PCCW's Media Convergence: Two Steps Back, One Step Forward

Abstract: Hong Kong’s former incumbent telecom carrier PCCW has been a leader in embracing telecom-media convergence and has paid a heavy price for doing so. PCCW is back for another try, and things are looking up.

By Andrew Chetham

Recommendations

- Content aggregation, delivery and billing are the carrier’s strengths, and it should focus on these areas, rather than seek to turn itself into a content producer in which the risk of failure is high.

- Carriers should consider partnering with third-party aggregators of content that have better experience/expertise of gaining distribution rights for international content.
Five years ago, Hong Kong Telecom (HKT), the territory’s former incumbent carrier, decided to go big into content delivery. It created a citywide broadband access network, signed up content partners and launched — to great hype — an interactive TV (iTV) service with video on demand (VOD) as its centerpiece offering. It turned out to be a hugely costly white elephant. Fewer than 100,000 customers signed up, and the cost for the whole exercise ran to several hundred million dollars. It was finally shut down in September 2002.

In the second half of 2000, Pacific Century CyberWorks (PCCW) bought HKT. At the time, PCCW was pursuing its own ill-fated media strategy of creating a global broadband TV service, called Network of the World (NOW), which was wound down in 2001 after soaking up more than US$500 million.

However, PCCW is back with a refocused version of NOW targeted only at its own DSL subscriber base, and it seems to be having some success. In the year since the new service was launched, it has signed up 130,000 paying subscribers — equivalent to a 30 percent take-up rate among its DSL customers.

Although revenue to PCCW from this new offering is tiny — the service costs just HK$30 a month (US$3.8) — it does show that priced correctly, residential customers will pay for content on top of broadband. In the main, PCCW partners for content, focusing its efforts on aggregation, billing and delivery.

The following are key differences from PCCW’s earlier forays into content:

- NOW has a large/ready pool of established broadband subscribers to build on.
- It is targeting more niche content, often unavailable through regular media.
- It uses revenue/risk sharing instead of taking upfront costs on content.
- And, perhaps most important, the market is becoming more mature in its acceptance of new media (an important point in the failure of iTV).

**The Bleeding Edge**

In early 1998, HKT (then controlled by Cable & Wireless) launched the world’s first commercial VOD service as part of a wider iTV offering. The service was delivered using fiber to the building and very high-bit digital subscriber line (VDSL) using Moving Picture Experts Group 2 (MPEG2) to set-top box. The price was pitched at about the same level as Hong Kong’s only cable TV operator’s basic package. But plagued by initial delays, technical problems and customer interface problems, and a failure to provide enough selection of content, the service never took off. More than anything else, it was, perhaps, too much ahead of its time.

Development costs were high. In 1999, HKT took a write-off of about HK$6.4 billion (US$825 million), a significant proportion of which
reflected costs associated with the project. Also in 1999, it received a boost in after HKT and Rupert Murdoch’s News Corp.’s local Asia/Pacific-oriented subsidiary Star TV agreed to provide programming for the service. But that partnership never materialized and was quietly dropped in 2000 when PCCW merged with HKT. In September 2002, PCCW finally closed the iTV service.

PCCW — initially a concept Internet company — also had its own vision of being a broadband content creator and distributor. At the time it was one of the hottest Asia/Pacific Internet stocks — powered by a vision of the global interactive broadband brand called NOW it was developing. PCCW saw itself as a media player rather than a telecommunications infrastructure owner, but in buying HKT it became very much the latter. At the peak, PCCW was spending US$500 million a year on NOW. This dropped to US$190 million before it wound down the service in 2001.

**Another Try?**

A byproduct of PCCW’s iTV service was the ability to offer broadband Internet via DSL at an early stage. In 1999, this was de-linked and offered as a stand-alone broadband product. Driven by aggressive pricing, the creation of an early wholesale environment for DSL and competition from cable modem services, Hong Kong’s broadband Internet penetration is second only to South Korea’s, with about a 40 percent penetration into homes as of June 2002. With such a pervasive high-speed delivery platform in place, PCCW has undertaken a third attempt at delivering content.

**Now.com.hk**

PCCW’s latest service is called now.com.hk and is delivered over its own DSL “Netvigator” broadband service onto the PC. It is a package of streamed and on-demand video-based and text offerings, with an emphasis on local Chinese and niche content.

Perhaps the most important content relationship is with Hong Kong’s dominant free-to-air TV company, Television Broadcasts (TVB). At the end of every week, PCCW takes all of TVB’s Chinese-language programming (other than drama) for the past seven days, digitizes it and makes it available for viewing through now.com.hk.

However it also streams Fashion TV, BBC World TV and Bloomberg TV live. In the on-demand section, it features on-demand popular Asia/Pacific drama and is the first carrier in Asia/Pacific to host Intertainer Asia, a movie content aggregator, which gives it access to Hollywood movie material from three of the big studios. It has also just launched Disney-on-Demand featuring Disney cartoons.

The service is a ”walled garden,” available only to its own broadband Internet customers. Since July 2002, according to PCCW, the service was used by 70 percent of the customers who had signed up, up from an initial 20 percent.
Live-streamed content is delivered using IP (Internet Protocol) multicast. Download speeds for on-demand and streamed content are 800 Kbps using Windows Media 8. There are no caches in the network. All the content is streamed from one data center on the PCCW network.

**Subscription and Revenue Share Model**

In other markets in which broadband penetration is high, such as South Korea, broadband portals have been designed more with pay-per-view on-demand content in mind as the main revenue generator. They are then surrounded by "sticky" free content.

To some degree, this puts broadband portals head-to-head with pay TV, or even free-to-air TV, for viewing share in the home, and the latter has the advantage of being on the television not the PC.

However, the South Korean portals have found that they do not match television well, and that most of the pay-per-view is adult material viewed mostly after 10 p.m. (with a smaller peak in the midafternoon).

PCCW says its main approach is not to sell pay-per-view but to sell now.com.hk as a value-added subscription service that layers on top of its broadband Internet offering. Its pricing structure reflects this — now.com.hk costs just an extra 20 percent over the basic broadband access bill.

PCCW says its most popular content based on click-stream data has been more of the niche offerings, such as Fashion TV, which fits with its aim of not competing with mainstream TV.

Pay-per-view cartoons and local Asia/Pacific dramas are priced about HK$5 (US$0.64) a view, and Intertainer Asia-Hollywood-type movies at HK$15 (US$1.93).

Revenue splits for PCCW and the various content contributors are all taken from the initial subscription, with a separate split for on-demand pay-per-view options. The splits are not disclosed, but typically, from experience in other markets, these can be 50-50 for on-demand content, although the share is less for Hollywood movies — about 30 percent.

The link with PCCW's broadband Internet service provider (ISP) service is perhaps one of its best attributes, making billing simple for the end user and for PCCW. Payment is added directly to the monthly ISP bill, and pay-per-view purchases also go directly on that bill.

**Gartner Dataquest Perspective**

After expensive forays into content, PCCW's approach now is one of moving forward without spending heavily to create or buy content or by subsidizing TV set-top boxes.

The model it has developed is simple and plays to the carrier's strengths — billing, aggregation, filtering and established customer relationship. It is
priced realistically enough to encourage take-up in this emerging and still-experimental environment.

However, the question remains whether PCCW can turn this into anything more than a small incremental revenue stream on top of broadband Internet access. Persuading users to pay more requires premium content and exclusivity. It will also face tough opposition from Hong Kong’s monopoly cable TV provider — which uses sports, especially football, as its key draw.

By sowing the seeds now, PCCW puts itself in a better position to sell higher value content as it becomes available. The larger its customer base for broadband and for its nascent content service, the more attractive it will make itself for partnerships with content owners/aggregators in the future.

**Key Issue**

How will the worldwide communications market develop, and which forces will drive market growth and future opportunities in which sectors?
This document has been published to the following Marketplace codes:

TELC-WW-DP-0326