IPTV Monitor—Issue 3

Produced by Accenture and the
Economist Intelligence Unit

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Welcome to the third edition of the IPTV Monitor, produced by Accenture in cooperation with the Economist Intelligence Unit. In this issue, we highlight the results of our most recent IPTV survey of executives in the communications, broadcasting and media industries. One interesting result of this most recent survey is that confidence in the three-year outlook for IPTV revenues is almost evenly strong in every geographic area of the world.

Yet several challenges remain to significant take-up of IPTV services: content rights is often the most-discussed obstacle, but the importance of technical and operational issues is also becoming more apparent. High levels of service quality are essential to IPTV success; an IPTV service must at least match the quality of standard TV programming. The impact of IPTV offerings on customer retention also constitutes a risk. Our experience from other triple play operators is that, if operators bundle IPTV with other services but then do not deliver on quality expectations, they may lose that customer across the entire bundle.

Amid the hype and expectation of the interactivity and flexibility that IPTV provides, it is essential to remember that the cornerstone of a TV service will remain TV programs that people want to watch and that are transmitted reliably. Thus, acquiring the right programming content and getting it to customers remains the first priority.

Nevertheless, the value proposition for IPTV remains strong. Newer generations of viewers are now well accustomed to the freedom of searching for content, and then viewing it when and where they want to. IPTV promises to bring that level of freedom to television viewing.

The results of the latest Accenture and the Economist Intelligence Unit IPTV Confidence Index underscore a central truth about how people think of the future: People tend to overestimate what can be done in one year and to underestimate what can be done in five years. Imagine being told in 2002 that by 2007 you could carry all of your music around in a pocket-sized device. Or that we would be recording a video on a mobile phone and then broadcasting it to a multinational audience the same day.

Caution in the short term is good advice when it comes to IPTV: solidifying content acquisition, getting service quality right, ensuring a good customer experience. At the same time, boldness in terms of a longer-term outlook is also going to be essential for those who intend to achieve high performance with their video offerings.

Ray Dogra, Accenture

Business confidence in IPTV: On the rise

Written in cooperation with the Economist Intelligence Unit

Key points:

- Executive confidence that IPTV will generate significant revenue for their firms within three years remains strong. Confidence in the shorter-term revenue prospects is lower but on the rise, particularly among network operators and consumer electronics firms.
- Network operators expect content to generate the lion's share of income, while other industry players believe advertising will be the leading revenue earner.

"An operator without content no longer has customers," claimed Didier Lombard, CEO of France Telecom, in a recent newspaper interview. France Telecom operates in a particularly competitive domestic market, where triple-play voice, television and Internet access now constitute a basic offering. But major operators worldwide are increasingly concluding that providing audiovisual content is the only way to keep subscribers on board, and are rolling out IPTV apace.

France Telecom can now claim to be Europe's largest Internet TV provider, with more than 400,000 subscribers at the end of 2006. This places it second worldwide only to Hong Kong's PCCW. Spanish incumbent Telefónica, meanwhile, with more than 300,000 customers in Spain, is exporting its IPTV model to its subsidiaries in Latin America, CTC Chile and Telesp Brazil, as well as O2 in the Czech Republic. Telefónica has its targets set between 1.2 million and 1.4 million customers for its Imagenio service by 2009. Verizon in the US planned to have 175,000 video customers signed up for its Fios TV service by the end of 2006, up from 100,000 at the end of September.

IPTV subscribers, selected operators

IPTV provider	Customers
PCCW (Hong Kong)	654,000 (October 2006)
France Telecom (France)	450,000 (December 2006)
Telefónica (Spain)	304,000 (September 2006)
Free (France)	270,000 (mid-2006)*
Neuf (France)	250,000 (December 2006)
Chungwa (Taiwan)	200,000 (October 2006)
Belgacom (Belgium)	100,000 (November 2006)
Telefónica O2 (Czech Rep)	10,000 (December 2006)

Source: Operators. All figures quoted are approximate.

* Free claims it has 1,260,000 subscribers who are "eligible for audiovisual services," although the meaning of the phrase is not defined.

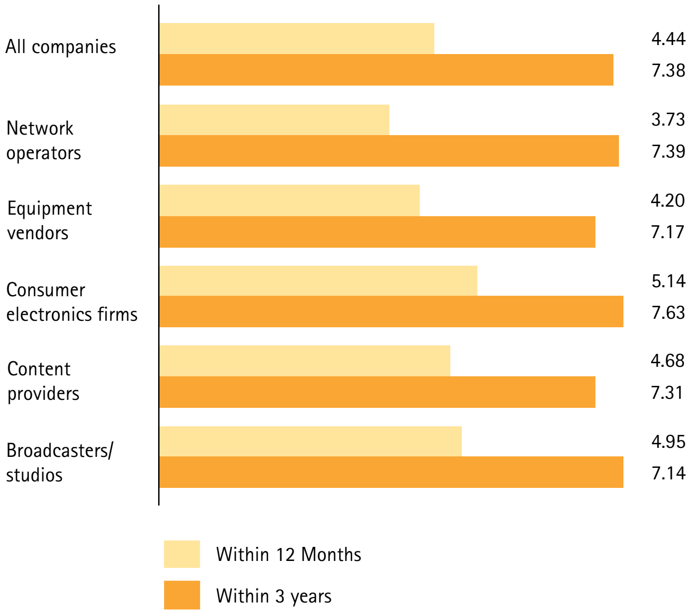
Operators clearly want IPTV to do more than just plug the dam of leaking subscribers. As attested by their aggressive rollouts, hope is building in the industry that IPTV will translate into major revenue growth.

According to the latest Accenture and the Economist Intelligence Unit IPTV confidence index—which is based on a survey of telcos, broadcasting companies and media firms conducted in October 2006— industry-wide confidence in the longer-term outlook for IPTV remains strong. A majority of respondents are confident or very confident that IPTV will generate significant revenue within three years. In index terms, the long-term confidence level of IPTV industry executives is 7.38 on a 1-10 scale, which translates as "fairly confident." This number is slightly down but largely consistent with the score of 7.55 from our previous survey in May 2006.

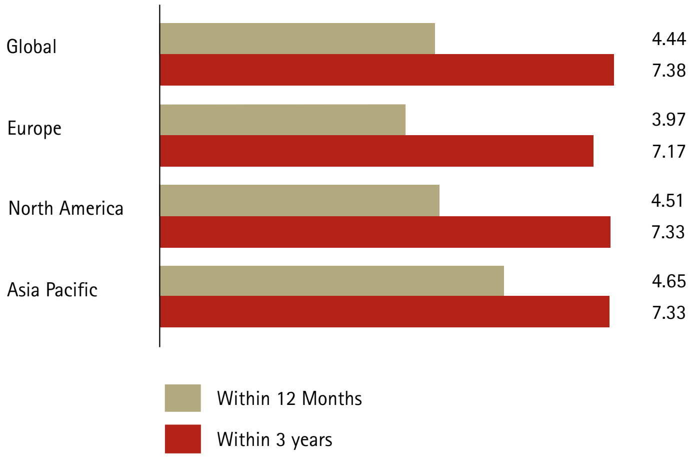
Confidence levels are naturally lower when it comes to short-term revenue prospects. A small minority of survey respondents say they are largely or very confident that IPTV will generate significant revenue within the next year. The short-term confidence level is 4.44 ("a little confident") in the index. However, this is noticeably up from the 4.06 level registered six months earlier.

Among different players in the IPTV industry, network operators are markedly more optimistic about one-year revenue prospects than they were six months ago, although they are still less confident than peers elsewhere in the value chain. Their confidence level regarding short-term revenue growth has risen to 3.73 from the 3.11 registered in May 2006. Of all the groups of executives, those from consumer electronics firms are the most optimistic, and account for the largest increase in confidence from the previous survey.

IPTV confidence index*: Confidence that IPTV will begin to generate significant revenue for players in the industry



IPTV confidence index: Geographic breakdown



* Technology industry executives' level of confidence that IPTV will begin to generate significant revenue for players in the industry. Survey responses are fed into a model which converts the data to an index using a 1-10 scale, where 1-2 = not all confident, 3-4 = a little confident, 5-6 = somewhat confident, 7-8 = fairly confident and 9-10 = very confident.

Source: Accenture and the Economist Intelligence Unit

So where will the money come from? The IPTV industry as a whole believes targeted advertising will generate the lion's share of IPTV revenue, according to 47 percent of surveyed executives.

Network operators, however, disagree: in contrast to executives from broadcasters, content providers and other IPTV industry players, network operators believe subscription fees for premium content will provide the largest stream of revenue, followed by subscription fees for basic content, with advertising positioned behind.

Such a calculation makes successful content acquisition vital. France Telecom in November became one of the first telcos to establish a subsidiary to invest funds in co-producing up to 15 films annually. The gamble reflects the difficulty operators typically face in securing content, and the financial incentives the French government offers to investors in film-making. But it also underscores the operator's commitment to building a large-scale content delivery business.

Yet uncertainties persist. Those surveyed suggest that rather than clamoring for a well-understood or differentiated product, customers instead buy IPTV principally because it comes as part of a cheap voice and internet package.

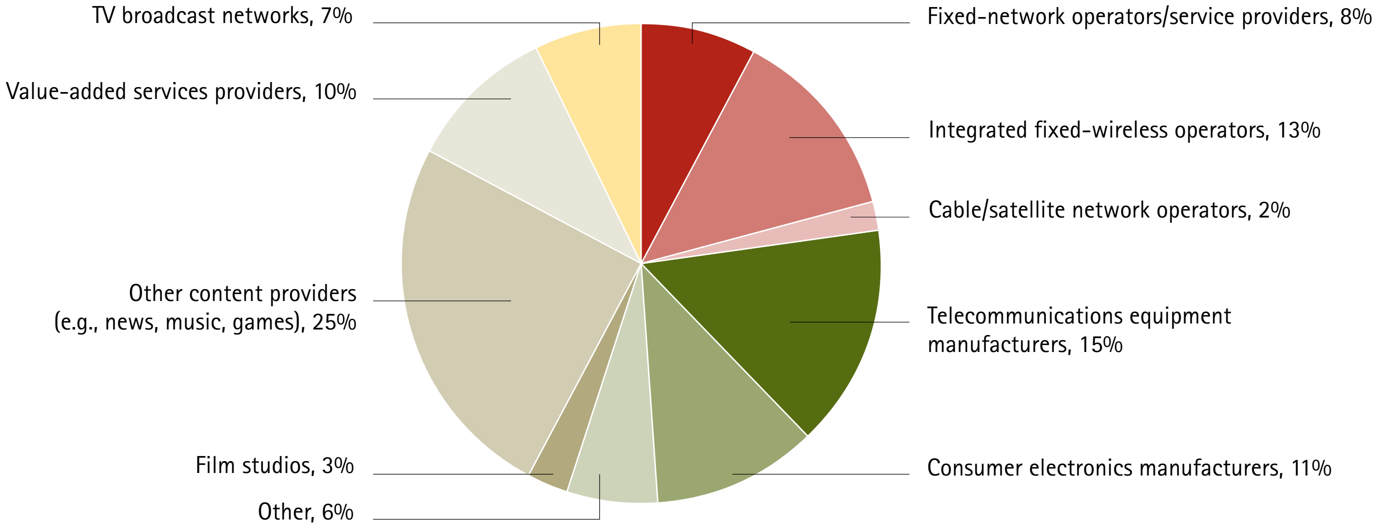
Indeed, only 11 percent of all respondents think that customer understanding of the IPTV value proposition is high enough to support a solid business case, and this figure sinks to 3 percent among network operators. And whereas 64 percent of those surveyed agree that discounted service bundles provide the greatest enticement to buy IPTV offerings, this figure rises to 74 percent among network operators. The trick will be to get customers, who are presently faced with a plethora of free television and online video, to readily pay for premium content.

What do you think will be the principal revenue sources for IPTV?

	Minor source of revenue	Moderate source of revenue	Major source of revenue
Network access fees	44.58%	39.94%	15.48%
Subscription fees for basic content	32.83%	40.36%	26.81%
Subscription fees for premium content	15.55%	44.21%	40.24%
Pay per view or action	19.06%	52.50%	28.44%
Advertising-mass market	30.51%	39.88%	29.61%
Advertising-targeted	16.11%	37.39%	46.50%

About the survey

In October 2006, Accenture and the Economist Intelligence Unit conducted their second semi-annual IPTV survey (the first having been conducted in May 2006). Participating in the most recent poll were 341 executives of technology and media firms that are involved in or close to the IPTV business. The survey covered 46 countries in three regions; 35 percent of respondents were based in Europe, 33 percent in the Americas and 32 percent in Asia Pacific. The types of firms represented in the survey are detailed below:



In addition to being cosmopolitan, our survey sample was very senior. 46 percent of respondents were C-level executives such as CEOs, CIOs and CFOs, and the other 54 percent consisted of senior managers such as heads of business units and directors of marketing or planning. Participants also came from a range of company sizes, with 51 percent reporting annual revenue of over US$500 million, and 22 percent over US$5 billion.

The business case: getting customers to pay

Written in cooperation with the Economist Intelligence Unit

Key points:

- Few industry players expect IPTV to drive profit growth at their firms; rather, securing new revenue streams and new customers are viewed as the chief benefits of IPTV. In contrast to peers in other regions, North American executives look primarily to use IPTV to drive adoption of other services.
- Forming content partnerships is priority one: operators look to partnerships rather than joint ventures or other vehicles to source content. Signs are that a lack of compelling content is receding as an obstacle to household IPTV adoption.

When people first started using the Internet, operators had no need to offer pricing incentives to get consumers online. Customers tolerated high per-minute access charges and the frustration of dropped dial-up connections because they were getting something useful. IPTV is proving to be a harder proposition. Operators such as Belgacom this year felt compelled to launch IPTV on a free trial basis to bring customers on board. Indeed, one of the largest challenges operators have to overcome when launching a TV service is converting free or low-paying customers into higher paying ones, according to Telefónica's chief technology officer, Vicente San Miguel, in a recent presentation to analysts.

Despite the difficulty of persuading the mass market that pay TV is good value, 43 percent of all respondents cite revenue growth as the principal business advantage to be gained from their involvement in IPTV. Substantial regional differences exist, however. In the Asia Pacific region, 52 percent of those surveyed believe new revenue streams are the greatest business benefits to be drawn from IPTV; that number drops to 47 percent for Europeans, and 32 percent for North American executives. There, the largest share of respondents (39 percent) instead emphasizes the ability of IPTV to drive adoption of other services.

What are the principal business benefits that your company hopes to achieve through involvement in the IPTV business?

Select up to two benefits.

Reduce customer churn	13.20%
Acquire new customers	28.15%
Establish new revenue streams	42.82%
Drive profit growth	12.61%
Increase take-up of broadband access connections	21.11%
Drive adoption of other services	17.60%
Acquire/develop new competencies	14.96%
Respond to competitor threat(s)	11.14%
Not applicable (we have no plans to become involved in the IPTV business)	15.84%

Even if revenues can be earned, they do not necessarily immediately translate into profits. The initial start-up costs to launch a service plus the technical and operational challenges of a rapid rollout mean that it will take a while before the services become profitable in their own right. IPTV as part of a bundled service is now proving to be an effective weapon against churn and is supporting new customer acquisition. Furthermore, it is only when a large enough customer base has been reached that the economies of scale, particularly in content acquisition, can kick in. This reinforces the need for providers to think about IPTV in the context of their overall video strategy, so that rights can be exploited across multiple distribution channels.

Assuming operators can achieve wide network reach and acquire content, profits should follow. Contrary to a popular assumption that content providers will squeeze operators severely in sourcing deals, more than 80 percent of industry executives in the survey—and 88 percent of those from content providers—believe operators are somewhat or highly likely to share in content revenue streams.

Even though large service providers have started signing content deals with major film distributors, complaints persist that Hollywood's distribution structure and its attitude towards IPTV needs to change. From a film distributor's standpoint, meanwhile, the IPTV customer base may be growing, but it remains relatively small. Given this context, 42 percent of surveyed executives overall—and 61 percent of those at network operators—say forming partnerships with independent content providers is the single most important measure to take if entering the IPTV business in the next 12 months.

But there are signs that the content provisioning difficulties are straightening out. In our previous survey in May 2006, 23 percent of operators cited a lack of compelling content as the main obstacle to IPTV take-up in the twelve months ahead; that number falls to 17 percent in the latest survey. Taking a three-year time horizon, however, only 10 percent of network operators think content sourcing will be a major hurdle.

Surveyed executives clearly feel there is much to gain for both content provider and telcos from the resolution of provisioning difficulties. Fully 87 percent of respondents believe that content providers have the most to gain from IPTV in terms of revenue, while 72 percent think telcos will be the biggest winners. But if content companies and telcos are to meet these expectations, they first have to loosen customers' and advertisers' purse strings.

IPTV providers can begin signing up advertisers none too soon, as strong competition for ad revenue can be expected to come from the likes of Google. The latter's US$1.65 billion purchase of YouTube loudly proclaimed its intention to make money from targeted advertising linked to free video content. Given where Google and other video sharing and content sites are seeking revenue, they represent a potentially large threat to the nascent IPTV business.

Bundling the customer in

Written in cooperation with the Economist Intelligence Unit

Key points:

- The customer proposition remains the least developed part of the IPTV business. Customer understanding of IPTV offerings is perceived by executives to be low, and operators' marketing and pricing strategies are relatively undeveloped.
- Quality-of-service problems are seen as the largest obstacle to consumer adoption of IPTV over the next year. These problems should recede in the longer term, however.

As any supermarket owner will tell you, nothing attracts a customer like a bargain. And compared to the combined pricing for voice services and Internet access that consumers were paying only a few years ago, the average triple play-offer is just that: a bargain. Executives from every sector and region in the survey agree that discounted pricing thanks to bundling will drive customer spending on triple- or quadruple-play services in the next twelve months.

The success of IPTV business plans, at least in Europe and Asia, depends on more than having television act as a form of loss leader for bundled access services. Service providers need to have customers spending on basic and—most importantly—premium subscriptions. For that kind of spending to occur, however, providers must have not only attractive content, but also realistic marketing and pricing plans.

The industry is still seeking its footing, however, when it comes to selling television and video services. Only 15 percent of those surveyed judge IPTV marketing and pricing strategies to be fully ready. Among Europeans that figure falls to 9 percent, compared to 18 percent of those surveyed in North America and 15 percent of Asia Pacific respondents. Just 12 percent of network operator executives surveyed believe their marketing and pricing strategy is sufficiently developed.

How ready are the following aspects of the IPTV business to enable the delivery of IPTV services by network operators, in your opinion?

	Not ready	Developing, but incomplete	Ready
Content provision	16.82%	57.06%	26.13%
Development of unified standards	40.79%	46.22%	12.99%
Marketing and pricing strategy	37.61%	47.76%	14.63%
Operational capability	23.12%	53.45%	23.42%
Transparent regulation	56.46%	36.04%	7.51%
Customer understanding of product proposition	48.19%	40.36%	11.45%
Access and head-end technology	20.18%	55.72%	24.10%
Set-top box technology	15.81%	53.19%	31.00%
Transport network technology	15.36%	48.19%	36.45%
Software & video platform technology	13.90%	51.36%	34.74%

There is hope among 39 percent of all executives that the ability to move content between different devices will draw customers to IPTV. But not every sector is convinced. Whereas 56 percent of equipment manufacturers believe customers' desire to transfer content between their PCs, TVs and mobile phones will spur IPTV adoption in the coming year, only 37 percent of content providers, 32 percent of network operators and 28 percent of consumer electronics companies think this is the case.

Given how much video is available for free online, whether pirated or otherwise, operators must (1) work out how to market and price an IPTV service, and (2) ensure the IPTV service is of high quality and easy to use. Here again, there are shortfalls in what is being offered. Quality-of-service issues such as low bandwidth and picture distortion will be the largest single obstacle to IPTV uptake over the next twelve months, according to the Accenture and the Economist Intelligence Unit survey. Within three years, though, all sectors of the industry expect quality-of-service issues to be largely resolved. By that point, competing television services from other TV providers, such as cable and direct-to-home satellite, will pose the largest challenge to IPTV providers' plans.

What do you view as the single most important obstacle to IPTV adoption by households over the next 12 months?

Insufficient availability of compelling TV programming or other entertainment content (e.g., games)	13.91%
High subscription fees due to the high cost of network access and/or equipment	19.53%
High subscription fees due to the high cost of content and services	10.65%
Quality-of-service issues (inadequacy of technology: e.g., low bandwidth, picture distortion)	25.44%
Increased competitiveness of offers from alternative TV providers (e.g., cable, DTH)	10.65%
Poor customer service and technical support	5.92%
Satisfaction with current services	11.54%
Other, please specify	2.37%

In three years' time, what do you expect will be the single biggest obstacle to IPTV adoption by households?

Insufficient availability of compelling TV programming or other entertainment content (e.g., games)	12.09%
High subscription fees due to the high cost of network access and/or equipment	9.73%
High subscription fees due to the high cost of content and services	12.68%
Quality-of-service issues (inadequacy of technology: e.g., low bandwidth, picture distortion)	14.45%
Increased competitiveness of offers from alternative TV providers (e.g., cable, DTH)	34.22%
Poor customer service and technical support	7.67%
Satisfaction with current services	7.08%
Other, please specify	2.06%

IPTV players thus have little time to develop a loyal customer base, especially as big-name content, broadcasting, cable and satellite pay-TV firms are angling for business in the developing market for delivering content over IP.

Certainly global brands such as Disney are indicating they take IPTV increasingly seriously by signing content distribution deals with operators such as True in Thailand and BT in the UK. But content does not have to come in the form of the latest Hollywood blockbusters or top-flight sporting events to draw paying viewers. In Italy, Fastweb, which expects to become profitable next year, has built revenue by selling local content and by catering to kids. Children's TV now accounts for more than 40 percent of Fastweb's on-demand programming sales, and the company claims to do a good trade in old Italian films and Italian television series from the 1960s and 1970s.

About Accenture

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