The answer to video piracy

Must video walk the same plank that music did?

Luis A. Ubiñas

Stop me if you’ve heard this one: a novel form of media distribution is promising to launch lucrative new content services, but the industries involved can’t agree on how to protect them from theft or how to split the revenues they generate. At the birth of the cable TV industry, in the 1970s, the story had a happy ending—the players collaborated to develop encryption standards and to set up a revenue-sharing model that now generates more than $40 billion in revenues yearly for the cable and satellite TV industries and has created more than $200 billion in business value for the cable companies, the content companies, and the makers of TVs, satellite dishes, and switching equipment.

Fast-forward 30 years and, as a famous baseball player once said, “it’s déjà vu all over again.” Companies in three industries—the content creators, the broadband providers, and the PC makers—find themselves stalled as they try to deliver digital video over broadband connections. This time, there is an added element of urgency: if they fail to act, illegal distribution will likely ramp up to meet market demand, and bootlegged movies could hurt box-office and downstream revenues, much as file sharing took a bite out of compact-disc sales. Video in 2004 stands where music did in 1998.

You might think it would be easier than this. After all, the haggling industries share a common dream: they all hope to offer—on demand, for a fee—deep repositories of high-quality multimedia content (including films,
archived TV shows, and short programs such as cartoons) to broadband subscribers. Each industry would get a cut of the revenues. Yet each has a reason to be wary of the new digital platforms.

The studios, production companies, and TV networks that create the content want some protection against theft before they offer their programs and films in an open digital environment. In addition, some of these companies are wondering if they should set up their own video-on-demand distribution services to avoid having to split the revenues with the broadband providers, which have so far proved hesitant to thwart piracy. But the cable and telecom companies that provide broadband services to their subscribers worry about a backlash if they act as watchdogs for the studios and networks. The result is that few studios are providing content. So even though more than 13 percent of US households have broadband Internet access, the market for legal digital-content services remains underexploited, with total revenues of less than $1 billion.

Meanwhile, the US personal-computer industry is struggling to recover after two years of declining sales. PC users tend to upgrade only after they hit “pain points”: their machines become too slow (or lack the storage or the screen clarity) to handle what’s being offered online. The last big pain point occurred in the late 1990s, when the rapid growth of interest in file-sharing services such as Napster boosted demand for PCs that had the storage and speed to suck down hundreds or thousands of pirated songs. Online gaming has also achieved encouraging levels of adoption. Right now, though, a three-year-old computer can deal with most of what’s actually out there. Downloading and managing films, TV shows, and short programs from online libraries is another matter. Today’s machines simply will not cope.

So why aren’t PC makers pushing for video on demand? Because they, like the broadband service providers, worry that consumers will resist products with built-in security measures, such as embedded chips that prevent the copying of films or songs without the copyright holder’s permission.

The situation facing the interested parties is even more urgent than it was in the 1970s, when there was no fear of rogue technologies and rival services. Today, file sharing is rampant despite high-profile legal victories against file-sharing services (which make it possible for movies and songs to be traded online) and prosecutions of flagrant abusers. Every day several million music files and several hundred thousand video files are downloaded without a penny to the copyright holders. In the meantime, after only three years Netflix, which mails DVDs to subscribers, has signed
up a million consumers, proving that the public is hungry for choice. How should the three industries move from pause to play? Content providers ought to make the first move by offering films and TV shows for on-demand viewing and by cutting deals with broadband providers so that, as with cable TV, they either split the subscriber revenues or collect a carriage fee. Some studios are still considering setting up their own direct-to-consumer distribution services, such as Disney’s MovieBeam. But they should recognize that the broadband gatekeepers—a handful of regional telecom operators and big cable television companies—are entrenched and getting stronger. Despite the temptation to go around broadband providers, partnering with them not only shares risk but also delivers access to their storage, distribution, and customer-billing capabilities.

Content players might also reassure themselves with another lesson from the cable industry: branded content that generates an audience and revenues stands to increase their market power. (The rising percentage of the cable operators’ budgets devoted to content proves the point.) If it is not yet feasible to offer movies on demand, studios have enough other content to get the game started.

Broadband providers, for their part, must help to enforce copyright laws on their networks by shutting down hubs of piracy—not to wipe out file sharing but to boot off the big offenders who trade the lion’s share of pirated content. This approach would not only please the copyright holders but also reduce illegal downloading, which eats up bandwidth. Broadband providers will lose a few subscribers, but the churn should easily be outweighed by revenues from new services, which won’t be offered unless piracy is monitored.

As for the hardware manufacturers, they can improve their position by agreeing to make their devices less friendly to theft. They might be under no legal obligation to embed copyright protection in PCs, MP3 players, and set-top boxes, but doing so would send a strong signal to the content providers, encouraging them to develop services that will in turn sell more hardware. Much as early makers of videocassette recorders learned to stop building machines with two slots for the easy copying of tapes, hardware manufacturers should ask themselves as they design a product whether it will facilitate theft.

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But it’s up to the content providers to set the ball rolling. Their films and other programming are what make video services desirable in the first place, and by suggesting deals to broadband providers they could lead all three industries involved to mutual gain. Broadband providers would attract subscribers by selling new services and upgrading existing ones. Content companies could get distributors to help protect copyrighted materials—something that hasn’t happened with music—and could develop the same kind of high-revenue services these companies have built on cable networks with some of the same partners. And hardware companies would ship new machines to consumers motivated to upgrade. Given the value created by the cable industry in the ’70s, when the US economy was smaller, there is no telling where such partnerships might lead.

Luis Ubiñas is a director in McKinsey’s Los Angeles office. Copyright © 2004 McKinsey & Company. All rights reserved.