with cost-effective SVoD solutions.

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Pay TV operators need to look ahead and offer a different 'value' to their customer base rather than solely premium content. Operators must also monitor replacement services and implement a strategy that would not merely generate a limited additional value and which can compete with cost-effective SVoD.

VALUE PARTNERS

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