



EchoStar Brings New Hope to Broadband Properties

By Jimmy Schaeffler ■ *The Carmel Group*

For many years, there has been a serious lag in the development of the private broadband¹ community. This gap involves the two major U.S. Direct Broadcast Satellite (DBS) providers, DirecTV and EchoStar, and their respective inability to really break into the Multiple Dwelling Unit (MDU) and Private Cable Operator (PCO) sub-sectors.

Yet at a two-day meeting held at EchoStar headquarters in Littleton, CO, during the second half of July 2003, joint commitments were made that appear to be causing a change of this rather frustrating scenario. EchoStar's Executive VP, Jim DeFranco, as well as top lieutenants in its MDU-division, Lloyd Nelson and Bob Grosz (formerly with EchoStar MDU ally, Petaluma, CA-based Castle Cable), delivered a set of remarks, charts and presentations to a solid contingent representing the Private Cable Operators (PCOs) from around the U.S. EchoStar told of its new-found commitment to the MDU and PCO marketplace. Apparently, EchoStar executives also made time to absorb concerns of the PCOs, as well, in order to fully invigorate the potential for a true "team" alliance. This latter exercise is critical, because it would be hard to imagine the real success of any multi-channel operator without the strong assist from PCOs.

Formerly, companies like EchoStar had tried and tried to break into this sub-sector. All along, creating a business model that satisfied the multiple parties involved remained an elusive goal. This meant that one of the bigger and better telecom services that could have been part of the MDU and PCO

marketplace—that of DBS-related services—had generally remained unavailable. Moreover, this meant that cable providers and an occasional Satellite Master Antenna TV (SMATV) service had the estimated 44 million U.S. MDU inhabitants in what a cynic might call an "entrenched monopoly." Add to that the existence of both exclusive and perpetual contracts between the outside cable companies and the MDU owners/operators themselves, and true change here became even more challenging.

What EchoStar Plans

With an estimated 8.8 million subscribers signed up as of mid-year 2003, EchoStar is the third largest multichannel video provider in the U.S. today. What's even more remarkable is that EchoStar has built this base in less than nine years, whereas its larger cable competitors have been operating their base businesses for two or three decades.

Nonetheless, the overwhelming majority of DBS subscribers making up this rich base are single-family unit (SFU) subscribers, not MDU subscribers. Were EchoStar able to substantially break into this MDU realm, The Carmel Group estimates its ability to add—conservatively—an estimated one million subscribers during the next five years. With average monthly revenue per unit (ARPU) running around \$55 these days, that equates to three-year incremental revenue of approximately \$660 million (Of course, this kind of modeling is way too simplistic, but it provides a top-level view of the real potential of the U.S. DBS marketplace, once someone or some company—like

EchoStar—taps into this Holy Grail.).

According to early reports from both EchoStar and the PCO/MDU industry trade group, the Independent Multifamily Communications Council (IMCC), EchoStar intends a three-way distribution plan. The first involves the services of EchoStar-authorized trucks and technicians, the latter of which would contact potential MDU owners and operators. The second would involve maintenance of existing contracts EchoStar acquired when it purchased the bankruptcy assets of the former WSNNet. The third would involve working with a solid number of reputable PCOs.

More EchoStar-PCO Details

Further reports suggest that, in the new EchoStar-PCO arrangements, the PCO would be the party responsible for revenue sharing payments to the MDU owner/operators. Focus is also expected to be more on newer MDU properties, following the idea that these would be less likely to involve the perpetual and exclusive cable telecom company contracts mentioned above. Also, analog and digital carriage is expected for the time being, with HDTV being added next year. Apparently, EchoStar mentioned little about the delivery of high-speed access under the new plan.

Further reports indicate that EchoStar will permit so-called "bulk" contracts (i.e., right-of-entry agreements that provide video services to all the residents in an MDU community, at a set price per unit, after which the MDU owner will include that amount, plus a mark-up, in the resident's rent). For the delivery of analog channels, EchoStar will apparently allow PCOs

EchoStar in The MDU House	
EchoStar Headquarters	Littleton, CO
Key EchoStar MDU Executives	Larry Nelson Bob Grosz
Total EchoStar Subscribers (1)	8.8 mil
Total DirecTV Subscribers (1)	12.4 mil
Total U.S. Multichannel Subscribers (1)	89 mil
Current U.S. DBS ARPU (1)	\$55
Current U.S. DBS SAC (1)	\$507
Total U.S. MDU Residents (1)	44 mil
Major MDU Competitors	U.S. Cable MSOs
EchoStar Revenue Gain From Additional 1 Mil. MDU Subs	\$660 Mil.
(1) Estimate as of June 30, 2003	
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to directly bill the consumer. For the delivery of digital services, it appears probable that EchoStar will itself do the direct billings. Customer service and maintenance functions would be the responsibility of the PCO. These terms recognize the traditional position of PCOs, who typically insist that they "own" (or control the management of) the customer. The new plan suggests a strong set of analog channels will be offered, accommodating the fact that in this telecom environment, PCOs make the majority of their money from the delivery of these analog channels.

EchoStar has apparently also conceded significant control to the PCOs by way of agreements 1) not to intrude on rights of entry or 2) to force the PCO to turn over control of the subscriber to EchoStar at the conclusion of the contract. Further in this regard, EchoStar has also apparently agreed that the PCO can actually sell the ROE at any time, and this would not involve a penalty. Plus, as long as the right of entry exists, EchoStar promises to not act to take the subscribers of the contracts away from the PCO.

As far as digital tiers are concerned, three tiers and three sets of prices are envisioned. Each would augment the analog package. For compensation, information gathered suggests the PCOs would be incentivized via payments for access to subscribers, as well as for commissions for products sold by the PCO itself. Additional options are reported that permit the PCO to charge what the market will bear, and that the PCO would be paid a percentage of the ARPU.

As far as specifics are concerned, the EchoStar-PCO arrangement suggests PCOs would pay EchoStar an initial digital system fee of \$10,000 per community. Set top boxes would be priced at \$100 per analog, and \$100-\$150 per digital, the latter being available in either L-Band or QAM versions.

Another surprise is the report that these EchoStar-PCO contracts would not be exclusive, and that the PCO could enter into similar service-and channel-delivery agreements with companies such as DirecTV and those in the cable industry.

A Note of Caution

IMCC executive director Bill Burhop, typically an advocate on behalf of his PCO membership, added this caveat on the deal: "It is also clear that some PCOs believe this is another bait and switch, that Echo will eventually endeavor to own the sub, and take control away from the PCO, during or after the contract expires, leaving the PCO as simply a reseller for Echo with little ability to price the products, to determine channel line-ups, or generate margin. This would leave the PCO with no ability to use the subscriber/ROE as collateral to finance new projects and leave the PCO without an exit strategy. This view is that signing such a contract, with any provider, means that the PCO becomes a captive of the deal and this would be the end of the traditional PCO business model and branded customer service or relationship. A trap about which to be weary. [sic] It also is unclear how such a deal might impact IMCC mem-

bers that are manufacturers/vendors or current providers of the DirecTV products."

Note also here that EchoStar was approached for comment and Messieurs DeFranco, Grosz or Nelson were not available.

Summary

This renewed effort by EchoStar to deliver services en masse to scores of millions of MDU tenants represents, if it is real, is a solid step toward the creation of new infrastructures and systems that could bring MDUs much further into the 21st century telecom experience. Yet, as the industry trade group cautions, there are contractual provisions that will have to be read and negotiated carefully. With that caveat in mind, EchoStar is to be congratulated for not giving up on America's (25+ VERIFY) million MDU occupants. Is that a light we see at the end of a long tunnel? ■

About the Author

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Footnote:

1. For the purposes of this article, the term, "broadband" means "A telecommunications service 1) that, according to the FCC, offers at least 128 kbps and 2) that provides multiple channels of independent data over a single communications medium, e.g., 5,000 telephone conversations and 132 TV channels all carried on a single line." Conversely, the term, "narrowband," or "baseband," indicates "A transmission that contains just one service, e.g., a single telephone line or a single ISP (such as AOL)."