Perspective

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The Content End Game

Capturing the Benefit Of Media and Telecom Convergence In the GCC

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CAPTURING THE BENEFIT OF MEDIA AND TELECOM CONVERGENCE IN THE GCC

As the wave of sector liberalization continues, Gulf Cooperation Council (GCC) telecom operators are facing increasing competitive pressure. On one hand, the market for traditional telephony, whether fixed or mobile, is so saturated that it can no longer be a viable exclusive source of growth. On the other hand, telecom-media convergence has brought about opportunities that could be considerable but that are fraught with uncertainty. Telecom operators will have to battle with a wide array of new competitors, including traditional media companies, information technology players, and even industries such as financial services.

By limiting their role in the value chain to the mere provision of traditional connectivity, telecom operators are posing a significant risk to their business: Differentiation has become more challenging, with technology being largely commodified and accessible to all players in the market. To address this challenge, many operators will leverage telecom-media convergence to develop a unique and sustainable competitive advantage in their markets. While there is no silver bullet for success, operators that are able to move quickly and capture the currently underexploited content market will create a sustainable competitive advantage in their markets and possibly beyond.

THE ADVENT OF TELECOM-MEDIA CONVERGENCE

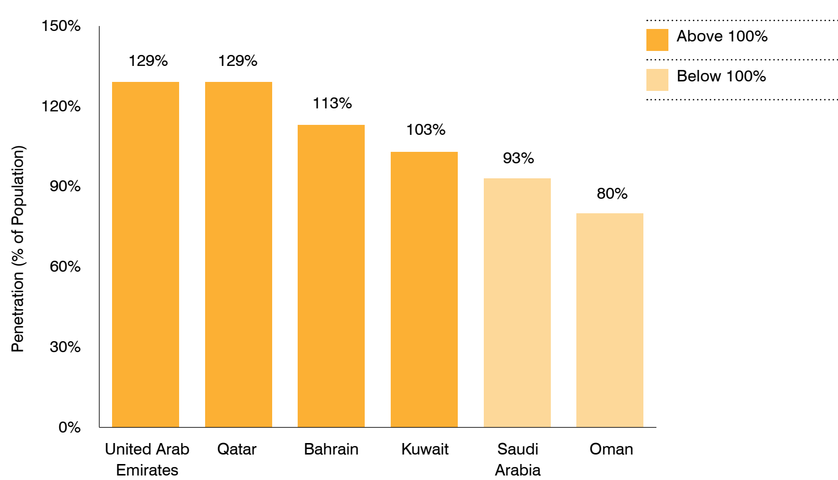
Broadband technologies in both fixed and mobile networks enable operators to broadcast or stream multimedia signals to their subscribers. This means that operators can become a new broadcast medium for content—including games, video, news, sports, weather, and music. This development is bound to create many opportunities for investors in the telecom space to start looking at the media world. A number of telecom operators in European markets have realized the strategic necessity of actively operating in the media space: Telecom Italia Group, for example, established a media arm called TI Media, which provides video, gaming, audio, and textual content.

While this convergence trend has not become very evident yet in the GCC, a number of market and technology factors will drive its acceleration, including:

- Telecom market saturation
- Telecom market liberalization
- Telecom end-user sophistication
- Threats from disruptive technologies
- Proliferation of enabling network technologies
- End-user device convergence
- Local media content and channel proliferation

Telecom Market Saturation
The GCC telecom landscape is quickly reaching saturation levels. Four out of the six GCC mobile telecom markets have crossed the 100 percent penetration mark, while the remaining two markets are rapidly approaching this threshold *(see Exhibit 1)*. As a result, operators have focused on customer retention strategies rather than customer acquisition. Additionally, operators are facing the challenge of declining voice average revenue per user (ARPU) and must find ways to reverse this trend.

Exhibit 1
Mobile Market Penetration in the GCC (First Half 2007)



Sources: Arab Advisors Group; Booz & Company

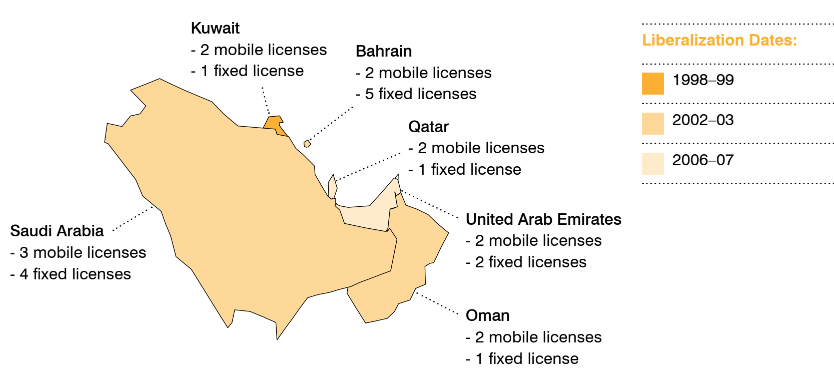
Providing content services is typically among the areas most commonly cited by telecom operators as enablers of differentiation and ARPU enhancement, and all operators in the region have initiated some serious efforts in this area. For example, Etisalat has recently started testing its triple play service in the United Arab Emirates, offering a bundle of voice, Internet, and television services. Similarly, Saudi Telecom has been reaping rewards from the success of Abwab, its text messaging service, despite the service's rudimentary interface.

The success of H3G Italy is a case in point for demonstrating the remarkable potential of content services. Despite being the fourth entrant into a saturated market, H3G has managed to gain a significant share of the Italian mobile market by offering differentiated content services. Within a period of two years, H3G captured 9 percent of the total mobile subscriber base and achieved a data ARPU level that is more than double the market average.

Telecom Market Liberalization
All GCC markets are now considered liberalized, with Qatar being the last to join its neighbors in auctioning a second telecom license *(see Exhibit 2)*. The resulting intense competition, especially as most of the markets are now saturated, creates the need for operators to differentiate themselves from their competition. Again, content could be one of the key opportunities for doing so.

Telecom End-User Sophistication
The GCC is a wealthy region with a relatively young population. The average gross domestic product at purchasing power parity per capita

Exhibit 2
Mobile Market Liberalization Time Line in the GCC Region



Sources: Arab Advisors Group; regulators' Web sites; Booz & Company stands at US$18,000, representing 1.75 times the world average. Additionally, 33 percent of the total GCC population is below the age of 18. These two factors combined present the opportunity to offer content services to the technology-savvy youth segment that will constitute the bulk of the operators' addressable market in the mid- to long-term future.

Threats from Disruptive Technologies

The emergence of disruptive technologies such as Internet protocol (IP) telephony will place increasing pressure on fixed and, eventually, on mobile operators. The threat from cannibalizing their core business is prompting telecom operators to find alternative revenue sources, including content services. The risk that voice over Internet protocol (VoIP) poses to traditional telecom operators is enormous: In Western Europe, for example, the number of outgoing VoIP minutes has been growing at a compounded annual rate exceeding 50 percent and is expected to exceed 10 million minutes by the end of 2007.[1] This trend is present across all customer segments, including enterprise and residential users. In the GCC region, the threat, though not yet evident, is nevertheless imminent. VoIP is expected to experience exponential growth as broadband penetration continues to expand.

Proliferation of Enabling Network Technologies

Because content requires so much bandwidth, the limited availability of enabling technologies has traditionally been the main obstacle for the mass usage of content services. This is becoming less of an obstacle in relatively advanced markets, such as those of the GCC. Fixed and mobile broadband technologies are becoming increasingly accessible with the phenomenal growth levels witnessed in the adoption of 3G and DSL services in the region *(see Exhibit 3)*.

End-User Device Convergence

Mobile handsets are increasingly converging with other multimedia devices, such as digital cameras, music and video players, and personal digital assistants (PDAs). Similarly, customer premises equipment (CPE) for fixed telephony is converging with personal computers and television set-top boxes. A number of set-top box vendors are becoming increasingly active in this space, including Scientific-Atlanta, Amino, Motorola, Thomson, and Humax. These manufacturers are driving rapid product development and increased innovation. Among the advanced features integrated into this new generation of equipment are high storage capacity, video-on-demand capabilities, digital video recording support, multiple format decoding, security support, and digital rights management.

This trend is a key enabler for telecom-media convergence, since it allows users to consume content beyond the traditional phone-only devices.

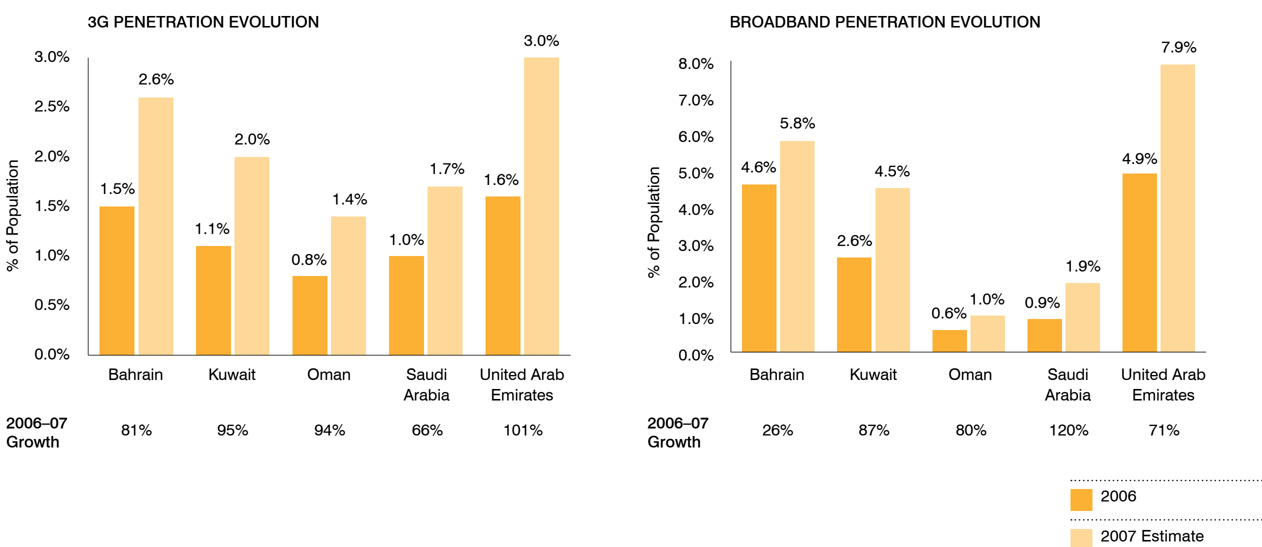
Local Media Content and Channel Proliferation

The TV media sector is highly fragmented in the Arab world. The number of Pan-Arab free-to-air television channels has been growing at a compounded annual rate of 45 percent during the past three years and now exceeds 250 channels. The total number of channels targeting the GCC region reached about 500 at the end of 2006, many of which are thematic channels focusing on highly targeted content. This trend of targeted channels is gaining momentum and market share at the expense of the traditionally successful general interest channels; and while in 2002 five TV channels garnered 80 percent of the gross TV advertising spend in the GCC, in 2006 that percentage was shared by 28 channels.

In parallel, content production has also been increasing to accommodate the vast number of channels, with music content production being among the highest-growing sector for audio and audiovisual content. In addition, print media content has also witnessed significant growth.

One content area often overlooked by telecom operators is gaming. Games are very popular with the youth segment, which will likely become the core target market of telecom operators in the region, given the age profile of the population. Gaming content comes in various forms, ranging from downloadable single-player to online multiplayer games.

Exhibit 3
Broadband and 3G Penetration in the GCC (2006–07)



Sources: Analysys Ltd.; Booz & Company

TELECOM OPERATORS' ROLE IN THE CONTENT LANDSCAPE

Telecom operators must consider a complex array of elements when offering content services. The content itself can encompass information, entertainment, education, transaction, and communication, while the formats range from text, image, and audio to more complex content formats such as video, multimedia, and interactive service. Delivery options are also varied, including broadcast, streaming, downloads, text messaging, browsing, and peer-to-peer. Telecom operators are faced with the daunting task of not only identifying the right content to be offered, but also determining the optimal format, technology platform, and end-user device. In addition, they must also determine the right language for each content service. Such activities are new to telecom operators. In order to succeed, telecom operators must enhance their understanding of the content delivery value chain and decide what part they intend to play *(see Exhibit 4)*.

Traditionally, telecom operators have been adept at the marketing and service provisioning elements of the value chain. However, they have been less familiar with the broader aspects of content creation, acquisition, aggregation, and end-user terminal management, having outsourced most of these activities to specialized service providers. To remain competitive now, they must develop or acquire some of these key components. Only by developing a clear understanding of the content value chain can telecom providers determine the best strategy for gaining a competitive edge.

Content Creation and Production
The first element in the content delivery value chain is the creation and production of content. Content creation is, as seems obvious, the activity of making new content, such as writing a book or taking a photograph. Content production refers both to the commercial distribution of content as well as to postproduction activities such as formatting, editing, censoring, translating, and dubbing.

In the past, telecom operators have seldom been involved in such activities, partly because large investments up front necessitate economies of scale for success, and partly because extensive expertise is required in this domain. For example, Disney distributes its product around the globe and across every possible delivery platform, an advantage that telecom operators do not have. Additionally, content producers are always ahead of the curve in understanding, or even shaping, user preferences. Such capabilities are necessary for continued success in the media sector, especially given the typical low success rate in creating

Exhibit 4
Key Value Chain Activities for Content Provisioning

Source: Booz & Company

"hits." Examples of leading content producers include Sony Pictures (movies), Warner Bros. (movies), the EMI Group (music), Rotana Records (music), and Electronic Arts (games).

While it is not advisable for telecom operators to get directly involved in content production, they may play an important role in postproduction activities. This is particularly true in the GCC region, due to the cultural sensitivities toward certain content. GCC telecom operators could become pioneers in adapting global content to local taste through "Arabization," cultural adaptation, subtitling, dubbing, or other postproduction activities. Early movers could create a sustainable competitive advantage and then distribute content to other operators in the Arab world and hence generate wholesale content revenues.

Operators can also play a major role in adapting and channeling regional content. As the popularity of regional content increases with a large portion of the addressable markets, telecom operators can play a role not just in distributing the content as is, but also in offering a value-added service such as interactivity, adaptation to mobile screens, or format manipulation for telecom channel consumption. It is very important that telecom operators provide an additional value to their users versus the traditional channels, which are predominantly free to air or very cheap to obtain. Otherwise, content will not be considered as a meaningful revenue generator to telecom operators.

In the region, content production is dominated by major studios, based mainly in Egypt, Kuwait, Lebanon, Syria, and the United Arab Emirates. Most of the content is commissioned by the traditional channels for various genres such as music, drama, film, and lifestyle. Among the major players in this space are StudioVision (Lebanon), Metro Media Production (Dubai), Media Byte Visual Communication (Dubai), Filmworks (Dubai), EMPC (Egypt), Studio Misr (Egypt), and Areen Productions (Egypt).

Content Acquisition and Management
It is increasingly urgent that telecom operators gain expertise in content acquisition and management. Large telecom operators could have more financial capability to acquire expensive content (such as premium sports and movies) than traditional media players: The larger the customer base, the higher the negotiating power, especially when acquiring premium content. However, it is critical that telecom operators focus on bridging the knowledge gap in content acquisition and management versus the experienced media players.

Content management is the process of storing, labeling, and managing the digital rights of acquired content. This activity has traditionally been outsourced by telecom operators to specialized service providers. Should telecom operators aspire to use content as a key differentiator, such activities should be brought under the control of operators. Telecom operators should also invest in reliable digital rights management (DRM) software to avoid potential disputes with content producers.

Fortunately for telecom operators, they have been mastering the process of billing for years. It is a clear advantage that can be leveraged to extend into the territory of DRM, either alone or through teaming up and pooling capabilities with players from outside the telecom industry. Billing systems and interfaces are critical for content transactions to work. Collection and revenue assurance systems are well established within telecom operators' IT infrastructures and are clear strengths upon which content management capabilities can be built.

Traditional media companies in the GCC such as MBC, LBC, ART, and Orbit have mastered such capabilities, especially in acquiring premium content, both regional and international. For example, ART has been the regional leader in providing

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premium football (soccer) content such as the World Cup and most European leagues to its subscribers.

An optimal content acquisition model is key to ensuring a balanced trade-off between risk and profitability and can be achieved using one of many possible content acquisition models. Such models range from executing a simple purchase transaction to forging strategic partnerships or possibly creating a joint venture with a content provider *(see Exhibit 5)*.

Content Aggregation
Content aggregation includes activities such as content program scheduling, data feed monitoring, content updating, portal development, program guide development, and advertising management. These are the core activities for TV stations such as MBC, LBC, and Rotana, as well as for Internet portals such as Yahoo.

Understanding customer behavior and demand patterns is key to offering the right content in the best time slots or portal positions. This area is new to telecom operators, and they will have to commit resources to build capabilities. In addition, telecom operators should develop expertise in handling time-specific content, such as news, and content with a short life span, such as novelty ringtones or blockbuster movies.

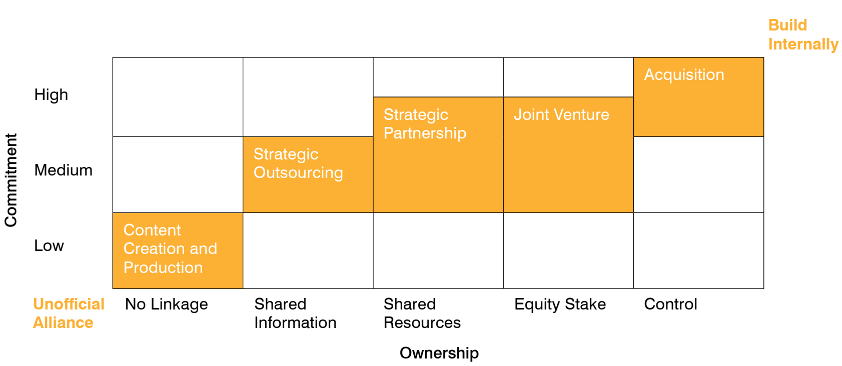
Furthermore, telecom operators should aim to develop streamlined portals to facilitate the content purchasing process for the user. This applies to content delivered on both the mobile and the fixed platforms. For instance, minimizing the number of clicks to access and/or purchase content on Internet, mobile, and TV portals maximizes the chance for completed transactions.

While these insights are hardly novel, they are not inherent to traditional telecom business models. As with billing, operators have significant experience in developing customer life cycle management capabilities, including customer insights (down to the household and individual levels), customer care, and advertising. Operators must be willing to build on their capabilities in understanding customer behavior and emerging trends and preferences. Content offerings can be developed with actual customer insights from operator databases and know-how from media management experts, who have built good track records in managing television grids despite largely unreliable consumer insights, given the lack of audience measurement technology and accurate consumer behavior readings in the region.

Application Service Provisioning
Application service provisioning includes the management of the technical platforms and the system design required for effective customer interface. Activities include the management of content storage servers, related software, billing and customer relations management (CRM) systems, and interface applications and systems.

Telecom operators typically outsource most of the service provisioning activities to specialized application service providers (ASPs). Examples of providers in the GCC are Mersal, Ducont, Info2cell, Saudi Bells, and PowerMeMobile. While ASPs have been quite active and successful in the region, their business model works by leveraging scale through dealing with a number of operators

Exhibit 5
Models for Content Acquisition and Management



Source: Booz & Company

in the region. This leaves little room for operators to differentiate their services and as a result could stifle innovation in this domain.

As differentiation in content delivery becomes increasingly critical, telecom operators should exercise more control over these activities to drive innovation, and hence differentiation.

Should telecom operators decide to venture into this area, ensuring quality of service and quick time-to-market will be critical. System integration is key to safeguarding quality of service. Designing technical platforms to be flexible and scalable is essential to reduce the time-to-market of new applications or features. Guaranteeing continuous connectivity between the technical platform and the content server on one end of the value chain, and the delivery channels on the other end, helps in creating a seamless user experience.

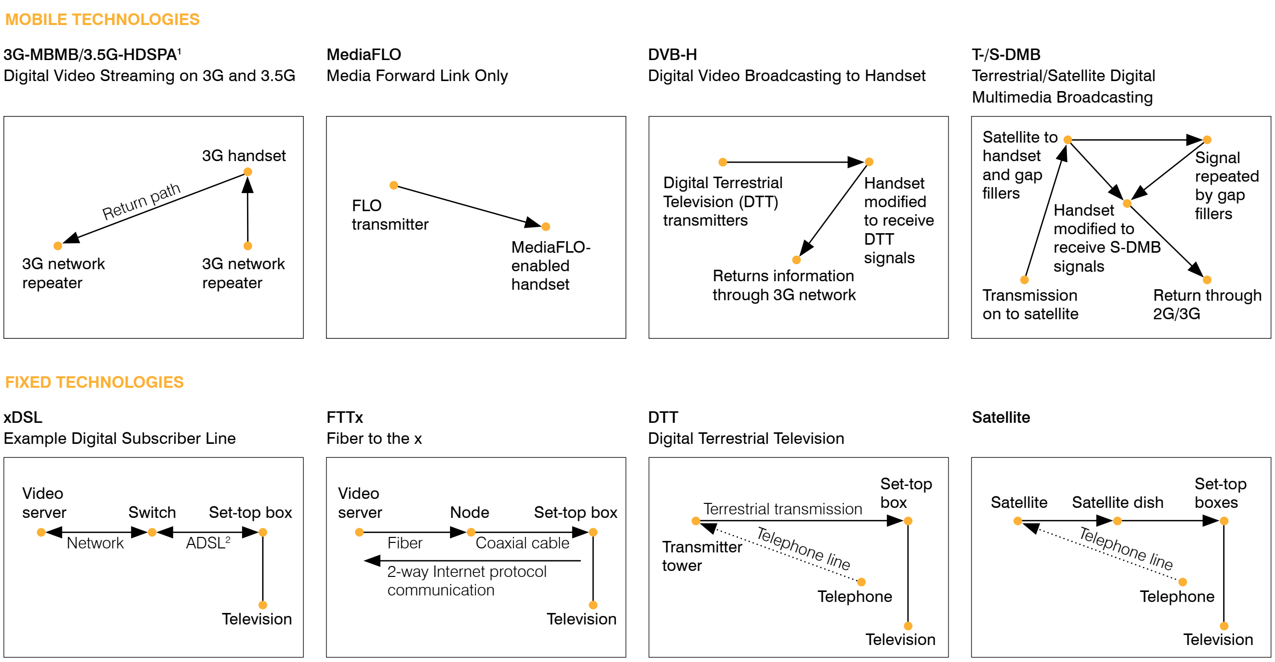
Service Access and Delivery
Service access and delivery is the core activity of telecom operators. In other words, it is defined as providing the connectivity to end-users through the operator's network. The activities include access network design, deployment, and maintenance.

It is critical to select the appropriate technology for each content category with the aim of achieving the desired coverage and quality of service. The objective is to minimize download time (i.e., access to content) in order to stimulate demand for content that requires a lot of bandwidth, such as video and music.

Telecom operators should carefully determine the most suitable technology required for effective content delivery, including GSM/UMTS, DVB-H, and MediaFLO, for mobile services, and DSL, fiber, and satellite for fixed services *(see Exhibit 6)*.

Mobile operators in the region are starting to offer mobile TV and video-on-demand services over their 3G networks. While offering such services over a 3G network provides a mixed customer experience, early signs of customer acceptance have started to surface. Etisalat, for example,

Exhibit 6
Key Fixed and Mobile Technologies to Deliver Video Content



[1] High-Speed Downlink Packet Access
[2] Asymmetric Digital Subscriber Line

Source: Booz & Company

offered a bundled "all you can view" TV package for a monthly charge of US$11; within two months, the service attracted 100,000 subscribers.

Marketing and Sales
While sales and marketing activities are familiar territory for telecom operators, the optimal customer segmentation for content services does not necessarily match that of traditional voice or data services. In addition to facilitating such activities as marketing segmentation, business development, and billing and customer care, operators must also direct their attention toward marketing mix development and data mining. Telecom operators should develop a different segmentation and marketing mix from their core activities to better capture content-related revenues.

Telecom operators can learn from traditional media companies how best to sell and market content. For instance, developing and maintaining extensive libraries for each content genre are critical to ensuring customer loyalty. Other strategies include transparent pricing to boost usage and offering simple and secure payment mechanisms.

Customer Terminal Management
Designing customized end-user devices allows telecom operators to enhance customer retention and facilitate access to desired content and can mitigate the risk from device manufacturers, who have also started moving down the content value chain. For example, Nokia is now moving beyond mere handset manufacturing and is offering content directly to its users through its newly introduced WidSets service, which is a mobile aggregator of Rich Site Summary (RSS) feeds. Similarly, new Nokia handsets include built-in Global Positioning System (GPS) services that aim at disintermediating the telecom operator and reducing its role to connectivity provision.

It is critical for telecom operators to carefully define the device technical specifications for each content delivery platform by collaborating with manufacturers. As mentioned earlier, the primary goal is to make the interface as simple as possible to encourage users to purchase content.

Providing customized devices (e.g., proprietary set-top boxes and mobile handsets) allows telecom operators to lock in subscribers and to facilitate customer access to content portals. Obviously, the larger the telecom customer base, the higher the negotiating power vis-à-vis device manufacturers, as well as the ability to achieve economies of scale. However, expertise in supply chain management and after-sales service is key, especially for devices with short life spans, such as mobile phones. Due to the historical absence of handset subsidies in the region, telecom operators in the GCC are not used to dealing with these issues.

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CONTENT ECONOMICS

The economics of content services in the telecom sector are driven by the flow of value across the value chain. Being at the front end of the chain and owning the customer interface, telecom operators derive revenues from content based on content usage and end-user prices. However, the respective profits from these services could vary considerably depending on the content acquisition model adopted by operators for each content type.

Until recently, most telecom operators in the region have followed a revenue-sharing model with their content providers—typically a fifty-fifty split. This model, however, is not sustainable in the long run, especially as operators introduce new premium content services. For example, in the case of premium international movie content, it would be difficult for regional operators to forge a revenue-sharing deal with the likes of Universal Studios or Sony Pictures. Rather, operators may be pushed to take on the full demand risk by acquiring such content in a simple one-off transaction. Such risks, however, could be considerable, especially for smaller operators. As a result, economies of scale will become increasingly important in the regional content game.

In order to achieve scale, operators may decide to resell their acquired content to other nondirectly competing players across the Middle East. This could be facilitated by the relatively homogeneous preferences and cultures across the Arabic-speaking Middle Eastern countries. In the case of reselling, however, operators should ensure that they negotiate their content acquisition contracts in a manner that gives them the rights to do so.

We estimate the size of the content market delivered through telecommunications channels in the greater Middle East region will reach around US$750 million by 2010, up from the current level of less than US$400 million. While currently more than 99 percent of these revenues are mobile specific, we expect the share of triple play services over the fixed platform to grow to about 6 percent of the overall market by 2010.

Overall, the value of the content market will not likely exceed 3 percent of the overall revenues of telecom operators. Although the absolute value may indeed remain small, the role of content services should be seen as a means of creating a differentiated competitive advantage aimed at safeguarding core revenues and profits of telecom operators. Content alone, however, is not expected to become a considerable source of revenue growth for telecom operators.

THE WAY FORWARD FOR TELECOM OPERATORS

GCC telecom operators are exploring ways to crack the content puzzle. They realize that content will play a key role in their differentiation strategy going forward.

The dilemma lies in the make or buy decision around content-related activities. If content is outsourced, then it no longer becomes a differentiating factor. If it is developed in-house, it may be very complex to manage and hence may lead to failure.

Unfortunately, there is no silver bullet. The key to success is in execution, and execution is indeed complex for telecom operators and will require significant capability development and joint activities with traditional media players.

Therefore, operators could choose between developing the required capabilities in-house or acquiring existing experienced entities. The difficulty, however, is in the level of fragmentation in the content delivery value chain. This means that the acquisition route could also prove to be a challenge, as multiple acquisitions may be required. Alternatively, creating joint ventures with media players could be a solution for consolidating talent. It must be noted that telecom operators bring immense value to content producers as an alternative delivery channel and have a great deal to offer by way of expertise in billing and revenue assurance as well as customer life cycle management and insights.

In the end, irrespective of the method, one thing is certain: Value chain consolidation is under way, and telecom operators are well positioned to play a lead role in driving it, should they decide to expand their role beyond pure connectivity provision.

Endnotes

1 IDC.

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