The Legacy of 8H

Tom Wolzien
Wolzien LLC

Opening Talk At NBC-Universal/GE Commercial Finance Conference
NBC New York Studio 8H
November 6, 2006

Good morning.

Here we are in Studio 8H, which provides a perfect setup for today's discussion of the potential and challenges across media, old and new. There is an interesting, and not too subtle point about being here in the studio built when the radio networks could afford to be the home for high art…built for Arturo Toscanini and the NBC Symphony 70 years ago ...being in a studio still in use after 30 years of SNL, and a studio that was the home of many election night broadcasts…I had the fortune to work on some. And now, even a place for this discussion of new media. The point is that this studio is still here. NBC is still here, now with a U. And GE, one of the original founders and owners of the Radio Corporation of America and NBC, actually owns it today. In fact, despite all the pronouncements of the death of old media…old media being radio back in the day, then network television back in that day, and now of course with the challenges of the web…companies like

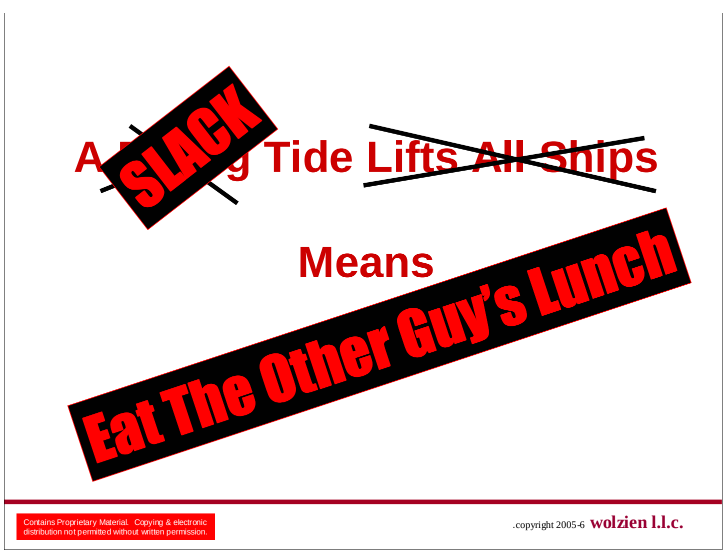
GE/NBC, Disney, and even Time Inc and Warner Brothers have survived multiple challenges, for the better part of a century and have managed to morph and remain strong in their own ways.

In fact, where three companies controlled 70% of the prime time audience 20 years ago…now, despite the proliferation of networks and declines in ratings…just five entities control that same 70% today across all their broadcast and cable properties. And ten years from now, as the web begins to mature, prime time will include online media consumption and the number of companies controlling that 70% may jump to seven, but probably not a lot more.

Surely some companies die or get absorbed because they are challenged by size or competence—remember the likes RCA, Dumont, ABC, CapCities, ABC/CapCities, and maybe even Tribune now. But the well managed corporations survive and reposition themselves for the latest realities…… Repositioning…not only of a big and powerful legacy companies, but also for the big and powerful newer companies and their smaller counterparts, who recognize sooner or later that double digit growth won't continue forever….no mater what they're saying today.

And that's want I want to talk about in this brief setup for your discussions today—the impact of spectacular growth on new players and on incumbents and a few cautionary tales that may make everyone take note because that same spectacular growth may drive the incumbents to turn their market strength against newer players at an earlier date than expected…just as they may also be trying to buy them.

The huge growth of internet advertising, broadband, cellular telephone, and satellite delivered video over the past few years would seem to suggest that the broad media, communications, and message transport industries used by consumers have been doing well. In fact, with all that money flowing across the sector, the impression would be that all ships should have an opportunity to rise on this tide.



But that's not the case. As I did work for Wolzien LLC clients this year, some interesting numbers emerged that suggested just how tough this broad sector has become. The numbers suggest that the tide is Slack…and certainly in media, a slack tide means companies have to eat each others' lunch.

I started by looking at what consumers spent directly or through advertising for all their media and communications needs from 2002, that was the peak year of dial up, through the end of last year. It was a period when the economy grew at just over 6% CAGR. But this collection of industries from electronic and print content, transport, first class mail, telephone, and the internet actually grew at about one percentage point LESS than the overall economy during that three year period . Certainly there were ebbs and flows helping or hurting individual industries within the broad sector, but basically the industries were rearranging the sector's collective deck chairs.

A Slack Tide Means
Eat The Other Guy's Lunch

	2002	2005	CAGR
GDP ($ bil)	10,470	12,487	6.05%
Media, Commo, Xport Sector Total	482	559	5.07%
Cable/Satellite Video, Phone, BBND	52	76	13.4%
Consumer Phone/BBND	151	170	3.9%
Print, Web, ISP, Messaging, FC Mail	167	185	3.6%
Studio, Network, Stations, Games, Music	112	128	4.5%

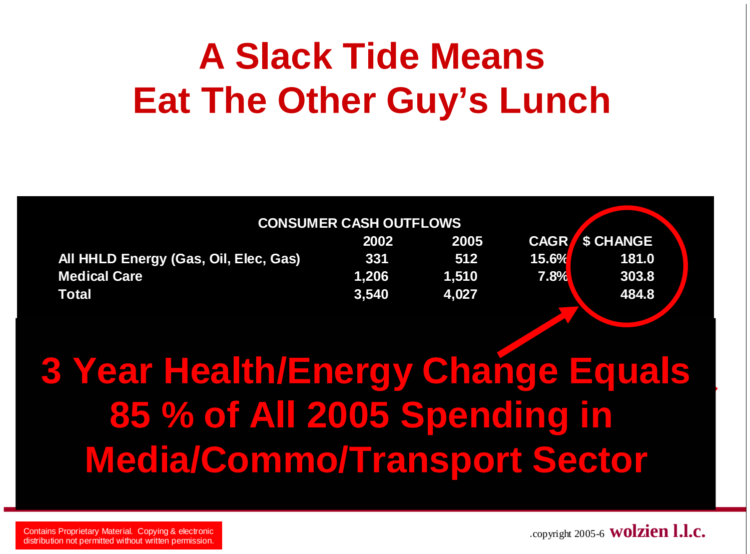
And of course, some got preferred seating in that rearrangement. Cable and satellite grew faster than the economy thanks to satellite video and cable broadband and phone, but not cable video, which was a poimt behind the economy.

The telephone companies grew more slowly than the economy at 4% CAGR...and actually lost 8% of you don't count the huge positive impact of cellular.

The great growth of online advertising was not enough to offset declines in dialup ISPS and first class mail, or slower than the economy growth in print advertising.

And collectively the electronic content providers—the studios, stations, networks, music, and even electronic games grew one to two points behind the economy.

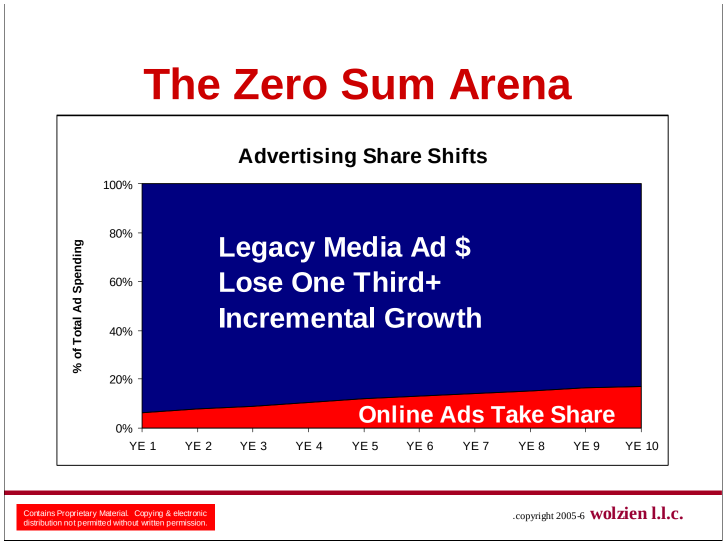
Now where, you might ask, was the money going if it wasn't going into media? Well, we're all part of the same economic ecosystem, so a partial answer might be found in energy and health care…just the increases across those three years amounted to 85% of all the money spent by consumers last year on content, transport, and messaging. Makes you feel pretty small, doesn't it.



There is, by the way, one media-related area that is growing even faster than health care…and half again faster than the economy. That's what consumers have been spending for their personal electronics. People seem to be willing to pay up for the fancy new consumer electronics tools that help them to consume content, even when they are happy to take the content itself without paying. Depending on your point of view you could say this is the natural course of things as new consumer hardware products are introduced, and as consumers shift to new digital processes in the home. Or, if you took a more content-centric view, you might be inclined to suggest this increase in consumer spending for tools is akin to a burglar stopping at Home Depot to buy a crowbar before breaking into your house.

There are many subsets of the slow growth problem that affect the content players in the sector today. One of the big ones is the question of a transfer of advertising from legacy media players to the web, where ad revenues likely will, in 2006, exceed those of the broadcast networks. Put simply, the legacy one way media companies are playing in a bit of a zero sum arena. And without changing their course, they will be coming out more on the side of the zeroes than the sums.

What I mean is that if you look at the speed of growth of the total revenue pool for all advertising, and subtract the dollars taken from that pool by the growth of online advertising, then what's left is what's available to the legacy media companies. To be more specific, all advertising has grown with the economy, on average, across the past half century—about 7.2% including the years of runway inflation in the '70s. In non inflationary years, advertising grows, on average, around 5% or so. Now any new player in the revenue pool takes its growth out of that 5%.

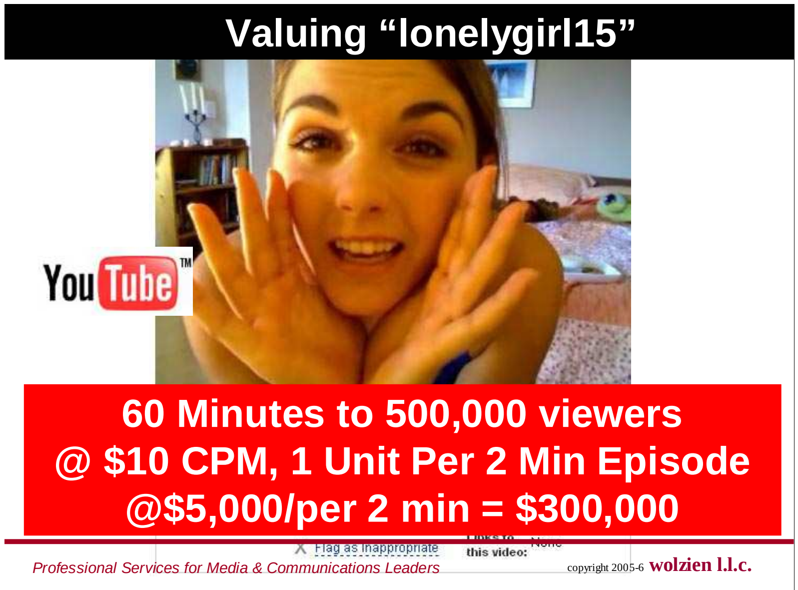


So even if internet advertising growth rates slow from say nearly 30% this year to perhaps 10% ten years out, what's left for conventional media is sub-par growth in the 3% range or so. Its simple math…with a limit on the top end of the overall ad revenue pool, and a component of that pool-- the internet--growing faster than the pool itself, the difference has to come out of the legacy players. Or the legacy players have to change their businesses to share in the faster growing Internet side.

What's going on…pretty simple. Nielsen data from the TVB suggests that legacy media—particularly television-- is still the best way to sell brands and products.

But even as one way legacy media motivates consumers, they can't respond directly. The internet answers that need --giving consumers a very simple way to follow up on the images and ideas provided by one way media. As a result, the web gets the credit…and one way media leaves money on the table. Newspapers were the first to be decimated because the early web could compete well in interactive text against one way classified advertising. Now the web can compete with video…and besides general competition for the overall advertising pie, that means a coming era of direct video advertising competition for legacy TV companies-broadcast or cable. And, of course, that is just what is driving the legacy companies onto the web.

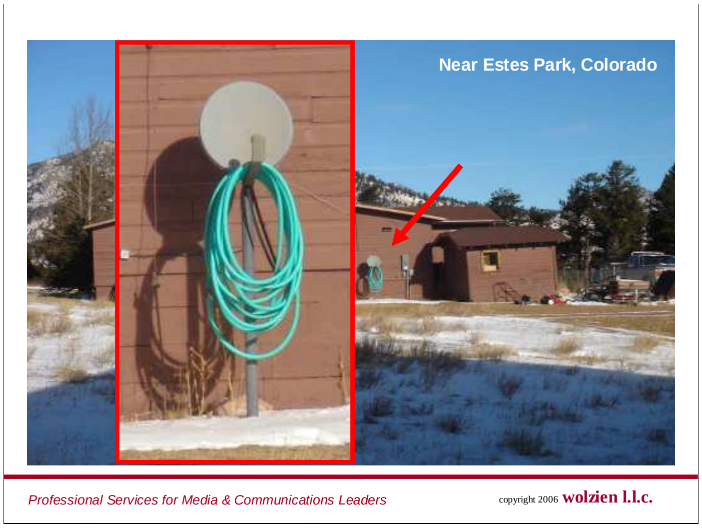
Do you know this woman? If you don't, you should. Think of this…if you could sell the 60 minutes of content from lonelygirl15 to the average audience of 485,000 that's already seen it on YouTube…and sell it at one unit per episode with a $10CPM or penny a view, that amounts to about $300,000.



Build, Buy, Partner, Harvest or Sell. The classic choices for legacy companies are self evident and there are enough players here in this room to support any choice that this company or any other might make to expand into new areas even as it protects its base. And this room has seen it all happen NBC in its various forms built radio, built television, bought Universal, Partnered with Microsoft, Sold Radio.

For the legacy companies today, the question is whether they can find ways to turn their one way businesses into two way businesses. Whether their products can have the same levels of accountability to meet advertiser demands as the web often can. And, perhaps most importantly, whether they can they develop methods to bring new dollars into the available revenue pool through direct response advertising and interactive purchasing—aka click to buy. Put another way, can the unsurpassed power of television to educate consumers on brands and products be translated into the revenues that come with consumer action?

Build, Buy, Partner, Harvest or Sell. The choices may be self evident, but not necessarily the answers…as those of use who spent time around the giddy world of AOL in the late 90s learned all too well. The answers probably aren't self evident because, the consumer is still trying to learn how to best blend old and new types of content, new technologies, and his or her everyday life. So I'd like to leave you with this as a last thought. You may be more expert than I when it comes to knowing absolutely what the consumer wants, but for me, when I think I've got the consumer figured out,



I remember what I found when I was visiting my brother back home in Boulder last winter… a home in the mountains with the obligatory satellite dish… but a satellite dish that had been turned into a holder for the garden hose.

Have a great day everyone…and thank you.

Wolzien LLC
www.wolzien.com