

**The Future Digital Economy
Digital Content – Creation, Distribution and Access**

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**Session 3: Overview: Digital content opportunities and challenges:
Changing value chains and business models**

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Background

The transition to digital is offering burgeoning opportunities for media firms, including content producers, distributors, advertisers and consumers. Driven by the growth of broadband, consumers now have access to an increasingly broad range of digital content, including everything from entertainment (music, videos, games) to research (medical and business information) and data. As a testament to the growth of digital content, digital music sales grew from US\$220M in the first half of 2004 to US\$790M for the same period in 2005, and now represent 6% of global retail music sales, a jump of approximately 300% in one year. Streaming video is also gaining momentum; over 94 million people in the United States, or 56% of the domestic Internet population, have viewed a streaming video. Online newspapers have also advanced in popularity with readers and advertisers; a recent report suggested that 26% of adults prefer the internet as their main source of news, while NY Times Digital reported a jump in 2004 internet ad revenues of 37.5%.

The transition to digital holds out the promise of deeper relationships with customers, improved economics, and a wide range of new business models. However, getting there continues to pose significant challenges to the industry. Traditional media companies have quickly realized that digital business models rely on innovative technology applications which they lack. As such, many believe the quickest way to develop these skills is to acquire new media Internet companies for high prices. However, with limited scale and profitability, are these companies worth their prices? Another challenge facing media companies is that younger consumers remain reticent to pay for digital content, especially music and print content, which have become ubiquitous via the internet. As a result, media companies are experimenting with new interactive media formats. Some are embracing the shift towards user-created content such as blogs, podcasts, community sites (MySpace, Yahoo! 360°), etc. Others are building models that serve niche content, greatly changing the model from one that has traditionally been driven by hits, to one of unlimited selection. Are these business models sustainable?

Current Issues

Old Media Adaptability: Traditional media companies face significant challenges as they attempt to develop digital businesses within their existing infrastructures. Now more than ever, media companies are finding it necessary to leverage technology resources as they work to build digital models. Further complicating their endeavor, the nature of communication with audiences has evolved from being one-to-many to one that is interactive. This is challenging traditional media firms to develop the tools and expertise which will facilitate managing deeper relationships with their audience. Are traditional media companies equipped to make the transition and adapt to becoming new media companies?

Enter the New Media Companies: After a decade of playing on the periphery, a handful of leading technology companies are aggressively competing with traditional media firms, and at present, are dominating the digital world. Combined, the top three technology companies (Google, Yahoo and MSN), generated approximately 42% of all internet advertising revenue last year – clearly dominating the fastest growing segment of the media business. Even more striking is that the market cap for these firms exceeds that of almost all of the largest media conglomerates. While arguably not yet a force in the overall media business, these metrics illustrate the dramatic changes occurring in the media landscape as the industry and its consumers rapidly go digital. Have we reached the tipping point where dominating technology is essential to surviving as a leading media company?

The Digital Acquisition Trail: Traditional media firms have been slow to develop business models that enable user-created content (blogs, podcasts, etc.) and foster community among users. Still reliant on

traditional one-to-many models, media firms have watched as young companies forge deep relationships with both mass and niche audiences. To play catch up, traditional media firms have been back in the market, seeking to build their digital presence through acquisition; in the last year for instance, NewsCorp paid \$580 million for MySpace (26 million subscribers) and Viacom purchased NeoPets (20 million subscribers) for \$160 million. While many consider these purchases expensive relative to the economic benefit acquired, most also recognize that expensive acquisitions are likely to be the way major media companies gain a toehold in interactive media. Are these high prices warranted for these businesses or are they short-lived fads lacking longevity?

Piracy: Digital technology continues to be a double edged sword, enabling ‘should-be’ consumers to engage in acts of piracy with great ease. The industry has attempted to move forward by embedding copyright protection mechanisms with content and offering legal download and peer-to-peer services such as *iTunes*, *CinemaNow*, *Mashbox*, and others. In addition, industry watch-dogs are taking legal action against perpetrators hoping to deter further acts of piracy. However, despite these efforts and the popularity of digital services, piracy continues to rum rampant, especially among the younger generation. How successful has the industry been in its battle against piracy? What other steps can be taken to combat piracy?

Future Implications

Monetizing digital content is still in its infancy and there will be many new, intertwined business models developed by a broad range of players before settling on successful practices. For traditional media firms, succeeding in the digital world will continue to provide many challenges. Developing digital businesses within the traditional infrastructures, without completely eroding existing businesses and without disrupting long-standing cultures, will be no easy feat. Instead, as new models that forge deep relationships with consumers are increasingly developed by younger, more nimble companies, we can likely expect more acquisitions of new media companies at prices that may seem hard to justify on the surface. The price of entry in the digital world may be high, but the rewards can be substantial.

Discussion Questions

- As media firms transition from a focus on products to services, what are the implications for these businesses?
- In what ways are the trends towards personalization changing traditional media products?
- How can M&E companies exploit user-created content?
- Are niche-media business models sustainable?
- Although the TV/broadcast world is currently separate and distinct from the PC/internet world, convergence is likely. What are the implications of such a convergence? What is the time frame associated with this melding?