



2014 Media and Telecommunications Industry Outlook Survey

Tuning into Transformation

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KPMG

cutting through complexity



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TRANSFORMING INNOVATION INTO TODAY'S REALITY

In business, change has often been something to fear. Change usually meant the rise of new competitors to challenge established companies, but that very word “established” also created the biggest hurdle to market acceptance of new ideas and new players. Remember around the year 2000, with the dot-com and tech bubble and its subsequent burst? Back then there were plenty of technological developments and the pace of change seemed rapid, people mused about the possibilities, but couldn’t necessarily see how innovation was immediately or significantly impacting their business and/or industry. The market acceptance hurdle was just too high.

In the early 2000s, we saw the beginnings of a digital economy and enabling technology, but initial usage gave little indication of how fundamental and ubiquitous its use would be today. It’s everywhere. It doesn’t even surprise us anymore. We expect it. Think of the vast array of goods available online and the ease of Internet shopping, which has had such a major impact on the way we buy products. But in the early days of online commerce, neither the retailers nor the consumer had a clear view of what a game changer this would become. Other innovations that were unpredictable in their infancy have changed the way we listen to music, watch movies, communicate and interact with others, and much more.

Now we can’t remember day-to-day existence without some of these truly transformative early stage innovations. As the “potentials” became reality the puzzle pieces of digital transformation began to fit together. In 2000, we were anxious spectators, but in 2014, we’re *participants*.

We are now in a much more mature digital market. We are now reliant on smartphones, social media, and other forms of communication and entertainment on a daily basis. The latest greatest innovations transforming media and telecommunications enter the market more rapidly and don’t have to wait for nascent technology or infrastructure to catch up.

Business transformation has reached a level of maturity with the media and telecommunications industries, and executives view this period of rapid and dynamic change with optimism. In the current environment, change—driven largely by technology, innovation, and consumer demand—is being viewed by participants largely as a positive, and it's creating new opportunities for them. Today, technology enables companies to change more quickly and efficiently, and though there is still inherent risk, it is greatly diminished. As transformation becomes the norm, and companies are forced to change, they become more adept at making changes more quickly. Companies that transform can take advantage of opportunities brought about by convergence. They need to adapt their business models to fight competitive threats and seize opportunities to grow.

Paul Wissmann

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Paul Wissmann, national sector leader, Media & Telecommunications at KPMG LLP, is tuned in to all things digital and mobile. Paul has more than 25 years of experience providing audit, business advisory, and transaction services to public and privately held companies in the media, entertainment, and telecommunications industries, with a special emphasis on business transformation in the emerging digital world. Paul has spoken at events including the Yujiapu Forum – Media & Entertainment Industry Summit held in China, Media Financial Management Association (MFM) conference, Rocky Mountain Securities conference, Association of News Media Internal Auditors (NMIA), and American Film Market, as well as at the Wharton School of Business.



TRANSFORMATION SWEEPS INDUSTRIES

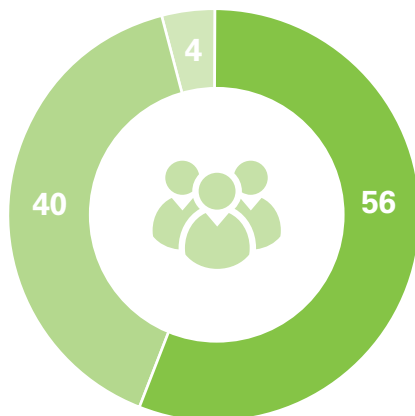
The continued impact of new technologies and digital services on the media and telecommunications industries combined with industry convergence of traditional companies and new market entrants will have a positive impact over the next year, and will lead to transformational changes in companies' core business over the next three years.

Historically, change has often had a negative connotation to established businesses. However, in the current environment, transformation—driven by technology, innovation, consumer demand, etc.—is creating new opportunities for media and

telecommunications companies to evolve their business models to become more competitive and agile.

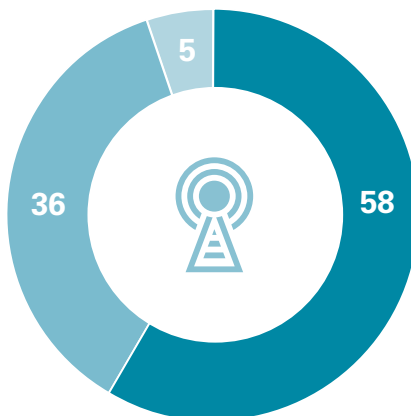
Not only did more than half of U.S. Media and Telecommunications financial executives polled indicate that their company will experience changes over the next three years that would be “transformational,” but 40 percent felt that their business will continue to evolve at a pace consistent with that of the previous decade. Combined results show respondents overwhelmingly believed that change is either already happening so fast, and also, is here to stay—or it is only going to accelerate. This awareness demonstrates the dramatic thought process of today's industry leadership, and its urgency to keep up with these changes.

Q: How would you describe the changes you expect in your core business over the next three years?



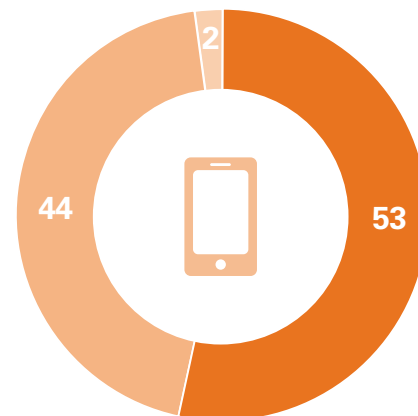
Total respondents

- Transformational
- Consistent with the speed of changes we have seen over previous decade
- Slowing



Media & Entertainment (including cable MSOs)

- Transformational
- Consistent with the speed of changes we have seen over previous decade
- Slowing



Telecommunications

- Transformational
- Consistent with the speed of changes we have seen over previous decade
- Slowing

Media & Entertainment, and Telecomm values do not equal 100% due to rounding



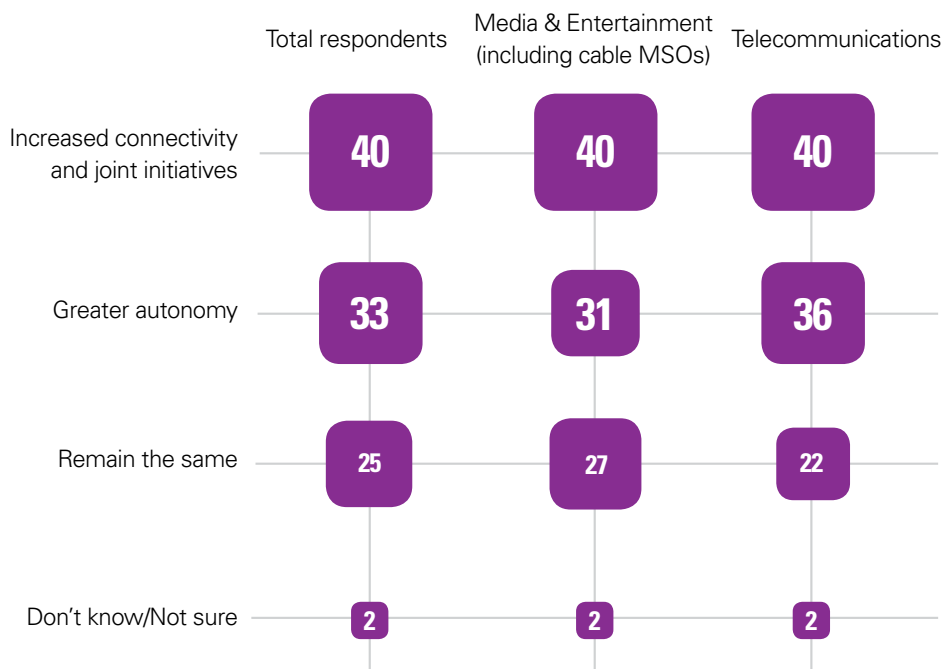
Inevitably, such sweeping transformation will impact not only business models, but will also shift the underlying business structure and processes, as well as back-office operations. When asked how they expect the involvement from their parent company or primary subsidiary companies to evolve over the next two years, virtually three-fourths of respondents anticipated a change in their relationship—whether by centralizing or decentralizing their operations.

Forty percent believe they will experience increased connectivity and joint initiatives, and one-third of

Media and Telecommunications executives believe they will experience greater autonomy. All in all, significant change is expected to cascade throughout both industries going forward.

The vast majority of companies will focus on cost containment strategies, and access to new technology and products. Regardless of the type of change, we will see evolution in core business and structure over the next few years.

Q: How do you expect the involvement from your parent company/or primary subsidiary companies to evolve over the next two years?



Total 100%

DIGITAL DISTRIBUTION LEADS THE WAY

Media executives are even more bullish than their telecommunications counterparts about how new digital distribution methods will increase their revenue over time.

There was also a small, but growing level of response to machine-to-machine (M2M) market opportunities, suggesting that although we are still many years away from fully optimized interconnectivity, M2M is an emerging trend.

The biggest driver of revenue growth differs between industries, with survey results showing 59 percent of media and entertainment executives feel that emerging digital distribution methods will be one of the top three drivers of their company's revenue

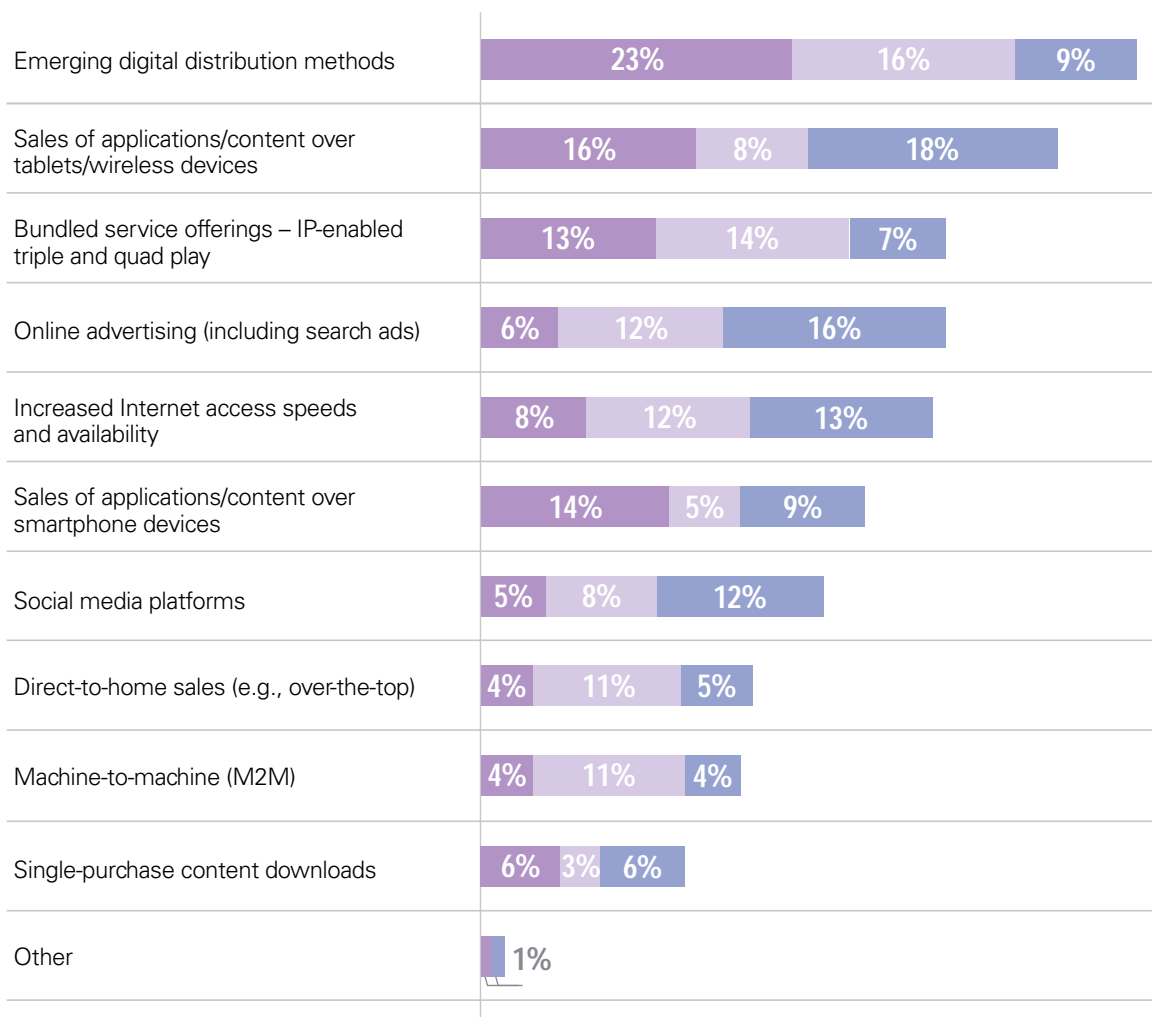
growth in the next three years (as compared to just 36 percent of telecommunications executives). Combined sales of digital applications and content over smart phones, tablets, and other portable and wireless devices are identified as another key driver for companies' revenue growth in the next few years. This explains the new momentum in online advertising.

Meanwhile, M2M opportunities are still in the infancy stage, but there has been rising interest from the telecommunications companies. Nearly 30 percent of telecommunications executives feel that M2M service will also be a top revenue driver.





Q: Which of the following market opportunities do you believe will be the biggest drivers of your company's revenue growth in the next 3 years? (Select top three drivers)



Total respondents



1st highest driver



2nd highest driver



3rd highest driver

Top three media results		1st highest driver	2nd highest driver	3rd highest driver
	Sales of applications/content over tablets/wireless devices	15%	5%	20%
	Online advertising (including search ads)	9%	22%	11%
	Emerging digital distribution methods	35%	20%	4%
Top three telecommunications results		1st highest driver	2nd highest driver	3rd highest driver
	Bundled service offerings – IP-enabled triple and quad play	16%	20%	7%
	Sales of applications/content over tablets/wireless devices	18%	11%	16%
	Increased Internet access speeds and availability	18%	18%	16%

THE SHIFT FROM OLD TO NEW

There is a clear shift from consuming media through traditional channels to viewing via personal, wireless devices.

More than 70 percent of both media and telecommunications executives believe the continued emergence of new technology devices and services will positively impact their business in the next year. Additionally, 70 percent of industry executives believe that their company's revenue will increase as a result of mobile device transactions. In fact, the sale of applications and content over smartphones, tablets and other wireless devices is also expected to be a top revenue driver over the next three years (65 percent media and entertainment executives, 76 percent telecom executives).

Emerging digital distribution methods are leading the way, and are extremely significant to the media and entertainment respondents, since there is significant potential for growth in this area, as content distribution continues to evolve.

Also, more than 65 percent believe that the media and telecommunications industries will continue to converge over the next year and that it will positively impact their business. Focusing on telecommunications, this optimistic view of continued convergence is further highlighted, suggesting that industry leaders anticipate major merger and acquisition deals in the next several years.



Key takeaways: Many media companies are reacting in the right direction, but no one knows what will ultimately grab the consumer's attention and significantly alter expectations for content access and consumption. But the audience is fractured, likely an irreparable outcome of the convergence of tech and media, and the resulting plethora of content options, anytime, anywhere create a set of challenges unlike any other time in the history of media. Companies that embrace a

traditional mindset risk slowly getting left behind. Media and telecommunications executives need to think like innovators to get in the game early, and find something that can separate them from the pack. As media companies realign business and creative strategies, we believe they need to shed old thinking and understand the potential impacts of innovation in technology and talent acquisition, data and analytics, and customer experience.



Q: What impact, if any, will the following market drivers have on your company in the next year?

	<i>Major positive impact</i>	<i>Minor positive impact</i>	<i>No impact/not sure</i>	<i>Minor negative impact</i>	<i>Major negative impact</i>
Media and telecommunications industry convergence	28%	40%	18%	14%	0%
	22%	29%	25%	24%	0%
	36%	53%	9%	2%	0%
Emerging new technologies, devices, and services	43%	30%	17%	9%	1%
	42%	31%	15%	13%	0%
	44%	29%	20%	4%	2%
Managing back-office system improvement	22%	27%	45%	6%	0%
	20%	24%	53%	4%	0%
	24%	31%	36%	9%	0%
Shift from consuming media in traditional ways to consuming media over personal devices	37%	28%	20%	14%	1%
	31%	29%	18%	20%	2%
	44%	27%	22%	7%	0%

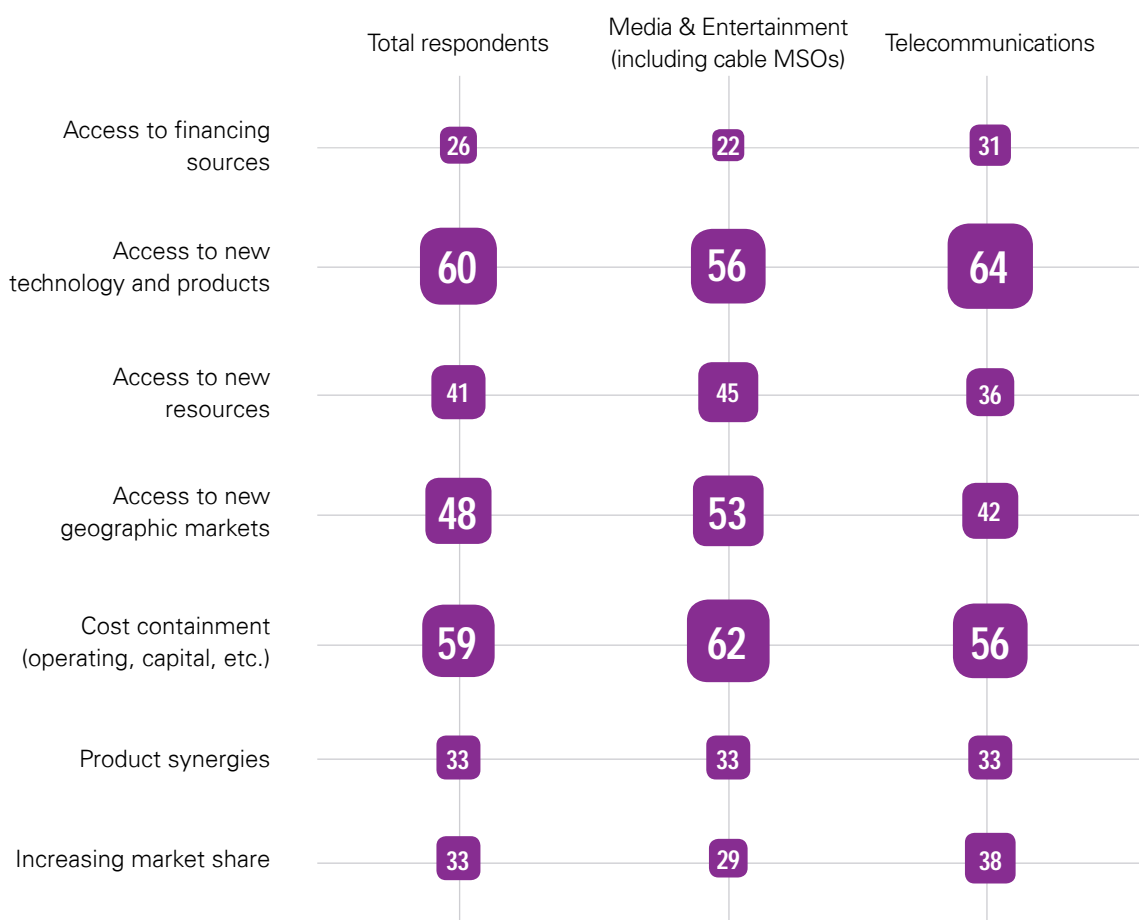
- Total respondents
- Media & Entertainment (including cable MSOs)
- Telecommunications

DRIVING FORWARD AMID A CHANGING LANDSCAPE

Industry executives are looking at transformation as both increasingly, and fundamentally, affecting the way they do business. They are rationalizing their business and operating models to take advantage of new emerging revenue sources and remain

cost competitive and profitable as technologies advance. The survey also yields an optimistic outlook about their digital innovation capabilities, with an uptick from last year, as well as a healthy overall positive impact.

Q: Which of the following do you think will be among the most important drivers of alliances, mergers and acquisitions in the industry? (Select top three drivers)



Total 100%



Key takeaways: As convergence occurs and new participants, technologies, and products enter the marketplace, media and telecommunications companies need to transform their business and operating models to align with new market realities and ensure they have created enough flexibility

and efficiency in their business, organizational structures, processes, and technologies and establish the culture and measures and incentives to be able to quickly adapt transformational change and stay competitive and profitable in these ever-changing market environments.



There is a large disparity when comparing future concerns between the two industries.

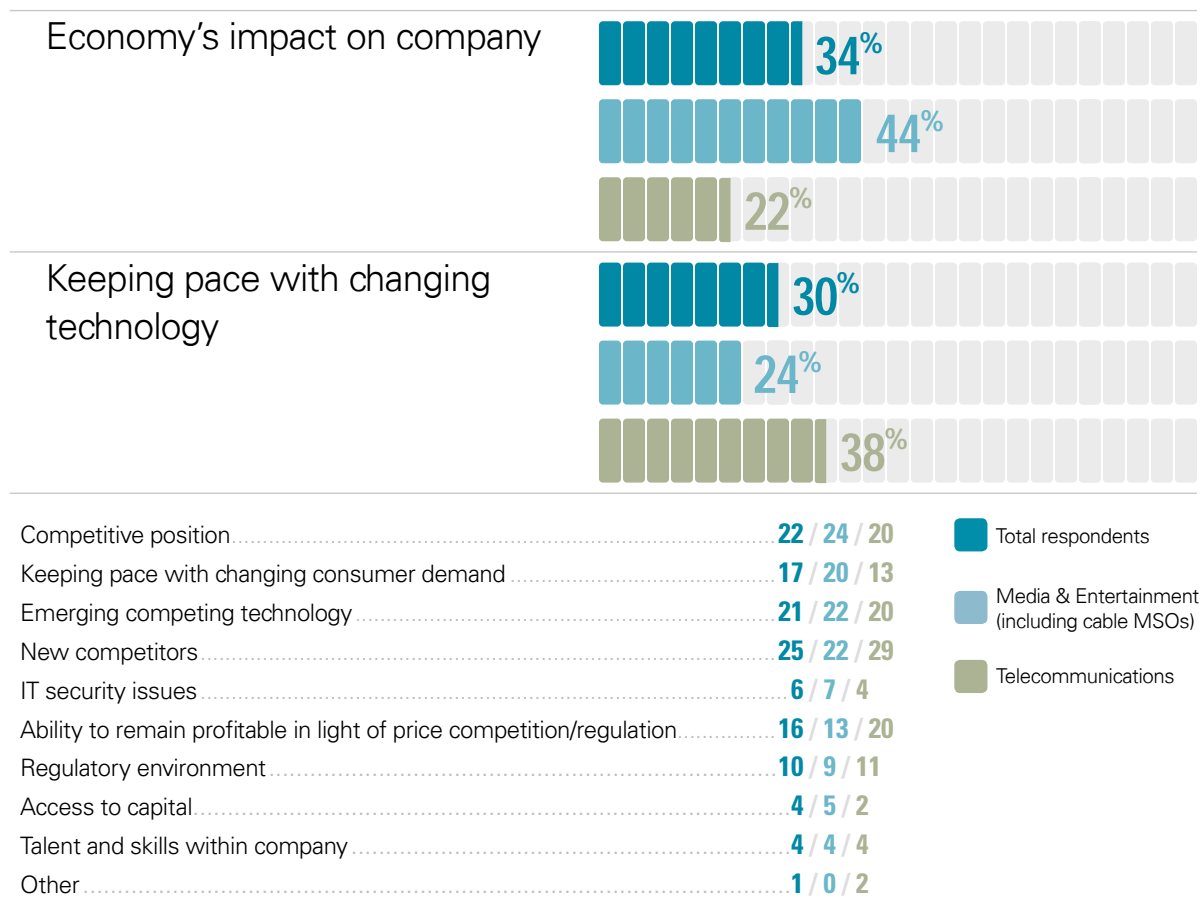
On the telecommunications front, 38 percent of companies are feeling the pressure of keeping up with ever-changing technology, as well as the ongoing threat of facing new competitors, especially from non-traditional players. Companies must remain profitable and competitive as the industries transform, and they are not only assessing the way they do business, but are also focused on rationalizing the capability and cost effectiveness of their operations in supporting their growth and profit objectives.

Telecommunications companies are seeing competition from established companies that are

now crossing over into mobility. This is being created by a couple of factors. We are seeing some device and app developers directly competing with Telcos, such as with text and instant messaging services, and they are starting to take revenue share with these methods. Also, new technology is creating more ways to provide alternative services outside of the traditional carrier model.

Meanwhile, it may seem surprising to some that 44 percent of media companies – more than double from the 19 percent of those surveyed in 2013 – are growingly concerned about the economy's future impact (and this was the biggest overall concern, with one-third of all respondents pointing to the economy). The sluggish economy and uncertain global economic and tax developments continue as lingering worries.

Q: What concerns you most about your company's future? (Select up to two)





IT SECURITY ISSUES ARE A LURKING FUTURE MENACE

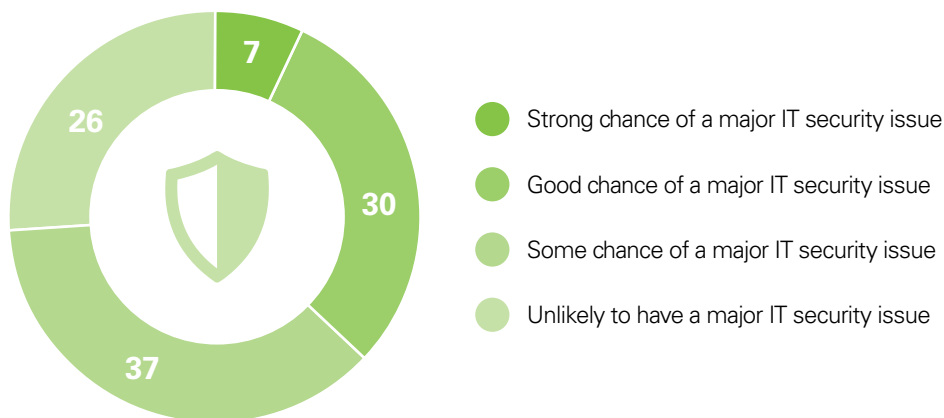


While the general views are optimistic regarding opportunities with access to new technologies, the fearful anticipation of cyber security threats loom for media and telecommunications companies.

Although about one-quarter of respondents think a future scenario is unlikely—with many

executives pointing out they have been fortunate enough not to yet experience a security related issue within their company—the other three-fourths said they foresee a possible to very likely chance of a major IT security issue within the next three years. Data vulnerability, computer security, and other cyber threats are among the greatest risks to an increasingly mobile future, and are not fading away anytime soon, experts warn.

Q: Considering your company's current IT security structure, and in light of recent security related issues at other companies, how likely is your company to experience a major security issue within the next three years?



DATA AND TECH ISSUES IMPACT REVENUE



Survey respondents said there were significant risks surrounding areas of access to data and experienced technology limitations.

Since 2013, there is a rise in the growing impact of the use of data by competitors, and so media and telecommunications companies believe they are behind in this. Also, technology is changing so fast, creating competitive advantages to those who are not as limited by these changes.

On the flip side, there are some very bright spots. Most participants expect their company's revenue from digital content distribution to increase in 2014. Also, the majority of survey participants added there is a moderate increase in revenue from transactions on mobile devices, with additional executives noting a significant increase, and so the survey results similarly reflect that around 70 percent are optimistic that app sales and other mobile transactions will continue to be lucrative in the future.

Q: Now thinking about your company's annual review, how much of an impact will each of the following factors have?

	Minimal or no impact	Revenue will decrease less than 5%	Revenue will decrease 5% to 10%	Revenue will decrease more than 10%
Lack of timely access to data surrounding customer sentiment and preferences	23%	31%	33%	13%
	24%	25%	40%	11%
	22%	38%	24%	16%
Technology or capacity limitations	18%	27%	40%	15%
	20%	29%	38%	13%
	16%	24%	42%	18%

- Total respondents
- Media & Entertainment (including cable MSOs)
- Telecommunications

LOOMING UNCERTAINTY OVER TAX ISSUES



Evolving U.S. tax policy affecting changing business structures will impact media and telecommunication companies' business strategy, since currently there is great uncertainty due to:

Proposed tax legislation and policies in the U.S. and abroad, and the increased appetite on the part of governments to require information reporting by corporations.

When business processes and flow of goods and payments change, usually the tax consequences do so too in a global business. "Companies are looking for the lowest tax rate jurisdictions and in structuring their business affairs due to the continuing pressure on their margins and to be competitive in the global economy," said Donald (Dut) LeBlanc, Jr., Tax Industry Leader – Communications Companies, KPMG.

Meanwhile, legislators and policy makers are looking at ways to maintain or increase their tax revenues, while at the same time attracting more businesses into their countries to stimulate their economies. This is partly to make up for the impact of changing business processes and continued evolution of the impact of

technology to business process, including engagement with end customers, but also to deal with a slow recovery and in many cases a continuing recession.

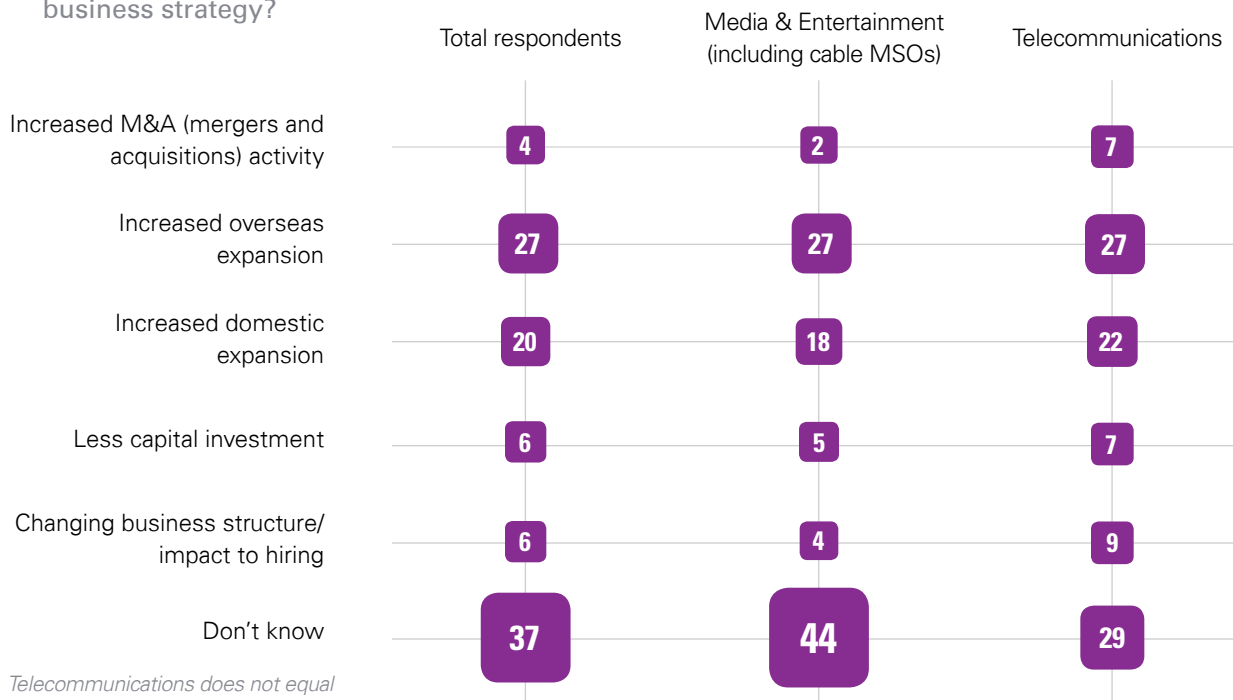
Public and political demands for including transparency in corporate tax policies.

When combined with measures to gain more transparency into company tax policies and strategies, partly due to public perception and political considerations, the global business community is facing unknown future tax costs while likely to face more and more information reporting requirements by taxing authorities, so they have opportunities to learn more about their company's business affairs beyond what is reported in local tax returns and financial reports.

The impact of technological advancement, causing company tax profiles to evolve.

"The business landscape has changed significantly over the years as a result of technological advancements, which has affected the tax profiles of companies on a global scale—including the levels and types of taxes they pay to governments around the world and longstanding agreements among governments to avoid double taxation," according to Anthony Castellanos, KPMG tax partner.

Q: How will evolving tax policy in the US and abroad impact your organization's business strategy?



STAYING TUNED IN

No one has a clear line of sight as to exactly where the industry will end up, but it is evident that companies that embrace a traditional mindset risk slowly getting left behind.

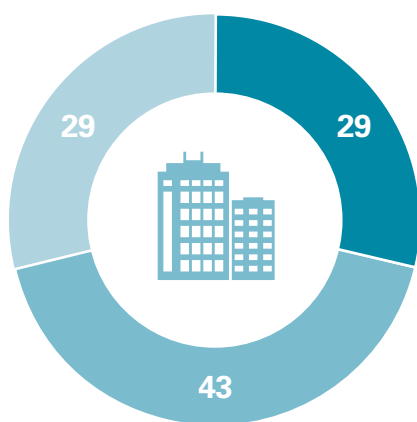
As media and telecommunications executives realign business and creative strategies, they need to think like *innovators*. Organizations need to be forward looking in the way they build their business, and create a level of flexibility that will keep them agile. The ability to recognize and adapt to change is partly about rebuilding or revising infrastructure, including technology, but also having the right talent in place. Things move quickly and businesses can't predict what they will need five years from now, but they can make the investments that lead to greater flexibility in the way they approach their business, such as their back-office operations.

Companies must remain profitable and competitive as the industries transform, and they are not only assessing the way they do business, but they are also focused on rationalizing their business costs and their overall cost-cutting strategy.

- **Focus on technology enablement.** Make your organization as nimble as possible. Engage your workforce and provide the information they need where and when they need it. Mobile technology can enable your workforce for business agility, and by equipping your employees with the best tools, you maximize their ability to do their job.
- **Know the ultimate customer.** We believe that timely access to data surrounding customer sentiment and preferences has now become critical in figuring out what is important to your customer. Integrating data analytics has become a standard part of the transformation roadmap. Companies can derive significant benefit from the ability to understand and build business solutions based on complex data.
- **Keep pace with the shifting technology landscape.** The enterprise needs to focus on IT transformation with an eye on process, not just technology. The dramatic and disruptive shift in consumer demand and delivery platforms over the past five years is driving record levels of demand for IT services. Transforming IT delivery, operating capabilities, and funding models meets business demand, but also enables innovation in the face of new and agile competitors.



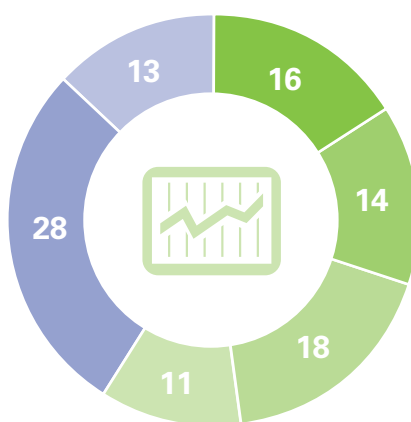
KPMG's 2014 Media and Telecommunications Business Outlook reflects the viewpoints of 100 senior executives in the United States. The web survey was conducted in the second quarter of 2014. Seventy-nine percent of respondents were from publicly held companies versus privately-held companies. Fifty-five percent of respondents represented media and entertainment companies (including cable MSOs) and 45 percent represented telecommunications companies.



Ownership

Is your ownership primarily...

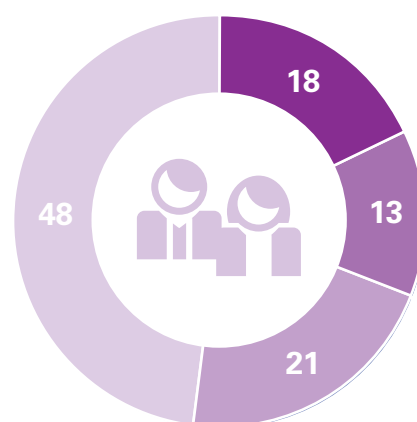
- Venture-backed
- Private-equity-backed
- Otherwise privately held



Most recent fiscal year (Revenues)

What were your company's revenues in U.S. dollars in its most recent fiscal year?

- More than \$10 billion
- \$5 billion to \$10 billion
- \$1 billion to \$4.9 billion
- \$500 million to \$999.9 million
- \$250 million to \$499.9 million
- \$100 million to \$249.9 million



Title

What is your title?

- CEO, president, owner
- C-class (CFO, COO, CTO, etc.)
- Executive vice president/managing director level
- Senior vice president, vice president or director level

Ownership values do not equal 100% due to rounding

About KPMG

As an established leader in serving communications providers, KPMG LLP combines global perspective with in-depth industry knowledge to offer a focused array of collaborative services.

KPMG's Telecommunications group is a major player in Big Four Audit and Tax in wireline and wireless, and maintains one of the largest Regulatory & Compliance Advisory service groups in the industry. Our people are meeting client challenges with performance, technology and risk issues, and are at the forefront of mobile commerce discussions.

Our Media and Entertainment professionals combine deep industry experience with knowledge of digital and traditional media. We help our clients to develop new business models that take advantage of digital revenue opportunities, while assessing their compliance and risk profiles. All of which can add up to helping companies address today's critical challenges as well as tomorrow's emerging trends. Our leadership in the industry is reflected in part by our market share. Globally, KPMG member firms provide professional services to 73 percent of the Top 40 media companies in the Forbes Global 2000.

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