



"Infinite Possibilities" television?

By Arjang Zadeh, Gregory K. Douglass and Raymond Dogra

Nagging questions swirl around the business case underlying Internet protocol television. To be successful, an IPTV strategy must be based on creative thinking about how delivering video content over the Internet will change the way people access and use that content, and about how it will enable new ways of delivering value-added services and advertising.

After several years of hype and hope, planning and testing, some of the biggest players in telecommunications, media and cable are poised to metaphorically flip the switches that will activate the flow of content—and, presumably, the flow of revenue—via Internet protocol television. The likes of AT&T, Telecom Italia and PCCW in Hong Kong—along with a host of cable and major media companies—are just a few of the hundreds of businesses vying for a share of what's popularly known as IPTV, which could be worth \$17 billion a year by 2010.

But nagging questions still swirl around the business case underlying IPTV. And some wags are already asking whether the "IP" stands for "infinite possibilities" or "impossible payback." The answer is that IPTV will be an important new business—but only if all the various types of companies going for a piece of the pie understand and surmount the hurdles they face.

A lack of consumer awareness of IPTV and the generally hazy notion of what its value propositions might be are among the first obstacles these companies will encounter. Almost half the respondents in a recent international IPTV study

conducted by Accenture—sampling the opinions of consumers in Western Europe and the United States—did not really know what IPTV is. Even those who claimed some understanding of it had widely differing perceptions.

Is that a problem? Not necessarily. People know what television is and what the Internet is, and our research also shows healthy demand for the types of services IPTV can provide. If consumers have value propositions in the form of information and entertainment options presented to them at attractive prices, then understanding and subscriptions should follow.

So first, service providers need to create those attractive value propositions. Some operators are marketing IPTV as just another way to deliver video services, with a bit of cool interactivity thrown in as a bonus. These providers might, for example, offer viewers watching the FIFA World Cup soccer tournament the option to make real-time bets on different features of a game or connect live with other fans around the world.

The hard truth, however, is that most of the interactive features and other functions touted in IPTV solutions are already available, with regular digital interactive cable. If

interactivity is the distinctive product feature an IPTV provider is using as a marketing pitch, then there are nearly 3 million digital cable subscribers in the United Kingdom alone, for example, who are likely to respond, “Ho-hum.”

Indeed, such a value proposition leaves a provider vulnerable to some of the consumer fears about IPTV that were also revealed in the Accenture research study. Consumers are painfully aware of how often their home Internet connection goes down, and they struggle with computer viruses and unwanted adware. Many believe they would encounter similar problems with IPTV services.

A channel of one

In fact, much more profound value propositions exist for IPTV. Here is a way to understand one of them. Glance through the weekly programming guide for the 100 channels of your cable service or the 500 channels of your satellite service, then ask yourself a simple question: How many of these programs are relevant to my interests? The most likely answer is that you have no idea.

But consider what happens when, through the combination of video programming, Internet browsers and content management software, you can search video content much like you surf the Web, finding and cataloging what interests you most. This is not just “video on demand,” a service to which consumers already have access. This is “*my video content* on demand.” Over time, it will not matter how many TV channels are available to you; that entire mental model of television will become increasingly meaningless. All that will matter is one channel: yours.

When providers know they can identify you as a “market of one,” they will be able to target services and advertising based on interests you have already expressed through your choices, thus increasing your satisfaction and loyalty to their company. Internet users already know about this feature: Commercial websites, such as Amazon.com or Apple.com’s iTunes, make educated guesses about your interests based on sophisticated software that analyzes your past purchases, and then suggest other products and services that might interest you.

Today, the issue of advertising is obviously a complex one, as TV viewers continue to find ways (through personal video recorders and the like) to avoid watching traditional advertising spots (see “Why TV advertising will never be the same,” *Outlook*, January 2006). Indeed, the Accenture IPTV consumer study found that “less advertising” was one of the more appealing features to consumers of video services delivered over the Internet. In truth, the issue with advertising may not be a desire for “less advertising” but rather for “less advertising that means nothing to me.”

IPTV will fundamentally alter the traditional television advertising model. Because the set-top box will become essentially a database of viewing and purchasing activities, IPTV will unlock opportunities for more personalized advertising—including one-to-one targeted offers and interactive ads. Advertisers will be able to identify the commercials that customers are watching, and this data will then be used to improve the efficiency of marketing campaigns.

Concerned about privacy? Consumers will be able to opt in or out

of IPTV's ad monitoring feature, and will weigh for themselves the pros and cons of both options. As with a frequent shopper card consumers use at the grocery store—which means the store knows every pack of chewing gum and jar of peanut butter they have purchased—the positive trade-off will come in purchase discounts, special offers and services tailored to their real interests.

Similar functionality will increase the value of advertising for everyone in the IPTV value chain. Consumers are more likely to pay attention to an offer targeted to their expressed interests, and advertisers are more likely to pay for it. Even small businesses—a pharmacy, a dry cleaner, a florist—might be willing to pay for

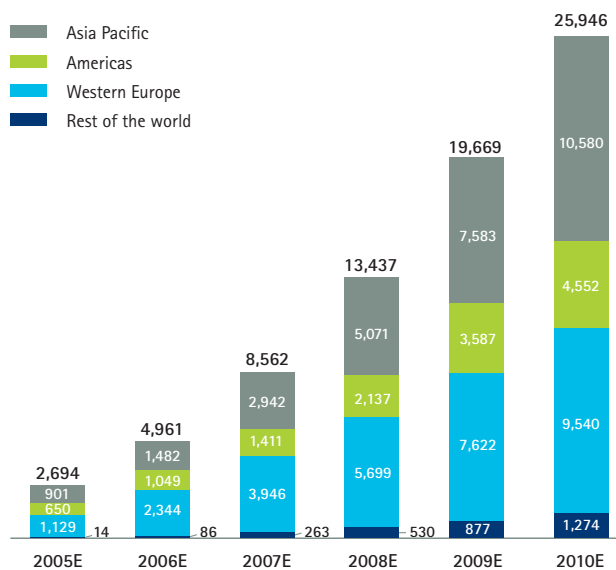
an IPTV ad if they knew it would be targeted only to people living within a certain distance of the store.

A community of many

Yet IPTV can also mean much more than creating increasingly cocooned individuals watching TV programming selected especially for them. Consider the innovative IPTV initiative currently being developed in Iceland by Reykjavik Energy, the utility that provides electricity and water to the city of Reykjavik and surrounding communities. Industry observers are watching the initiative closely because Iceland, though small in population, has a technologically advanced economy with high levels of broadband penetration. Thus it serves as a lab test for larger-

Regional IPTV subscribers (thousands)

The number of IPTV users could increase more than twelvefold in the next six years.



Source: "IPTV: A Global Analysis," Informa, 2005

scale IPTV initiatives elsewhere in the world.

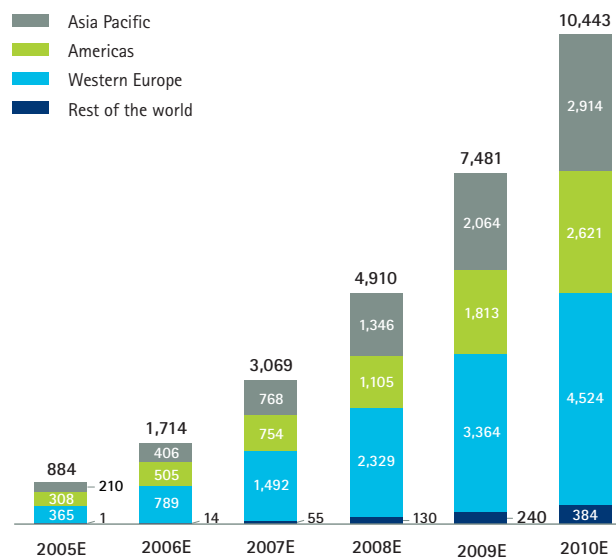
Reykjavik Energy is working to connect every home and company in the city with a high-speed, interactive IP/fiber network and then put in place an IPTV platform to deliver content. Why would a utility be in the IPTV business? According to CEO Guðmundur Þóroddsson, “We are looking at fiber to the home today as another essential utility—in addition to the wires that bring energy to homes and the pipes that bring hot and cold water. One utility brings electricity, another water. But fiber and our IPTV platform will provide a form of energy just as important to our citizens: information.”

Listen to Reykjavik Energy executives speak of their IPTV initiative and you will hear about more than just revenue-generating strategies. Their vision is also about connecting municipalities and citizens, about enabling better sharing of government information, better educational opportunities and even improvements in the democratic process by offering people more opportunities to interact with one another.

Each municipality in the region will have its own portal and will be able to both supply content to the network and receive content from other municipalities. According to Steinunn Valdís Óskarsdóttir, the mayor of Reykjavik, “We believe our IPTV platform will significantly increase the quality of life for our

Regional IPTV revenues (US\$ millions)

IPTV revenue growth is expected to be particularly dramatic in Western Europe.



Source: "IPTV: A Global Analysis," Informa, 2005

citizens, and also make our city a more attractive place for people and businesses.”

Overcoming the challenges

Despite visionary thinking by some, the fact remains that IPTV technologies and solutions are immature and the market is fragmented. There is no “out of the box” IPTV solution—complete, integrated and ready to go. This technical reality has already led to setbacks for several providers that waited until far too late in the development process to consider integration challenges and the impact on their existing systems, especially operational systems like rating and billing.

In addition to technical issues, providers looking to create a success-

Content acquisition will become the most significant component in the IPTV cost/revenue model.

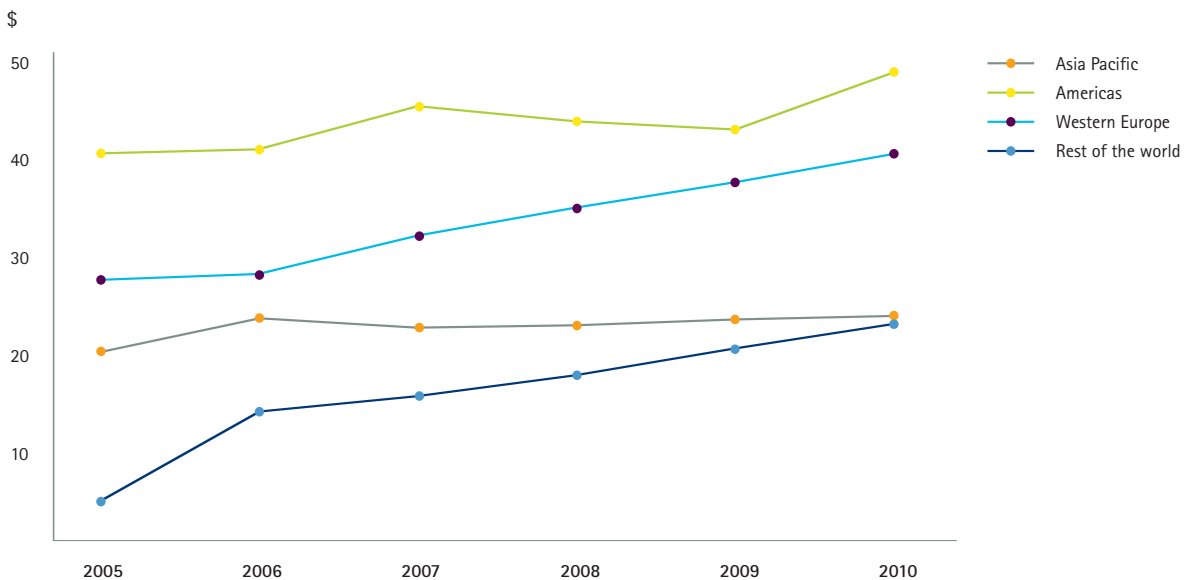
ful IPTV strategy must address a number of complexities and realities.

1. Content is king

The experiences of providers in both Europe and the United States have made it quite clear that the “killer application” for IPTV solutions is the programming content. Acquiring and processing that content are not skills that telecommunications providers necessarily possess, so they must decide how to get those skills. One option is a joint venture model, in which the IPTV provider teams

Regional IPTV average revenue per user (US\$)

The Americas and Western Europe are expected to be the biggest IPTV markets on a revenue-per-user basis.



Source: "IPTV: A Global Analysis," Informa, 2005

with cable and satellite operators to acquire wholesale premium content. A second option is a sales package model, in which a company forms a direct content acquisition relationship with film studios and other content providers.

In either case, the cost of content will be substantial for IPTV platforms. Accenture's business case analysis indicates that content acquisition will become the most significant component in the cost/revenue model, accounting for more than 40 percent of costs by the fifth year of operation.

2. Transmission quality must be high
Since content is king, the quality of the programming feed itself must be as good as or better than existing TV services. Monitoring and measuring

the quality of an IPTV feed can be a challenge, however. Network experts know how to measure network quality, but that does not necessarily indicate what a customer actually sees on a TV screen. If a customer is paying for video on demand and then complains about the picture quality during a movie, knowing where the problem occurred is vital to deciding whether to give that customer a refund.

3. Creating a viable IPTV business case is not simple

Based on our research and our work with clients, the business case for IPTV as a stand-alone product can be challenging. Because content providers have the supreme position in the IPTV value chain, margins may appear discouraging. In fact,

Much more than entertainment

Although the most obvious impact of IPTV—television programming delivered over the Internet—will be on the communications industry (see story), reverberations will be more widespread. Here are a few examples of impacts and opportunities in other industries.

Media and entertainment. The most important success factor in an IPTV strategy will be the quality of the content itself, so media and entertainment companies will occupy, arguably, the highest spot in the IPTV value chain. IPTV presents opportunities for targeted programming and content, and obviously a much broader set of channels to consumers. The impact of this new consumer channel into the home will be nothing short of revolutionary.

Health care. With the proper video links, doctors and other health practitioners could make "21st century house calls," extending their ability to provide care to patients, especially the homebound. As large numbers of the population in many industrialized nations approach retirement age, such an offering could be both important and lucrative.

Pharmaceuticals. In pharmaceuticals research and development—or, really, in any industry in which R&D is a critical function—IPTV will finally enable more satisfying forms of

virtual collaboration at much lower costs. IPTV has the potential to have a huge impact on the ability of many kinds of organizations to innovate and grow by making it easier to connect workers in meaningful ways, anywhere in the world where there is an Internet connection.

Government services. Visionaries like those in the Icelandic city of Reykjavik and those at Reykjavik Energy (see story) now see IPTV as a way to link communities, to share information and to enhance the democratic process.

Education. Online educational offerings are likely to soar in popularity, as the rather "flat" kinds of interaction in current distance learning applications become more robust through low-cost video links—either in real time or as video files that can be accessed anytime.

Financial services. Financial advisors and insurance agents will have a more direct channel to reach clients and to provide ongoing services. For example, a broker or money manager might be able to target an investment suggestion to a client, based on something he or she hears during a financial news program—a corporate earnings report or regulatory change, for example—that might have an impact on the client's portfolio.

IPTV will probably be simultaneously the most complex service a provider has and also the one with the lowest gross margins. What this means for most providers is that they must squeeze as much cost as possible from elements of the platform, including the set-top box and the hardware, software and middleware.

In an attempt to make the business case for IPTV more compelling, some providers are working with hybrid solutions—using either satellite or digital terrestrial TV for regular broadcast signals, and then using IPTV for interactive and on-demand services. BT in the United Kingdom, Telecom Italia in Italy and Telefónica in Spain have all publicly announced their intentions to include a hybrid strategy in their IPTV implementations.

4. Excellent customer service is imperative

Many providers today are finding that the bundling of services in areas like IPTV is a double-edged sword. Yes, a provider can get a bigger share of each customer's spending across the spectrum of related communications services. On the other hand, providers that fail to deliver excellent customer service with any part of the bundle risk losing the customer across the entire bundle. Studies have shown that operators that have trouble with the quality or value of one of the components or services in the bundle find that their customers are actually as much as 60 percent more likely to churn than a customer of a single service.

Clearly, operators must monitor and rigorously measure both customer satisfaction and the stability of the services they're offering. This may require ensuring that customer relationship management capabilities are fully integrated throughout the entire solution.

To be successful, an IPTV strategy must take more than a simple "me too" approach to television programming. It must be based on creative thinking about how delivering video content over the Internet will change the way people access and use that content, and about how it will enable new ways of delivering value-added services and advertising.

The current craze with MP3 players offers a hopeful parallel for IPTV providers. The iPod obviously turned out to be much more than just another way to listen to music. The ability to catalog music, to organize it and search through it, to download a variety of content and to bring it with you anywhere has changed the buying patterns and listening behaviors of millions of people around the world.

In much the same way, the marriage of video content with the search and cataloging capabilities we have all become accustomed to on the Web will produce a variety of compelling applications and services. IPTV will be one of the products that will alter the worlds not only of communication and entertainment but of government, education and business.

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