The dish-free Sky Q service marks the beginning of the end for triple-play

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The European pay-TV company Sky set out its timetable for launching its pay-TV package, Sky Q, as an IP-only service at the end of January 2018. This marks both a logical progression for the company and a portent of more significant change within pay TV and video – consumer spend on OTT video in Europe will grow from EUR8.1 billion in 2017 to EUR18.0 billion by 2022. This article discusses Sky's service launch in the context of the wider shift in TV and video consumption and of a potential change in the business model for video.

Sky's move to an IP-only service fits with their wider strategy to broaden their audience while controlling costs

Sky now has a well-established record of delivering video over IP through its multi-screen service Sky Go and its OTT pay-lite service NOW TV. Sky Q (the operator's new set-top box, electronic programme guide (EPG) and platform) also delivers video-on-demand (VoD) content over IP. As we wrote in 2017 when Sky announced their intention to 'go OTT', the delivery of full Sky TV packages over IP is an evolution in terms of delivery, rather than a revolution from the supply perspective; it allows Sky to widen its delivery to an IP-only distribution approach for its core pay-TV service without needing to manage the migration of its full customer base.

Sky, in their annual results, refer to the move as "a major development for Sky that will open up headroom in existing markets, improve our cost to serve for some customer segments, and offer a future way to take Sky into new markets."[1] Indeed, the implementation of the European Commission's Digital Single Market strategy in 2018 will potentially pave the way for Sky to offer both their lighter NOW TV service and their full Sky Q service to a much larger target audience. Sky has been canny in its positioning of NOW TV relative to its full Sky service to-date, and it is likely that this service will serve as a beach-head in Europe, as indicated by earlier plans to launch in Spain.

OTT video will be a significantly larger part of the total pay-TV and video market than it is today

Traditional pay-TV access methods, particularly satellite (DTH), serve a useful function by providing almost 100% geographical coverage,[2] and for this reason major operators such as Orange, BT, Telefónica and Türk Telekom have used satellite as a means to ensure that their investment in valuable and exclusive sports rights are not constrained to their IPTV footprint. As truly ubiquitous high-speed IP access is reached – in December 2017 the UK government committed to making 10Mbps broadband access a legal right to all by 2020 – the value of

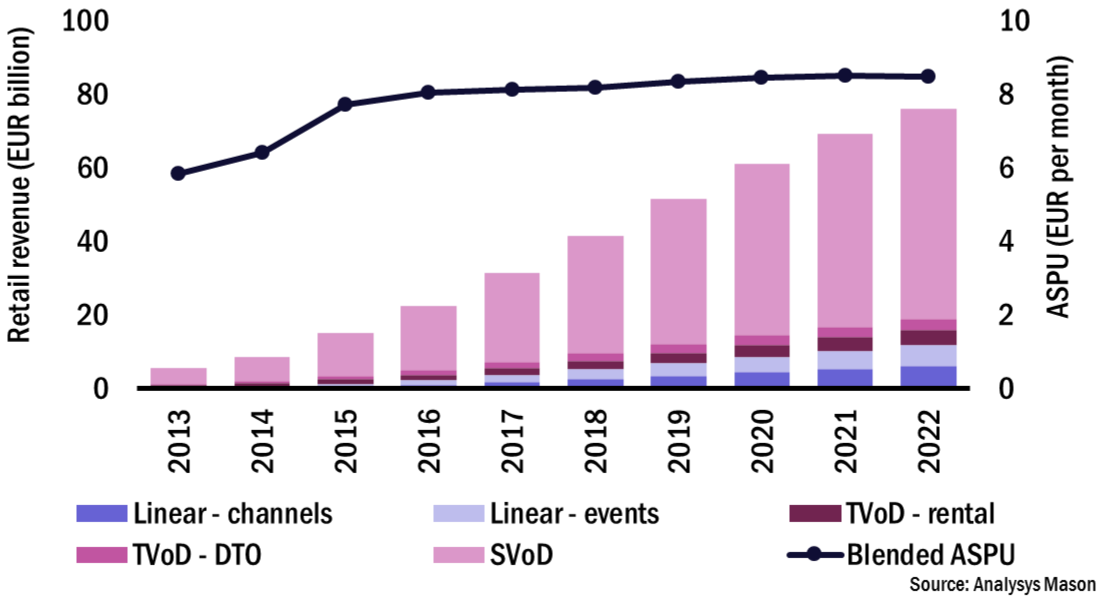
1 https://www.skygroup.sky/corporate/media-centre/articles/en-gb/results-for-the-six-months-ended-31-December-2017

2 This, though, is counterbalanced by sites where a dish is not permitted or practical. Sky estimates that there are 6 million such premises within its footprint.

satellite as a delivery method will begin to erode. Indeed, Sky noted cost-control as one of several reasons for making the move to IP delivery.

The upshot for the overall shape and value of the pay-TV market is interesting. Consumer spend in the European pay-TV and video markets will increase by approximately EUR12 billion between 2017 and 2022; of this delta, EUR10 billion will be attributed to OTT video. Worldwide consumer spend on IPTV reached USD35 billion (EUR28 billion) in 2017 and OTT video spend reached the same figure. By 2022, however, OTT video will be the more lucrative business of the two: the spend will grow with a CAGR of 19% between 2017 and 2022, and OTT video will generate a spend per year of USD84 billion (EUR67 billion) compared to the USD47 billion (EUR38 billion) produced for IPTV.

Figure 1: OTT video retail revenue by service type and blended ASPU, worldwide, 2013–2022



From DTH to triple-play and ultimately to video service provider

Sky's move throws into sharper focus the future role of its telecoms services and its broader role in customer connectivity, whether broadband, mobile or satellite. In every market in which it operates, Sky is reliant on a set of wholesale services: in its main market, the UK, these are principally from Openreach and from O2. Hence its margins in telecoms are probably low enough to be dilutive of its overall margin. Sky has always been extremely cautious about telecoms investment, and in this respect it is asset-light, especially in access. It has few defensible assets in consumer telecoms, though of course it has a highly defensible set of content assets. For satellite delivery, Sky buys capacity ultimately from SES and Eutelsat; this is a direct cost that ultimately it will not need to incur, as long as broadband is up to the job. Sky Q over IP will be a bring-your-own-access service where most consumers will have a choice of connectivity options.

Over a 10-year period, we think that this move may turn out to be a key staging-post in the journey of Sky towards being a pure content service provider, and a direct competitor to IP-based video providers, whose retail offerings involve, increasingly, a mix of scheduled and on-demand material. Sky Q over IP will move from the sidelines to the centre-ground: the supplementary option will supplant the legacy option, just as is happening with VoIP. These providers are not without physical network assets, but they have little interest in consumer connectivity, and their assets are increasingly those of tiered data centres, massive core fibre networks and

CDNs. In fact, how to deal with the staggering growth in video data traffic in the core network in the UK is a major concern for Sky, as a recent presentation to the UK Network Operators' Forum makes abundantly clear.[3]

If we are right about the broad direction of travel for Sky – and potentially other content-focused service providers in a similar situation – we expect the following consequences.

- Sky will eventually become complementary to, rather than a competitor of, infrastructure-based broadband and mobile operators. Specialists with their own sets of defensible assets will pursue their increasingly divergent aims with a decreasing amount of friction or even transactional value between the two.
- Multi-plays of access and content will start to crumble. We think that IP-only Sky Q is a sign that access-content bundling is under strain. There is little network logic to it, and margins on wholesale-based service mean that there may be little retail logic either in the long run. We do not see many such bundles holding together in 10 years' time unless operators have genuinely defensible assets on both sides of the equation, and then the logic is a retail one, not a network one.
- By becoming a service provider at a transnational, web-scale level, Sky will have to learn to fight, among a few others, Netflix and Amazon.

Analysys Mason produces detailed forecasts of the size and value of the OTT video market in 47 countries worldwide, including Europe as a whole. The latest edition of Analysys Mason's OTT video forecasts, titled 'OTT video worldwide: trends and forecasts 2017–2022' will be published in February 2018.

3 See https://indico.uknof.org.uk/event/41/contribution/7.