

FULL DISCRETION

Extra Credit

Cable is Dead? Hardly...

We often get questions from clients on our view of the cable industry. With so many consumers “cutting the cord” and new competition emerging, many expect a complicated path ahead for the sector. While we agree there appear to be challenges near term, we believe the long-term outlook for the cable industry could be positive. As of June 30, 2024, the cable and satellite sectors combined make up 6% of the Bloomberg US Corporate High Yield Index.

Near-Term Challenges

While many attribute video cord cutting as the primary culprit for the cable industry’s recent challenges, the decline in video subscribers appears to have had a limited impact on earnings. The large majority of cable company earnings are generated by providing broadband internet. That being said, broadband subscriber growth at the industry level has declined more recently due to competition from fixed wireless broadband (FWB), copper to fiber upgrades in duopoly markets, and the apparent expiration of the US federal government’s affordable connectivity program (ACP). Competition for new subscribers has increased while cable companies are midway through making expensive capital improvements to upgrade speeds. In short, we believe a perfect storm of factors exists today.

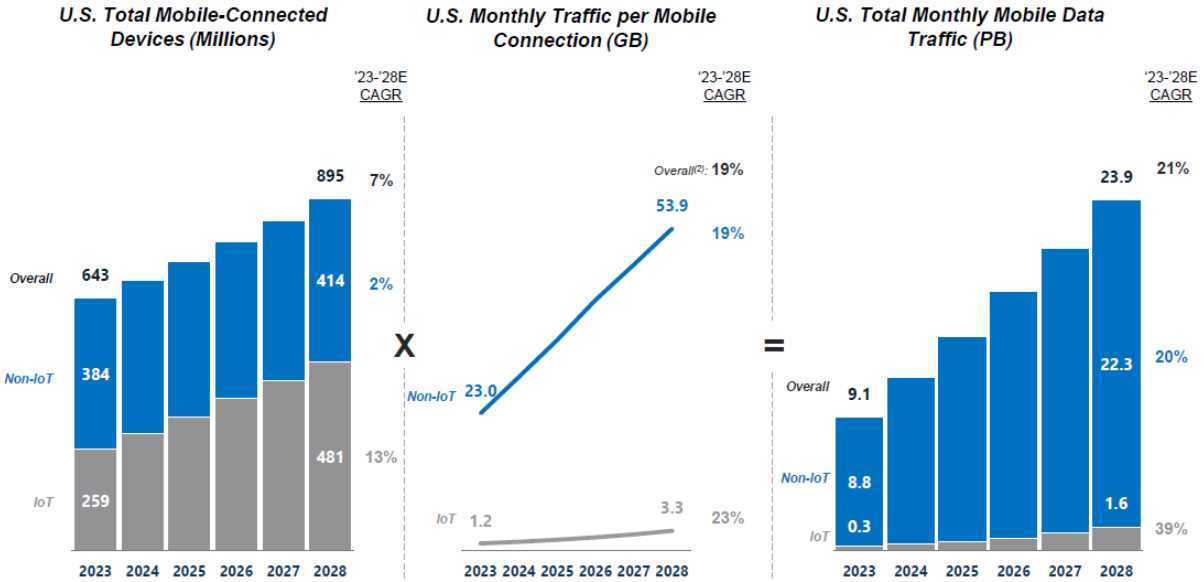
In Our View, There is Insatiable Demand for Data

The consumption of data is growing rapidly, evidenced by the proliferation of high-powered smartphones, video streaming, and a tsunami of consumption from generative artificial intelligence (AI) use cases. According to *American Tower* (see charts on the following page), as of November 30, 2023, total mobile-connected devices will increase by approximately 7% compound annual growth rate (CAGR) from 2023-2028, while US total monthly mobile data traffic will increase by 21% CAGR over that same period. It is also expected that data consumption per US occupied household (gigabyte per month) could nearly double from here through 2027. This demand for data must be met with sufficient supply in the next decade.



U.S. Total Mobile Data Traffic Growth⁽¹⁾

Expected to grow at 21% CAGR through at least 2028



Source: American Tower, Ericsson, and Altman Solon Research and Analysis, as of 11/30/2023

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Limitations of Fixed Wireless Broadband

FWB is a technology that uses radio waves to connect homes and businesses to the internet. It is the equivalent of receiving internet via a cellphone attached to your home rather than cable coming from the street. The largest wireless carriers are currently using excess spectrum capacity on their networks to provide FWB internet service to customers in targeted locations throughout the US. However, our analysis of data consumption curves against spectral capacity and suggests FWB market share gains could begin to slow over next 12-24 months.

We believe market share gains could slow because we expect national wireless carriers to prioritize mobility over FWB customers. As of September 30, 2023, T-Mobile disclosed 450 gigabytes in monthly consumption for its average FWB subscriber versus approximately 5-20 gigabytes for mobility users, according to the Ericsson Mobility Report from November 2023. In other words, we believe there is a strong incentive for the wireless carriers to prioritize mobility over FWB subscribers when excess network capacity is exhausted. In addition, speed limitation of 50-130 megabits per second for FWB can also limit the total market opportunity to a specific consumer cohort. So while we expect FWB to continue to grow, that growth could be constrained, leaving cable companies with an opportunity to recapture a fair share of industry growth.



Structural Advantages in the US Market

In the US, participants in the broadband market have a structural advantage given their regional wired duopoly footprints. In Europe, regulatory bodies have mandated three or more competitors per market, but the US still remains largely restricted to duopoly regional footprints for wired high-speed internet providers. Without a regulatory need to expand access, cable companies are unlikely to do so, and we believe the structural advantage will persist in the US.

Potential Growth Trajectory of the Cable Industry

A common misconception is that the broadband industry is fully saturated and has no growth potential. On the contrary, our analysis of addressable households suggests 2-3 million new subscribers annually, driven by household formation and increased penetration. We anticipate cable companies stand to gain a fair share of the growth potential.

Pricing Power is the Other Leg of Industry Growth

Pricing power, or average revenue per user (ARPU), can also be a lever for cable companies to grow revenue. We continue to observe participants taking price in the market, whether it be FWB, fiber-to-the-home, or cable. The unceasing demand for data consumption and the duopoly market structure lends itself to a utility-like product, and logically, pricing power.

Conclusion

We look through the cycle with a long-term mindset toward extracting alpha. Given the likelihood of growing demand, high barriers to entry for new competitors, and pricing power within duopolistic markets, we think cable companies have the ability to overcome the challenges that are priced into the market today. While there may be winners and losers, we do not view the entire industry as a melting ice cube to avoid.

Please see Important Disclosure on following page, an integral part of this document.



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