TV industry sees digital threats rising

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Is it time for big television to start worrying about digital?

For years, the threats to traditional television have been present, but the digital revolution now appears to be gathering momentum, raising the prospect of shifts in viewing habits which could devastate an industry that has been lucrative for years.

The decades-old model for the industry has been built around cable and satellite TV offering high-priced "bundles" to consumers, and sharing revenue with the operators of cable and broadcast channels.

But viewers today have increasing choices through the Internet. They can subscribe to Netflix, Hulu or Amazon video, pick and choose subscriptions to individual channels like HBO or Showtime, or get slimmed-down packages of channels through new service providers.

Some viewers also watch free programs streamed over YouTube or other websites.

The big threat to the industry is from "cord cutting," which has been modest until now. If it accelerates, that could unravel the model which has worked for the industry for years.

Panic mode

After the latest quarterly updates from major television groups, Wall Street investors appeared to be panicking over the future of the industry.

Disney—which owns the broadcast ABC network, and several cable channels such as sports TV group ESPN, saw its shares take an unprecedented nine percent dive after reporting earnings.

While Disney reported a "modest" number of subscriber losses, some investors saw red.

"Investors are reacting to a growing sense of the risk," said Brian Wieser, analyst at Pivotal Research Group.

"The negative perspective is suggesting that the whole bundle, the whole business model is falling apart."

Wieser said these fears are "overstated" but that did not stop a bloodbath in media stocks over the past week, with only a modest uptick at the end of the week.

Viacom and 21st Century Fox, which have prominent cable channels, each saw a 17 percent plunge over two days. Time Warner, owner of cable channels like TBS and TNT, saw a 10 percent drop.

Neil Macker at the research firm Morningstar said it is not time to panic.

"While we share the concerns around cord-cutting, we note that 96 percent of sports viewing is done live, providing some defense to the linear channel," he said in a note to clients.

The big question for the industry is how fast the landscape changes.

A study by Deloitte found more than half of American viewers watched films or television programs on streaming video, but only three percent had canceled pay TV subscription over the past year and seven percent were considering such a change.

While sports appears to be anchoring the pay TV model, other segments such as children's channels and programs appear vulnerable.

"The challenges facing linear ad-supported kids networks are greater than in other network genres," said Morgan Stanley analysts in a research note.

"Aggregating kids channels across Viacom, Disney, Time Warner and Discovery, we estimate relevant demo viewership is down 30 percent from mid-2013 to today versus 12 percent for broader TV (ex-kids)."

Fears appear greatest for Viacom, which owns the Nickelodeon channel known for kid programming like "Dora the Explorer" and "Spongebob Squarepants."

"Viacom has long been considered one of the most exposed to risks around the future of the cable bundle," said BMO Capital Markets analyst Daniel Salmon in a research note.

"Viacom's more youth-oriented audience and lack of major sports rights makes its networks more vulnerable to being excluded from a lower-tiered bundle."

Join 'em

The television companies are not sitting still amid the changes. Many are investing heavily in content to make their channels more attractive, or joining the move to streaming.

Disney chief executive Bob Iger said threats from firms like Netflix can be managed with the right programming.

"We look at Netflix actually right now as more a friend than foe because they become an aggressive customer of ours," Iger said on the Disney earnings call.

Others are embracing the shift to digital with their own streaming offerings.

HBO, part of Time Warner, has begun offering the premium channel as a standalone service online, even though this has been losing money so far and may continue to see red ink this year.

CBS, which has its own streaming service as well as one for its Showtime premium channel, says this can generate income for the company.

At Showtime, "every million subscribers equals $100 million of profit, so it's not a whole lot of subscribers for us to break even," said CBS chief operating officer Joe Ianniello.