

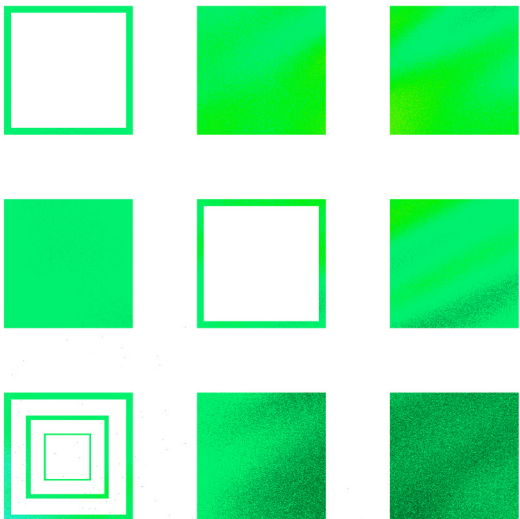
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Can SVOD survive the future of media?



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CAN SVOD SURVIVE THE FUTURE OF MEDIA?

The long road to profitability is leading video streamers into new territory. Their business models may be forced to adapt.

The streaming revolution didn't just disrupt the delivery of TV and movies. It turned the entire industry upside down. As the glory days of cable TV fade and the behaviors of younger generations spread their attention across myriad options, streamers and studios should consider that pay TV business models may never recapture the profitability enjoyed in the past.

Streaming audiences are fragmented and appear increasingly cost-sensitive, and many reduce their spending by moving on and off subscriptions that are easy to cancel.¹ Persistent churn—when people cancel a subscription—makes it harder for subscription revenues to drive profits over high costs of operation. Streamers may hope that ad-supported tiers will help overcome churn by lowering subscription prices, but streaming ad tech must compete with spending on social media services, which enable more targeted ads. Offering cheaper ad tiers may satisfy more subscribers, but can streamers drive enough value to advertisers?

Streamers are familiar with these challenges. But the evolving behaviors of younger generations—now half of the US population²—show that TV and movies are no longer the dominant form of media and entertainment.

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As we've seen in our annual *Digital media trends* survey, Gen Z, millennials, and likely the generations that follow them are spreading their time more evenly across an interconnected tapestry of streaming video, social user-generated videos, and video gaming, finding more value than just entertainment.³ These younger generations also seek community and meaning in digital media, having spent much of their lives connected through technology. This is a different world than it was when the streaming revolution began.

DRAGGED KICKING AND STREAMING

Studios, broadcasters, and cable providers didn't want to become streamers, but they may not have had a choice. Younger, more tech-savvy millennials drove early adoption of streaming subscription services. As it matured, the streaming revolution has unbundled a handful of highly profitable and concentrated cable TV providers into a myriad of a la carte streaming services. In doing so, streaming removed the stickiness of bundles and yearlong contracts, fragmented the huge audiences that were sold to advertisers, and contributed to the living room becoming a strong competitor for the once-lucrative theatrical window. Indeed, profitability relied on windowing—the staggered release of content through theaters and pay TV, DVD sales, and syndication—and maximizing the value of content across those different windows. These windows were collapsed with the shift to direct-to-consumer streaming services, eroding the profits available to the industry.⁴

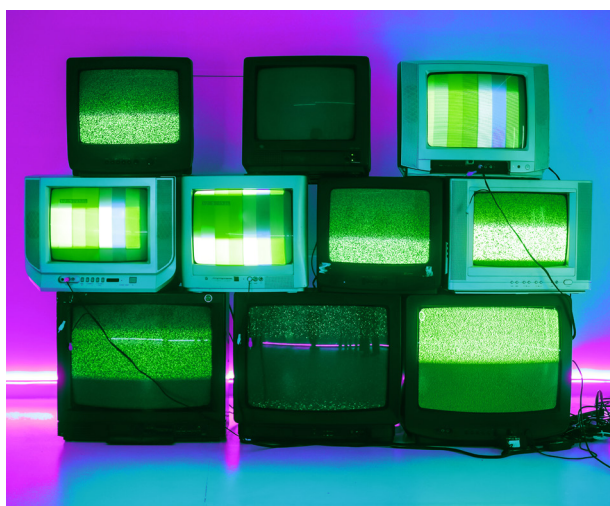
Now, cable audiences are aging and getting smaller, anchored by nightly news and live sports that are slowly being sold off to streamers willing to pay very high prices for their rights.⁵ With rising interest rates, the era of cheap debt that helped fuel the streaming expansion is likely over. Hyperscale platform players with numerous lines of business have also entered the streaming market, able to readily fund their efforts without worrying much about overall profitability.⁶ They can drive down subscription prices, mitigate churn with bundles, and pay extra for content and talent.

As the world churns

Studios and broadcast networks may find themselves between a rock and hard place. They've been forced to scale back on their cable and theatrical business but have a hard time unlocking similar profits on large streaming audiences. Subscription growth in the United States has slowed,⁷ and there are challenges of entering and cultivating new and foreign markets—markets that may demand cheaper subscriptions that can lower the average revenue per user (ARPU).⁸

Worse, churn is persistent, with 44% of those in the United States having cancelled a paid streaming service in the past six months.⁹ When subscribers churn, not only do streamers lose subscription revenues, but they can fail to recoup their acquisitions costs for subscribers that cancel too soon. While many streamers want to raise the cost of premium subscriptions, opportunistic audiences are churning and returning—moving on and off subscriptions to keep their costs down while accessing the content they want.¹⁰ This is especially true for Gen Z and millennials who carry the most subscriptions, who are most likely to churn, and who churn and return at the highest rates.

This highlights the subscription video on demand (SVOD) issue. Streamers have high costs for their operations, for subscriber acquisition, and for content but are pursuing cost-conscious subscribers that churn and return, grab cheaper or free ad-supported options, and increasingly engage with free social media and interactive gaming just as often. Consequently, nearly all paid SVOD services are operating at a loss.¹¹



CAN ADVERTISING UNLOCK PROFITS?

More streamers may hope that cheaper ad-supported tiers can help meet the growing cost sensitivity of audiences. If the monthly fee is low enough, the reasoning goes, then maybe consumers won't be so quick to cancel their subscriptions amid content droughts or tightening household budgets. Cheaper tiers may even grow subscriber counts, expanding the value of an ad model.

Embracing advertising has become more of a necessity for streamers, but it may not deliver the revenues it did for cable. Ad-supported subscriptions are cheaper by nature, meaning that direct revenues from subscriptions could go down while the dependency on revenues from advertisers goes up. Advertisers will still look for large addressable audiences on streaming services: They pay based on CPMs—the cost per 1,000 unique impressions. Acquiring content libraries and audiences through acquisition is one path, with considerable costs. As broadcast rights come under renegotiation, more streamers are looking to live sports streaming as another path to aggregating and retaining addressable audiences.¹² But these deals are very expensive and could further extend the runway to profitability—or the rights may be acquired by the largest services, leaving smaller or more risk-averse streamers behind. In each of these cases, more spending is necessary to enable better economics of their ad-supported business.

Better modeling and targeting

Advertisers also want to reach the right audiences to have a better chance at converting an impression to a sale. Streamers may also need to advance their ad tech to deliver more targeted ads and add more value to advertisers.

For consumers, there's often a balance between the amount of ad time they must watch and how much they're willing to pay for the subscription. And this balance is different for different streamers. Our research has found that the most popular services can keep prices a bit higher while delivering more ads. This puts them at a greater advantage over less popular services with less pricing power behind their brand.

But there's another challenge for ad-supported streaming: Most people tune out if an ad doesn't immediately capture their interest.¹³ One way to address this is with better modeling and targeting—especially if streamers want to compete with social media for ad dollars. Our study found that more than half of millennials and Gen Z feel that the ads they encounter on social platforms are more relevant than those they find on SVOD. But better targeting doesn't guarantee engagement or conversion.

Shifting the nature of advertising

To be more effective, the nature of ads may also need to change. Streamers and advertisers will likely benefit from much greater experimentation in style, format, and duration of ads. They could shift away from interstitial ads that disrupt shows and instead try 2–3-minute ad pre-rolls before the show starts. They can look to social media trends and consider leveraging the trust that younger generations give to the influencers and user-generated content creators they follow. And they should lean into generative artificial intelligence for faster discovery of novel approaches to ad content and copy. These approaches could help streamers enhance the economics of their ad model and become more effective with younger generations.

CAPTURING PAY TV SUBSCRIBERS MAY NOT BE ENOUGH

The emerging generational shift presents a different world for streamers. Hopes that the profits of the cable TV era can be rebuilt in streaming often rest on the notion that, over time, more cable subscribers would migrate fully onto streaming, driving up SVOD subscriptions and offering more eyes to eager advertisers. But the most ardent audiences for TV, movies, and streaming—those who prefer it more than all other digital media options—are getting older.¹⁴ Most are age 40 or older, and many are still on pay TV with few SVOD subscriptions. For younger generations, TV, movies, and streaming are not the dominant destination.

Gen Z and millennials (and the alphas who follow them) have grown up with smartphones, social media, and popular multiplayer game worlds. We've found that half of them spend more time interacting with others on social media than in the physical world, and 40% do so

more often in games. For these younger generations (the eldest among them are moving into their 40s), TV and movies are part of a larger tapestry of connected experiences that offer different kinds of value. They aren't just watching shows—they are using media for interaction and immersion, and to build community and meaning.

This generational shift from TV to tapestry presents a more complex challenge for streamers. SVOD may have disrupted the delivery of video, but social user-generated content (UGC) and gaming disrupted the medium. In this context, migrating cable viewers to streaming subscriptions and unlocking advertising revenues may not be enough to rebuild the heyday of profits.



HOW TO SURVIVE THE SHIFT FROM TV TO TAPESTRY

Streamers, studios, and investors now face a different world. They may need to make their streaming services more profitable by offering more pricing tiers, growing the productivity of their ad platforms, reducing churn, and reducing the costs of their content. At the same time, they should find ways to meet and engage people in social media, user-generated video content, and gaming.

up and what keeps them there. The industry is still immature in this understanding, leading to higher costs for programming and marketing—a scattershot approach with a limited view of what content will work and with which audience segments. This approach can bring more risk into production decisions.

To mitigate churn and make their content more productive, streamers should focus on customer insights.

By pursuing both paths, they may unlock more value for more customers, while enabling more holistic—and affordable—content strategies. However, it's likely they will need to spend more before they can make more.

Shift the focus from supply to demand

The industry has traditionally been driven by supply: Identify and produce good content and then distribute it. This worked when audiences were captured within a handful of pay TV subscriptions. Profitability in the streaming world may instead call for a demand-based approach that understands what makes people sign

Better customer insights

To mitigate churn and make their content more productive, streamers should focus on customer insights. A strong data model could make it easier to understand customer preferences in order to get the right content and ads in front of the right eyes. Data insights can drive subscriber acquisition strategies, create better engagement through sharper content recommendations, and predict churn before it happens, allowing providers to intervene more surgically with personalized offers and incentives. Like content recommendations, ad targeting can be more precise and relevant, leading to better conversions—and higher CPMs. Streamers should modernize their ad tech on top of a holistic data strategy to show more value to their advertisers and compete more effectively with social media channels. This can help streamers evolve from volatile subscriber counts to gaining more durable customer lifetime value (CLV)—shifting from subscribers to relationships.

Build a strong social and gaming strategy

To reach and engage younger generations, streamers may need to look beyond their programming and tap into the tapestry of entertainment and value. Social media, user-generated video content, and content creators are important for enabling discovery, generating buzz and hype, and driving viewers back to streaming services. In our *Digital media trends* survey, more than half of Gen Z and millennials say they prefer user-generated videos to SVOD, and a strong majority look to content creators for more authentic and trusted recommendations for services and products.

Three-quarters of Gen Z and millennials in the United States are also playing video games. The challenges and mastery offered by gaming can create strong engagement, but younger generations are also socializing and finding community in multiplayer game services. Like social media, streamers should view games as an opportunity to reach younger audiences. Social game services in particular offer large audiences and novel platforms to bring brands, products, and franchises into game worlds. For streamers willing to develop their own games or partner with game studios, their TV and film franchises can be expanded into gaming experiences, enabling people to watch the stories unfold and then step into the world and become the hero—while staying within the streaming universe.

Weaving the tapestry of video, social, and gaming

More of the largest film and TV franchises are expanding into video games, and more video game franchises are developing their stories for TV and film. With virtual production tools, assets can be developed in game engines and then readily deployed into interactive video games and TV and film productions.¹⁵



This demands a larger scale, more capital, and potentially more risk, but it reflects a seemingly inevitable convergence of digital media. Stories are becoming grander and more immersive and interactive through SVOD and gaming, while also becoming shorter, much more democratized, and essentially bottomless with the creator economy and social media.

BECOMING BIGGER THAN TV BY BEING MORE THAN TV

Digital media is becoming more interconnected and interdependent. More people, content, and advertising are moving across streaming services, user-generated content, and gaming. And more synergies between them are being unlocked. To recover profitability, more streamers may need to move beyond the pay TV model and embrace a new world of media convergence. They should focus on the value of their content, how each piece performs, and which titles can be grown into broader franchise offerings, within TV and film but also in gaming and UGC.

TV and movies will continue to be essential parts of our entertainment, but they may no longer dominate like before. Because of this fact, streaming video has become an increasingly challenging business.

However, streamers and studios have an enormous opportunity to get closer to their audiences, create better and more profitable customer relationships, and shape the next generation of entertainment experiences. They should embrace these opportunities and experiment more with innovative combinations and multimedia experiences.

Success may demand greater spending before profits grow, as well as a more holistic view across the dominant digital aggregators of our time and attention. This could also require more partnerships to forge a stronger ecosystem of media that adds more value to all players. But by focusing on their customers and the kinds of value they seek, those with the vision and willingness to execute can develop a more durable and contemporary business.



MAKE ON DEMAND IN DEMAND

Learn how Deloitte can help you engage and excite streaming audiences in a new world of media convergence

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