The Entertainment Industry is Cracked, Here is the Patch !

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Sommaire

Introduction

The products coming from the Music, Movie and Video Games industries have never been in such a hot demand. They are traded and consumed as never before. However, despite this success, the Entertainment industry is facing a major crisis. Therefore the weak financial results of the "Majors" of the industry call for new solutions, since losses are not generated by a lack of demand. More than a business model, it is a brand new approach of the relation between companies and customers that will pave the way to a profitable outcome.

The common meaning of the word "consumption" is not sufficient to refer to the new utilization of entertainment products. The traditional value chain, which outcome is the transaction, is no longer relevant to represent the increasingly active participation of customers in the design of their consumption environment. This subject is developed in the first chapter.

A good product is not sufficient to satisfy the individual needs of each consumer : people are rather looking for a good "experience". In fact, the role of an entertainment company is not limited to distribute a Compact Disk of good quality : it has to be adapted to the experience environment of consumers, such as listening to music on a MP3 player, on a mobile phone, on the computer, or in the car. Anything that does not match each individual experience environment will destroy value. So entertainment companies will create maximum value by designing personalized experience environments. It implies alliances with stakeholders of the experience environment to form nodal networks, as explained in the second chapter. Such personalized environments, and therefore such value, can only be co-created : In fact, personalization is enabled by participation. Interaction with clients is mandatory to understand their specific needs and to address them.

In the third part, the statement that value creation is not the monopoly of companies will be developed. Customers also create value for companies, for themselves and for communities such as communities of fans. Therefore

the Internet and the new technologies become a fantastic opportunity for the entertainment industry : The Internet transforms literally "customers" into "firms", since any computer can indifferently play the role of "host" or "server" by distributing music for instance, movies, or by hosting websites of fans. Another example are consumers who are also developers, and who fix software or create add-ons for video games.

By building a business model on the active participation of clients, peer to peer Networks, word of mouth, support from communities of fans, or even hacking, that most of the time enhance the functionalities of entertainment products, the entertainment industry has many opportunities to turn a crisis into a co-creation of value, and therefore a creation of new value. Activities online such as file swapping exist today. The business model of the entertainment industry is cracked. It is a matter of fact. Instead of ignoring these activities and considering them as out of the value creation system, I propose a new business model that incorporates them. Co-creation of value is the patch to fix this issue.

The internet and the new technologies have modified our experience of entertainment products on a long term basis

1. Consumers have been empowered by the internet and the new technologies

1.1. The role of intermediaries is put into question

1.1.1. Music Majors are challenged by Peer-To-Peer Networks

Digital formats have enabled peer-to-peer networks (P2P) to develop. The advent of P2P has created new distribution networks. The two consequences are :

- Music Majors do not earn money on transfers of ownership based on P2P technologies, interfering with the value chain of the industry

- The monopoly of music majors on distribution has been eroded

Projects that directly link artists and final consumers, such as distributing music on eBay, are under study. In this extreme situation, the distribution function would almost disappear. Even more threatening for Music Majors, some P2P companies and independent music labels have entered into talks to work directly together to distribute songs. The English independent label *Ninja Tunes* for instance is exploring new methods of promotion and distribution of artists thanks to P2P network and the internet.[1]

A new type of 100 % online distribution is emerging. Communitymusician.com is a good example of this trend. This website allows to create a personalized web page on a music store online to sell home- or studio-created music. It also proposes to make copies of original and personal creations on CDs or DVDs.

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[1] According to Tariq Krim, founder of a website dedicated to online music named *Generationmp3.com*, in an interview realized by the newspaper *Le Monde*, October 7,2003

Consumers, through P2P networks, and artists, through the internet, tend to become more and more independent from the Music Majors. New online platforms have been recently been created to ease cooperation between artists. Music75.com for instance delivers to its subscribers (professionals or not) some virtual space on the site dedicated to a music-related project. Authors, composers, singers, guitar players or drummer can join a project and meet potential group members. Eric Cougniot, co-founder of the website *Music75.com* shares his experience in this terms "I have composed the tunes, they have written the lyrics, other people have sung, and all this was possible thanks to the internet. We never met, but our songs are not virtual at all !"[2] After ten days of operations, the website already counts 570 subscribers from all over the world. More than 230 songs are broadcast on the online radio. A first "best of" CD will be released in the coming month under the label music75 to promote young artists. Next steps after promotion would be to link music75 with the *Apple music store*, *Altnet*, *od2* or *e-compil* to distribute the songs on fee-based downloading platforms.

Not only do Music Majors lose money from an increased competition, but also from parallel distribution networks that directly link consumers with one another. The current business model of music companies includes controlling distribution networks to extract value from the consumers at the very end of the value chain. P2P is disrupting the value chain. Tomorrow the movie or the book publishers industry will also face radical changes in their value chain. This evolution can be prepared and anticipated today by changing the configuration of the value chain as explained in Chapter 2.

1.1.2. The promotion of entertainment products is more and more direct

Whether it be songs, books, movies or video games, promotion of new entertainment products is faster than before. We all have a close friend that has watched everything, read everything, and who can give us his opinion about a CD, a movie, or a video game 3 months before the release date.

The traditional functions of promotion and marketing are put into questions. If a CD or a movie is bad, people will know it even before it is available on the marketplace. Online communities are challenging entertainment companies because it becomes more and more difficult to sell mediocre products, even with massive marketing investments.

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[2] Source : http://www.music75.com

Today the most efficient marketing technique is the consumer (or reader, or viewer) opinion. Consumers become spokesmen for a product. They are more reliable than companies according to other potential consumers, since they have no interest in advertising the product. Consumer reviews on *amazon.com* are far more persuasive than a simple ad, because most of the time they assess the pros and the cons of a product, and give all the elements to the consumer to make up its mind. Whereas current traditional marketing methods are seen as biased by consumers since they only mention advantages. And consumers know it. So the aim of promotion and marketing investments initiated by entertainment companies has evolved : Marketing and promotion efforts are adapted to inform the public about the release of a game, a CD or a movie, but they no longer ensure that consumers will buy it. Opinions and reviews have created a mediation between entertainment companies and the public.

Consumers' opinions now play a determinant role in triggering the act of buying, more determinant than marketing investment that are less and less persuasive. Among the people who read consumers' reviews on *amazon.com*, largely more than one out of two find them useful.

It is so easy to find critics about a movie for instance, that the act of reading reviews before going to the movie theater and after having been informed of the release of a movie is a "must do" step to make up one's mind. In the case of *the Blair Witch Project*, marketing investment were even reduced to the minimum. The whole project barely cost $50,000[3]. Critics were essential to the success since they called the movie "the scariest ever". Communities of fans were informed with a newsletter about the successes and difficulties encountered to release the movie. The word of mouth was all the more efficient since fans were involved early in the production process. So this major role of communities is representing potential cost savings for entertainment companies willing to co-opt consumers.

1.1.3. Direct added value is determinant for intermediary services

With the internet, consumers can directly find everything they want. Let's assume that I watch *MTV* and discover a new song that I immediately like : will I take my car, go to a store, look for the CD that contain the very

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[3] Source : http://www.videouniversity.com/blairw1.htm

single song that I have just heard and buy it, and then rip it ? Or will I go to my room, turn my computer on and launch *Apple iTunes* or any P2P software to download directly the digital song ?

25 % of the French web surfers admit to use P2P network : can we still call this massive phenomena "piracy" or a deep change in consumption methods ?[4] Money is not the main driver for file swapping online : In France the proportion of persons using P2P network is the same among those who earn less than $1000 per month and those who earn more than $3500 per month.

In the price of a CD, almost half of it are distribution and marketing costs[5]. Are consumers willing to pay for costs that represent no value to their eyes ? On the contrary, the success of *Apple iTunes* that delivers good quality songs shows that consumers are willing to pay for valuable services : consumers are looking for an easy-to-use and friendly music store[6]. In this case, an intermediate makes sense. An illustration of this statement is the fact that payments on the internet are more and more developed : 16 % of American surfers have used a fee-based downloading platform in 2003 compared to 8 % in 2002. This expansion is parallel to user-friendly and cheap online music stores. Otherwise, there is no reason not to pick up songs directly from P2P networks.

The value delivered by music majors few years ago is disappearing. Having good quality music on CD format has less value today than having digital music "on the go". By offering services such as edition of library, rapid downloads, information about artists and concerts, organization of musical events and a free thirty-second preview of any song, the *Apple music store* creates value for consumers. It has set itself as a valuable intermediate. Otherwise consumers will overlap any intermediate that does not meet their requirements

Tomorrow the distribution of movies might face the same issue : when home theater devices will all include a hard drive, the value represented by

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[4] Source : Forrester research

[5] According to Eric Tong Cuong, Head of EMI Music France, in an interview with *Le Monde*, October 3, 2003

[6] "Apple store is integrated into one of the best MP3 programs around, rather than being a clumsy Web interface", according to *E-Commerce Times,* September 30, 2003

the DVD format will decrease, opening space for alternative digital distribution channels such as P2P networks. Distribution channels also start to evolve in the gaming sector : some video games created by individuals are distributed directly on the web without the interaction of publishing companies. Priced at around $20, this type of games can directly be downloaded on PCs.

The progressive disappearance of intermediary services on the internet has triggered new alliances to aggregate content and audience : *Disney* for instance has purchased a majority stake in the *Infoseek* search engine and portal. Similarly *NBC* has taken stake in *C-Net* and made a major investment in its search engine, *Snap*. Search engines are the new intermediary companies[7]. They point the audience directly to content providers. The interactions between content providers and their audiences are increasingly direct.

1.2. Consumers have higher expectations toward entertainment products

1.2.1. Consumers look for individualized information

Thanks to forums, consumers have the ability to discuss any subject they want. For instance the *Wiki* platform enables direct cooperation between web surfers online : *Wiki* is a piece of server software that allows users to freely create and edit Web page content using any Web browser. *Wiki* supports hyperlinks and has a simple text syntax for creating new pages and crosslinks between internal pages on the fly. Therefore *Wiki* Pages enable to share projects online and capitalize on mutual expertise on specific subjects[8]. More and more consumers will refer to the net when looking for answers to specific needs. Technical support, in the case of video games for instance, is not broadly used. Hot lines are rather expensive for most teens. And when players are stuck in a level, they'd rather turn to other players online to find a solution.

Gamers will look for discussion forums or postings to get an individualized answer to their problem. Most of the time editors don't have the financial resources to answer individual problems : it is very costly to their eyes and they assume it is not worth it, even if they would like to do it. Ga-

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[7] Source : Michael J. Wolf, *The entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999
[8] Source: http://wiki.org/wiki.cgi?WhatIsWiki

Gamer communities sometimes even create their own patches to correct defaults.

The internet is the most global medium that can be found, but it allows for individualized and local information. A French project called *TVWEB Regions* broadcasts local news on the internet : it deals with information geographically and therefore emotionally close to the web surfer, since emotions reach a pick when dealing with local matters. *TVWEB* was the first network regrouping 5 local channels. Synergies occurred with the constitution of a databank, the split of broadcasting costs, technological transfers, and the new ability to propose national commercial campaigns. If the local coverage of each channel could first be seen as a limitation, it became an opportunity once networked. And local information has additional emotional value. So even if the internet is a global network, it enables individualized answers, local information, and one-to-one interactions

1.2.2. Consumers want to pick up what they like, and strictly what they like

One of the main reasons of the *Apple music store* success lies in the possibility to buy one song at a time. The traditional Compact Disc format is adapted to fans who really like an album. But what if a fan only likes half of an album ? Will fans have to buy five singles ? This solution has recently shown some limitations, since for the first time ever the number of songs bought on the internet was higher than the number of singles sold in traditional retail stores : between July and October 2003, 7.7 million songs have been downloaded on fee-based platforms, whereas only 4 million CD singles have been sold during the same time period.

Another sign of the inadequacy between the current offer and a new demand may be related to the media. Ahmet Ekin, graduate student from the university of Rochester, has just invented a new device that automatically makes summary of highlights of a soccer or football game[9]. For instance a four-hour football game can be summed up in one hour by cutting commercials, time out and half time. TV viewers may no longer be willing to spend four hours in front of a TV set just to watch one football game. Ahmet is negotiating with a Swiss company that plans to beam soccer and hockey highlights to cell phones during the 2004 Olympics. Some new VCRs al-

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[9] Source : *Wired*, December 2003 issue

ready cut commercials. This evolution poses a serious threat to the business model of media companies : what if tomorrow we can skip commercials ? Will advertising be the first source of revenues for media companies ? Or are we evolving toward a consumer-centric business ?

Another illustration of this new type of increasingly focused consumption habits is news flash : with the 3rd generation of mobile services to come in 2005 in France, a survey conducted by *Siemens* and *CA Marketing* reveals that one consumer out of two wants to receive short news flashes on its mobile at any given moment. Future users are willing to pay on average $2.5 per month for this service, but 38 % of them refuse any form of commercials. Short summaries without commercials have extra-value : professionals are willing to pay $5 on average for the same service, and 48 % of them refuse any form of commercials.

When the Offer exactly meets the Demand, there is an additional transfer of value. For instance *CanalWeb*, a French TV portal on the internet was proposing several types of programs. Programs were ranging from broad target audiences to thematic niches. Thematic programs were targeting specific communities of fans, limited numbers of highly passionate viewers. The themes were as specific as chess, Californian music, cartoons… Those programs were totally in line with the very single desire of a limited community, and therefore were highly valuable[10]. This portal was created during the internet bubble when only a few people in France had access to broadband internet connection at that time. In 2002 the website was closed. But the idea remains.

New consumption habits are emerging, more and more focused. These are signals of an evolving demand. According to George S. Day and Paul J.H Schoemaker from the Wharton business school, companies have to learn from lead users : they are people who usually are not happy with current products and make one on their own, or adapt the one proposed to their own needs. They may try to solve their problems by making their own equipment[11]. So Ahmet Ekin can be considered as a lead user, as well as P2P designers. Therefore the entertainment industry should learn to adapt to an

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[10] Source : The association of French schools of telecom, under the direction of Danielle Bahu-Leyser and Pascal Faure, *La documentation Française*, *Media et e-media*, 2001
[11] Source : George S. Day and Paul J.H Schoemaker with Robert E. Gunther, *Wharton on Managing Emerging Economy,* edition John Wiley & Sons, 2000

evolving demand by understanding lead users and new consumptions patterns. They will turn out to be the main source of profits in the coming years, as developed in chapter three.

1.2.3. Individualized mass marketing is gaining momentum

There is a lot to learn from mobile phone companies. Today mobile phones are not simply devices to make phone calls, but very efficient Trojan horses to advertise for entertainment products. Demographic data about mobile phone subscribers enables targeted advertising campaigns. For instance in Japan the Tsutaya chain of video and CD rental has experimented a new type of marketing : they have used the *I-mode* (I-mode is the capacity of 3rd generation Japanese mobile phones to access a "simplified internet") very effectively[12]: they have announced the arrival of new CDs via I-mode mail and also issued electronic discount coupons. Both promotions provoked huge customer responses. Those informed about new CDs by I-mode mails outbought others by a large proportion. Those who received electronic coupons had total monthly rental fees 59 % higher than the other members.

A similar marketing technique was applied in France, with the release of the DVD of *Friends* season 9 : 100,000 SMS (Text Message Service) were sent the 26th of November 2003 to the mobile phones of potential buyers based on their age with a little game attached. Pierre-Emmanuel Cros, member of *Carat Interactive* that have designed the campaign, claims that : "In addition to reinforcing the notoriety of the product, this technique enables to develop proximity contacts with the targeted public, fond of SMS."[13]

Other recent marketing evolutions may change the way we behave in movie stores for instance : Already, thanks to cell-phone technology that can track subscribers' whereabouts, retailers can view when a particular customer walks into a store. With that information in hand, stores could conceivably tailor marketing messages to people based on demographic data or on answers to questions they were asked when they signed up for cell-phone services.

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[12] Please for a complete description refer to Takeshi Natsuno, *I-mode Strategy*, Wiley edition, 2000
[13] Source : http://www.silicon.fr

Underhill, author of the bestseller *Why We Buy,* explains that "It isn't futuristic, it's right now, it's real. That technology is out there now. It's just a matter of finding people willing to pay for it." Shane Booth, a researcher at *Mitsubishi Electric Research Laboratories*, or MERL, believes that he has found one approach that works. When it comes to market, this approach could change the way in-store merchandising is done. Booth's team is developing a system that projects product information onto a wall. As a customer approaches the wall, the system senses that someone is getting closer and alters the message it projects, incorporating data about the person gleaned through facial-recognition technology. The closer the customer approaches, the more specific the information gets. Eventually, the message would focus on the actual product the person is handling.

The system can also tailor messages based on demographic information gathered when consumers walk around a store. It lies on facial-recognition technology built into the system that can determine race, age and sex. Thus, demographically tailored messages can be projected instantly onto a wall near specific customers. Wouldn't it be interesting in a movie store to advertise for DVDs based on the age of the customer ?

In another bid to increase sales of old fashioned CDs, Virgin is trying out technology provided by a New York company called *MusiKube*, whose *Personal Music Guide* allows customers to hear samples from tracks on a CD as well as read reviews and recommendations for similar artists. The information appears on a portable device so customers can try out a CD while wandering around the store rather than lining up to hear tunes at a stationary listening post.

Steven Wimmingham, senior vice president of operations and IT for Virgin Entertainment USA, claimed that "We wanted to get technology in people's hands that is easy to use so that when you find something you like, you'll try it. The more products you'll try, the more you'll buy." The device is a customized *Compaq iPaq* PDA that comes with a bar code scanner, headphones and WiFi connectivity. A shopper scans the bar code on the CD. This is sent via the in-store 802.11b wireless network to a central database and the relevant information is delivered to the *iPaq*.[14] A fairly intuitive way for individualized commercials. Marketing methods are evolving toward a consumer-centric approach : a future trend in marketing are

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[14] Source : http://www.wired.com

techniques that go-along with consumers as they hang around in stores. They will provide individualized information, on-demand. Consumer will search products and ask for information, rather than promotion being directed by companies unilaterally.

1.3. From a logic of offer to a logic of demand

1.3.1. Consumers impose technological standards, not companies

Consumers influence technological standards. Their influence is so determinant that companies are ready today to reduce switching costs. Wired magazine has analyzed the evolution of technological standards in the past 50 years[15]:

- By the time of WWII, products were simple, worked, with few buttons.

- With the mid-80s came the plastic age, with stand-alone islands of proprietary technology, loosely connected by lowest-common-denominator cables. No matter how digital the electronics got, the companies were still stove piped. Companies wasted time fighting for standards, rather to sit down to iron out one superior system.

- Then came the PC industry with common standards and commoditized parts : they know that if documents, pictures, video and music are merely streams of 1s and 0s, it makes sense to put software in computers, cameras, and DVD and CD players. And they know how to do it for less money. For the computer industry, going digital means putting the same chips and circuits in every device, knowing that commodification reduces manufacturing costs (whereas in the consumer electronics industry, lots of different components triggered high costs)

Consumers grew tired with the fact that their products are not transferable from one platform to another. Everybody knows that consumers are linking together electronic devices from different manufacturers (VCR from Sony, TV from RCA, Home Theater from Yamaha…) and nothing is done to ease compatibility, until recently at least : just like the PC industry that has understood that consumers buy accessories from multiple companies, electronic devices manufacturers start to ensure devices compatibility. By

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[15] Source : Wired Magazine, December 2003 issue

adopting a consumer-centric point of view, electronic devices manufacturers have understood that if they want to find a place on the consumers shelves, they have to be less focused on their proprietary technological standards, according to Wired magazine : to maintain consumer loyalty, products will be competition-friendly in the future, easy to use with competitors products. Switching costs will decrease to increase brand loyalty ! This statement makes sense only because consumer electronics companies are giving up a firm-centric approach to adopt a consumer-centric strategy.

This idea is developed by Takeshi Natsuno, one of the creators of the *I-mode* in Japan, who explains that the internet and the new technologies have put an end to an age in which one major company, working alone, could carve out a new market : the rules now are to use the de facto standard technology : there is no way a unique, proprietary technology is going to be accepted by potential customers : it has to be supported by somebody else. The horizontal integration phenomena that is happening today, such as the alliance between Sony and Samsung, can be seen as a natural consequence of this logic.[16]

1.3.2. The logic of "on demand" is slowly supplanting the logic of "flow"

Media companies are experiencing determinant mutations. Whether it be newspapers or TV channels, the advent of the internet is changing the range of services offered. These sectors are becoming similar to databanks. With the close links between information, content, the internet and video, consumers are watching TV differently. At least on PCs so far. With new software such as *SnapStream MEDIA*[17], anybody equipped with a TV tuner (around $50) can transform his PC into a recording station. The software combines a program-listing service, recording and playback options that allow to "pause" live TV. TV viewers gain command and control on TV programs.

In addition, TV channel portals such *M6.fr* in France (a TV channel targeting young adults) are proposing newsflashes on demand. *Nba.com* offers highlights and video summaries of basketball games. Newspapers on the net such as *Lemonde.fr* in France have developed comprehensive archives of past articles available online. Digital video browsers such as *Real Networks*

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[16] Takeshi Natsuno, *I-mode Strategy*, Wiley edition, 2000
[17] see http://www.snapstream.com for further details

allow to stream video clips and TV shows on demand. For a part of the public, it is a constraint to be available at a fixed time everyday to watch the news on TV for instance. With a PC equipped with a hard drive and an access to the web, surfers can store and access information at any time.

As far as the traditional TV set is concerned, the *Microsoft Media Center* is a box to be connected on TV, and that offers the same features as Snap-Stream, plus a hard drive to watch DivX, DV and MPEG videos. The TV set is transformed into a device to store and watch data and video. Related to the same concept, the software *Sesam.tv Navigator* eases the transfer of data and video from PC to TV, using remote controls.

Many people are leaving TV because they spend more time on their computers (recently, cable subscriptions dropped by 10 % while internet subscriptions increased by 10 %). Why pay 30$ per month for HBO when one can only see two or three movies because of conflicts of activities ? Pay per view systems are better adapted to new consumption habits. The development of too many channels has partly cannibalized channels. If there are too many channels, they no longer become viable : people cannot watch them all and they will spend only a little time watching each of them anyway, so the return on investment is low. It is less and less worth it and pushes the development of pay per view systems[18].

Lastly, Video On Demand (VOD), Subscription Video On Demand (S-VOD), Network Personal Video Recorders (N-PVR), and "Anything On Demand" (X-VOD), are all being made ready for wide spread deployment. During 2007, the worldwide dollar value for Video On Demand Servers will be about $627.2 million. Worldwide subscribers to cable VOD services are projected to increase from about 5 million at the end of 2003, to almost 14 million in 2007[19]. This forecasted development of "On Demand" is the illustration of a system that places consumers as business drivers. Products, programs and services are not pushed in this system, they are pulled by consumers. It forces to articulate the organization around consumers, and literally include the consumer inside the organization. Consumers are less and less external to companies and are now part of their value chain through multiple interactions.

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[18] Source : *The Harvard conference on the internet and Society*, edited by O'Reilly & associates. Inc, distributed by Harvard University Press, March 1997, especially from page101
[19] Source : InstatMD, http://www.instat.com/newmk.asp?ID=732

2. Thanks to new technologies, consumers are more active and involved in entertainment

2.1. The construction of an "experience" by companies and consumers is the new competitive advantage

2.1.1. Entertainment products matter, entertaining experiences matter more

The concept of "experience" is relatively new. It does not exclusively refer to the entertainment industry. An experience of a product or a service represents the good or the bad feelings people get with the use of the product. The term "experience" refers to something emotional, active and involving. Therefore the concept of experiencing a product is richer than consuming a product. People may consume a product but have a disappointing experience of it. The consumption environment is included into the experience environment, but the reverse proposal is not true, because an experience environment refers to something active and emotional.

For instance going to the movie theater is an experience, it is not simply about paying to watch a movie. The difference in price between watching a movie on TV (with the pay-per-view system for instance) and watching the same movie in a movie theater shows that one consumption environment delivers more value for the customer than the other. Going to the movie theater is richer in term of emotions and feelings : the screen is bigger, the sound system is enveloping the audience, seats are more and more comfortable, pop corns and soda participate in creating a feeling of well-being. The dark room transports the audience into the action. There is a "magical" atmosphere that unleashes the emotion of viewers. Therefore the experience is richer.

All these aspects are creating an experience environment, because there is a physical and virtual environment in addition to the very simple action of going to the movie theater. Companies that have understood that the environment in which products are consumed is as important as the product itself have built successful business models. Michael J. Wolf, in the book "How Mega-Media Forces are transforming our lives", explains that creating an experience is a reliable way to stand out from the rest of the pack : " With so many similar products, how do businesses get their products to pass the 'Who cares ?' or 'must-have' test ? The answer is entertainment content and experiences. Not entertainment alone, content is key : companies must

exceed the efforts of their competitors to amuse, arouse, and inform customers : Companies need to provide experience that engage the consumer." And in order for consumers to be engaged, they have to be fully part of the experience, and not simply spectators or passive consumers. Consumers have to be involved and active in the construction of their experience environment.

An experience is a gathering in a very attractive way of several elements related to the consumption environment around the product. In restaurants for instance, the proliferation of themed "experiences" such as the *Hard Rock Café*, *Rainforest café* or *Planet Hollywood* shows that casual dining is not just about getting a burger and fries anymore. The decoration, waiter and waitress, prestige, and fun around the meal are determinant to the eyes of the client. They add value to the meal through a richer experience. It creates an identity, an atmosphere, an emotion. These type of services are much more focused on the user than before. An Experience is consumer-centric by definition. The concept of Experience is so determinant in corporate strategy today that *Microsoft* has decided to call its latest operating system *XP* for eXPerience.

Experiences are also simply suggested through a marketing style that puts the emphasis on what can be achieved with the product, suggesting an attitude or a situation. For instance Takeshi Natsuno from *NTT DoCoMo*, explains his way of promoting I-mode for mobile phones in Japan in these terms "What would the internet-style marketing be ? (…) it is to push service, not technology. Our message is what you can do with I-mode, not why it is possible to do it." For Natsuno, this type of advertising is similar to the one used on the internet, with the core message being the service and the context of use : "Today when advertising for the wired Web, you will not see anyone announcing, 'our service uses the internet'. What you will see instead is 'Bank from home' or 'make reservations from home with our service' (…) The message is structured from the perspective of the potential user of the service, not that of the service provider". This reversal described by Natsuno shows that we are evolving toward a consumer-centric system : and the objective is to articulate and co-construct with consumers a personalized experience environment.

What has more value for the final customer than the features of a product ? The answer is the good experience the customer has with the product. But this answer implies migrating from a firm-centric point of view toward

a consumer-centric point of view. This migration is not easy : In fact, Most managers assume that it is the physical product that they sell (such as a 3rd generation mobile phone) that contains all the value. Professors C.K Prahalad and V. Ramaswamy from the University of Michigan explain that managers rarely think about the aspirations, frustrations and wishes of the heterogeneous group of consumers who experience their products or services[20]. If mom buys a mobile phone for instance, she will usually have a better experience with a big screen and large display, even if technically, a 320*160 pixels display cost more, so would be considered as delivering more value. This type of reasoning is typical of a company-centric approach of value. Small digits and font sizes create a bad experience for this mom because she cannot read the screen properly. So the products are not the only source of value, and therefore it is not sufficient to calculate an appropriate price simply based on features. Experiences of products and services are more determinant to evaluate the real price or value of a product.

2.1.2. Constructing experience with consumers is an efficient answer to the heterogeneity of needs

When a company starts by recognizing that consumers are driving their business, then organizational consequences are huge. Evolving from a company-centric point of view to a consumer-centric organization implies several changes : if we start with the paradigm that consumers are driving our business, than it appears that the experience of a product matters more than the product by itself. Having a good product is determinant to have a good experience, but most companies do not take into account the wide range of experiences for a very simple reason : experiences are individual by definition since they are mostly an emotion and emotions are highly subjective. Can a company take into account the whole range of experiences into its business plan and still be profitable ? On the other side, a perfectly adapted experience environment will have a higher value in the eyes of consumers. And some consumers, not all of them, are willing to interact more with companies to improve their experience of a product. To develop this idea, we can compare the two experience environments provided by the rental stores *Blockbuster* and online rental company *Netfix*. Professor V. Ramaswamy from the University of Michigan has taken this example in his

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[20] Source : C.K Prahalad and Venkatram Ramaswamy, *The future of Competition : Co-Creating Unique Value with Customers*, Harvard Business School Press, 2004

class about The Future of Competition[21] to illustrate the concept of a successful experience environment.

So we can start buy adopting a consumer's point of view, since experiences are consumer-centric. Let's assume I want to rent one or two DVDs for the week-end. I can drive to the nearest *Blockbusters*, or I can walk to my room and switch on my computer to connect to Netfix.com. Netfix enables to order as many DVDs as I want for a flat monthly fee under $20. I order the DVD online and receive it usually the day after by post mail with a prepaid envelope to send it back. I can keep the movies as long as I want as long as I don't hold more than 3 DVDs at home at the same time.

Back to the example, let's say I don't know what I want to watch, but a movie with special effects for sure. At *Blockbusters*, I can walk through the DVD section, and look for each title, probably by alphabetical order. On *Netfix* website, I can search by directors, actors, or category like SciFi for instance. Let's say I have found this new movie I have never heard about, but the jacket looks cool. How can I know if it is a good one : if I am lucky, I can find a salesperson at *Blockbusters* who might have seen this unknown movie and can give his opinion. On *Netfix*, I will find a lot of viewers opinions attached to a short summary of the movie, or I can search on google otherwise. And let's say on top of that I want to rent the latest big success : first at *Blockbusters*, I have to ask which DVD is in hot demand whereas on *Netfix* there is a weekly ranking of the most viewed DVDs. Bad luck at *Blockbusters*, it is in such an hot demand that no more copies are available for rental until tomorrow. On *Netfix*, if a DVD is not available at the time of order, I can put my name on the waiting list and receive it later.

With *Netfix*, I can travel with the DVDs : most people have time to watch DVDs when they are on holidays and mostly when traveling or on-the-go. With *Blockbusters*' solution, I would hardly travel with a rented DVD. Whereas the absence of time and localization constraints with *Netfix* enable me to experience rented DVDs in many more situations, especially during travels. So now let's say the week-end is over and I didn't have time to watch the second DVD : I will have to give it back to *Blockbuster* and pay for it anyway. With *Netfix* I can keep it longer. In addition *Netfix* has eliminated the late-fees that worsen the experience by abolishing due date.

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[21] Source : Class MKT742, University of Michigan Business School, Fall 2003 semester, MBA program

Netfix and *Blockbuster* provide two different experience environments for the same action : renting a DVD. One method is more flexible than the other, and is based on a consumer-centric organization of the value chain. Consumers have the possibility to interact a lot with *Netfix* if they want through the features proposed by the site ; or they may simply order directly a DVD through a few-click session. Companies that have adopted a consumer-centric point of view are in a position to deliver enhanced experiences : they do not try to push their products, consumers are designing an experience environment. Just like the logic of "on demand" is replacing progressively the logic of "flow". With the opportunity to better serve their needs, consumers may pay a premium for this service. *Netfix*'s revenues for 2002 were about $150M.

Netfix was a pioneer because it was the first company to adopt this type of business model. Now in 2004 several firms have adopted this type of consumer-centric approach. *GameFly* for instance rents games for the major consoles for $20 per month with a maximum of two games in possession at the same time. Consumers have access to a wide range of games, and this access may become ownership by adding $15 to $45 to keep it. *RedOctane* and *Gamelender* are active competitors on this segment. The adult movie arena is also crowded with this type of business with *SugarDVD.com*, *WantedList.com* or *XRentDVD.com*. As far as books are concerned, *booksfree.com* offers revolving-rental business starting at $8 a month for the right to hold one paperback book at a time. More than 40,000 titles are available.[22] Adopting a consumer-centric point of view helps to better represent an experience environment and find new profitable business models.

2.2. Video Games are all about creating an interactive experience

2.2.1. Building a universe, appealing to emotions

Video games, whether it be on consoles or PCs, are immersing players into an interactive environment. The keys to the success of a good video game are all about creating an attractive experience environment. The following features are determinant :

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[22] Source : Lore Sjoberg, *Netfix imitators are everywhere*, http://www.wired.com, February 19, 2004

- Gameplay, which is the interaction with the various elements of the games. Games like *GTA Vice City* have made innovation in the freedom given to players to interact with the environment.

- Graphical beauty : video games now must look as nice as a movie. Animated sequences in games like *Final Fantasy X-2* or *Warcraft3* are by themselves worth buying the game.

- Story : the interest of the game is linked to the originality of the universe created for the player. The vastly successful *Medal of Honor* deeply immerses players into the World War 2 period for instance.

According to Pierre Gaultier, journalist in a newspaper dealing with artistic issues, "Video games are nothing but the logic sequels of this process that tends to erase the borders between various arts : drawing, animation, music, production, architecture, drama… and to place players in the midst of a surrounding environment in which they can interact".[23]

Even more interactive and enveloping are games requiring physical involvements on behalf of the player : games during which the player needs to dance in tempo on a carpet linked to the PS2 such as *Dance Dance Revolution* ; or games that capture the body and face of players thanks to a camera to place their image in the game in real time.

All these technologies are already available. In the near future 3-Dimension environments, and especially 3-Dimension environment that can rotate and zoom, (commonly called Virtual Reality) will gain momentum : Teleimmersive Virtual Reality is the next step for a total experience environment. Created in 1992 by the university of Illinois at Chicago, the Teleimmersive VR is a 3D environment in which the user can physically move.[24] No need for a TV or a screen, the virtual environment is remotely created in the room. This technique is the illustration of how experience environments are going to literally envelop players. The gaming environment will deeply involve players in an individualized universe.

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[23] Source : Pierre Gaultier, *Beaux Arts Magazine,* October 2002 issue.
[24] Source : Debra Cameron, *The internet2 : the future of the the internet and Next-Generation initiatives*, Computer technology Research Corp., edition, 1999, especially page77 and upward, chapter 5 "Next-Generation Applications and services"

2.2.2. Players interact in games, but also with games

Video games allow players to customize a large part of the characters or even part of the story. Games like *Lord of the Ring-the Return of the King* are a way to experience and watch the movie differently, since gamers control the story and the characters. Role playing games such *World of Warcraft* are all about creating a unique character, with unique features and competences to evolve in a virtual environment online.

Recent games such as *Top Spin* on *Xbox* allow gamers to create their own tennis player. So not only can players choose among a comprehensive range of tennis capacities, but the tennis player can also be physically customized to a point never experienced before. And the hard drives added on recent consoles help to store local profiles, created characters, adapted features etc…An other example of customization is the new game from Electronic Art called *NFL Street* : the gamer is prompted to give his age the first time the game is launched. Three categories are available : 12 to 17 year-old, 18 to 23 and 24 to 32 year-old. Depending on the category of age, three different experience of the game are available with adapted music, customized speed, and the most appropriate level of violence.[25]

Even more interesting is the concept of "mods": these are additional levels, extended features, modified universes created by gamers for gamers. They are available mostly on the net and are created by programming-literate gamers who intend to renew or increase the interest of the game : for instance the mod *Counter Strike* has transformed the one-person-shooter game *Half-life* into the most online popular game played in teams of terrorists against counter-terrorists. To access this new feature, players need to have a copy of the original *Half-Life*, and download the mod called *Counter-Strike* for free. And then players have two games for the price of one. Another example is the mod *Dragon Ball Z* for the popular *Quake3* : this new feature allows to play with characters from the popular Japanese manga *Dragon Ball Z* : the gameplay remains the same, but new levels are added. And games such as *Unreal Tournament* even include a map editor to create new customized levels. Gamers who create mods that increase the interest of the game are highly valuable for other players. And valuable for the gaming company too. The success of Counter Strike has boosted the

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[25] Source : Steve Yanovsky, Vice President Marketing at Buzztone, during a lecture at the University of Michigan Business school, October 17, 2003

sales of Half-Life for a long period of time, even though the original game had been outdated by the competition.

2.2.3. Gamers participate in improving their experience

Gamers are more and more knowledgeable, and many of them have taught themselves how to program. A lot of communities of hardcore gamers exists online where gamers exchange tips, programs and ideas. They program useful patches that correct defaults, or enable to play games on PC without requiring the CD. These kind of patches called "no cd" are not provided by gaming companies for fear of piracy but are valuable because they allow LAN games : Let's assume I have bought a war game and I have two computers at home. Let's also assume that my two computers are linked together with Ethernet cards and I want to play the game with a friend : How can I run the game on two different computers at the same time ? "No-cd" patches are highly valuable in this case, and create value for other players and for companies, as people buy some of these games mostly for the multiplayer experience.

Gamers have also invented emulators that allow PC users to play mostly old console video games on their PC. An emulator is a program that recreates the firmware of the console in the Windows environment. The emulator *Game Boy Advance* for instance is widespread on the internet and the quality of games called "roms" is equivalent to the originals. Leaving apart legal issues that do not allow to play a rom if you do not own the original copy, emulators are a good way to become familiar with a game. Given that emulators are mostly old consoles for technical issues (recent consoles are too powerful to be "emulated" on current PCs), the potential losses for gaming companies are reduced to the minimum. But the benefits are huge : given that most game titles are adapted from one generation of console to another (*Zelda* has been adapted to each new generation of *Nintendo*'s consoles for instance), emulators can allow gamers to discover a title on an old platform, and if they like it, they might want to buy it on their new or recent console. This is a new way to try a game before buying it. And it has also a huge marketing impact : Roms are mostly ranked by popularity.

2.3. Participative entertainment products provide an enhanced experience with emotional links

2.3.1. Emotional feelings link the creator to its creation : Pop Idol analysis

Whether it be *American Idol* in the USA or *A la recherche de la nouvelle star* in France, the underlying principle remains the same : the public can choose to create a future star almost from scratch. By being involved in the selection process of potential future singers, emotional bonds are created.

Every time the public votes for a candidate, it persuades itself that the candidate is a future great singer. They have chosen the candidate to be a star. And then by the end of the selection process the success of the remaining candidate is ensured, since the public is convinced that the candidate is gifted. They are emotionally convinced that the candidate is a star, so they will buy his first album and the candidate in turn will become a "real" star.

American Idol is based on emotional interactions with the fans. By the end of the selection process, the public can only recognize the candidate as a great singer since it is the same public that has enabled this adventure. Given that entertainment companies will compete on the basis of the quality of the experience provided, accrued emotions through active involvement of the audience is a path to follow.

2.3.2. If consumers choose TV programs, they can only be good programs

Based on this simple principle, the success of interactive television is certainly ensured. Interactive television consists in personalized TV programs through the internet, and active participation of viewers in programs broadcast on computers through the internet. Even if this technology is not currently available, some similar experimentations have taken place : In France programs like *Loft Story*, similar to the *Big Brothers* RealTV concept, have created an interactive experience : Viewer could watch every day on TV the highlights of the day. And the experience of the program was prolonged through the website of the RealTV show : viewers on the internet could choose a camera in the house to watch the candidates, and they could also interact with the program by voting for the elimination. These interactions were possible through fee-based type of connections.

Another evolution toward a more active role of viewers will come from the Hypervideo. This technology will consist in watching videos or TV programs on a PC through the internet, with hypertext links on the screen. Then let's say if the viewer wants to know the biography of the actor playing in the movie, he or she can click on the actor and access a summary of his life. Or clicking on an hypertext link would open another video related to the original one. The experience will be similar to surfing on the internet from one "video page" to another "video page".[26]

2.3.3. DVDs prolong interactively an emotional experience

For a while, watching a movie has been a passive activity. With DVDs, interactions between the viewer and the universe of the movie are eased. DVDs are a simple answer to the need to go further, to get more involved, to prolong the experience of a movie. Before the DVD format, there was a frustration to watch a good movie ending. What if fans wanted to learn more about the characters, the director, or the story ? Well, they would have to wait until the sequels of the movie.

And when emotional links are strong, the more fans get, the better : for instance the movie hit *Alien*, whose community of fans are numerous around the world, has just been re-released in 9 DVDs with director's cuts : almost forty hours of movie to prolong the emotional experience of the quadrilogy. At least fans have the opportunity to recreate the atmosphere attached to the movie, and to know everything around the universe : the emotional frustration of the movie ending is overcome. Fans (who are people with tight emotional links with movies) will want to watch this horror movie with popcorns and in a scary dark atmosphere to recreate an experience environment that appeals to emotion, that will place them in the midst of the universe of Alien.

Recent DVDs such as *Finding Nemo* not only propose an easy and interactive navigation in the story, but add features to prolong the experience of the movie : interactive games, quiz or dialogues place viewers in an active position in front of their TV set. They become involved in Nemo's environment, they can play with the principal characters to deepen their relationship with the movie.

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[26] Source : Michel Agnola and Rémy Le Champion, *Que sais-je ? la television sur the internet*, PUF edition, April 2003

Another way to create a comprehensive experience environment of entertainment products is to propose several complementary formats of the products : for instance fans of *Matrix2* will be able to prolong their interest for the movie with the video game, and then with cartoons inspired from the movie, while waiting for the making-of on DVD and ultimately *Matrix3*. Great movies are not just a two-hour experience environment in movie theater : fans want the experience to last in answer to their curiosity, interest and emotional involvement.

2.3.4. Pokemon and Yu-Gi-Oh ! or when watching cartoons becomes a game

New successful cartoons have managed to become more than a simple cartoon and to look more like a video game. For instance the worldwide hit *Pokemon* is all about tiny monsters fighting each other. But kids have the opportunity to buy cards representing monsters watched on TV, and recreate combats based on the competences and specificities of each monster. Every monster has strengths and weaknesses, a bit like characters in a fighting video game. Or kids can directly play *Pokemon* on their *Game Boy Advance*, the adaptation being so natural. Kids are moving from a passive experience (watching TV) into an active participation (playing and simulating combats of monsters). The second experience is rich in emotions and link kids with the heroes of the cartoon since kids can in reality identify themselves with TV heroes.

Even more troubling is the recent hit coming from Japan *Yu-Gi-Oh ! :* in this cartoon, monsters are also fighting each other, but before each combat, a number of "lifepoint" directly inform the viewer, in a way similar to the "lifebar" of video games. Viewers are involved in the cartoon since they can rationally predict the issue of combats : it is no longer pure fiction, but there are video-games look-alike principles for each combat. And cards also allow kids to actively experience their favorite cartoon and immerse themselves in the universe of monsters' fights.

3. Virtual worlds and communities have added a new dimension to entertainment

3.1. The separation between "virtual" and "real" entertainment has collapsed : "virtual" benefits can become "real"

3.1.1. A new gaming experience environment

Games, online or "offline", are considered pure fiction. The split between virtual world and reality is supposed to be obvious since we insert or eject a CD to remind us in which world we live.

But a new game recently developed by *Ubi Soft* requires a dual type of involvement on behalf of the player : *In Memoriam*, released in October 2003, is more than a fictive investigation. The entertaining aspect of the game has merged virtual and real quest. The principle is innovative : The CD-rom of the game is a key to conduct an investigation about a mysterious kidnapping. The game takes into account the fact that gamers are in front of a computer screen. Therefore part of the investigation will take place on the internet.

Not only has the developing team of Ubi Soft created false websites to misled players, but original websites also contain information related to the game. Several forums have been created to discuss the kidnapping with other players, and partnerships between *Ubi Soft* and web search engine such as *google* enable to fool gamers on the net. Finally an e-mail account is mandatory since some pieces of information are sent directly to players on their mail box. The involvement of players is broader than before since they can play the game during lunch break at the college for instance while checking their individualized e-mails related to the investigation and browsing the web for pieces of evidence[27].

Online games take the process to the next level, particularly in Asia : online games have build a bridge between virtual and real world : virtual success now means success in the "real world". Fame in online games means fame in reality. For instance 70 % of households in South Korea have high-speed internet connections. That level of access has fuelled a craze for cyber games. Gaming over the internet has proved to be so popular that pro-

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[27] Source : http://www.jeuxvideo.com

fessional teams backed by corporate sponsors now play in the world's first pro league.

For instance ten members of a professional gaming team sponsored by the mobile phone company *KTF* train all day long in a cramped three-room apartment. Some of them make more than $100,000 a year. *KTF* manager, Chang Ki-uk, said sponsoring a professional team makes good sense for his company. Fifteen million people, or 30 % of the population, are registered for online gaming, which represents huge marketing opportunity.

"Online gaming started out as a hobby, of course, but it's amazing how it's taking off as a professional sport. There are three cable channels that broadcast games and 10 professional leagues. Electronic sports like this have become a way of marketing and promoting our company, particularly with young people," Mr Chang said. South Korea proudly plays host to the annual World Cyber Games and the country is becoming a Mecca for online gamers around the world[28].

Real value is coming from Games online because money used to trade in games such as the Simoleans (the currency of *The Sims Online*) can now be traded for real money : The Gaming Open Market, or GOM, is a recently launched website that serves as a currency exchange of sorts. It lets players of a group of online games (including *Ultima Online*, *Star Wars Galaxies*, *Second Life*, *The Sims Online*, *There* and others) traffic in the currencies of those virtual worlds, trading game money for U.S. dollars or, soon, even allowing players to trade across games. GOM allows players to post blocks of game currencies they want to sell, along with an asking price. For example, a block of 250 of *Second Life*'s Lindenbucks sells for $1.06, but that price fluctuates based on demand. To date, nearly $10,000 has been traded on GOM according to *Wired magazine*.[29] Gamers have fructuous exchanges that can be really valued and cooperate as well to improve their experience of games.

If role playing games, where people play imaginary characters in a real environment, are so popular, it is due to the experience environment. In role playing, people are emotionally involved since they play a character and

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[28] By Charles Scanlon, BBC correspondent in Seoul, October 2003
[29] Source : Daniel Terdiman, *Virtual Cash Breeds Real Greed*, http://www.wired.com, January 23 2004

identify themselves with imaginary characters through costumes, decoration, and rules. Most of the time role playing games are taking place in environments that add some emotions to the experience such as a hood, an hidden room with candles, any place that creates an appealing atmosphere. The experience is created through surrounding emotional elements. The more emotionally-involved people are, the better the role playing game is.

3.1.2. Communities are not restricted to a virtual environment

Virtual communities have the clout today to influence real life. Apart from dating websites that help to find a real girlfriend or boyfriend online, other types of services create useful links between people. *Friendster.com* for instance is a website that create links between friends and friends of friends. With *Friendster*, people can make new friends and literally "network" with new people. The community phenomenon is literally illustrated by the number of "friends of friends" that people count in their personal networks. Every time a new friend is included in the network, the latter adds his own network. By Only adding one popular person to my network, the number of people in my network grows exponentially. This networking software is so popular that in February 2004, the website announced that "the 2004 Presidential candidates have joined Friendster – So keep an eye out for John Kerry, John Edwards, and George W. Bush !". Politicians use it to promote their campaign, and we will see in chapter three that the entertainment industry had better use it too !

Messenger services such as *AOL Instant messenger* have also created a community of real friends that virtually appear on computers. And *AOL messenger* is creating new links between virtual and real world : a new service has just been opened in France that enables to send SMS (Small Message Services) from *AOL messenger* to the mobile phone of a friend, whether he is connected to the internet or not. A chatting session on *AOL* that initially took place in front of a screen can now be prolong in the street or wherever people want. *MSN* is proposing the same functionalities in France thanks to an alliance with the mobile operator *Bouygues Telecom* called *MSN Mobile*. *MSN messenger* can send messages to a friend in front of a screen or directly on its mobile phone.

Other services such as *NetInTheCity.com* have merged dating functionalities with party guide. People looking for a bar or a club to party will have the opportunity to meet other persons interested in the same venue.

Communities online are more and more advanced, illustrated by the development of MetaWorlds (chat room with enhance graphics). Websites such as *Thepalace.com* or *there.com* help to create an own chat room, or enable to chat in 3D with one's avatar. An avatar is a virtual representation of one's face. *There.com* looks like a virtual island where people own a virtual piece of land with a 3D house built on it that represents one's "home". People are represented by a virtual character and can chat with other virtual characters who have settled the islands. This virtual land dedicated to communities is a mix of chat room, Virtual Reality, video games, color forms and MMORPG (Massive Multiplayer Role Playing Games).

3.1.3. When music overlaps virtual and real world

Activities such as downloading music on P2P network may not be very social at first sight, even if today more and more P2P software come with chatting features to talk to the one that shares the same passion for an artist. The future of on-the-go peer-to-peer music sharing is already starting to work in Ireland according to *Wired magazine online*. *Media Lab Europe*, research partner to MIT Media Lab, is testing *tunA*, a software application that employs Wi-Fi to locate nearby users, peek at their music playlist and wirelessly jack into their audio stream. Pronounced like the fish and signifying music "tunes" and "ad hoc" file sharing, *tunA* is being designed for wireless PDAs, cell phones and even its own hardware device.

The research fellow Arianna Bassoli, who masterminded the project late last year after researching the way young people in Dublin interact in public spaces, explains that "*TunA* alleviates the alienation of using a Walkman, and it makes it more of a social experience. You can listen to your music and still open yourself up to people around you."

"The main issue was a way to connect people subtly, without being intrusive," said Bassoli. "And music is the way teenagers want to open themselves to people around them." When alone, a tunA-enabled device functions like a regular MP3 player. But around others like it, the interface displays other in-range users, identified by the avatar of their choice. Avatars appear or disappear automatically as users go in and out of range. Clicking on others' avatars let people see whatever personal information or messages they want to share with the world. It also displays their playlist and the song they are listening to at that moment so one can decide if one

want to tune in. There is also instant-message capability, the possibility to change skins and a virtual stalking feature : One can bookmark not only songs, but also people.

"So even though the people around you might change, you can bookmark those you like, so next time you see them, (tunA) would notify you they're around," explained Bassoli. "Also, if there's a song that you don't you know, you can bookmark it so the next time someone nearby has it, you can ask them about it." Bassoli's next step is observing *tunA* users' interactions at a small art college in Dublin. "I am interested in the overlap between the virtual and real world," she said. "I think that since you know the people you are connecting with are nearby, it would get you curious about who they are (based on their music tastes). "It's not like sharing music with someone far away on the internet ; you might actually want to meet these people."[30]

3.2. Communities of consumers create the buzz around entertainment products

3.2.1. Community, club and experience environment

We spend more and more time one-on-one with technology (watching TV or working on computer). But still most of us want to belong to some-thing with our fellow humans. If we have not seen a certain movie or television show or read a certain book, we feel left out of social conversa-tion. In general we want to feel that we are part of something larger than the individual. Religion used to play this role for most people. According to Emile Durkheim in *The elementary Forms of the Religious Life*, the religion is a particular kind of group dynamic wherein the act of assembling for a common purpose creates the feeling of being in presence of a spirit greater than individual. A similar dynamic is at work with live entertaining events such as pop music concert according to Michael J. Wolf[31]: from waving small flashlights to call-and-response singing, a rock concert generates spiri-tual energy. Entertainment products put the mass audience on the same wavelength and, while engaging the emotions, they replace the sense of sha-red community that is disappearing in regular life.

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[30] Source : Kary L. Dean, Wired magazine online:
http://www.wired.com/news/digiwood/0,1412,61427,00.html
[31]Source : Michael J. Wolf, The *entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999

In virtual, rather than physical, gatherings, there is also a sense of community that the internet chat groups promise : when people are online with their fellow Sci-Fi enthusiasts, Matrix fans, or whoever it is they chat with, there is a feeling of a larger "us" out there.

When a million viewers buy a book such as *The Deep End Of the Ocean*, as recommended by Oprah Winfrey, they become members of her club and gain some satisfaction and sense of belonging from the knowledge that each of them is reading something similar, thinking about it, talking about it simultaneously with all the other members of Oprah's club. An experience environment is in some sense a club : we feel that we are part of a group that gets use, pleasure, and enjoyment out of a product.

Entertainment, which speaks directly to emotions, can give consumers a sense of belonging to a group that sets them off as cool, sexy, tough or rebellious. The products we buy are increasingly seen to make a statement about the buyer. Apple *iMac* cool design played a great role in its success. Products also bind that particular buyer to other like-minded consumers ; Communities of consumers create hits.

3.2.2. *Word of mouth from influential communities : the case of Titanic*

Some communities and group of people are very influential. Teenage people are at the heart of new trends, and like to experience everything before everybody. They follow new trends to be the first to be followed. The movie *Titanic* is a good illustration of the potential economic impact of communities of "trendsetters". The success of Titanic as analyzed by Michael J. Wolf[32] is based on two factors described previously :

- This movie appealed to deep emotions, involving the viewer

- This movie benefited from an active community of fans represented first by teenage girls

While the movie was being made, it was severely troubled, running way over budget, and the experts predicted a movie disaster. Fox and Paramount (the rival studios that pooled their risk for this project) were really scared by the risk of failure. With a $200 million budget and close to $70 million

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[32] Source : Michael J. Wolf, *The entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999, Pages 170-180

committed to distribution and marketing, both companies felt in danger of losing a lot of money.

James Cameron, who bet his salary and his future on what the industry kept predicting would be a disaster, was answering critics' questions before anyone saw the movie. "Why would people buy tickets when they already knew the ending – a sad one at that ?" Cameron kept saying, "It's not what you think… it's a love story… the most expensive chick flick ever made, but you won't be able to see it without crying."

The TV rights were sold for almost nothing. *Titanic* was even compared as the failure of *Waterworld*. But then came the teenage girls. They filled the front rows of the theaters, and they came back for two, three, and more rounds of collective sniffling according to Michael J. Wolf. So great was their allegiance to the movie that they pulled in the other segments of society. The buzz was on. Word of mouth brought in more kids, then parents, then everybody.

The executives at Fox and Paramount sprang into action, throwing gobs of money and marketing muscle at the new release. *Titanic* became a culture-changing phenomenon. A quickie book topped the best-seller list ; 10 million sound-track CDs were rushed to market and became the longest chart-topping sound track of all time. Cruise ship bookings soared, as did the sale of jewelry patterned on the Coeur de la Mer jewel that graced Kate Winslet's neck.

Titanic is expected to have generated over $3 billion. There is no clearer case to demonstrate the absolute influence and real power of trendsetter and word of mouth to create a phenomenon. *Titanic* quickly reached a core group composed mostly of teenage girls and created a community that propelled the movie into the wider consciousness of the entire culture. Women dragged their husbands. Office workers compared how many times they had seen the movie. Titanic violated the traditional rules of blockbuster success : a romantic movie was not supposed to get repeat ticket buyers ; this one did. By tapping into simple, deeply felt emotional longings among teenage girls, *Titanic* created a unique experience and went from a disaster movie to a unanimously acclaimed hit.

3.2.3. When gamers are in contact, the experience of video games is improved

At Joypolis, a massive 100,000 square-foot entertainment center created by Sega in the Odaiba section of Tokyo bay, 3000 adults and teens play games each afternoon. In Times Square's Lazer Park, people can play Star wars race game, collaborate with their teammates via on-screen nicknames as they attempt to maneuver their legged tanks across hostile terrain. At game's end, these newly battle-tested vets can watch a video of their exploits, discuss the race, and then get back into their simulators to play again. Friends or simply other anonymous players are adding challenge to the experience.

With *I-mode* in Japan, and in the case of any online games on the internet in general, gamers boost the attractiveness of games : this is a win-win situation between gamers and service provider when players enrich the interest for other gamers. For example tournaments with *I-mode* games have a lot of success : the best players can monitor their ranking everyday to see if it has moved, and therefore use more *I-mode* connections. Online gaming provides nationwide rankings and informed people when their personal ranking increase or decrease, and create more involvement in the game. The customer-gamer is oblivious to the process, but his or her participation in itself makes the game more enthralling for the others.

Finally Online games have an edge over games distributed on CD-rom : the story line of the online game can be modified in response to players' e-mail : the game gets better and better thanks to player feedback.

The internet and the new technologies have modified the structure & equilibrium of the entertainment industry

1. New technologies have modified financial risks for Entertainment companies

1.1. The access to information and data online is impacting the strategy of entertainment companies

1.1.1. Selling entertainment products online is different from offline

E-commerce is forecasted to play an increasing role in the future, especially for entertainment products. In fact *Amazon.com* has initially built its success on selling entertainment products online, such as books, CDs, video games and DVDs. This category represents today over 90 % of *Amazon.com* sales[33]. *Forrester Research* predicts that in 2004, online commerce will reach $6.8 trillion. This figure includes B2B and B2C e-commerce. In fact, 8.6 % of total sales in 2004 will take place online. In France, e-commerce has increased by 56 % between 2002 and 2003 according to a pool of e-companies called ACSEL. This expansion is driven by new types of consumers : the number of women ordering online has increased by 65 % ; the number of people over 50 ordering online has increased by 80 % !

This trend will impact the sales strategy of entertainment companies. In fact, when shopping online, buyers are only one click away from consumers' reviews or buyers' opinions. When buying CDs in a supermarket, it is difficult to get any help to make up one's mind except by asking people around if they like this artist, for better or for worse. From a company point of view, it may be easier to sell mediocre products with massive marketing investment if consumers do not have access to peers' opinions. Rules online are different.

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[33] Source : Ian Clarkson, senior financial manager at Amazon.com and Bart Hoemann, Finance Manager at Amazon.com, during a lecture at the University of Michigan Business School, October 15, 2003

Amazon.com has recognized the added value and the impact on the pur-
chasing decision of consumers' reviews, since it has systematically added
them below the description of products. When comparing the room dedi-
cated to the traditional description of products and the room taken by
consumers' opinions on any Amazon webpage, the persuasiveness of the
two categories is largely in favor of peers' opinions. The good news for
entertainment companies is that massive marketing investment may not be
needed to sell a very good product. But in today's situation, for companies
who have not yet integrated this element as an entire part of their marketing
strategy, we observe increasing marketing expenses for a non proportional
evolution of sales. Risks of failure have increased.

Some companies have taken what seems to be a risky path, because they
have decided to "co-opt" users : General Motors on the *Saturn* web page has
included a lot of buyers' comments. GM has gained the help of consumers
to sell their cars. Part of *Saturn*'s whole advertising campaign is to get peo-
ple buying cars based on the personal recommendations of other persons
who have bought *Saturn* cars. GM has taken a bit of a risk by allowing third
party to add materials and content to their website, but the return on risk is
high. Even if the example is not really part of the entertainment industry, it
highlights a new trend parallel to the development of e-commerce[34]. Enter-
tainment companies could get inspired by this sales strategy.

To come back to the example of music, the *Apple music Store* has pushed
the concept of fans and consumers' opinions a bit further : in fact, *iTunes*
offers the possibility to chat with other viewers who are shopping for the
same artist at the same time. And who can be a better salespersons than fans
of the artist themselves ?

1.1.2. From scarcity to abundance, consumers are more and more demanding

When considering the internet as a database and P2P networks as digital
libraries, it appears that any body equipped with a computer can almost in-
stantly find online the book of his dream, his favorite artists, or the movie
missing in his collection.

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[34] Source : *The Harvard conference on the internet and Society*, edited by O'Reilly & asso-
ciates. Inc, distributed by Harvard University Press, March 1997, Pages 400 – 410

Very unique and specific needs can be filled up : for instance the sales of what publishers call "backlist titles", meaning elder books, are way up as people find it easier to locate that old mystery, special cookbook, or early novels by their new favorite author by shopping on *amazon.com*. On-line music retailers such as *CDNow* have created strong new demand for the sales of '50s jazz, classical music, and early rock.

But then consumers are more demanding. In fact, when the vinyl was the only way to get music, it might have taken almost 20 years to become an expert in jazz music for instance. Imports were not easy and music was relatively expensive. With digital music spreading online, a week may be enough to get round the jazz musical movement. This evolution means that consumers are more and more knowledgeable, and it implies more difficulties to sell new entertainment products.

In the long run, while digital technology has opened up new markets for old entertainment products for instance, it has also raised the ante and consumers' expectations from the last wow project to the next one. In a contest in which a company is only as good as its next production, the most recent special-effects-heavy blockbuster requires that the next one be even more elaborate. Increased investment in new projects prevent entertainment companies from being to creative and innovative : innovative entertainment products bear higher risks and entertainment companies cannot afford failure since financial investment at stake are enormous. This phenomenon poses a terrible threat to the entertainment industry as a whole, since the functioning of the industry depends on creation and innovation. Creations that would come from consumers, and therefore that would directly meet their expectations, would reduce financial risks to the minimum. Co-opting customers to co-create entertainment products and therefore value is an axis for future development and profitable business models. This idea will be the theme of Chapter Three.

1.1.3. Financial success may be measured differently

There are inherent risks in entertainment : as Chris Rock put it when he hosted the MTV Video Music Awards, " It used to be that music was here

today, gone tomorrow", he said, "Now it's here today, gone today". Business will grow more quickly. It will die more quickly too[35].

But on the other side, entertainment products are not just one-shot-products : when you make a movie, you can potentially release it again and again. Next it can be released on video, DVD. It can play on network television and cable and overseas. It can sell related sound-track of albums. It can be novelized too. Years from now it can be re-released again to nostalgic fans : like great wine, great entertainment assets hold the possibility of becoming more valuable as time goes by. And every new format is an opportunity for a re-launch later on.

When movies are produced, Movie Majors are already thinking about the second life of the picture : making of, behind the scene features, and deleted scenes add new interests to the movie when it is released on DVD. The success of a movie is no longer based solely on the box-office. Even more challenging is shooting three episodes of a movie at a stretch to make economies of scale. Then the producer can sell each episode with the idea that the movie does not end with the credit titles, but more will come soon, not in DVD format but as a sequel. Harry Potter and Spiderman were shot with room left for sequels. Matrix 2 and 3 were shot at a stretch with a second episode ending as an opening for the third one.

Given that box-office earnings are mostly realized during the first week of opening, revenues coming from derived sales and the second life of the movie are determinant. DVD, soundtrack, royalties, TV rights are more than marginal profits and are already taken into account when calculating movies' budget.

But this business model is threatened by what is commonly called piracy : P2P networks and some websites make it possible for web surfers to download for free movies "ripped" or digital music in MP3 format. Therefore earnings from the second life of entertainment products are reduced. And with the development of broadband internet connections, more and more movies will be exchanged on P2P networks. This is a serious threat to current business models. It can be overcome by considering Intellectual Property differently as developed later on.

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[35] Source : Michael J. Wolf, *The entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999

1.2. Current business models are impacted by higher investment

1.2.1. The entertainment industry is adopting a multiplatform strategy

The time-to-market of entertainment products is long : Video games are increasingly complex and development expenses often reach 5 to 8 million dollars[36]; Special effects in movies are determinant and more and more numerous. For instance in the movie *Lord of The Ring-The two towers,* special effects totalized 72 minutes of a 180-minute long movie. By themselves special effects could have been a movie. Money at stake is increasing from one blockbuster to the other. But then the first week of exploitation is enough to determine the success or the failure of a movie. For video games or new consoles, the success is assessable even before the release date thanks to pre-orders.

On some P2P networks, some movies are available even before their releasing in movie theater. *Finding Nemo* from Pixar was available for instance at least 3 months before the release date in France. Entertainment companies have to adapt to the fact that information and content is circulating faster on the net : they are faced with the alternative of preventing content from spreading on the net by law ; Or adjusting their strategy, and in a way their functioning and their distribution method, to the pace of the internet.

In order to avoid to lose money in the case of people having watched a movie on a computer before the release date, Movie Majors are investing a lot of money to synchronize worldwide launch. The movie *Matrix 3* for instance was released on the same day, at the same time in the entire world. In this case, the marketing strategy is seriously altered by the fact that the movie-crew cannot travel around the world to promote the movie.

In addition, not only entertainment products tend to be released in several countries at the time, but there is a new trend toward the launch of entertainment products on several platforms at the same time. *Matrix2* (the movie), *Enter the Matrix* (the video game), the *Animatrix* (the cartoon) have benefited from marketing synergies. These sectors represented for Warner Bros a whole environment that could be used to capitalize on the release of the episode 2.

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[36] Source : Max Verbatim, http://www.Silicon.fr, December 15, 2003

With the digital revolution, movies, songs, books, or newspapers can all be expressed in the same binary code. Content is becoming a very liquid asset. The message is now independent from the medium. Whether we experience *Spiderman 2* in Theater, on HDTV, on a computer, on a portable media center, or streamed on the internet, the digital content remains the same. Digital technology is thus uncoupling entertainment products from any specific medium and making them portable across multiple platforms. In a world where most content moves at the speed of light, there is an even greater need to be available in every medium and every platform in order for any new product to have a chance against the competitor's blockbuster multi-platform effort[37]. The risk for entertainment companies is increasing since a multi-platform strategy implies multiple investment for a unique product.

1.2.2. The competitive landscape evolves and forces to adjust strategy

The internet has removed boundaries between countries ; Digital entertainment products travel from one region of the world to the other. Access to content from remote regions of the world is easier. Music Majors will face more and more competition from local or foreign artists whose sales were too marginal to be handled by one of the big five. On the other side, some artists will have a chance to travel without borders. The internet may open new markets and serves as a Trojan Horse in East Asia for instance for entertainment products coming from Hollywood.

The internet is merely the latest vehicle by which the icons of entertainment have become the closest thing we have to globally shared cultural icons : more Hindus are probably more familiar with Madonna than they are with Abraham Lincoln. Through the spread of entertainment thanks to new technologies we are creating a worldwide consumer culture. While Hollywood's dominance over the movie industry may be hard to displace fully, impresarios in other countries are building strong businesses in every other form of entertainment. India's "Bollywood", Hong-Kong, and newer entrants such as Syria are more and more important in regional and local entertainment businesses.

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[37] Source : Michael J. Wolf, *The entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999

The internet is opening consumers to entertainment products from all over the world because it is the most convenient way to reach them. New players are emerging, modifying the competitive landscape : India's Bollywood for instance, the first producer of movies in the world with 1,000 movies produced per year, has understood that it may reach a broader public by making the most of P2P networks. *IndianFM.com* is an organization regrouping 35 Indian movie producers. It has decided to enter into partnership with *Altnet*, the paying platform from *Kazaa*, to distribute some movies in the future. The movie *Supari* is the first title and is proposed at 2.99 dollars. Is India a big threat for Hollywood with 10 millions web surfers ? Well, not directly but this distribution method will enable Bollywood to reach the community of 20 millions Hindus leaving outside India.

Monetary issues for fans have vanished into thin air when considering discovering a whole new type of music : free advertising songs, samples, online radio from all over the world have eased access to global culture. Let's assume a consumer wants to discover typical Indian music, because he had heard for the first time Indian music while watching an Indian movie for instance. Will the consumer go directly to a store and buy a CD without knowing anything about Indian music, or will one preferably download randomly music on P2P networks to "try" and get to know Indian artists before spending money on CDs ? This second act reduces the risk of buying something that one may not enjoy. It is especially true for products from other culture or countries. In this case, help is necessary for differentiating between good and bad products : such support may be found online. Trying before buying is easier on the net. And the choice is greater.

If major entertainment companies are barely profitable, one reason is competition : there is too much choice in entertainment. Just to get noticed by consumers, every producer of entertainment products has to increase advertising, marketing, and promotion expenditures. In some case, advertising, promotion and marketing outweigh pure production costs by 100 percent. In France, marketing expenses for music promotion have increased by 7 % between 2002 and 2003[38]. The Co-Creation of value through controlled word of mouth would be the perfect answer to decrease marketing expenses. Successful examples will be studied in the last part.

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[38] Source : La Tribune, *Le marche Francais en chute libre*, January 26, 2004

Higher costs have played a role in the accelerated trend toward media consolidation. To spread their risks and to enhance their distribution, entertainment companies are typically forced to own a combination of assets that might include a motion picture studio, a TV network, cable networks, a book-publishing company, a magazine division, TV stations, retail stores, theme parks, and merchandise. As will be analyzed later in this chapter, the merger between *AOL* and *Time Warner* was a form of answer to an increased competition : marketing expenses are exploding to get noticed by final consumers, and it exists marketing synergies between *AOL* and *Time Warner* : 43 % of adds diffused on *AOL* websites during December 2001 were related to entities owned by the group[39].

Entertainment companies are aware that their competitive landscape is evolving. This evolution may be a threat for companies who are not ready to adapt to the internet generation and may spend money pointlessly, or huge opportunities for those of which business model takes into account digital competitive landscape as a whole. The concept of "synergies of experience" will cast a new light on this evolving competitive landscape.

1.2.3. Do new technologies mean new investment for new revenues ?

Every time a new format has been widely adopted by the public, it has meant renewed revenues for entertainment companies. In the gaming industry for instance, new consoles are driving demand for new versions of old games. Between the early eighties and 2004, The game from Nintendo *Zelda* has kept the same principle of quest with the same main character, and the franchise has recurring high sales.

DVD format has generated new sales of older movies given that bonus and enhanced quality are attracting fans. Why MP3 could not be the future technological revolution that drives revenues for the music industry for instance ? Digital formats for movies have paved the way for more consumption of movies : portable device needs to be filled up with content. A great potential of development has appeared with digital formats, but investment are needed to make the most of it. And some legal issues are blocking the positions of stakeholders.

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[39] Source : Jon Fine, *AOL Time Warner does great selling job – to itself*, Advertising Age, March 18, 2002

The reluctance of movie and music Majors to rush into the digital market may be driven by investment. Today entertainment companies are not sure to derive as much money as before from migrating to the digital era. It would means a complete reshaping of distribution channels and partnerships, a modified value chain and huge technological investment. The risk is high to forecast revenues from a value chain wholly based on the internet, since it is a user-driven tool difficult to control. But it seems that these companies are currently losing even more money by promoting CDs and entertainment products not adapted to their experience environment.

"Younger consumers have made music downloading part of their lifestyle" noted the research firm *Forrester* : according to the survey, 49 percent of 12- to 22-year-olds have downloaded music in the month of December 2003. the proliferation of legal download services is adding momentum to the subsitution of CDs by MP3 according to *Forrester Research*. A long list of large corporations, from *Coca Cola* to *Apple*, are now purveyors of music downloads for a fee. The CD is not dead yet, "but the more energy a company puts into trying to preserve the CD business, the worse off they're going to be," Forrester stated, "and the more energy they put into trying to get the download business right, the better off they're going to be." [40]

1.3. The internet culture of "free stuff" poses a threat to financial revenues

1.3.1. Free entertainment online is consistent with the logic of the internet

A lot of users browse the web for leisure and entertaining purpose. Even when looking for serious information, most people open simultaneously an entertaining web page. The internet has become the fastest access to fun and leisure. The rapidity of the diffusion of data online is well suited for digital entertaining content. Entertainment is all the more determinant online that it makes the difference between two websites : the web presents everyone's site equally. It is a world where everything takes as much "virtual real estate". To attract users, websites need to propose the most entertaining or most informative content. The website that offers expensive entertainment for free will have more success than a website that proposes not that much high quality content, or charge for it. The competition for attracting "eye-

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[40] Source : www.Zeropaid.com, *P2P and Legal Downloads will kill CDs*, January 28, 2004

balls" has moved toward higher and higher quality content for cheaper and cheaper or even for free.

The most telling example may be *Napster* : it was appealing to a wide range of websurfers thanks to 3 magic words : "Join the largest, most diverse online community of music lovers in history by downloading and installing *Napster*. It's fun, simple and free": *Napster* claimed 63 million registered users by the end of its life (15 % of all the internet users)[41]: which company has not dreamt of such connectivity and brand awareness with little marketing efforts ? Entertaining content of high quality for free was the key to *Napster* success.

In a way, the internet obeys the same rules as TV : With TV the qualities of design, sound, graphics must be arresting in order to keep the viewer's thumb off the remote control. With the internet, a mouse click is just as fast as the TV remote. Viewers expect not less from internet content than they have become accustomed to on their other small screen : so when a company decides to stake out a position on the web, it must also decide to become an entertainment company : when visiting the *Gap* site, for example, one sees ads for and information about *Gap* clothes, but one can also download music by performers as diverse as rapper Missy "misdemeanor" Elliot and Herb Alpert. One can also consult entertainment and travel guides for Stockholm, Boston and other cities with a *Gap* attitude. Is this advertising or entertainment ?

Pepsi has even more entertainment options on its site, which is organized as a virtual theme park called *Pepsi* world. You can download music and a movie clip, you can play a demo of interactive video games, and you can watch a concert by the group of rock *Kiss*. There are contests and prizes. All is designed to keep audiences on their site and not click away. "On TV, you tune in a show and see messages about a product. On the net, you look up a product and get a show", said Michael J. Wolf. The internet is consumer-centric and companies are competing with entertaining tools.

One direct consequence of this trend may be the necessity for any company on the web to propose high quality content to net surfers (news, music or movies for instance) to stand out from the rest of the pack. And the chea-

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[41] Source : Edward Burman, *Shift ! The unfolding the internet Hype, hope and history*, Wiley edition, 2003

cheapest they offer it, the more effective it will be. Therefore companies are willing to pay for adding content to their websites, and on the other side web surfers may be not ready to pay for having fun. It means that a repositioning of "pure" entertainment companies and content providers may be needed to do business on the internet efficiently. More and more entertainment products may be sold to non entertainment companies, looking for content to offer for free to attract customers online.

1.3.2. Legal issues are blocking entertainment companies from benefiting from the internet

Music and movie Majors, video games companies, books' editors, have all realized that their products are traded online, mainly through P2P networks. And that they do not earn any royalties related to these transactions. Some of these programs have turned to be illegal, some of them are legal. In any case, they have modified the value chain of entertainment companies by altering the extraction of value between companies and consumers.

The music industry is reluctant to recognize this evolution in consumption because they sue P2P users. Only recently a legal and cheap platform was proposed by *Apple* to download digital music legally. But it seems that there will always be people reluctant to pay on the internet and who would find a way to avoid being charged for downloading software, music or movies. In fact, some solutions have been found to limit the spreading of copyrighted content on the internet : MP3 downloaded on *iTunes* are protected and cannot be copied on more than 3 different computers (so it cannot be uploaded on P2P networks more than three times). *Apple*'s Digital Rights Management (DRM) scheme is supposed to be the solution for Music Majors to sell fairly their content online. But even this scheme has been hacked : according to the Norwegian website *ITavisen.no,* the program called "So Sue Me" and available online on the site *http://nanocrew.net/blog* by the end of November 2003 allowed users to share MP3 downloaded legally on *iTunes :* The DRM was bypassed.

The protection of Intellectual Properties and creative assets is the heart of entertainment. Software, books, music, movies are increasingly the currency in which the world trade. Perhaps the greatest problem of all today for the entertainment industry is intellectual property rights online, as explained by John Perry Barlow : "If our property can be infinitely reproduced and instantaneously distributed all over the planet without cost, without our

knowledge, without even leaving our possession, how can we protect it ? How are we going to get paid for the work we do with our minds ? And, if we can't get paid, what will assure the continued creation and distribution of such work ?[42]"

If Intellectual Property cannot decently be managed on the internet, entertainment companies will try to block this distribution channel. But is suing a 12 year-old-girl consistent with the image of fun of the entertainment industry ? And do 60 million users of P2P networks can be sued ? If the current evolution is not acceptable, but cannot be stop, then perhaps an adapted business model will help to create new value : Recognizing the role of consumers in the value creation process opens the doors for a new business model explained in Chapter Three.

1.3.3. Movie piracy is "three years behind music", if no reliable solution is provided

Current business models are highly impacted by online trades of entertainment products. The popularity of P2P services, such as *Kazaa*, have cost the music industry $700 million in sales since 1999, according to a survey made by Forrester research. Online file swapping is also affecting the Movie industry. One in five young file-sharers have downloaded a movie, according to Forrester, which reported that movie piracy is "three years behind music."[43] According to Eric Garland, CEO of *BigChampagne*, which tracks the most popular downloads on P2P networks, 10,000 copies of the *LOTR-The Return of the King*, have been bouncing around the internet one week after the official release date in theater.[44]

The number of U.S. households downloading music from P2P networks rose by 6 percent in October and 7 percent in November after a six-month decline, according to a study of computer use in 10,000 U.S. households conducted by The *NPD Group*. In a separate, bimonthly survey, 12 million individuals reported getting music on the free networks in November, up from 11 million in September, *NPD* said. Copyright infringement lawsuits against individuals have not stopped the trend.

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[42] John Perry Barlow, 1994
[43] Source : www.Zeropaid.com, *P2P and Legal Downloads will kill CDs*, January 28, 2004
[44] Source : Katie Dean, *Film Piracy still the show,* wired magazine online, http://www.wired.com/news/digiwood/0,1412,61673,00.html, December 22, 2003

Worldwide sales of music in value have decreased from a high in 1999 at $39bn to $32bn in 2002. On the other side, sales online through legal downloading platforms are forecasted to increase from $92M in 2003 to $190M in 2004. Perhaps making money thanks to the net is the future of the industry. At least it deserves to be considered with attention. And it may means a reshaping of current value chains and business models.

2. Today the entertainment environment is more complex than before

2.1. Consumption habits are constantly moving and evolving

2.1.1. The Corporate strategy needs to consider the entertainment environment as a whole

When considering the entertainment industry, companies can no longer be exclusively focused on their "traditional" competitive landscape. To what extent are laptop manufacturers in competition with MP3 player- and digital jukebox manufacturers for instance ? Are home theater devices in competition with PCs ? Are digital mobile devices part of the experience of listening to Compact Discs ? Below is one possible diagram to represent the entertainment environment. It is inspired by the classes from professors C.K Prahalad and Venkat Ramaswany from the University of Michigan Business School. They explain that it would be a misinterpretation to consider this galaxy of products as fixed in time and space. As it would be a mistake to only focus on a particular competitive environment : consumers are not concerned by the split between sectors, and use products across categories.

One possible diagram of the Entertainment Environment :

Digital TV set	Cable TV	scanners	Fax		PC
	WEB TV				
Interactive TV		Printers	Laptop	Tablet PC	
HDTV	Satellite TV				
		Graphic cards			
Reality TV	Pay per view		Hard drive	Memory card	
	Home networking				
	Video rental	CD Rom			
Flat display	Digital camera		PDA		
	Movie theater	USB Key			
DVD		Digital jukebox	Smartphone	Handheld	
	Home Theater				
Digital camcorder	MP3 player	Multimedia edition software		Mobile operator	
	Internet provider			Online games	
CD player	CD	E-mail	Cell phone		
Stereo system	Wifi device	P2P software			
		Electronic toys		Game console	
	Voice through IP	Specialized press magazine			

We can take the use of Compact Discs and related consumption habits to illustrate the reasoning : Until recently, when a consumer liked a music band, he would go to the nearest store and buy the CD of the music group. Then he would listen to the CD on his HiFi device in the leaving room. That's the way imagined by the music industry to consume musical products until very recently at least. Let's imagine now the same consumer wants to listen to his favorite band in his car or on the go : he will buy an MP3 player. Let's imagine also that he has bought a Wifi device that enables him to broadcast music from his computer to every Wifi speakers in his house. To respond to this two different needs, the next step for the consumer is to encode the WMA files on the CD into MP3 formats to get music in digital format to be played on the PC or stored on his MP3 player. But then he realized that the CD he has just bought is protected and cannot be read on his computer.

The experience of this consumer will be very frustrating. The environment in which people listen to music has evolved and include new digital utilizations. By restricting the use of its products to Hifi devices in the leaving room, the music industry may not have taken into account the whole environment of musical products. By protecting their products against pi-

racy, music majors deliver products that do not comply to the evolving use of music. It is counterproductive. Then consumers may be tempted to turn to other distribution channels such as P2P, or more recently *Apple itunes*, that fully meet their expectations in terms of experience environment.

One possible experience environment around the Compact Disc
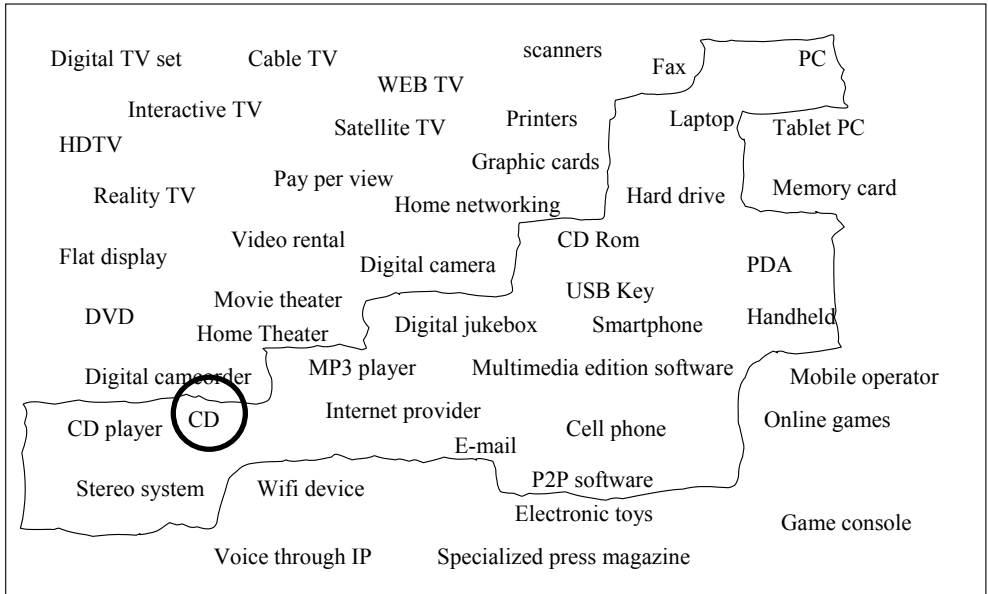
Hollywood will face the same issue in the coming years, if they do not take into account new consumption habits. With the advent of multimedia jukebox such as the *Archos AV320* or the *RCA Lyra*, people more and more want to watch movies on their portable device. It is a natural consequence of the development of portability. But the DVD format is not adapted to these devices : most DVD are 9 Gigabits large, when most portable device are limited to a 40 Gigabits hard drive. In addition, the DVD format is not compatible with multimedia jukebox. And ripping DVD on a personal computer takes a lot of time and resources. How can a consumer easily get movies that suit his specific needs except by downloading them illegally ? By proposing a platform to download movies of adequate format, Hollywood would avoid being marginalized from the distribution environment in the

future and make the most of the development of broadband access to the internet[45].

2.1.2. Companies that do not want to be marginalized have to accept consumers' standards

The evolution of the consumption habits are partly driven by the development of portable devices : sooner or later our mobile phone will have the same features as a PC or a TV set. For example the English mobile phone operator *3* (subsidiary of *Hutchinson Whampoa*) has signed an agreement with *MTV Europe* to broadcast exclusive video clips from *Dido*, *Bjork* or *Radiohead* on Third Generation (3G) mobile phones. Long extracts from the programs *Jackass* and *Dirty Sanchez* will also be available for streaming[46]. The transfer of content from one place or one device to another is gaining momentum, driven by consumers' needs. They are reshaping the industry by claiming access to content when they want and where they want.

Companies from the Hi-tech sector are mutating to better serve the disparate needs of their consumer. For instance Takeshi Natsuno, one of the inventor of the I-mode in Japan, explains that "In the internet age, service providers and their customers are engaged in a cooperative effort and, in doing so, form a harmonious whole. Or perhaps we could describe it as the age of complex systems. In short, the day when one company, one technology, one industry provides all platforms is over[47]". These "complex systems" correspond to our complex "experience environment" with new links and partnerships between various actors and sectors. This trend is reinforced by the convergence of technologies and formats we observe today. For instance the company called *Mustek* has just invented a device called *DV4000* that combines six functions : camera, camcorder, MP3 player, USB key, Webcam and voice recorder.

For Takeshi Natsuno, this convergence is an answer to consumers' needs : "Thanks to the IT revolution, it is technically easy to organize cooperative efforts involving a number of companies (…) the basic rule is to use the de facto standard technology (…) Today using the de facto standard is

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[45] The share of broadband connections is forecasted to raise from 50 % today to 60 % in 2007 and the number of web surfers in general will raise from 572millions to 870 millions. Source Gartner Group, December 2003.
[46] Source : http://neteconomie.com, October 10, 2003
[47] Source : Takeshi Natsuno, *I-mode Strategy*, Wiley edition, page 36

the name of the game : there is no way a unique, proprietary technology is going to be accepted by potential customers (…) A technology that no one else supports is not going to win acceptance."[48]

Every manufacturer is adding a hard drive to entertainment products. For instance 70 percent of the toys presented at the 101st annual American International Toy fair in New York include at least one microchip.[49] Digital formats have been widely accepted by the entertainment industry. This convergence responds partly to the one-stop-shop logic, but also because manufacturers are afraid of being marginalized, excluded from the entertainment environment, because they are not a "natural extension" of the latter. The act of buying music on CD forces consumers to make efforts to enjoy songs on portable devices or PC. Therefore this format tends to be marginalized, especially when other formats more convenient are spreading on the net. Music Majors become marginalized for refusing to adapt to consumers' extended entertainment environment.

2.1.3. The experience environment has new extensions, especially at work

Entertainment is gaining everywhere : most airlines companies now have a video screen for every seat (previously a luxury reserved for the expensive seats up front). For leisure-starved big spenders, *Virgin airlines* also offers pleasurable gimmicks such as acupressure massages. Other companies offer in-flight gambling : passengers can use their Mastercard or Visa to play video slot machines, video poker, and keno : this is not just another way to kill some time. The U.S Department of Transportation concluded that foreign airlines can generate nearly $500 Million per year from in-flight gambling. Is a ride to London on *Virgin Atlantic Airways* a party in the air or just a way to get from point A to point B ? The separation with entertainment and non entertainment is not clear.

This trend is reinforced by the fact that "traditional" entertainment companies have had to develop markets outside their core industry. While there may be a difference to the consumer if Elton John is performing on *VH1* video or in a *Citibank* commercial, to the composer, performer, musicians,

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[48] Source : Takeshi Natsuno, *I-mode Strategy*, Wiley edition, page 36
[49] Source : Michelle Delio, *Toymakers bet big on Microships,* Wired magazine online, February 20, 2004

soundmen, lighting technicians, and makeup artists, it is all paying work : new venue, same skills.

We become multitasking in our business and professional life, so we can look for products and services that include entertainment content as an additional part of their offering. According to the *New York Times*, in more and more offices, 5 to 10 hours of the workweek are spent on recreational use of the internet. Instead of taking a cigarette break, many people are doing a little surf on the Net.

With the expansion of TV through phone lines[50] or cable connections, it is possible to watch TV during working hours. In the trading room of major banks, sales and traders have access to *CNBC* 24 hours and other TV channels are available on their five-screen computer. More and more graphic cards such as the *Nvidia Geforce 6* allow the user to plug several screens to the computer. Then it becomes easier to work on a spreadsheet while browsing the web for instance. The workspace has been identified today as a potential experience environment of entertainment products.

Some media companies have built their success on the fact that they can reach an audience at work : for instance the *Wall Street Journal* is read by most bankers because it is a financial newspaper, but also because it offers an increasing section related to fashion, sports, cinema and shopping in addition to business matters. The online issue is also one of the happy few to be profitable[51], with entertaining content available at the same time as financial content.

In addition, people less and less accept to be disconnected from their environment during the day at work, especially when they work longer hours. The use of mobile phone is not viewed as disruptive in many companies. Instant messenger services are gaining momentum at work. Electronic mailboxes are used to send personal e-mails. The workplace becomes a place where people take entertaining breaks. Listening to music while working is tolerated in some professions or after certain hours at work. Some consult-

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[50] For instance in France, it is possible to receive a range of TV channels on the TV set or on the computer through a broadband connection called "ADSL". This is different from WebTV such as CanalWeb that uses the the internet to broadcast their channels and that are not available on a regular TV set.
[51] Source : The association of French schools of telecom, under the direction of Danielle Bahu-Leyser and Pascal Faure, *La documentation Française*, *Media et e-media*, 2001

ing companies propose laptops with DVD player to their employees who travel a lot.

The major trend to keep in mind is that even during working hours, consumers are willing to take a break and being entertained ; or they can also work and be entertained at the same time, just as teens are doing their homework while watching *MTV*. The entertaining environment is not simply limited to home, but is gaining momentum at work.

As far as cars are concerned, while the viewing screens in headrests are not new, *Audiovox Electronics* takes it one step further with built-in DVD players and the ability to plug in other media. For David Shalam, *Audiovox's* vice president for mobile video technology, "the race is on in the mobile-technology industry to provide as many fun-filled applications as possible in one or two devices." There's a reason why *Delphi's* slogan for this line of equipment is "Entertainment : The best seat isn't even in the house." And that's just the start. *Visteon* is showing off its plans to bring to market in the coming months the *Dockable Family Entertainment System*, a 10-inch DVD and MP3 player mounted to the car's ceiling that can be removed and used elsewhere.

Yet *Visteon* sales representative Mel Sarnowsky said that the precursor to what are essentially internet-capable laptops docked to the back of headrests is due out in a couple of years. That system, demonstrated at the 2004 International Consumer Electronics Show at Las Vegas but not yet perfected, would come with wireless keyboards that can be hidden inside the back-seat armrest. Web access would be provided through cellular communications, or through a high-speed link if the vehicle is in a Wi-Fi hotspot, Sarnowsky said. "This takes the whole thing to a new level, People like flying *JetBlue Airlines* because it has gate-to-gate TV".[52] Entertainment is becoming crucial for these new sectors. They become part of consumers new expectations. The experience environment of entertainment products has larger extensions.

And the consumption of entertainment products is forecasted to increase even more in the next decades. By 2025, spending on magazines and news-

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[52]Source : Steve Friess, http://www.wired.com/news/autotech/0,2554,61859,00.html, Wired magazine online, January 10, 2004

paper in the US are to reach round \$40Bn ; Spendings on cable TV will be up to \$55bn, and spendings on video games and Virtual Reality \$35bn.[53]

2.2. Mergers seems to be a potential, but limited answer to the extended entertainment environment

2.2.1. The expected "Convergence" helps defining overall profitable strategies

Entertainment is invading new sectors. Consumers are modifying their habits of consumption. Determinant technical evolutions have occurred. Therefore the entertainment environment is constantly on the move. The consequence of this evolution is a greater need for flexibility : the experience environment has to be constantly reshaped. Entertainment companies needs to mobilize new types of expertise, knowledge and resources to meet the requirements imposed by consumers. Partnerships and acquisitions are the easiest way to overcome this challenge.

Hewlett Packard for instance has understood that sooner or later consumers who store MP3s on their desktop computer will want to listen to them somewhere else : therefore they have decided to manufacture *iPods,* that benefit from higher margin compared to the PC industry. *HP* has no experience in manufacturing MP3 players : instead of entering this highly competitive market with no consumer's awareness on this segment, they have partnered with *Apple*. Even if the two companies are competitors, an alliance is a punctual answer to a forced move. "Forced move" because it is an answer to the recent use of PC as digital jukebox. So if *HP* do not want to be marginalized, it has to propose a solution that transforms PCs into platforms for digital music.

Some entertainment companies have understood that their growth would come from better serving all the various needs of consumers. The various developments of the entertainment industry are intended to better mobilize and adapt resources to the complex and evolving needs of consumers. By manufacturing *Mac* computers, *Ipod* MP3 players and designing *iTunes* software, *Apple* is in a position to be highly reactive to consumption evolution : *Apple* can fulfill the needs of consumers to buy cheap music online by

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[53] Source : Joseph F. Coates, John B. Mahaffie and Andy Hines, *2025 : Scenarios of US and Global Society Reshaped by Science and Techno*logy, Published by Oakhill Press, 1997

discounting *iTunes* songs (*Apple* earns no more than 10 cents on each song[54]) and overcharging the *iPods* (30 % margins). This strategy could not have been possible without a deep understanding of the music industry as whole. And the positioning on several part of the musical environment has enabled Apple to make a lot of profit when all segments are put together and profits added. The link between MP3 songs and MP3 players is so close in the experience environment of music that profitable sales strategy can be built upon these two products at the same time.

The media landscape is very unstable according to Larry Collette, who explains in the book *The motion picture mega industry,* that "the transformation of the media landscape, due to rapid advances in technology and changes in government regulation, herald an unsettling period of disequilibria within the entertainment marketplace. Perhaps the most convulsive of these transformations is the expected convergence of information and entertainment services onto switched, broadband networks, which will eventually reshape the relationship between consumers, distributors, and producers[55]". Vertical integration is an answer to synergies between cable channels and the content broadcasted on these channels. By broadcasting one's own programs on one's own channels, what *Disney* is doing for instance, one spares money. But this integration offers less flexibility, and may not be adapted to a constantly evolving entertainment environment. *Time Warner* and *Vivendi Universal* are offering two interesting cases of study.

2.2.2. Time Warner's strategy is bearing fruit this year

Time Warner (formerly *AOL-Time Warner*) has understood that profits would derive from a strategy that takes into account the experience environment as a whole : by merging Internet Services Providers and entertainment content producers, *Time Warner* expects to use its content to fill its networks. And maybe earning money from where consumers are willing to pay (for access to the internet for instance), with content as appealing products.

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[54] Source : Fred Anderson, CFO and executive VP of Apple Corp, during a lecture at the University of Michigan Business School, November 13, 2003
[55] Source : Larry Collette, *The motion picture mega industry*, chapter 8 : *the wages of Synergy,* p123

This strategy is going to be more and more profitable as broadband access to the internet will flourish, and as content will be of better quality on the net. Legal streaming and downloading platforms must also be ready to derive value from this future evolution. This mega-structure guarantees that money will be extracted from consumers sooner or later : for instance the money that *Warner Music* is losing due to P2P networks, is partly gained by *America Online* through broadband subscription. Or when *Sony Music* is going through financial difficulties, CD-burning devices manufactured by *Sony* are thriving. This vertical integration is only a partial answer to an evolving consumption environment since it generates structural rigidities. Acquisitions and ownerships are limiting the flexibility of the group. The value chain has been reinforced by including new distribution channels to derive values from where the contact with consumers occur. But we have seen that the entertainment environment is flexible and complex, less and less linear or foreseeable. Massive corporate structures are rigid.

There are definitely complementarities between the internet and entertainment products. At least since they are both part of the entertainment environment. Maybe this complementary nature should not be measured in term of industrial synergies as financial analysts are tempted to do : the value of stocks of *Time Warner* has decreased from $50 in January 2000 to $8.7 during summer 2002. The business model that has driven the merger in 2000 was not ready to be applied instantly since broadband access to the internet was limited and was not a major broadcasting channel. Therefore 2002 financial results were disappointing. But in the coming years, the whole portfolio of *Time Warner* will be suited for a diffusion on the net. The net profit of *Time Warner* combined is equal to $2.64bn for 2003 after net losses of 98.7bn in 2002[56]. The merger is bearing fruits at the same time that high-speed internet connection enable content to be broadcasted online.

2.2.3. With additional time, Vivendi Universal could have done better than DoCoMo

The strategy of *Vivendi Universal* was in a way similar to *Time Warner*, except that the emphasis was not so much on the internet, but rather on mobile phone as access to "eyeballs". With the advent of 3rd generation mobile phone in 2005, mobile operators will be able to propose high quality music, games and video. The strategy that has driven the merger between *Vivendi*

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[56] Source : http://www.Boursorama.com

and *Seagram*'s entertainment assets was not ready to be fully applied before 2005. Therefore financial results were disappointing. But similarly to *Time Warner* situation, faster access to data would have supported this strategy. As long as the library of *Universal* is not accessible on mobile phones, synergies are reduced to nothing. Consumers will prefer other types of access.

Similar structures have proved to be highly profitable : *NTT Docomo* in Japan has based its success on offering high quality entertainment on mobile phone. Since 1999, 3Rd generation mobile phone are available. Takeshi Natsuno explained that the take-off of the *I-mode* could not be possible without the increasing participation of content provider that would fill the *I-mode* portal with entertaining products[57]. *DoCoMo* jointly developed entertainment services ranging from 67 in February 1999 to 665 in October 2000. And the increase in subscription followed a parallel trend : as the portal became richer, the number of subscribers increased. *Vivendi* could have followed the same path with the mobile operator *SFR* and fully-owned content from *Universal* by proposing its own entertainment products on its own mobile phone network, a strategy similar to fully-owned TV programs on fully-owned TV channels. This strategy would have been even more profitable than the solution proposed by *DoCoMo* since they do not own any of the entertaining content they propose on I-mode. But *Vivendi Universal* was not in a position to wait until 2005 and the advent of the UMTS and sold part of its entertainment assets to *General Electric* in September 2003. Not surprisingly in fact *GE* won the bid for *Vivendi*'s entertainment assets : their strategy was consistent with the complex experience environment of entertainment products : *GE* has a strong media activity, and coupled with entertainment, the company is equipped to construct an evolving network of competences.

There is no obvious industrial synergy between mobile phone operator and entertainment content producer. But there are complementarities between this two activities. They enable companies to provide consumers with global solutions, that can be more easily adapted to meet their needs than if they were operated separately. These complementarities are at the root of what can be called "Experience Synergies" to be explained in chapter 3.

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[57] For information, the I-mode is a kind of simplified the internet for Japanese mobile phones.

3. A nodal company can create a unique experience environment

3.1. Networking people and companies creates a pool of various competencies

3.1.1. A structure in network will pave the way for personalized experience environments

The current revamping of the entertainment industry is led by disruptive technologies that have modified established relations between consumers, suppliers and distributors. Consumers for instance do not need Music Majors to access artists' works. Some filmmakers distribute their work directly on P2P networks. The value chain can no longer be represented as linear or sequential according to Professors C.K Prahalad and V. Ramaswamy from the University of Michigan[58]. The actors and stakeholders may be as numerous as needed to create an individual experience. If entertainment companies want to create an experience for consumers, they will have to adapt to their particular needs. This goal means changeable configurations. Entertainment companies can play the role of nodal companies that drive a network of partners to deliver valuable experience to consumers.
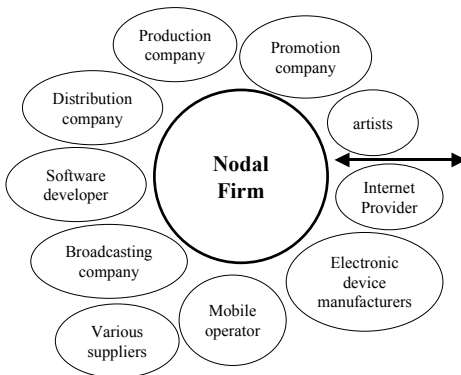
Adjustable Nodal network   Personalized Experience environment
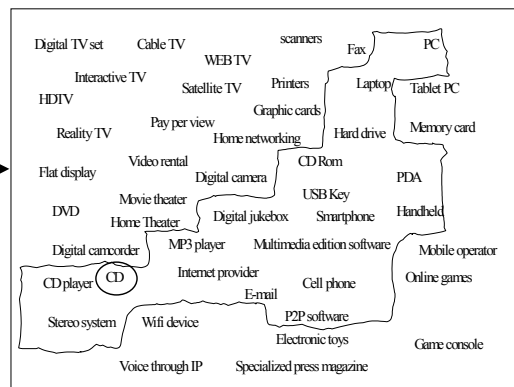
According to Prahalad and Ramaswamy, "An experience network is not simply about supplying components, products, or even information. It is not the same as a supply chain, although the traditional supply chain is part of it.

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[58] Source : C.K Prahalad and Venkatram Ramaswamy, *The future of Competition : Co-Creating Unique Value with Customers*, Harvard Business School Press, 2004

The Experience Network is about building communities, connecting suppliers, dealers, and support staff with customers, as well as customers with one another." One company must play the role of gathering data from every player and building on it to create an appropriate Experience Environment. For the two Professors, "It is about becoming a nodal company, providing intellectual leadership, building a coalition, and creating pathways for the flow of products, information, and expertise. Nodal companies are like traffic cops, making the rules and allowing for free flow with adequate constraints." For Prahalad and Ramaswany, creating an experience network entails the following :

- "To facilitate the construction of a different experience for each individual consumers"

- "To rapidly adapt and re-configure resources, accommodating wide swings in consumer demands in the experience space"

- "To selectively activate competencies associated with the co-construction of personalized experiences"

The co-construction of personalized experience is key since nobody better than consumers themselves can define their needs. Of course the issue of being able to address the very particular needs of millions of people will be addressed in the next chapter.

3.1.2. At stake is the capacity to leverage competencies when needed

Mergers and acquisitions have enabled "traditional" media companies such as *Time Warner* to learn from "new technology" companies such as *AOL*. The expertise brought by *AOL* was determinant to better serve a new generation of consumers. *Disney* bought *infoseek* and *Starwave* in 1999 to develop activities online. This strategy that consists in buying competences and expertise is a big issue in the Nodal Network configuration. In fact, the range of expertise needed to match consumers' needs and create a perfect experience environment would require nodal companies to own more or less the entire entertainment industry ! Partnerships and alliances, rather than mergers and acquisitions will be one key to the problem. Prahalad and Ramaswamy explains this issue when they state that "the nodal firm usually does not own most of the resources it deploys (…) People tend to equate access with ownership. We need to separate the two. Similarly, we tend to equate control with ownership. We have to separate the two as well. To-

day's challenge is to find new ways to achieve both access and control without ownership"[59].

A network structure, similar to the one we create when we meet people and keep their business card, is a reasonable comparison. Partnerships and common interests may serve as a base to build a network of competences identified as key. This is a win-win situation for all stakeholders, since "Nodal firms are increasingly creating new business opportunities by providing other firms with access to their competence base" according to the two Professors. Takeshi Natsuno has made the same observation, when explaining that "In the age of the internet, launching a new business requires engaging in a cooperative enterprise that builds win-win relationships for all participants. That is why, when I am speaking about I-mode and am asked for the secret of our success, I invariably talk about moving away from a telecom way of thinking to an internet way of thinking.[60]"

This "internet way of thinking" may be seen as a network organization that derives value from the various interactions with users. Companies may no longer be viewed as the sole source of expertise and competences : why should companies refrain from using the competences of their consumer base for instance : some consumers are highly knowledgeable and could bring their enthusiasm through feedbacks for instance. In fact on the internet, individual users or communities create as much value as companies when they create WebPages. Competences are shared and no distinction is made between personal Web pages or corporate Web Pages : they have more or less the same chance to be viewed. They are as valuable.

The Nodal Network configuration is all about resource leverage and reconfiguration. The cooperative environment is always moving thanks to mutual contributions. For instance Music Majors and *Apple* have cooperated to create a valuable Nodal Network. Various manufacturers of MP3 players have joined the network to provide MP3 players that accept *Apple's* MP3 format (called AAC). And Internet access providers such as *AOL* have agreed to offer a music storefront based on the *iTunes Music Store*. As far as marketing is concerned, *Pepsi* has decided to offer coupons on its bottles for free songs on *iTunes*. Apple may be seen as the nodal company in this configuration, capable of building a network of partners.

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[59] Source : C.K Prahalad and Venkatram Ramaswamy, *The future of Competition : Co-Creating Unique Value with Customers*, Harvard Business School Press, 2004
[60] Source : Takeshi Natsuno, *I-mode Strategy*, Wiley edition, page 36

3.1.3. The role of communities is at the heart of experience networks

We have seen in Chapter one that communities were of great help when deciding which product to buy. Their opinion counts when making one's mind, especially online. *Ebay* is a good illustration of it. The whole system lies on trust. Communities also enable individual consumers to share and deepen their experience. For instance consumers who have difficulties with an electronic device will turn to specialized forums for help. The gaming console from *Sega* called *Dreamcast* has a huge community of fans online that explains how to modify the console to create new games.

The *Dreamcast* has been kept alive by an active community of fans called the *Dreamcast homebrew Scene*. Since the beginning of 2002, the production of *Sega*'s gaming console has been stopped. But the creation of KalistiOS by hackers, a boot method that enables to access the framewarE of any *Dreamcast* connected to a PC, is sustaining the interest for the console. KalistiOS has been developed using an open-source method, since it is a totally legal boot system that do not use *Sega*'s library. A lot of fans are legally developing their "Homebrew" games. Some of them such as *Feet of Fury* are so advanced and successful that they are distributed in official re-tailed stores. *Feet of Fury* cost $19.90 and was in the top ten of *Dreamcast* highest sales for 6 months in a row.[61]

In addition, the active community of fans of the console have prolonged the commercial use of the *Dreamcast*. *Sega* thought that its profits would die at the same time as the production ended. But Max Scharl, a German student, founded *Dreamcast-petition.com* to protest against the announced stopping of the *Dreamcast* gaming server, the announced stopping of the sales of games, and to ask for the development of new games. Thousands of fans have signed the petition. The dialogue was established between *Sega* and the community of fans and hackers. Sega decided to officially encour-age professional gaming companies to develop new games. Successful games such as *Border Down* and K*ing of Fighters 2002* were released in 2003 following the active dialogues with fans. Sega extended its royalties earned on the edition of new games and on new licenses. And all this activ-ity also created the buzz around elder games : Last year *Sega* decided to re-publish at half price no more than 30 of its most successful games given the high demand. At least three new games are announced by official develop-

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[61] Source : http://www.jeuxvideo.com, http://homebrew.dcemulation.com/, http://www.dreamcast-scene.com

ing studios for the first semester 2004. A competition have been organized among the Homebrew scene called the Dream On Contest : the amateurs who develop the most innovative game on *Dreamcast's* KalistOS will be officially published. The website *jeuxvideo.com* analyzes this phenomenon in this terms : "By regrouping their efforts and by being highly organized, players from every part of the world have succeeded in convincing *Sega* to continue to exploit the *Dreamcast*. They have managed for the first time to successfully impose their view to the Gaming Industry [...] They have demonstrated to the gaming industry that publishing games for *Dreamcast* is not a donation but rather an additional source of profits." Since the 3rd of June 2003, the freeware PSO-Loader 1.0 has been released by hackers to access the frameware of the *Nintendo's Game Cube*. Is it the beginning of a similar beneficial cooperation leading to a co-created value ?[62]

Communities are at the heart of brand loyalties. The *.Mac* community is one of the most loyal group of consumers. Anybody who buys an *Apple* computer knows that he will join a large group of people "who think different". The difference is so obvious that it creates a strong feeling of solidarity and assimilation to the brand. Communities have special emotional relations with a brand, an artist, or an entertainment product such as a movie. The *iPod* for instance has created a whole new phenomena : the image of the MP3 player is so cool that some bars in NYC have created special "iPod party". It consists in special nights during which clients can plug in their *iPod* on to the sound system and share their interest for a special type of music. *Ipods* are also used in some clubs in New York such as the *APT Club* to mix music by plugging two ipods at the same time.[63] More than a simple device, the iPod is a "cool attitude".

Therefore the previous diagram would not have been comprehensive without adding communities. One role of the nodal network is to enable consumers to interact which each other to build communities. Companies benefit also a lot from communities because they represent a pool of knowledge that can be rapidly mobilized and highly flexible compared to expertise deriving from partnerships with other companies. Communities are monetary value in our current business world.

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[62] Source : http://www.jeuxvideo.com
[63] Source : Eric Campbell, journalist in NYC for the Japanese TV channel TV Asahi, in an interview for the website http://neteconomies.com, December 11, 2003

Adjustable Nodal network   Personalized Experience environment

Communities of consumers
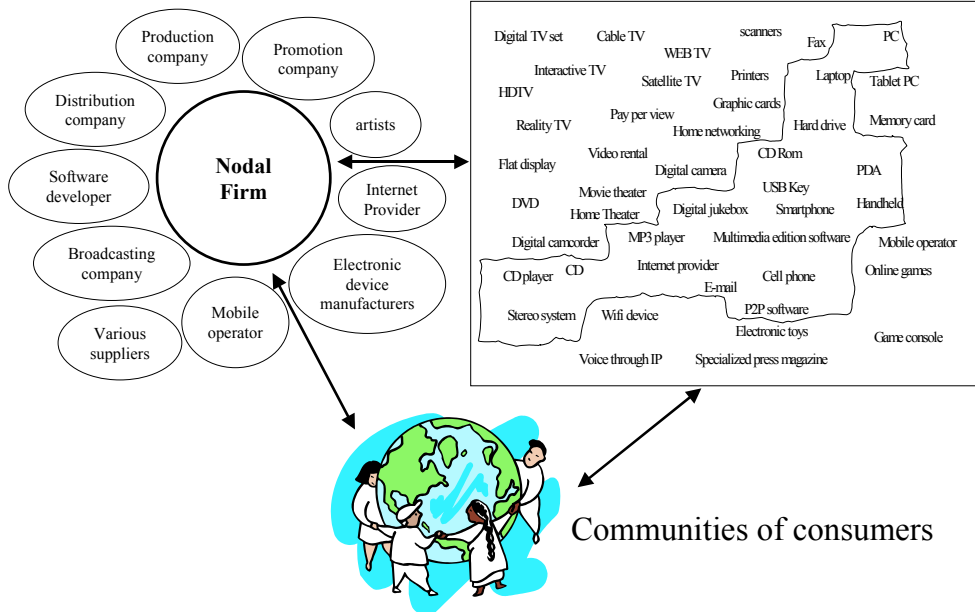
3.2. New forms of cooperation into the nodal network environment are creating value

3.2.1. Two nodal networks can work together : the Xbox example

Several nodal companies may exist in a Nodal Network. Prahalad and Ramaswamy have developed the example of *Microsoft* inventing the *Xbox* : "How does a software company get into manufacturing the videogame console *Xbox* ? It doesn't. Instead *Microsoft* collaborates with *Flextronics*".

Flextronics is a $15 billion firm operating in 25 countries with 75 factories, specializes in high-volume electronic devices. *Flextronics*, by working with a large number of firms such as *Palm* (PDAs), *HP* (printers), and *Cisco* (routers), develops unique competences that are difficult for any one of them to develop. With its access to a global supply base of component-makers and its significant design and development expertise, Prahalad and Ramaswamy explain that *Flextronics* provides the competence required to effectively participate in the video console business, working along with such secondary suppliers as *Intel* for microprocessor, *nVidia* for graphic card, *Micron* for the memory, and *Western Digital* for hard drives.

Hence one core nodal company like *Microsoft* can connect with another core nodal firm like *Flextronics*, to jointly create a symbiotic ecosystem rooted in "competence on demand". There is a continuous learning process on both side according to the two Professors, as each nodal firm nurtures and builds its competencies. In the case of *Xbox, Flextronics* gains access to a wide market base, while *Microsoft* develops markets downstream.

3.2.2. A fructuous two-way cooperation : Silliwood

New partnerships create additional value : the exchange of competences between the Silicon Valley and Hollywood is working so well that the term of Silliwood has been invented. There has been a long-standing relationship between Hollywood and gaming. For nearly as long as there have been games, there have been licensed Hollywood games. But new links have appeared recently :"There's a whole new generation of Hollywood producers, writers, directors and actors that grew up playing games," explained Boesky, the video-game agent for *International Creative Management*, an Hollywood agencies that cut deals for TV programs and movies. "These people understand games, they play games, and they often want to become involved in games."

Endeavor, also an Hollywood agency, which has five people working in its games division, has been working on integrating some of its clients, including porn star Jenna Jameson (in the games *Tony Hawk's Pro Skater 4*, *Grand Theft Auto : Vice City*), actress Jennifer Garner (from the series *Alias*) and scribe Michael Schiffer (writer for the game *Call of Duty*) into video games. The company also worked with the actor Vin Diesel in setting up his new game company, *Tigon Games*.

Hollywood involvement is various : licensing a hit game franchise like *Tomb Raider* for a big-screen adaptation, or incorporating Hollywood talent (writers, directors, actors) within a licensed game like *Enter the Matrix* or an original game property like Activision's *True Crime : Streets of L.A.* featuring the rapper Snoop Doggy Dog.

"*Electronic Arts* received critical accolades for its Hollywood-licensed games like *James Bond 007 : Nightfire*, *The Lord of the Rings : The Two Towers* and *Harry Potter and the Chamber of Secrets*," said Rob Sebastian, managing director of games and technology at *Endeavor*. "The games were also huge sellers, which opened a lot of eyes in Hollywood and in the games business." On the other side, *Creative Artists Agency* has been busy on both

fronts, setting up the adaptation of id Software's games *Doom III* at *Warner Bros*. and *Return to Castle Wolfenstein* at *Columbia Pictures*.

Directors like Davis and John Woo, who has a game deal with *Sega* and a video-game company in Tiger Hill, also are getting into the act. And more actors, including Oscar winners like Gary Oldman and marquee names like Jennifer Garner and Arnold Schwarzenegger, are getting into games. The trend these days is to go beyond licensing a Hollywood property, instead casting a game with the likenesses and voices of professional actors.

Further bridging the gap between games and linear entertainment is the creation of original properties for games. Jet Li's likeness, voice and mo-tion-captured action are featured in Sony's February release, *Rise To Honor*, a Hong Kong-style video game. Taking things even further, agents now are beginning to shop movie scripts with game-design documents together, so that a movie studio and a game publisher can nurture a potential franchise simultaneously across mediums. Movie studios and game publishers are literally co-creating value with this cooperation. Shared expertise and re-sources enrich the two partners.

3.2.3. Successful mutual benefits : Harry Potter example

Time Warner is a good illustration of the benefits that could come from alliances in the form of Nodal Network organization. Even if the different entities in Time Warner network are fully owned, the exchange of expertise between internet-related companies and media-related firms is very fructu-ous. It can serve as a model of cooperation for future Nodal Network based on partnership and not necessarily based on ownership.

In fact the movie *Harry Potter and The Sorcerer's Stone* released in 2001 is a good example of cooperation between diverse media to build a true network articulated around the movie. The movie has generated $972M to date. Huge investment were realized to combine and allocate efficiently the resources of the group :

- *AOL* was responsible for internet-related business

- *HBO*, *CNN*, *WB* and *Cartoon Network* did promote the movie on TV and gave information about the shooting from time to time

- *Time*, *Entertainment Weekly* and *People* were newspapers mobi-lized for the paper promotion

- *Moviefone*, owned by *AOL*, worked closely to sell tickets online, in partnership with distributors such as *Loews Cineplex Entertainment* and *United Artists Theatres*

The official site of Harry Potter[64] set up by *Warner Bros.* was key to prepare the success of the movie. The survey company *Nielsen/NetRatings* estimated the traffic at 573,000 visitors during the week of the 4th of November 2001, two weeks before the release of the movie. Six weeks before the release date, the traffic was already equal to 169,000 visitors per week.[65] The official site had an e-commerce platform coming along with games, trailers, making off, and interviews. Derived products are part of the strategy since links toward online merchants were proposed by them. So even before the release of the movie, *TimeWarner* was earning money through *AOL* and the traffic generated on the official website.

Results are exceptional since surveys realized during the first week-end of exploitation have shown that 100 % of people surveyed knew exactly that the movie was played in a theater close to their home[66]. On the internet, 31 millions of subscribers have received newsletters or informative and commercial e-mails about the movie. The *AOL* portal was broadcasting extracts from the movie. Adds were added on *AOL Instant Messenger*. The video games inspired by the movie was prepared roughly at the same time as the picture. Fans could win the video game online and could announce the release of the games through a "send to a friend" method[67].

This example is not just about communicating on the most numbered platforms available. *TimeWarner* has capitalized on the expertise of each division, and tried to network them : newspapers were redirecting readers toward the official website. The official website was proposing online tickets. *Electronic arts* created the *Quidditch world cup* to continue online the famous game played in the movie. A real global cross-fertilization was implemented for the first time with success.

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[64] http://harrypotter.warnerbros.com
[65] Source : NewsFactor Network, *Harry Potter website magnet for kids,*
http://www.newsfactor.com, Robin Weisman, November 9, 2001
[66] Source : Julien Teisseire, *AOL Time Warner*, Research paper, HEC business school, June 2003
[67] Source : Capital, *Harry Potter, l'enfant prodige du marketing*, issue number 123, December 2003

A new business model is emerging based on Co-Creation of Value with consumers and economic partners

1. The entertainment industry is already experiencing a mutation in the value chain

1.1. Current business models are challenged by the internet in addition to difficulties in making profit at the end of the value chain

1.1.1. Consumers are transferring profits where value lies in their eyes

Internet Service Providers (ISP) have been held partly responsible for the destruction of value faced by the music and movie industries. In fact, some new taxes are under study to charge ISP for providing broadband access to their customers who then will be able to download copyrighted content.

Profits that should come from the sales of songs are reduced to nothing since these songs are available for free on P2P networks – for free, or almost for free since P2P users pay ISP for broadband access. To caricature, one would say that people pay ISP for listening to music whereas ISP have nothing to do with the music business ; And on the other hand, Music Majors are not paid for discovering and promoting artists. Music Majors' business model is challenged.

A deeper analysis would show that consumers are just paying for something that has real value in their eyes. For instance when buying a DVD that is "protected", which means that consumers cannot use their laptop as DVD player to be plugged on a TV set, some value is destroyed in the eyes of consumers. The value coming from the possibility to watch a DVD on a bigger screen than the one of a laptop has disappeared. On the other side, if downloading enables consumer (or "pirates" in this case) to plug their laptop to the TV set and watch it on the TV screen : There is value created by P2P networks, also by the other consumers who have ripped the movie, and the ISP that has allowed a quick download of the movie. Therefore people would be willing to pay the ISP for the valuable service that consists in getting a movie they can watch using their laptop plugged to a TV set. But

People will not be willing to pay a product whose format is inappropriate to their needs : The DVD format is of no value for multimedia portable juke-box. Whereas ripped movies perfectly match the needs. Why pay for a DVD that do not correspond to my needs ? If there was a legal and cheap down-loading platform of digital movies, people would use it as well for sure. This consumer-centric view of the experience around the DVD helps to unders-tand why do consumers have to find some "illegal" solutions and "steal" through P2P networks. There is not that many thieves in the real world, why would there be 50 % of thieves on the internet ?

The same issue can be applied to protected CD that are not compatible with some devices in some cars or with some CD-ROM drive on some computers : there is destruction of values in the eyes of consumers by re-stricting the experience of music. Profits will go to other services that provide consumers with what has value in their eyes : music that can be read on computers or in cars. Money goes to ISP and P2P networks as distribu-tors.

A transfer of value is also happening between PC manufacturers and con-sumer electronics companies. In fact, margins on PC are smaller and smaller whereas margins on MP3 players or digital multimedia jukebox are high. An explanation would be that there is less and less value in having digital movies and songs on a computer, and more and more value in being able to travel everywhere with digital content. In a way, PC manufacturers are only one link in a new value chain that consists in downloading digital content with a PC, with the ultimate goal to be able to travel with this content. An important value in the eyes of consumers lies in portability and mobility. Dell, HP or Toshiba, by manufacturing MP3 players and PDA, are gaining market share where the new value is : value and therefore profits have partly moved from PCs to portable electronic devices. Core competences are evolving to reflect an extended experience environment. Can companies still be profitable by largely diversifying their range of products and increasing their internal complexity ? To what extent partnerships and co-creation of value between companies are a more appropriate answer ? This question will be addressed by analyzing "experience synergies" later in this chapter.

1.1.2. Business models for online activities need to be readjusted

Online issues of most newspapers are not profitable. Although there is value in the fact of being able to access information from any where at any

time of the day and the night. But the competition of free and legal informative sites is so developed that getting free information is easy. But when looking to online business as a way to reach an additional audience, or to advertise for the papered issue, or to prolong the experience of the newspaper, there is indirect value more than direct profits deriving form online activities.

The profit model based on ads online is encountering difficulties. With a new generation of web browsers such as *CrazyBrowser*, or with the *google'*s toolbar, pop-ups and commercials on the net can be blocked. Some software enable to load Web pages without loading commercial banners or pictures. Consumers have been empowered by new technologies, and the way business is done online is different from the "traditional way". The internet is a user-centric tool, and users have the clout to refuse non-valuable services that slow down their browsing for instance.

Revenues from ads are limited. Several portal have turned to fee-based services. *Yahoo !* decided in 2003 to launch *Platinium Yahoo !* in the US, a subscription service with no commercial : for $3.95 per month, subscribers have access to a range of videos and news from *ABCNews*, *CBS* or *Fox Network*. *MSN* is also moving toward fee-based services with *MSN 8* launched at the end of 2003 : by proposing online storage space, parental control services, anti-virus and anti-spam features, MSN is diversifying its offer to get money directly from users. The model based on commercial banners may not be sufficient in the future to be profitable. In fact, the search engine *Terra Lycos* has announced in February 2004 that it would develop a business model with fee-based services such as website publishing or hosting features. *Lycos* free portal services were not beneficial.

TV channels and cable networks are facing similar issues with their business models. They are evolving from a system were their clients are mainly marketing companies toward a consumer-centric system. According to *News.com*, *Comcast* is interested by *Disney* because the latter would help to boost its launch of "Video on Demand" services by expanding its portfolio of movies. *CBS MarketWatch* has also put the emphasis on the strategic aspect of content in a consumer-driven business : Cable Network activities seems to move toward commercial free services according to *CBS Market-Watch*. Content that perfectly meets the expectation of viewers will be determinant to win subscriptions on a long term basis. In parallel the development of new VCRs that skip commercials is reinforcing this trend.

1.1.3. Communities are under exploited in current business models

Marketing expenses are becoming colossal. But only few entertainment companies are taking into account the importance of communities. Groups of influent persons may interfere in marketing campaigns. For instance the French operator of mobile phone *Orange* decided last year to calculate the consumption of communication time by seconds, instead of minutes. This system was supposed to calculate more fair consumption prices. But *Orange* did not communicate about the fact that this special feature would go along with additional charges, so that in the end this change was not in favor of users. E-mails were sent from groups of friends to groups of friends with all the detail of the additional charges, which highlighted the problem and gave *Orange* a bad name. A lot of subscribers switched operators and *Orange* was forced to step back and to remove the additional charges.

When communities are fully integrated into the strategy of an entertainment product, such as a movie for instance, the cooperation is very fructuous. The trilogy *Lord of The Ring* is a perfect example of mutual benefits. Communities of fans of Tolkien were contacted by the production team as soon as the idea of adaptation was taking shape. They gave their opinions about some crucial aspect of the scenario, such as the role of Liv Tyler in the movie that needed to be a little bit different from what Tolkien had imagined. The director of the trilogy, Peter Jackson, wanted Aragorn (Vigo Mortensen) and the Elf Arwen (Liv Tyler) to appear more often together on the screen than they do in the book. So Perter Jackson proposed to fans the idea of Arwen as a warrior to fight side by side with Aragorn. But the fans rejected this idea, too far from the spirit of the book, and proposed to make flashbacks during the movie to help reminding the love story. This proposal was adopted, Peter Jackson and the communities of fans were happy with this solution[68] that respected the original story and was easier to shoot in the end.

Even if today no monetary value is attached to established communities of fans, interactions with them are source of value. So why not including them into a business model that acknowledge their role ? For instance the promotion of *Microsoft* gaming console *Xbox* was partly based on a co-optation of communities of active fans. According to François Collet, head of *Heaven*, the firm in charge of the relations of Microsoft with online

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[68] Source : interview of Peter Jackson, *Lord of the Ring-The Two Towers*, "behind the scene", DVD appendix 3

communities, "We have signed partnerships with more than 30 sites of fans than generate 360,000 visits per month": *Heaven* provides these websites with exclusive information and content about the gaming console, and a technical support to help these websites to attract more visitors.[69]

Communities are expanding the appeal of a product, a brand or an artist. People choose a brand partly because of the quality attached to it, but also because of the community of users. Communities of fans are loyal to the brand, and active consumers of products. Any brand should take care of creating a community since they add huge value for the company and other users. If *Apple* has survived even during difficult time, it is mainly because of an active core of fans of the brand. The unique design of *Apple* products creates emotions and makes them non interchangeable with other computers for instance. Whereas other PCs were all interchangeable based on their "cold" external appearance. Communities are built with emotions and feelings that tie them to the brand. And emotions are created with unique experience. Any brand should work to move the audience, create an experience, and then build a loyal community to sustain its success.

1.2. On the other hand, consumers are creating new types of value for entertainment companies and other users

1.2.1. Hackers are creating more value than they destroy

The life and the interest of some entertainment products has been extended by fans. For instance *the Lego company* has created an electronic device to control the move of some *Lego* constructions. This electronic device has been hacked by fans who are confident with programming languages. So they have reprogrammed the core functions of the electronic device, created a new interface that allow to connect and to control *Lego* construction with a computer. It is possible for other *Lego* fans to find tutorials on the net about how to extend the possibilities of the Lego devices. It has extended the features and help renewing the interest for the device with new programs created by users from all around the world. It supports the "buzz" around the *Lego* brand, and has transformed a community regrouped around few websites into avid consumers. Is it legal or not ? Well, *Lego* reacted by publishing some keys to decrypt the frameware of its electronic

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[69] Source : Frédéric Brillet, *Pub sur the internet : les techniques qui font mouche*, Capital issue number 150, Mars 2004, page 99

devices : they opened up the *Lego Mindstorms* programming source code to encourage this "positive hacking" highly valuable since appealing to a new audience[70].

A bench of users of *Texas instruments'* calculator *TI92* have also created a lot of value for the company and other users : in fact, they have pro-grammed a whole new operating system called *Fargo* that can be downloaded from the internet. This new operating system transforms the calculator into a powerfull gaming device. Thanks to this new operating system that comes in addition to the actual, it is possible for users to pro-grams more powerful games. The interest around *Fargo* is so important that a lot of people are buying the *TI92* just because of the new gaming features ! This little group of fans have created value by customizing their device. They have created a community online where they can exchange their "Ho-mebrew" games and capitalize on every body creativity.

As far as the *iPod* is concerned, the frameware has been recently hacked ! Can we still call "hackers" these fans who give additional value to an entertaining product ? A group of people have discovered a year ago how to load Linux operating system on the *iPod*. It allows to run various pro-grams on the device that was initially created to listen to music. A website was opened last year with downloadable version of the operating system. Since last year, half a million of web Pages have been viewed.[71] The project leaders have partnered with *SiK Inc.,* a company that manufactures elec-tronic components. *SiK Inc*[72] is sponsoring the project and has given hardware to programmers such as a sanDisc compact flash reader to help them adapt Linux. The Project leaders are also asking for donations in order to continue developing their programs. So there is a real value attached to their work since they have found monetary sponsors.

1.2.2. Players co-expand their experience of video games

The business of games online would not exist without a common interest to play games. When a player decides to join a gaming site online, there are other individuals who are currently playing : gaming partners are adding

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[70] Source : Michelle Delio, *Lego : a Hacker's Best Friend,* http://wired.com, November 7, 2003
[71] Source : http://ipodlinux.sourceforge.net/
[72] For more information about the company, visit http://sik.com

interest to the whole universe of the game. This is a totally different experience from playing alone. And it could not be possible without other gamers. Games such as *The Sims* from *Electronic Arts* have totally integrated the additional interest coming from the possibility of playing online : *The Sims* is about educating and managing a group of friends or a family. Their behavior is influenced by decisions taken by the player. An additional entertaining part of the game is to go online on *The Sims Online* website to confront the behavior of one's virtual character with the others. Three million of people have subscribed to *Electronic Arts'* newsletter to receive in exclusivity news from *The Sims* franchise[73].

The Sims is the most popular franchise ever. One of the reasons of its success are the active community of fans that constantly creates "add-ons" and new features by themselves to keep the interest for the game alive. The latest add-on is called Slice City[74], and was created by Slimslice, one of the numerous communities of fans. *Wired magazine* explain that Slimslice designer Steve Aley has no relationship at all with *Maxis*, the company that publishes the game. However the add-on is so perfectly designed for the game that Maxis decided to spotlight Slice City on the official Sims site for a couple of weeks. For Aley, it is all about co-creation of value : "Sharing the fun of *The Sims* game is the backbone of the Sim community, and it's a driving force that keep us running. As long as the community exists, we plan to be part of it".

The Sims 2 to be released this year will partly consist in creating a virtual town online with every players populating this town with their Sims. Therefore the simulation will be enriched by the various players bringing their virtual creations online : *Electronic Arts* is creating the framework and the tools, gamers are designing their own virtual characters called "Sims" to populate the game online.

The game *Sim City 4* also from *Electronic Arts* allow players to control and develop a city. An additional interest is created by the exchange of cities on the net, and the fact that other players can be instantly contacted

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[73] Source : Steve Yanovsky, Vice President Marketing at Buzztone, during a lecture at the Unversity of Michigan Business school, October 17, 2003

[74] Slice city allows the main characters of the game The Sims to play the game Sim city ! A game to be played into the game. Source : Daniel Terdiman, *The Russian Nesting Doll of Games*, http://www.wired.com, February 14, 2004

through the portal *SimCityscape.com*. Hints, tips and cheat codes provide the player with a new vision of the game or a totally different approach to building a city. Some scenarii can also be created such as recovering after a fire or an earthquake and exchanged online. This type of creation extend the lifetime of the game. This type of extensions is similar to new maps created by the map editor of *Unreal Tournament* : the game is no longer to be played on 10 or 15 maps, but on an infinite number.

1.2.3. Music and movie fans are making new things from old

The concept of "bootlegs" is spreading on P2P networks. Bootlegs are new songs deriving from the original one. Fans of an artist or simply people who like an album will make remixes of their favorite song. Digital editing software enable anybody to create MP3 by simply mixing various sources. Bootlegs are widespread for electronic music such as techno or house. Digital DJ have invaded the web. Some of their works have helped old songs to re-surface such as dance music from the early 90's. Artists are getting a second life such as the DJ Scooter, or simply are gaining a new notoriety. It is a win-win situation.

But issues of copyright are preventing this type of experimentation to take-off. The example of the Gray Album released by DJ Danger Mouse is a telling example of how local DJs could create value for music majors if the copyright problem was tackled differently : The *Wired magazine* online explains that the DJ called Danger Mouse has released on album in January 2004 called the *Gray album* because it mixes the voice from the *Black album* of the rapper Jay-Z with the rythms and chords from the Beatles' *White album*. File traders turned the remix published on 3,000 copies only into an internet hit. But reactions were differing :

- On one side the rapper Jay-Z practically begged DJs to pair his rhymes with new beats because the rapper released a words-only version of *The Black Album* so DJs could "remix the hell out of it". The rapper is aware that remixes help keeping the interest for the album alive by allowing songs to evolve and adapt to new beats.

- On the other side, *EMI music* that owns the rights to the Beatles' sound recordings has asked Danger Mouse to cease and desist. Danger Mouse had not asked the permission to use the copyrighted songs.

However the Gray Album is a huge success : *The Boston Globe* called it "the most intriguing hip-hop album in recent memory", and the music magazine *Rolling Stones* added the name of "Ultimate remix record"[75]. Copies on *eBay* are going for $81. Danger Mouse has won fame thanks to this remix. Jay-Z got additional buzz around its *Black Album*. There would also be value for *EMI music* by signing DJ Danger Mouse, and licence the record. It may be a more fructuous solution than ceasing everything, given that the Gray Album is already widespread on P2P networks and will continue to spread online.

A new concept in the creation of music has just appeared following the development of bootlegs and remixes : Some new records labels are going further in the co-creation of value, since they are giving back the rights to the artists and anyone else who wants to use the music too. *Wired magazine* gives the telling example of *Loca Records*, an independent label that wants to foster experimentation and freedom in music by building a stable platform of free music to be shared, remixed and manipulated by anyone. Songs are not locked by digital rights management technology. The music is available for free in MP3 format, but the label also sells its CDs and vinyl in retail stores throughout Europe. Artists earn a percentage of any record sales ; *Loca Records* makes its money through record sales, gigs it promotes and merchandise.

Wired magazine cites David Berry, managing director of *Loca Records* and an artist himself : "You're free to copy it, give it to your friends and you can play it. If you're really interested, you can sample it and then re-release it ; Because at the end of the day, if you sample the work and create a fantastic remix, we think you're entitled to try and make some money from it." *Loca Records* licenses its music using *Creative Commons*. This organization offers free copyright licenses to anyone who wants to share his or her work with the public while reserving some rights. Using these licenses, *Loca Records* permits anyone to copy and distribute the content, make derivative works and sell it, as long as they attribute the work to the original creator and distribute it under the same "share alike" license.

Copyrights issues, that are at the heart of the preoccupation of Music Majors, are handled with an original approach : in fact, the benefits coming

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[75] Source : Noah Shachtman, http://www.wired.com, *Copyright Enters a Gray Area*, February 14, 2004

from the co-creation of music are worth modifying the control of copy-rights : "I do worry that copyright is getting out of control. This gives us an opportunity to create a new culture and a new sound. If we are greedy and we lock down our culture now, there will be nothing for the next genera-tion," Berry said in the article of *Wired*. This approach helps potential artists to learn by using models as tutorial for instance, and create new songs from old one.

The label has published the work of six musicians so far. In January, it has released its first album complete with added music source codes, includ-ing samples, MIDI files, the score, drum sounds, any text files and the arrangement itself. Every materials to build on the original works are avail-able to make one's own and customized songs. Berry said that *Loca Records*, which does not sign exclusive contracts with its artists, is investing in musicians by giving them the freedom to experiment and build on each other's creations[76].

This trend of remixes is a sign of involvement of fans, and a deeper rela-tion with entertainment products, whether it be a song, a movie or a cartoon : the manga industry for instance has been releasing episodes of its most famous pieces of work on CD-rom for years. In fact, this format is well suited for piracy, since a CD-burner is enough to make an infinite number of copies. But on the other side, it allows consumers to directly copy the episodes of the manga on their digital multimedia jukebox for in-stance, without having to download any ripped files from a P2P network. And more importantly, it allows users to create the equivalent of "bootlegs" for mangas : Fans are editing episodes of their favorite cartoons and are cut-ting the story, mixing the scenes and adding music in the background to create video clips. Most of these video clips are available on P2P networks, and help expanding the universe around a character, or a manga by giving new materials to understand the story. Video clips are like little extra-episodes that are in hot demand among fans. They are like trailers created by fans for fans. They help to advertise for the original piece of work.

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[76] Source : Katie Dean, *Record Label Sings New Tune*, http://www.wired.com, November 20, 2003

1.3. Interactions with consumers are not just additional costs for entertainment companies

1.3.1. It is about building trust, confidence and brand royalty

Movies that are adaptation of books, comics, video games, or are sequels, have a large community of fans even before the shooting. When fans hear that their favorite book is going to adapted to the cinema, they want to know more about it because it is going to be an event in their life of fans. Fans want the movie to as faithful as possible to the original piece of work. The success of the first two movies *Batman* based on the comic book were partly due to a total respect of the universe around the main character. The third and fourth episodes were highly disappointing according to the profits made, mainly because the movies had transformed the characters into something more Hollywood-related and not fan-related product.

Peter Jackson knew that fans would be a great source of ideas for the adaptation of *Lord of The Ring*. Fans who liked playing role-playing games like *Advanced Dungeon & Dragon* or had skills in drawing monsters based on the world created by Tolkien, were contacted to help to adapt the book without altering any crucial aspect of the story. The public knew before the release date that huge efforts were made to be faithful to Tolkien. Fans were posting regularly news and images online during the shooting. A large community of fans' websites was created under the name "The Fellowship". The production team was nurturing the sites with trailers, exclusive information about the shooting crew, and the description of the involvement of community members. Fans' critics were determinant in the success of the movie because they were in the best position to give their opinion about the quality of the adaptation. And the co-creation of value between the director and the fans came from the advice given about some crucial scenes that could not be faithfully adapted to the screen, such as the love story between Aragorn and the elf Arwen.

Dialogues help building trust : To come back to the example of *Orange* which has more or less hidden charges, the brand loyalty was seriously altered. When communicating using transparency with consumers, trust links consumers to the company or service : Some researchers from Harvard[77] consider *Yahoo !* as a good example of dialogue and transparency : its initial

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[77] Source : *The Harvard conference on the internet and Society*, edited by O'Reilly & associates. Inc, distributed by Harvard University Press, March 1997, especially pages 407

success was based on brand loyalty. Yahoo ! has built trust in the highly competitive environment of search engines in five complementary ways :

- First by delivering a competitive product, which means accurate and easy to use.

- Second by adopting a consumer-centric point of view, which means focusing exclusively on users' needs. *Yahoo !* accomplished this by understanding users : they have an organization of 80 people, over half of whom spend eight to ten hours online every day, living and looking at sites and truly understanding the medium.

- Third by being responsive to users : on *Yahoo !* portal, users have just to type a sentence and hit "Send" to contact the support team. On every single page of Yahoo ! except the top page, there's a navigational bar with a button that says, "Write us"; *Yahoo !* receives about 2000 email messages every day. The company answers over 80 % of them personally. That provides an extremely valuable source of information. During the first 8 months of life of *yahoo !,* the two founders answered every email messages : users felt as though they had a stake in helping build the search engine, and in fact they did since the founders acknowledged to have implemented many of their suggestions. Value was created through active interactions

- Fourth by being loyal to its consumers : For example when users cannot find what they are looking for with *Yahoo !,* instead of giving up on them, the search engine point them to the competitors which are linked at the bottom of every *Yahoo !* search results page. As a results, users go to *Yahoo !* to start their webpage search, because they know that the search engine will ultimately help them to find what they are looking for.

- Fifth by perpetuating the perception of editorial independence and inclusiveness. In the very early days of the company, *Yahoo !* got some generous buyout offers from large companies. The founders did not sell to these large companies because it would have fundamentally changed the way users perceived the *Yahoo !* product. Yahoo ! wants to convey the image that it is built solely for the purpose of helping users find what they what on the web to keep the trust alive.

Dialogue, transparency and reliability were key to *Yahoo ! s*uccess in the early years. Maybe it was partly additional costs and a more challenging way of doing business, but it is a rewarding path.

1.3.2. Providing tools to interact create additional entertainment

Radio stations for teens and young adult such as *SkyRock* in France have understood that radio could not be as interactive as the internet. They have also integrated in their strategy the fact that their audience would like to use this medium as a way to get to know other people who like the same type of music. Therefore the radio station *SkyRock* has created a network of affiliated websites[78] with *SkyRock.com* as nodal website. The galaxy of websites counts 160 millions of pages viewed and 7.2 million visitors per month, according to *Mediametrie-eStat*.

Since January 2004 and the take-off of weblogs on *SkyRoc*k websites, the traffic has increased by 55 %. Weblogs (also called blogs) are a webpage that regroup the characteristics of a personal webpage, a forum and a visitors' book. Weblogs help refreshing the content of websites on a daily basis since it is websurfers who constantly interact and create contents. The audience of *SkyRock* can also freely interact through chats, e-mails and SMS (Short Message Service) sent to speakers. The tools at the disposal of the audience have helped to co-create a personalized entertaining environment.

Samsung is also trying to foster a unique and direct relationship with its consumers. Thanks to the "Funclub" that counts 2,700,000 subscribers around the world[79], *Samsung* is creating a true loyalty to the brand. The "funclub" is like an entertaining fan club for consumers : it provides consumers with tools to interact which each other such as chat room online, but also with content to customize their mobile phones and their experiences of *Samsung*'s range of products. The "funclub" has access to downloadable images, ring tones and games. In order to achieve its objective of 5 million subscribers by the end of 2004, *Samsung* will partner with different companies to provide additional content to subscribers : *Quicksilver* (surf, skate) and the DJ Bob Sinclar (techno and house music) have agreed to cooperate

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[78] Such as tasanté.com, yazata.com, bonbiz.com, chantefrance.com, skymobile.com ; Source : Jerome Bouteiller, http://www.neteconomie.com, February 13, 2004

[79] Source : Jerome Bouteiller, http://www.neteconomie.com, *Samsung mise sur son funclub pour fidéliser ses clients,* February 13, 2004

with *Samsung* to create videos, pictures and sounds that would further enable the personalization of mobile phone in an entertaining way[80].

1.3.3. Interactions are essential to co-construct a valuable experience environment

A business case competition took place at the University of Michigan Business school in November 2003. *Apple*'s executives wanted students to think about a new competitive advantage for the *Apple Music Store*, given that several online Music Store are threatening *Apple*'s dominant position. The CFO of Apple Fred Anderson decided to reward a business proposal based on improving the experience of consumers.

How does *Apple* can renew its competitive advantage over the other digital music stores ? The winning proposal explained that *Apple* should invest in a more personalized shopping experience. Several elements could help *Apple* to individualize the experience :

- Customer Profile

- Purchasing History

- Music/Audio Library

- Promotions Database

Thanks to this four elements, Apple would be in a position to deliver :

- Targeted content and recommendations

- Albums purchased by "similar" users

- Customized bargains and sales

By analyzing how consumers behave online in the music store, and gathering data about their preferences, *Apple* will be in a good position to create a personalized experience environment. This approach is the same initiated by *Amazon.com* that creates a personalized store by comparing consumption habits between users : the column "others who shop for this item also shop for this other item" aggregate several products together based on similar consumption patterns. Hence two products from two different categories are

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[80] Source : Jerome Bouteiller, http://www.neteconomie.com, *Samsung mise sur son funclub pour fidéliser ses clients,* February 13, 2004

regrouped in the same experience environment to construct a personalized online store.

The implementation of this strategy to the *Apple music store* will create an edge over other competitors who have not adopted a consumer-centric point of view. Companies usually think that personalization equals additional costs, whereas new technologies enable to co-opt "for free" consumers to deliver individualized experience environment.

2. Looking at current economic mutations through the lens of Co-Creation of Value opens new perspective of profits

2.1. The Co-Creation of value is the interpretation of current radical changes in the business model of the entertainment industry

2.1.1. Today consumers create value for the company, and also for other consumers

The current economic mutations faced by the entertainment industry are coming from two fronts :

> - On one side consumers are increasingly networked, more and more active and knowledgeable, and looking for a good experience. This phenomenon was the subject of chapter one

> - On the other side entertainment companies are increasingly partnering, passive to a certain degree with regard to current economic evolutions, and creating nodal experience networks. It was the object of the second chapter

These observations are signs that an evolution is occurring. The relationship between consumers and companies is entering a gray area. Professors C.K Prahalad and V. Ramaswamy have analyzed these signs to define the future of competition[81]: according to these two professors of Corporate Strategy and Marketing at the University of Michigan Business School, current economic systems are evolving toward a new business paradigm that consists in Co-Creating Experiences with Customers. For the authors of the book *The future of Competition : Co-Creating Unique Value With Custom-*

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[81] Source : C.K Prahalad and Venkatram Ramaswamy, *The future of Competition : Co-Creating Unique Value with Customers*, Harvard Business School Press, 2004

ers, the goal of interactions between companies and customers is moving from "a traditional extraction of economic value at the end of the value chain, toward the Co-Creation of value through compelling co-creation experiences as well as extraction of economic value anywhere in the system of interactions."

The basis for this new business model is very simple : it is the acknowledgement that today consumers create value for the company, and also for other consumers. Starting with this statement, a lot of organizational and strategic consequences have been identified by the two Professors :

	Traditional Business Model : Value is created by the firm	**New business model : Value is co-created by the customer and the firm**
Goal of Interaction	Extraction of economic value	Co-creation of value through compelling co-creation experiences as well as extraction of economic value
Locus of Interaction	At the end of the value chain	Anywhere in the system
Company-Customer Relationship	Transaction based	Set of interactions and transactions focused on a series of co-creation experiences
View of Choice	Variety of products and services, features and functionalities, product performance, and operating procedures	Co-Creation experience based on interactions across multiple channels, options, transactions, and the price-experience relationship
Pattern of Interaction between Firm and Customer	Passive, firm-initiated, one-on-one	Active, initiated by either firm or customer, one-on-one or one-to-many
Focus of Quality	Quality of internal processes and what companies have on offer	Quality of customer-company interactions and co-creation experiences

The two Professors have identified four key "building blocks" to enable the Co-Creation of Value. They are mandatory for co-creation between companies and consumers, but also between companies and other partnering companies since this paradigm is not limited to interaction with "non institutional" consumers. Institutional consumers such as companies are included into the generic term of "consumers". B2C interactions as well as B2B economic relations are Co-Creating value.

The first block is Dialogue : it implies that there are equal roles between the two persons interacting. It links interactively companies with individual consumers or communities, or with other companies. It helps to improve consumers' experience through feedbacks and reactions for instance. Gordon Paddison, senior vice president for worldwide interactive marketing at *New Line Cinema* illustrated this point through the role of communities in the success of *Lord of The Ring* by claiming that "It would have been arrogant to say 'we are Lord Of The Ring', come to us". On the contrary, a genuine and respectful dialogue did occur between the movie-crew and the fans of Tolkien.

The second block is Accessibility : it enables trials, testing to adapt products to personal experiences. It is also an answer to the fact that value is no longer created at the very end of the value chain through a transfer of ownership, but inside an experience network through permission of access. The Co-creation model cannot be viable if consumers have to own the product every time they want to interact. This point was illustrated by Ian Clarkson, senior financial manager at *Amazon.com* and Bart Hoemann, Finance Manager at *Amazon.com*, during a lecture at the University of Michigan : in order to match the experience of a brick and mortar book store, *Amazon.com* is currently scanning pages of most books proposed on the virtual shop. Most tables of content or some specific chapters are accessible on the Web Site.[82] This initiative represents one of the largest in the world and would give access to hundred of thousands of documents.

The third block is Risk : usually firms, alone, define and assess risks for consumers. Their responsibility is fully at stake. In a Co-Creation environment, a redefinition of risk assessment may be necessary since customers may be ready to bear part of the risk, or to alter risks through interactions. For instance the possibility to order in advance video games has changed the risk assessment of publishing companies : Steve Yanovski, Marketing Vice President at the "Change Agency" *Buzztone,* explained that previews, trailers, playable demos and tests before the release date of a video games enable future potential buyers to make up their mind before buying. Thanks to this unique access before the release date, it is more and more usual that gamers pre-order video games. These pre-orders help to assess the financial

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[82] Source : Ian Clarkson, senior financial manager at Amazon.com and Bart Hoemann, Finance Manager at Amazon.com. This point was developed during a lecture at the University of Michigan Business School, October 15, 2003

risks generated by the release of games : sales forces and marketing resources can be readjusted early enough to modify a strategy of promotion[83]. Pre-orders usually give information about the gender and the age of the gamers, which is useful to better allocate marketing investment.

The fourth block is Transparency : Customers are increasingly looking for information. The internet is a gold mine of data and pieces of information. Transparency helps to establish an atmosphere of confidence and develops brand loyalty. And in order for consumers to be willing to interact with companies, trust is determinant. Jeff Bezos, the founder of *amazon.com*, has pushed this fourth block to its limits with his advice "don't invest in things that the customer can't see". Anything opaque is doubtful or counterproductive, or not valuable since no co-creation can take place.

2.1.2. What P2P networks claim is not different from a recognized role in the value creation process

Kazaa is claiming the right to exist. The founders of the website explains in an initiative called "Kazaa Revolution" how they create value for the entertainment industry. The "revolution" they are talking about is highly similar to the one exposed by Professors Prahalad and Ramaswamy : when looking at the characteristics of this revolution brought by the internet, communities and P2P networks, one will find the basic principles of the new business paradigm based on Co-Creation of Value.

Considering the description of the "Kazaa Revolution" as explained on *Kazaa.com*[84] through the lenses of Co-Creation of Value is highly instructive :

- According to the founders of the most famous P2P network "There is a revolution underway which is changing the world of entertainment. It will effect how you discover, buy and share songs, movies, games and ideas. Peer-to-peer technology is driving the revolution and it could make life better for everyone. Lower prices, unlimited catalogs and more"

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[83] Source : Steve Yanovsky, Vice President of Buzztone, during a lecture at the University of Michigan Business school, October 17, 2003
[84] Every quotation in this section comes from the website http://www.kazaa.com

Sharman Networks, that owns *Kazaa,* has started its description of the Revolution by employing terms that describes an experience. Therefore the announced revolution is above all experiencing entertainment products differently.

> - "Peer-to-peer is good for consumers. Why ? Peer-to-peer is about more than just music, movies and games. Peer-to-peer lets people share new ideas, collaborate on projects and communicate more efficiently. It's a freedom of speech opportunity worth developing and defending. It's fast and based on a convenient self-service model."

Sharman Networks explains through this question that the revolution is an evolution toward a logic of "on demand" where customers can freely define and fill up their needs. Collaboration and dialogue is at the crux of P2P networks

> - "It is unlimited in size. Unlike a Web site or shop, a peer-to-peer network will never fill up or slow down. This means more diversity. Content owners and libraries have for the first time a cost effective way to distribute their huge volumes of digital information, opening up amazing new resources to internet users. The cost efficiencies should result in lower cost which should be passed on to consumers in the form of cheaper prices. "

Kazaa puts the emphasis with this statement on the diversity of needs and how P2P networks are an efficient tools to address personalized demands. Companies will derive value from a flexible system that delivers individualized experience on a large scale.

> - "Peer-to-peer is good for Artists, Producers and Developers. Why ? Emerging stars can share their works with the world without big budgets or a big deal. A song, video, game, idea or image can be shared, tried and bought based on how good it is. Major stars can access a huge, global audience instantly."

The founders of *Kazaa* try to show with the above explanation that every stakeholder of the entertainment industry may find value in this new cooperative system. P2P networks offer accessibility to pieces of work in order to be able to co-create value. And consumers are co-opted to share, promote and diffuse the entertainment products they like. The economic value of this

capacity to promote and diffuse entertainment products has not yet been recognized in current business model. We know that this role is determinant, but there is still no "amount of money" attached to it, because most companies think that value comes from consumers only at the very end of the value chain, where transactions are made and money is exchanged physically.

> - "With peer-to-peer, less money will be taken out of their [artists'] royalty checks to reimburse their publishers for promotion costs. It's easy to set up a "digitally rights-managed" account that lets artists decide how they want their fans to experience their work. They choose the length of free trial, determine payment criteria and wrap their files in digital protection. "

P2P networks enable direct interactions and therefore a different price-experience relationship. Consumers and artists are totally free to decide at which point money will be extracted through variable free trials and individualized digitally rights.

> - "Peer-to-peer is good for Labels, Production Companies, Libraries, Owners. Why ? These companies own a lot of the content that peer-to-peer users want. They can protect this content through digitally rights-managed solutions and give users the option to buy it. They can reach a huge, global audience instantly. Kazaa alone already has 60 million users. Costs are dramatically reduced through this new distribution technology. Potential new markets await these companies and their content."

As described above, the success of P2P networks are a very good news for the entertainment industry : it shows that consumers love the products of the entertainment industry and want to own or experience a lot of them, more than they could do in the previous experience environment before the existence of P2P networks. *Kazaa* has found a system that enable to answer the need of consumers for more experiences of entertainment products. By co-opting consumers and therefore P2P networks through methods explained later in this chapter, entertainment companies will benefit from this accrued consumption of their products online.

> - "Who's Trying to Stop It and Why ? Kazaa and other peer-to-peer applications have been under attack from the major Record and Movie companies and their industry bodies, the Recording Industry

Association of America and Motion Picture Association of America. The Record and Movie companies are suing peer-to-peer software developers and the RIAA are suing peer-to-peer users."

Recent studies have highlighted the fact that the most active users of P2P networks are in general those who also buy entertainment products the most. It works as if online file-swapping triggers the discovery of new sounds and new tastes that generates more buying decisions. And in fact, very active file-swappers gain a very high expertise in specific type of entertainment products : therefore they often serve as reference for their friends who hesitate to buy a particular product : they usually ask them for pieces of advice. And this "counseling" and influential role of active file-swappers is highly valuable. Suing the persons who are the most active on P2P networks, and so who like the most the products of the entertainment industry, may not be the better incentive to consume more. Maybe there is a win-win solution to be found.

- "This Revolution can benefit everybody. So why are they trying to stop it ? Copyright owners companies own the copyright to material that they sell. Some of them are afraid that peer-to-peer means everything is always available for free. Some of them don't believe that peer-to-peer users would pay a reasonable price for files. Since May 2002, peer-to-peer applications like Kazaa have offered copyright owners the ability to protect, promote and sell their works to millions of users. Everything is in place. They just need to try it."

Business models such as the *Apple music store* shows that there are profits coming from the handling of the experience environment as a whole. They are profits when adopting a consumer-centric approach to define the best point of interactions to exchange value. Of course, everybody is not ready to use *Apple music store* or any fee-based P2P networks in the future. Maybe those who had not the financial resources to pay will continue to look for free solutions. But at least they will take part in the promotion and diffusion of a product if co-opted. They will create value. And in addition the population with a higher purchasing power accustomed to high quality services will continue to use fee-based high quality services online.

- "Record and Movie Companies make money out of developing copyrighted material, distributing it, promoting it and selling it. They are concerned that peer-to-peer will reduce their control over every step of this process. This is because peer-to-peer is a market

driven by the people. They'll have to change some of their business practices to succeed in a peer-to-peer environment. Peer-to-peer should not be stopped because of this. The benefits of the technology are great. There should be no reason to try to halt a revolution."

This statement puts the emphasis on the fact that the traditional organization of the value chain of Record and Movie Companies is challenged by the evolving experience environment. Therefore the revolution claimed by *Kazaa* is to recognize that consumers have a role to play to create the most adapted experience environment that serves their needs. It is all about recognizing that value can be co-created, and therefore that companies should adapt to consumption evolutions, and not refrain it as if it was only destroying value.

> - "If peer-to-peer provides a bigger market, lower costs and unlimited space in packaging music, videos and pictures and these companies tried it, they could make so much more. They need to stop fighting this technology and start working with it. We'll say it again. Since May 2002, peer-to-peer applications like Kazaa have offered record and movie companies the ability to protect, promote and sell their works to the millions of users. Everything is in place. They just need to try it."

Sharman Networks has been suing some Movie Majors for not allowing the fee-based platform of *Kazaa* called *Altnet* to sell some of their content online.

> - "Changing to a New Way ? Nobody can accurately predict how this will work out. Peer-to-peer represents a massive and complex change to traditional music and movie industry models. Consumers will drive it and companies will compete to offer them the best service, value and quality."

The paradigm of Co-Creation of value explained by Professors C.K Prahalad and V. Ramaswamy is based on a consumer-centric approach. *Kazaa* through this statement is also taking consumer as the driver of future economic interactions. Similarities between *Kazaa* Revolution and Prahalad & Ramaswamy new paradigm of co-creation speak for new opportunities of development in the future. Part of the entertainment industry considers that future growth prospects are equal to zero and try to block any change. But on the contrary, bright opportunities of additional profits are there for the

taking. The end of this chapter will highlight some of them, maybe to serve as a basis for future development.

2.1.3. The software & video games industry has already implemented some rules of Co-Creation

Kaleb Kain, an editor for the web portal *StartNow.com*, has analyzed for the website *warez.com* more than 20 years of online file trading. According to K. Kain[85], video games and more generally software were among the first things to be swapped online. Before the late 90's, the trading of music and movies online did not exist. From the early 80's on *Apple* computers through to today, people have been trading software nicknamed "warez". The software industry panicked, fearful of being marginalized. They did not have a vision of today's internet, but they foresaw a world of pirates making copies of warez and hitting the streets like drug dealers according to K. Kain. They implemented copy protection schemes on Discs, and launched many "Don't Copy That Floppy" TV ad campaigns with the aim of reducing what they considered to be piracy. Even backing up software was made difficult. But that initiative from the software industry backfired as copy protections were defeated and people were determined to make backups of their games and applications that were on unstable media : magnetic Discs and scratchable CDs.

In the late 80's and early 90's, computer technology was advancing fast. CPUs from competing companies and different video card standards had everyone wondering what software or video games would actually work on their particular system. The PC industry was not as standardized as today and since full demos did not exist, warez trading was a way for users to try before they buy. Trading also helped many people to discover games that they would have never bought. However K. Kain puts the emphasis on the fact that the industry still profited in some way, either from word of mouth promotion or from that once "pirate" who downloads version one of the game, but buys versions two through ten in the future. By having access to software, consumers could test it on their PC : the software and video games

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[85] Kaleb Kain is an editor for StartNow.com, a web portal. He is working with high traffic websites to promote the future of P2P networking. On February 1st 2004 Superbowl Sunday, he has released The Great File Trading Survey on Warez.com and other P2P sites. This survey gathers data to show the file trading practices of the world and eliminate any myths. Results are available for the entertainment industry to view. Email : kaleb@warez.com

industry avoided pure losses coming from products sold and then reimbursed because of incompatibility. This consumption habit of testing has become today part of the strategy of the software industry that counts on the feedback of larger and larger groups of "beta" testers to fix some incompatibility issues.

Another indirect value comes from the brand loyalty that is created through recurrent use of a particular type of software. Applications like *Adobe Photoshop* or *Microsoft Office* are so high in price, that students or small businesses cannot afford them. Students download warez versions to keep learning. The industry now knows that it's those same students who will become the executives and workers that will buy or influence the purchase of many applications to come. Because of the help of a few warez, small businesses grow from a pirate employee operation into big businesses that buy hundreds of software titles. Very recently *Microsoft* has adapted its strategy to this new deal since students at the University of Michigan can buy *Office XP* for less than $30 and *Windows XP* Pro for $15. *Microsoft* has understood that students could never afford to buy a $300 software or operating system. And even sold at a loss these software are an investment since students are those who will become managers in the future and decide which software to buy for their companies.

K. Kain comes to the conclusion that while the software industry still will not tolerate the sell of fake packaged copies or the serving of mass warez over the internet by a website, they are not directly attacking the individual nonprofit downloader who uses the software or trades it to a friend. However, in these times, it takes a very skilled downloader to avoid fake copies infested with viruses and spyware. Most users are fully satisfied with full demos that most makers offer for free now. The video games industry is offering access to its products without ownership to enable co-creation : Full free demos to download, previews, tests in specialized magazines, trailers, screenshots are enabling consumers to really get a feel of a game before buying. *Microsoft* has even released 30-days full demo of *Office XP*. *Microsoft* early on has recognized that customers are a source of competences and value since more than 650,000 customers have tested a beta version of *Windows 2000* and have provided the giant software companies with personal feedbacks and potential sources of improvement[86]. Shareware[87] are a means

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[86] Source : C.K Prahalad and V. Ramaswamy, *Co-opting Customer Competence*, Harvard Business Review, January-February 2000

to get consumers feedback : in case of incompatibility problems, companies can adapt their shareware and send an individualized version with the problem fixed. Then consumers are sure that the shareware will fully work on their PCs and may pay the company to get full access to the software. The fear of piracy has been ousted by the perspective of profits based on Co-Creation.

After two decades, the software industry has analyzed the trading of warez among peers and concluded that the growing online community is a wonderful tool for promotion, and that their profits are higher than ever, even if they will not announce it officially.

2.1.4. The music industry does not seems to be ready to benefit from the new rules of making business

When *Napster* exploded onto the scene, the RIAA (the recording industry association consisting of the 5 big record labels) got scared and brought it into the media spotlight. Before September 11, it was the number one topic, as explained by K. Kain, editor for the web portal *StartNow.com*, who has analyzed for the website *warez.com* more than 20 years of online file trading. The media hype has introduced the uninformed world to the fun of P2P file trading. It has also highlighted the practices of the music industry and the amount of propaganda that spread during the battle with file traders.

The first reaction of the industry faced with a new trend that was challenging the traditional value chain was to explain that "the artists are losing so much money." However some investigation made by media companies shed new light on the share of revenues that goes to artists. The public learnt that some labels make 95 % or more on all CD sales, and artists make their money touring and merchandising their name. This new transparency was not handled carefully by the Music Majors and created some suspicion among consumers. The image of some Music Majors was attacked and the loyalty of some music fans was eroded.

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[87] Shareware are software distributed for free. But the free use is limited in times or limited in terms of the features accessible. Usually a fee is necessary to unlock the blocked features of the software, or to get unlimited access in times. Freeware are software that are distributed for free without any constraint of use or in time.

Music Majors directly imputed the decline in CD sales to P2P networks development. But interestingly, CD sales began to actually rise during the *Napster* hype as did the number of P2P users. CD sales did eventually start to decline, especially in 2001 and 2002, but some economists reported that declining CD sales were most likely the effect of the slumping economy. The sales of 1999 that serves as a reference were a peak only reached once before by the music industry. The thriving economic context of the end of the millennium can not be compared with the American recession in 2001 [88]. So it seems that P2P networks have also succeeded in generating additional sales since the decline in CD sales is rather due to the economic environment than file-swapping. In fact the sales of singles have reached a peak in 2003. It is the sound transposition of consumption habits coming from P2P usage. The success of *iTunes* may not have been that huge without the previous development of this type of consumption method through P2P networks.

Kain justifies music swapping rather as a message for Music Majors : for him, consumers have not been taken into account over the last twenty years. Therefore when the occasion to be emancipated from traditional consumption methods arose, the public turned to new solutions : "In the early 80's, cassette owners were told that CD quality was better than their analog tapes, and that CD's would last forever. I remember salesmen in those days pouring coffee on CDs, scratching them, and throwing them across the room to show how durable they were" Kain said. If the CD was bringing a lot of value to consumers, now the situation is different : "Today, although the cost of making a CD is pennies, they now are made at a much lower quality. A slight scratch ruins the CD. The industry saves more money, but has never lowered their prices. The user ends up re-buying his favorite CD many times, while that old cassette still lives. Now the industry sells 24-bit DVD audio discs after realizing that 16 bit audio CDs don't sound better than your old analog tapes."

But most of all, the relations between labels and consumers have been tarnished over the years by a lack of dialogue : "After years of playing games with the consumer, the big labels need to do something big to gain any respect. Suing 12 year old girls for downloading songs may not be the best public relations move" said Kain.

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[88] Source : La Tribune, *L'avenir du disque passé par the internet*, January 26, 2004

Music Majors are offering solutions that do not match a consumer-centric experience, at least until very recently. The case of people trading songs to discover new music from regions all around the world is a good illustration. P2P networks are the only place to experience new and exciting music, trying it before buying it. But instead of satisfying a demand by consumers to hear and buy a wide range of music, K. Kain said that "The industry stocks a very small selection of artists in stores, mainly only those they have chosen to heavily promote. Many people would like to go to a store to buy music they discover through online trading, but it's usually not there unless they live in a major city". One argument would be that everything can be bought online. But a consumer-centric approach would have highlighted the fact that the music industry's biggest buying demographic is 11-18 and mostly does not own a credit card.

American radio is no answer either to discovering new music as one corporation, *Clear Channel*, owns a majority of the stations, a practical monopoly. It broadcasts music to the different regions based on "market data" analysis of what they feel the listeners want. But accrued interactions with the audience would have revealed slight differences of expectations : *Clear Channel* has quit playing music submitted by independent record labels according to Kain. Whereas at the time independent artists were in hot demand on the net. The independent artists overwhelmingly support the trading online of their music as it is now their number one medium for promotion. A few years ago *MP3.com* became a huge site for spotlighting independent and unsigned artists. Its popularity as well as some potential legal issues scared the music industry. It was bought by *Universal Records* and partly, dismantled. The attitude of Music Majors destroyed a lot of value in the eyes of music fans by indirectly refraining the expansion of independent artists.

During the past concert season, the power of the internet and how music tastes spread through online communities was made obvious. Music festivals like *Bonnaroo* and *Austin City Limits* featured artists with practically no radio play or major store promotion. While most promotion and ticket sales were handled online, the festivals were a sell out attracting hundreds of thousands of people[89]. However it seems that the economic value represented by communities is still underestimated in current business models.

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[89] Source : Kaleb Kain, *Got Warez ? Twenty Years of Online File Trading,* http://warez.com, February 2004

A lack of flexibility may prevent Music Majors from benefiting directly and indirectly from new consumption habits : Total concert revenue is high year after year. A live concert experience is something that cannot be traded online. But unfortunately, Music Majors have set in stone a tradition that they will get most album sales money and the artist will get concert money. It seems today that online music works directly as a promotion method for concert. Money that may not be spent to discover new artists is partly spent on concert. More and more non-official recording of concerts are exchanged on the net, fostering the experience of an artist. So on one side Music Majors are indirectly promoting artists through the expansion of digital music and P2P networks, but on the other side do not have the appropriate contracts and alliances to directly benefit from this type of promotion. This business model would be similar to the situation of Apple and the iTunes Music Store, but without the iPod : all the value created online would go to other stakeholders by considering half of the experience environment.

For Kain, that has a rather critical attitude toward Music Majors, there is definitely money to be made out of current evolution : "It's up to the music industry to find ways to romance this huge market instead of alienating it. The trading of music is a revolution that won't stop, and where there is a large group doing anything often, there are ways to make big money. The question is : Can the RIAA stop panicking long enough to see the light ?". The light may be the Co-Creation of Value.

2.1.5. The Movie industry has understood that the business environment is evolving but no real actions have been yet taken

The movie industry has feared the copying of movies for years. Copyright protection was put on VHS tapes, but users found ways around it to make backup copies of tapes. The movie industry spent years perfecting a copy protection for DVDs before they were introduced, according to Kaleb Kain, editor for the web portal *StartNow.com*, and analyzing the attitude of the movie industry faced with file-swapping. In no time, the encryption method was broken and software came available for people to backup their DVDs. "DVD John" became famous for being the one who diffused on the net the method to crack DVDs. However, DVD sales continue to increase despite the increasing number of methods that people use to make copies of their DVDs. DVDs are an interactive experience far better than watching a ripped movie on a computer screen. But when broadband connections will

be very popular, and portable media center cheaper, consumers will start looking for digital content convenient to download and easy to watch on-the-go. If no consumer-centric solution is found, losses might endangered the development of the whole industry.

For Kain, the big scare for the movie industry (MPAA) was when they discovered bootlegs of movies that were still in the theater or yet unreleased being traded over the internet. Online movie bootlegs have not put a dent in ticket sales. However, technology progress frightens the industry into thinking that someday the user will be able to bootleg a movie and match the theater quality experience in their own home. If this happens, many feel that the movie industry must adjust their income methods or advance the theater experience. New theater experience have been developed in recreational park such as *The Futuroscope* in Poitiers, France. Technologies such as 3D, holograms, or interactivity are ready since the beginning of the 80's. Why not advance the theater experience to keep it alive by implementing on a large scale these "not so new" systems ?

The recent alliance between *Microsoft* and *Disney* to distribute content online shows that the Picture industry is on the move. However, The movie industry is rather passive than active in the emergence of a new economic environment. *Universal* for instance has refused to partner with *Altnet* (the fee-based downloading platform of *Kazaa*) to sell movies online. In addition, the movie industry is currently running ads before movies featuring low paid film workers who tell the moviegoer (who just bought a ticket) that downloading movies takes away money from the workers. These ads are not adopting a consumer-centric approach and deny the whole experience environment of moviegoers : Downloading movie is convenient. If legal platforms were available, maybe people would rather use them. Maybe filling this need may be more profitable than trying to change new consumption patterns, at least in terms of image for sure. In addition, the effect of the ads may not be the one expected, as Kain explains on warez.com : "It's doubtful that the salary of workers on a movie will suffer from warez trading, but they also never see a cut of the huge profits from a successful movie. Following propaganda methods used by the music industry may be the fastest way to anger the movie going audience". A consumer-centric approach with accrued dialogue will enable the movie industry to make more money in the future, the success of *Lord Of The Ring* is leading the way.

2.2. In the business model based on Co-Creation of Value, consumers are artists and creators of entertainment content

2.2.1. A business model for consoles that considers players as developers : The Game Park 32 example

The video game industry has acknowledged the expertise developed by lots a consumers in term of programming. The gaming industry has also realized that numerous "emulators" were available on the internet. Emulators are downloadable software that simulate the operating system of a gaming console on a computer. "Roms" are games for emulator. Emulators and roms are the sign that the hardware is no longer necessary to play video games initially designed for consoles. Hopefully emulators are only available for elder consoles, which means that the sales of recent consoles are not threatened by emulators.

This trend could be seen first as a destruction of value. But emulators mainly concern old gaming devices that are no longer sold. The programmers of roms and emulators are even creating money and value for gaming companies : The *GP32* is a telling example of a new breed of gaming device. The *GP 32* (*Game Park 32 bits*) is a Korean portable gaming device. It is more expensive than competitors such as the *Game Boy SP* because it costs around $160-$180. But on the other side, the business model fully integrates gamers and consumers as co-creators of value. Only few games are sold by the Korean manufacturer, maximum ten games. So the strategy of the company is not the traditional one that consists in selling the console at a loss and sell high profit margin games. On the contrary, it makes high margins on the portable gaming device, knowing that consumers will be provided with the tools to create their own amateur games for free.

In fact the gaming console is nothing but a small computer that allows to listen to MP3, read Div'X and, the most important, to load emulators. A USB port allow the *GP32* to be connected to a PC and then to a server (http://english.gamepark.com) where demos, screensavers and sounds are available. The *GP32* is compatible with emulators such as *Nintendo NES, SNES, Game Boy, Game Boy Color, Sega GameGear, Atari 2600, Atari ST, NeoGeo Pocket, PC Engine, Coleco Vision, Wonderswan* etc… Roms can be found on the net, and some games have already been especially created by other users for the *GP32* such as *Wolfenstein 3D* or *LucasArts' Day Of*

The Tentacle[90]. This new business model allows users to personalize their gaming device and co-create with the company and other users by exchanging online their "homebrew" creations. It is a perfect example of a profitable business model based on co-creation of value.

2.2.2. A business model for music that considers consumers as artists : The Opsound label example

Opsound (opsound.com) is an independent label that has built a business model based on co-creation of value. The culture of bootlegs is included in the strategy of the label since it encourages cooperation between musicians to mutually improve their songs ; And naturally to share the benefits of a potential commercial distribution. *Opsound* invites any musician to submit songs to its website, where others can listen, share and remix them. Music is licensed using *Creative Commons*.

The guidelines for using this pool of songs are pretty detailed : they are inspired from the open-source system widespread in the software environment. *Opsound* puts the emphasis on a set of rules that guarantees a win-win situation for every partners. Copyright issues are tackled differently to create new source of profits. The main rules of the game are the following :

- "Most of the files in the pool are full length songs in high quality MP3 or Ogg Vorbis formats ; They are fairly large files intended for downloading rather than streaming."

- "All sound files in the pool are released under the Creative Commons Attribution-ShareAlike license (a copyleft license similar to those used in the free and open source software communities) or placed in the public domain."

- "This means you are free (and encouraged) to download works, make copies, share them, include them in other works, remix and rearrange them, and even sell them. The Attribution-ShareAlike license requires only that you attribute the works to their original authors/musicians (attribution), and that any derivative works (anything you make using the sound files) be licensed under the same license (share alike)."

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[90] Source : http://www.Jeuxvideo.com

- "If you use work from the pool as part of something you make publicly available, you are encouraged to email us and let us know, and to let the original artist know as well."

Music majors could be inspired by this model of Co-Creation of Value : P2P networks are creating a gigantic pool of MP3s : Almost anybody that owns a computer today has some MP3s stored on its hardrive. The model of *Opsound* shows a way to make profit out of a pool of MP3s that exists already. It is a means to make profits a posteriori from local creations, remixes and bootlegs. P2P networks would create new value for Music Majors by helping spreading a pool of MP3s to be remixed. *Opsound* explains that money will come from fairly shared revenues : "The Opsound licence does not restrict commercial use of the sound files. However, you are strongly encouraged to get in contact with the artist if you wish to do this, and to make arrangements to share any financial benefits. It is hoped that we can develop a community that operates with a great deal of freedom and which uses that freedom in a way that is both generous and ethical."

The concept of community is critical to the success of such system, since it fosters cooperation, and help artists to know who is doing what with their music : " If you are interested in discussing further how this might be done, please consider joining the conversation in the the opsound forum." Today Music Major cannot easily know how their music is used since there is no discussion platform. Then it is difficult to negotiate any shared profits that would come from a remix with Music Majors, just like the situation of DJ Danger Mouse with its *Gray Album*.

Artists who know about this type of copyrights are enthusiastic : The *Wired magazine* give the opinion of David Kusek, associate vice president of the Berklee College of Music, which recently announced a plan to distribute music lessons for free over P2P networks : "I think it's a wonderful idea. Historically, building upon one another's music was common", Kusek said. "Jazz, in particular, was based on improvisation, theme and variation and "who could outdo each other" with each interpretation of a piece."

Kusek also noted that "We lost a lot of the spontaneity that was inherent in music when it became a package that could be stamped a million times and resold. The existing labels of the last 50 or 60 years have been all about controlling the expression, the packaging, the distribution and the scarcity of the music in order to turn a profit. That forced music to be defined as a

product. It can be a product, but in its pure form it's entertainment."[91] Remixing is an additional entertaining part. Allowing remixes and fair shared profits may further help the music industry to recover : potentially it would means co-opting thousand of millions of music fans that could potentially create value for Music Major by remixing and selling MP3s. What if tomorrow buying a CD means also buying half of the copyrights : maybe it would add some interests to the entertainment products, and maybe some value in case remixes based on original creations turn to be successful. In any case, *Opsound.com* is co-creating new value by co-opting and linking consumers together.

2.2.3. A business model for movies that capitalize on "homebrew" creations : The Sundance Film Festival example

Part of the audience of Hollywood's movies are fans who are or want to be artists. Some of them are passionate by films, or simply create homebrew movies as a hobby. The popularity of some Hollywood's stars can be measured by the number of "home-made" clips and remixes available on the net. Fans create non-official websites for movie stars that help creating the buzz around an actor. Amateur video clips, movies, parodies are valuable content for actors spontaneously created. All type of parodies of the movie *Star Wars* for instance are exchanged through the net and help maintaining a mystic atmosphere alive around the trilogy, even if no new episodes are to be released in the coming one or two years.

Online film festival have acknowledged the expertise and potential source of value that lies in individuals. In the entertainment industry, creative products are profits. Hence consumers who create are potentially a source of profit. Digital editing software make it easy for individuals to make good quality "homebrew" movies. Online film festivals, an offshoot of the commercial film channel, are making the most of this evolution. The *Sundance Online Film Festival*, in its fourth year, has launched its biggest and most ambitious program to date. *Anarchy*, the monthly online movie contest produced by *Slamdance*, has seen a steady rise in submissions. And *TriggerStreet.com* is becoming an increasingly high-profile site for aspiring filmmakers and screenwriters.

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[91] Source : Katie Dean, *Record Label Sings New Tune*, http://www.wired.com, November 20, 2003

All three presented movies in Park City, Utah, during the 2004 *Sundance Film Festival*, which run Jan. 15 to 25. John Cooper, the director of programming at the *Sundance Film Festival*, pointed out in an interview for *Wired magazine* that more viewers now see shorts online at the *Sundance Online Film Festival*, or *SOFF*, than at the festival in Park City. More than 600,000 unique visitors came to the *SOFF* site in 2003, each watching, on average, four films[92].

"It's impossible for industry executives to see all of this material, but with all of the movies online, everyone will have their chance to see everything." Cooper said the number of submissions for Web-based work rose to more than 200 this year from about 10 for the 2001 *SOFF*. Cooper predicts the number of Web-based movies will continue to increase as a new generation embraces digital tools. "When I was in high school, I hung out in art class and worked at a potter's wheel," Cooper said. "But if I was a kid now, I'd be sitting at a computer. Young filmmakers are more likely to use Flash than film because that's the technology they know. I didn't want to let the work of this whole new generation go untapped and unnurtured."

Nurturing is also the goal for *TriggerStreet.com*, initially created as a way for Oscar-winning actor Kevin Spacey to cope with the burgeoning number of short films and scripts that people tried to hand him at coffee shops. *TriggerStreet's* online festivals are designed to promote these aspiring filmmakers and screenwriters. Scripts and shorts uploaded to the site are critiqued by other members of what President Dana Brunetti called the "TriggerStreet community". The site counts 100,000 members.

Several times a year, the top-rated films move from cyberspace to a festival theater, where a jury of entertainment professionals picks a winner. A bridge from virtual creation to sound money has been built. The whole process, according to Brunetti, has a festive feel. "Once we announce the festival, there are a lot of hoots and hollering in the message boards," Brunetti said. "And people get excited when a new movie arrives and starts moving up in the rankings."

On Jan. 22, a panel including actors Kate Bosworth and Billy Bob Thornton, Finding Nemo director Andrew Stanton and hip-hop artist Q-Tip has

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[92] Source : Jason Silverman, *Online Festivals Nurture Film*, http://www.wired.com, January 15, 2004

selected a new *TriggerStreet* short-movie champion from 10 finalists. Commercial movie channels have recognized the appeal of online festivals : traffic has spiked for each of the first two Star Wars Fan Film Awards, produced by *Atom* and *Lucasfilm*. As Shane Kuhn of *Slamdance* points out, all of these festivals are basically jockeying for position, waiting for average folks to be able to download high-quality video to their computers. Once that happens, Kuhn said, the established online festivals will become key outlets for alternative cinema. "*Anarchy* is still a grass-roots operation, not a moneymaker," he said. "But it will eventually become a much bigger part of *Slamdance*'s future. Someday, *Anarchy*, with its global reach, will probably dwarf *Slamdance*'s physical events."[93]

Online films festival are in a better position to benefit from individual and amateur creations since they require less investment on behalf of participants. And the reward may be increasingly high both for professional producers and amateur directors : The *Wired magazine* gives the example of an amateur filmmaker whose work edited on Apple *iMovie* software has become a huge success : Jonathan Caouette, 31, used his friend's *iMac* and the editing program *iMovie*, to distil his VHS home movies, his Super-8 experimental films, and a suitcase full of photos and audio tapes into *Tarnation*, a hybrid documentary that premieres in January 2004 at the *Sundance Film Festival*. *Tarnation* may be the first feature-length movie edited entirely on *iMovie*, and it cost $218.32 in videotape and materials. Despite its low budget, the movie has already earned a high profile. Both John Cameron Mitchell, the actor and director of Hedwig and the Angry Inch, and independent film maverick Gus Van Sant have signed on as executive producers.

Jonathan Caouette explain his experience in this terms : "People told me, 'Why don't you throw *iMovie* away and graduate to Final Cut Pro ?' But iMovie is so easy. I didn't know any editors, didn't know anyone in the movie industry. Everything that has happened with this movie has been an explosion, and happened so quickly." The self-taught Caouette obviously has a native talent as a filmmaker. "*Tarnation* is a very strong statement for low-budget filmmaking," said *Sundance* programmer Shari Frilot. "It's a testament to what someone can accomplish with simple desktop tools, and exciting and encouraging to see how much can be done with so little." Gus

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[93] Source : Jason Silverman, *Online Festivals Nurture Film*, http://www.wired.com, January 15, 2004

Van Sant described *Tarnation* as "amazingly original," and the kind of movie he had been waiting to see since the 1970s. Any business model based on co-creation would capitalize on this type of amateur talent whose existence is known by the movie industry. "People assumed that one day movie would be as accessible and inexpensive as writing, and now it practically is," Gus Van Sant said. "For the price of a typewriter, you can make movies with sound and burn them on a DVD… Filmmakers can afford to work now. No more excuses, or filmmakers' block, or procrastination."[94]

2.3. In the business model based on Co-Creation of Value, communities and P2P networks are distribution and marketing tools

2.3.1. New marketing strategies have already implemented successfully the principles of Co-Creation

New types of marketing strategy based on new technologies have proved that communities may be the best vector of information related to entertainment content. *Buzztone* is one of this new and successful type of marketing company that describes itself in this terms : "Buzztone is an agency challenging traditional marketing ideas. We are 'The Change Agency' – a new type of marketing company that disrupts the conventional and challenges the imagination through the emotional enzymes that energize consumer's connection to a brand experience. We are a company that embraces the power of bold idea, employing the element of surprise. We serve in transforming passive consumers into active participants… Inventing new communication practices within existing and never developed channels."[95] *Buzztone* has summed up most of the basic principles that compose the new paradigm of Co-Creation of Value :

Firstly consumers are looking for more than a product, they are looking for an experience. The experience creates emotional links with the product and brand loyalty. It is similar to *Buzztone'*s reference to "emotional enzymes that energize consumer's connection to a brand experience". One example may be the commercial campaign designed by *Buzztone* for *Heineken*. How to create an experience around the consumption of *Heineken* bier ? Steve Yanovsky, VP of marketing at *Buzztone* started from a consumer-centric point of view to answer this question : people usually drink

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[94] Source : Jason Silverman, *Here's the Price of Fame : $218.32,* http://www.wired.com, January 20, 2004

[95] Source : http://www.buzztone.com

bier and listen to music at the same time. Bier and music are part of the same experience environment. The idea to create a commercial campaign around Heineken and music was decided. But which music band would agree to attach its name to a brand of bier ? Hence the idea of creating the "*Heineken Music Foundation*": the funds raised would go back to musicians. *Heineken* co-founded the recording of a video and a CD featuring new artists. Alicia Key and Ray Lewis accepted to promote the record and the *Heineken Foundation* on TV through 3 TV spots that looked like a video clip. The spots were related to music education, therefore the initiative was backed by a lot of artists. Only at the end of the video clip was referring to the *Heineken music foundation*. Music is something appealing, that arouses emotions. Associating the consumption of *Heineken* to music would create an experience around the product and give a funnier brand image. That was the first time a commercial for *Heineken* was not talking about *Heineken*.

Secondly, Interaction with consumers is at the crux of the Co-Creation of value. It is similar to *Buzztone*'s motto of "transforming passive consumers into active participants". In fact Steve Yanovsky detailed during a lecture the example of the promotion of *Kangoroo Jack*. The targeted public for this movie was mainly composed of children. In order for the child to become familiar with the hero of the cartoon, Jack the Kangoroo, *Buzztone* decided to create books with ten to fifteen pages, with black and white images of Jack to color, games more or less related to the movie, and little funny stories to read around Jack. 800,000 books were distributed. The release date was added on the cover for children to ask their parents to go and watch it. These books were mostly distributed at the exit of primary schools. In addition, a person with a *Kangoroo Jack* costume went to schools to promote the movie. This character started to be viewed on TV, in shows for children. An emotional connection was born between *Kangoroo Jack* and its audience. And children have also been co-opted to promote *Kangoroo Jack* online : instead of waiting for children to send in the core of e-mails the URL of *Kangoroo Jack* official website to their mailing list, *Buzztone* wandered : "what if you can directly send the website to a friend ?" In the case of *Kangoroo Jack* promotion, a 60-Ko-light website was created with a lot of very light games. Children could then directly send in attached piece the entire website about *Kangoroo Jack,* and these websites were entirely traceable, giving valuable marketing information about the fans and the public. Kids were co-opted to help spread the word about the movie.

Thirdly Co-Creation of Value requires a brand new approach toward the value chain. *Buzztone* illustrates this concept by "Inventing new communication practices within existing and never developed channels". Steve Yanovsky has given the example of a new communication channel to be used for the promotion of *The Sims 2*, the sequel of the most profitable gaming franchise ever. *Buzztone* is working in partnership with *Electronic Arts* to create little characters inspired from the game to be released in 2004. These small characters will be downloadable on *The Sims2* website. These characters will be similar to the *Microsoft Office's* little animals that pop-up everytime an *Office* application is launched. They are called "Desktop Agent". Once installed on the system tray of the computer, the characters would give exclusive information about *The Sims2*, tips, links with the community of fans, and why not potential instant messaging features with other players. Messages delivered by the characters will be remotely controlled by *Electronic Arts* thanks to a remote connection to the internet. Hence information and messages could be updated on a daily basis and directly pop-up on the screen of fans who have installed them.[96] A consumer-centric approach was also adopted to invent this Desktop Agent. *Buzztone* started by answering this simple question : "if you target a 13-year-old girl, what makes her excited ? Boys, shopping, music, video". Therefore the Desktop Agent will also deliver messages about entertaining products.

2.3.2. A 100 % "underground" promotion is gaining momentum

The method of "word-of-mouth" is particularly well suited for entertainment products. When implemented and controlled perfectly, it is more efficient than any other marketing investment, so efficient that the expression of "viral marketing" is now employed. And the internet and new technologies make it the cheapest promotion investment. After the commercial success of the *Blair Witch projects*, recent promotion methods have capitalized on communities of fans and group of "trendsetters" to create the buzz around a movie. The "Change Agency" *Buzztone* has made innovation in marketing by targeting no more than 6,000 "trendsetters" to arouse the interest for the movie *The Ring* released in 2002.

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[96] Source : This three examples have been explained by Steve Yanovsky itself, Vice President of Buzztone, during a lecture at the University of Michigan Business school, October 17, 2003

Steve Yanovsky, VP marketing at *Buzztone,* explained during a lecture at the University of Michigan in October 2003 how they created a mysterious and communicative environment around the horror movie *The Ring*. There was no star acting in the movie, and it was a remake of an obscure Japanese legend with minimum customer awareness. The story of the movie is about a video-tape that kills seven days after having watched it. So *Buzztone* decided to make 6,000 copies of the video-cassette similar to the one that kills in the original movie. The video-cassette did not contain more indication than the short video clip that kills in the original movie plus a message announcing the date of release in movie theaters. The video-cassette was paint all black, just like the one in the movie, with nothing written on it. In order to be sure that the few copies would spread rapidly to create enough buzz, *Buzztone* went to trendy places in New York City like all types of bars and clubs, and simply put the videos on some tables without mentioning anything about it. People started to replicate it and even to sell it. The buzz was created. The first week of opening reached 70 million dollars.

In parallel, *Buzztone* made use of the internet and underground communities. The marketing team started by interviewing the author of the legend, to understand the big picture, target an audience, and learn about fans of the original legend. *Buzztone* built an official website linked with 6 parallel and false websites to create a mysterious atmosphere online. Some webmasters of obscure websites were contacted to distribute the trailer of the movie, because they were in good position to reach a potential public for the movie. During the first 7 days of exploitation of the movie, the trailer was also on the *Smashing Pumpkins* website, and a link to the official movie website was added on the *Rage Against The Machine* official site. Search engine such as *Yahoo !* were paid to automatically give the link of the movie official site with requests related to horror movies for instance. This method of promotion was so completely new that *DreamWorks*, which was producing the movie, became concerned about the real impact of such communication campaign.

But this method was rather cheap, fast and the word-of-mouth did work since the profits made by *The Ring* are around $200m to date. A sequel is currently in project. Another detail is even more striking : approximately two weeks after the beginning of the promotion, *Buzztone* received an unexpected visit at their New York office : The CIA (Central intelligence Agency) came to ask for explanation ! In fact, the copies were really widespread, and some reached the hand of CIA officers. A terrorist message was

immediately suspected given the type and the efficiency of the propagation method used by *Buzztone*. The investigation lead the CIA to *Buzztone*, confirming the importance of word of mouth and the potential unleashed when co-opting consumers to promote a movie.

2.3.3. Music and Movie Majors would benefit from the integration of virtual networks into marketing strategies

P2P networks are a new distribution channel. Anybody who wants to download the full collection of the *Budweiser* commercials "Wazaaaaa !" will turn to P2P networks to find them all. Considered as a marketing tool, P2P networks may be really efficient. For instance the French director of the movie *Blueberry* Jan Kounen has totally used *Kazaa* as a commercial tool : in January 2004, one month before the release date, Jan Kounen played a trick to P2P users to promote its movie.

Jan Kounen created a 20-minute video clip in Div'x format to be diffused on P2P networks. The clip was similar to the "behind the scene" or "making of" bonus to be found on DVD. This clip in itself is valuable because it could have been sold with the DVD. It features trailers, pictures, interviews of actors, and invite the viewer in front of his screen to discover the world of *Blueberry* one month before the release date. It works as a teaser and compare the experience of viewing *Blueberry* in front of a computer screen and in a movie theater. The name of the file could deceive P2P users since it looked like the movie ripped ("Blueberry.2004.DVD.Rip.Divx.Avi") with a size similar to the one of a CD-Rom (700 MO). Jan Kounen comments the initiative in this terms : "This video clip is a wink. It shows to P2P users the spirit of the movie *Blueberry* and explains the interest of watching it in the best conditions, the one offered by movie theaters."[97] At least the message was diffused across the country, and was an excellent way to get people talking about *Blueberry* before the release date.

As far as music is concerned, Tarik Krim, founder of the website *generationmp3.com*, explained in an interview for the newspaper *Le monde* that Music Majors would be well advised to consider P2P networks differently : "in the future, distributors of music will have to take into account the fact that consumers take part in marketing and promotion of artists". In fact,

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[97] Source : http://www.netconomie.com, *Blueberry veut instrumentaliser le Peer-To-Peer à son profit*, January 8, 2004

people who swap music online may not be a pure source of losses. The benefits from this activity could even outbalance the losses : "Music Major should probably rethink their marketing strategy, their management of Human Resources and their business model. Let's say in five years time, the person who will be capable of diffusing and sharing its interest for an album with millions of web surfers may be more valuable for Universal Music than the person who deals out CDs in music counters."[98]

This idea is gaining ground. Tom Mennecke for instance, who analyzes P2P trends for the Web site *Slyck* (*slyck.com*), said that "People (…) know artists aren't being hurt, and that in fact P2P helps artists by putting people in touch with their music." Example are numerous of people who have discovered unknown artists on the web, and offered albums to friends as a gift.

Websites such as *Friendster.com* are a good materialization of networks and their potential power. Every time a new friend is included in one's network, this friend adds his own network. Popular persons may easily count 10,000 persons in their network of friends and of "friends of friends". By targeting 5 to 10 influential consumers based on their personal profiles (that include age, address, favorites TV series, favorite artists, favorite movies…) and the size of their networks, entertainment companies would have the cheapest and most accurate marketing tool ever. Co-opting influential potential consumers (based on the size of networks) and "trendsetters" (based on tastes and their fame on P2P networks) will Co-Create Value in a marketing context.

Economic actors have already recognized the value of networking site such as *Friendster* : *Google* for instance would like to advertise on website specialized in networking and dating. *Google* has already bought the two community-related websites *DejaNews* and *Blogger.com* in order to promote its sponsored links *AdSense*. A former employee of *Google* is managing the site *orkut.com*, similar to *friendster*, and acknowledges some affiliation with *Google*[99]. Advertising directly on networking websites would enable *Google* to capitalize on the "word of mouth" effect.

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[98] Source : Tariq Krim, founder of a website dedicated to online music
http://www.Generationmp3.com, in an interview realized by the newspaper *Le Monde*, October 7, 2003
[99] Source : http://www.silicon.fr, *Avec Orkut, Google met un pied dans les réseaux sociaux*, January 23, 2004

Steve Yanovsky from *Buzztone* has built a whole marketing strategy on "word-of mouth" and its virtual equivalent feature "tell your friend". An online contest about the game *The Sims* was launched by *Buzztone*. Players were alerted by an e-mail that included a "tell your friend" feature. The game was launched by sending five e-mails on behalf of *Buzztone* for *Electronic Arts*. Five days later 100,000 e-mails had been exchanged about the game between players thanks solely to the "tell your friends" feature.

2.3.4. P2P networks can be co-opted to distribute entertainment products

Web surfers are Co-Creating Value with entertainment companies by lowering distribution costs. In fact, entertainment companies may lose money because of copyrighted file-sharing, but on the other side, they are lowering their costs of diffusion for instance. The business model proposed by *Apple music* store where users are spokesperson for an album or an artist will lower marketing costs of Music Majors. In addition online distribution networks are cheaper than retailers such as supermarkets.

When looking at the functioning of P2P network through the lenses of Co-Creation of Value, it appears that users participate in advertising for artists and in distributing content. In fact, P2P users are paying for distributing digital music, movies or software. By allocating a part of their hard drive to entertainment products and sharing them with other users through expensive broadband access, consumers are co-opted in a way by companies. They create value for companies because they store the products "for free" on their computer and become similar to virtual stores or virtual shop window. Steve Jobs itself, CEO of *Apple* said that "in the coming years the upload trend is going to explode : clients and servers are going to become exactly the same thing on the internet[100]." Several business models have been proposed to Music Majors to make sound money from these individual shop windows. One of the most advanced proposal based on this observation was proposed by the Distributed Computing Industry Association (DCIA).

According to Reuters, the DCIA claimed that "rather than losing millions of dollars in potential sales to online song swappers, the recording industry should give them a cut of the revenues when they distribute songs in a pro-

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[100] Source : *The Harvard conference on the internet and Society*, edited by O'Reilly & associates. Inc, distributed by Harvard University Press, March 1997

tected format." DCIA chief executive Marty Lafferty said record labels could see sales grow by 10 percent over the next four years if they embraced the new technology based on new protected formats. Each time there is a technology breakthrough in entertainment distribution, once it's harnessed and embraced and an industry finds a way to capitalize on it, the industry does enjoy accelerated growth," he said.

So what is this new protected format that would transform online song swappers into creators of value ? Under the plan described by the DCIA, record labels would encode their songs with copy-protection technology so users would have to pay a small fee, between 80 cents and 40 cents, to listen to them. Prolific song-swappers would be encouraged to convert their collections of unprotected material into the protected format, and then paid a portion of the fees collected each time somebody purchases a song after copying it from them. Eventually, user-friendly software would allow amateur musicians without recording contracts to make their music available as well, DCIA said[101]. This proposal at least shows that with some investments, the business model based on Co-Creation of Value would be able to take-off. Unfortunately, a spokesman for the Recording Industry Association of America said he had no time to look over the proposal and declined comment. In order to transform profits in losses, entertainment companies have to adopt first a consumer-centric point of view, then they have to acknowledge that some good ideas may come from consumers. This starting point will open better growth prospects.

New P2P software such as *BitTorrent* are extremely efficient to distribute large files. *BitTorrent* eases file sharing so that anybody with any type of access to the internet can pretty decently download large files : If *Napster* started the first generation of file-sharing, and services like *Kazaa* represented the second, then the system developed by Mr. Bram Cohen, known as *BitTorrent*, may well be leading the third. Firm numbers are difficult to come by, but it appears that the *BitTorrent* software has been downloaded more than 10 million times.

BitTorrent cuts up files into many little pieces, and as soon as a user has a piece, they immediately start uploading that piece to other users. So almost all of the people who are sharing a given file are simultaneously

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[101] Source : Andy Sullivan, Pay, *Don't Sue, Song-Swappers, Trade Group Urges*, http://www.zeropaid.com based on Reuters, February 5, 2004

uploading and downloading pieces of the same file. The practical implication is that the *BitTorrent* system makes it easy to distribute very large files to large numbers of people while placing minimal bandwidth requirements on the original "seeder."

The software designed by Bram Cohen has rapidly been recognized as a huge breakthrough by professionals. It has opened new opportunities for distribution, as confirmed by John Gilmore, the free-software entrepreneur, who had also been one of the first employees at *Sun Microsystems* : "Part of what matters to me about this is that it makes it possible for people with limited bandwidth to supply very popular files. It means that if you are a small software developer you can put up a package, and if it turns out that millions of people want it, they can get it from each other in an automated way." Said Mr. Gilmore in an interview with Anna Mia Davidson for *The New York Times.*

BitTorrent really started to take off in early 2003 when it was used to distribute a new version of Linux and fans of Japanese anime started relying on it to share cartoons. In fact, P2P networks are more and more specialized based on their technological features and the public they reach, similarly to usual distribution channels : *Soulseek* for instance regroup an active community of music lovers : rare music of all kind, including a lot of "homebrew" remixes are available. *BitTorrent* is a golden mine for cartoons and Japanese animation. *Kazaa Lite* is very popular among games and software "swapper"; *eDonkey* and *eMule* propose a lot of movies in several different langages.

BitTorrent technology is interesting to prepare future distribution network. For instance according to *The New York Times*, *Valve Software* is developing what gaming experts anticipate will be a blockbuster video game, *Half-Life 2*, but it is also creating an online distribution network that it calls *Steam*. Because of Bram Cohen's expertise in just that area, Valve offered him a job. "When we looked around to see who was doing the most interesting work in this space, Bram Cohen's progress on *BitTorrent* really stood out," Mr. Newell said. "The distributed publishing model embedded in *BitTorrent* is exactly the kind of thing media companies need to build on for

their own systems."[102] By co-opting P2P networks, the video game industry will create an online distribution network, for the benefit of everybody.

2.3.5. The "Kazaa Revolution" is a tentative business model that shows the way toward Co-Creation of value

Kazaa is claiming that a new type of cooperation between the entertainment industry, software editors and consumers would create a world where "everyone is happy". In fact, the Revolution explained by *Kazaa* is preparing the ground for a new business paradigm of Co-Creation. The description of the marketplace imagined by *Kazaa* is gathering most elements of Professor Prahalad and Ramaswamy Co-Creation paradigm. "This is how we [Kazaa] see the new marketplace working":

> - "Artists and copyright owners will protect their works with security technology. The works will be promoted to consumers via search tools and via peer-to-peer web pages. Consumers will download the files they think might be interesting. This depends on promotions, offers, and what they have heard is good from friends, web sites and magazines. " according to Kazaa Revolution.

This statement is the acknowledgement of the economic role of users in the promotion of artists and entertainment products. The acknowledgement does not means that money will be given by Music Majors to users and communities because they promote artists, but it rather means that some value is created by users because they are taking part to promotion, and therefore the final price may be lower for them because they have done part of the job of Music Majors by themselves.

> - Then *Kazaa* explained in its dreamt vision of the marketplace that : "They [the consumers] will try them out. Each file can have a different trial period set by the owner – 20 minutes, 20 days or 20 years. If the consumers like it and the price is fair, they will buy it. Fans are satisfied and artists get rewarded. Everyone is happy ! In the ideal world everyone is happy."

This method is providing access to copyrighted content without ownership. It is similar to the shareware system found by the video games and

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[102] Source : Anna Mia Davidson for The New York Times, *File Sharing's New Face*, www.zeropaid.com, February 12, 2004

software industry to enable constructive interactions : *Kazaa* is promoting a shareware system for songs or movies. This shareware or freeware system has worked well the software industry, so why not for the music industry ?

> - "Consumers are happy because they can get what they want, when and how they want it at a good price. Content owners are happy because their get paid when users want their content. And they get exposure to a vast audience, which may result in future sales through albums, merchandise and even concerts" according to *Kazaa*.

The experience environment has to be taken as a whole to define profitable strategies. Merchandise, concerts and any indirect products such as MP3 Player are part of the same environment. Music and Movie Majors may derive increased profits from these extensions of musical experiences if new partnerships are found to Co-Create value.

> - Lastly *Kazaa* explains that "Artists and content developers are happy because they also get fairly rewarded for their work and/or they get great exposure. And the peer-to-peer software developers are happy because they get paid, which means that they can continue to develop peer-to-peer applications so everyone can benefit. This revolution can be for everyone !"

All stakeholders have been taken into account. The point of view of *Kazaa* is not the one adopted traditionally by companies, since it is rather a decentralized one. It means that value can come from several sources and entertainment companies have not the monopoly of value creation.

3. New partnerships will help the Co-Creation model to take place

3.1. Integrated into a nodal network organization, economic partners will provide customizable solutions

3.1.1. New type of synergies will link economic partners in the network

An organization in nodal network as described in the second chapter provides entertainment companies with the flexibility and the expertise mandatory to Co-Create Value. Most entertainment companies today do not own the entire value chain, although such ownership would be necessary in current business configuration to pass the feedback and the personalized

needs of final consumers on to "suppliers". Such ownership of the entire value chain would create gigantic group that may be not well suited for providing consumer-centric solutions. Hence a structure in nodal network based on partnerships avoids the needs to control the entire value chain. This structure provides personalized solutions while acknowledging the fact that traditional value chains are collapsing and replaced by value networks.

Partnerships, that give access to expertise without ownership, will allow nodal companies to pass the feedback of final consumers on to "suppliers", artists or production companies. Industrial synergies are not numerous enough to merge these business partners into a giant group. Therefore simple alliances that generate other types of synergies are better suited : "Experience Synergies" are appearing when people look at sectors with a consumer-centric point of view and not a traditional industrial point of view : Experience Synergies exist for instance between Internet Service Providers and entertainment content provider. These new types of Experience Synergies between two sectors are sufficient for them to make an alliance. Whereas industrial synergies maybe be better suited to justify a merger.

The concept of Synergy of Experience means that every company in the network is a stakeholder in the experience environment around the product delivered by the nodal company. It means that every company in the network play a role at any time when the consumer is experiencing the entertainment product. So the nodal network organization is driven by Experience Synergies that justify partnerships.

When considering at Experience Synergies, alliances between *Comcast* and *Disney* for instance make sense. Content from Disney for instance are available on P2P networks, and Comcast provides access to P2P through its ISP function. The merger between *AOL* and *TimeWarner*, in addition to some marketing synergies[103], has generated huge Experience Synergies.

3.1.2. Guidelines to become a nodal company

Analyzing the network around digital music is a good starting point. More and more consumers turn to *Apple Music Store* when they want a musical experience. When adopting a consumer-centric approach, it appears

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[103] Described in Chapter 2, part 3.2.3

that the stakeholders may be more numerous than solely the music industry. One possible illustration of the buying process of a song on *Apple iTunes* is detailed below, adopting a consumer-centric approach :

- First an artist is signed by *EMI Music* for instance. (It is not the purpose of this example to go through the whole process of distributing an artist, but rather showing the diversity of interactions)

- Then *MTV* diffuse the video clip that is heard for the first time by consumers

- Possible next stage, the magazine *Rolling Stones* gives very good critic about the artist and is read by potential consumers. The potential consumers still hesitate to buy the song

- Then bench of friends who receive the newsletter from *RealNetwork* about music have talked about it. The song is definitely worth it

- The next step once the decision to buy the song is taken is to connect to *Apple Music Store* thanks to *Comcast*, ISP

- After chatting online with people on *iTunes*, consumers buy the song

- Finally the song is downloaded and transferred to *HP* MP3 player, and copied on a CD with a *Phillips* CD-Burner

The different stakeholders in this experience environment have in common a direct or indirect interaction with the final consumers : Hence Experience Synergies between the various actors that will take form into a consistent nodal network organization. By linking all the diverse companies mentioned in this example, the nodal firm will be in position to deliver a global, comprehensive and personalized experience environment. The nodal firm will be able to ensure that there is homogeneity when needed between the various stakeholders brought into the same experience environment by this typical consumer. It means for instance ensuring compatibility between formats used in the entire experience environment. The nodal company is then in a good position to provide a personalized experience that includes in this example portability, but not HiFi environment for instance.
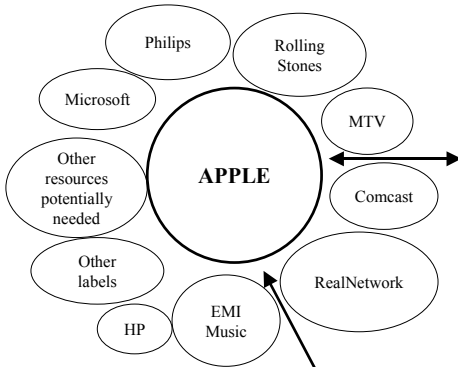
Before drawing the diagram of this particular experience environment, a simple question need to be answered : which of these stakeholders is the

nodal firm ? Similarly to the case of any network such as the internet, the nodal firm may change at one time since it is a decentralized business model with a decentralized value chain. But some factors may point out which company is in a better position to be the nodal firm and to work as conductor in a given configuration :

- First the direct contact with consumers is key : the nodal company is in position to interact directly with consumers and ideally collect individual feedbacks

- Second a critical position in the network : it may come from a patent, a technical standard, a monopoly etc…

- Third close links, partnerships or alliances with most stakeholders of the nodal network

- Four the nodal company is nurturing a community

In our example *Apple* complies with these four requirements. In addition *Apple* is providing personalized shopping experience through *iTunes* and a personalized experience environment by being able to put together the expertise from Music Majors, electronic device manufacturers, ISP, operating system designers, and a large community of fans. For instance *HP* computers come bundled with *iTunes* software since June 2004, and A*OL* has agreed to offer a music storefront based on the *iTunes Music Store*. The diagram of this experience network is the following :

Nodal Network　　　　Personalized Experience environment

Philips
Rolling Stones
Microsoft
MTV
Other resources potentially needed
APPLE
Comcast
Other labels
RealNetwork
HP
EMI Music

Digital TV set
scanners
Fax
PC
Interactive TV
WEB TV
Laptop
Printers
CDBurner
Tablet PC
HDTV
Satellite TV
Graphic cards
PDA
Reality TV
Pay per view
Home networking
Hard drive
Memory card
Flat display
Video rental
Digital jukebox
CD Rom
USB Key
Movie theater
Digital camera
DVD
Home Theater
Cable TV
Handheld
CD
Digital camcorder
MP3 player
Online music store
Mobile operator
Voice through IP
Internet provider
Specialized press magazine
Online games
Wifi device
Smartphone
Stereo system
E-mail
P2P software
Electronic toys
Game console
Multimedia edition software
Cell phone

Apple iTunes Community

A company may be the nodal firm in a given network, but also be a simple economic partner in another network that does not require the same type of expertise. The reversal proposal is also true : Music Majors are nodal companies in the case of an experience environment built around their "traditional" distribution channels.

3.1.3. The High tech industry will grandly help the entertainment industry to provide a personalized experience

If entertainment companies want to make the most of the new paradigm of Co-Creation of Value, partnering with Hi-tech companies is almost mandatory. Most Hi-tech companies have the capacity to handle individual feedbacks from users. They also have direct access to final users. They have established technological standards that involve them in any decisions. Whereas entertainment content seems to have been more or less "commoditized" over the last few years[104].

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[104] This expression has been used by Michael J. Wolf in the book *The entertainment economy : How Mega-Media Forces are transforming our lives*, Times Book edition, 1999

Digital music could have been integrated into a nodal network with mobile phone network operators, TV networks operators, or even internet networks operators as nodal company. In fact, the business model would have consisted in using entertainment content to sell network subscriptions. But far more valuable economic partners have disturbed this mutation. Entertainment companies would have earn less money than partnering with software editors. Rather than pipes, software editors as nodal companies seem to offer more profitable perspective. Digital music is taking off thanks to software editors : Apple with *iTunes, Napster2* from *Roxio*, *RealOne Music Store* from *RealNetworks*, and other digital music servers based on Windows Media software from *Microsoft*. So software editors are partnering with Music Majors, but also with electronic devices manufacturers : *Roxio* with *Samsung*, *Microsoft* with *Creative*, *RealNetworks* with *Nokia* and *Palm* ; *Sony* and *Apple* on their side have the internal expertise to propose their own electronic devices. Experience Synergies are driving these numerous alliances : all these companies may be part of the same experience environment at one time or another.

The Picture industry may face the same issues when digital formats will be widespread. Some companies have made strategic moves in this direction to prepare for the future : *Microsoft* is partnering for instance with *Disney* to distribute digital movies on the net. *Microsoft* will also propose a portable media center compatible with its proprietary format, to be sure to be a nodal company in the distribution of movies online. Agreement have also been signed between *Warner Bros* and *Microsoft*, *Universal* may join the partnership later in the year. *Microsoft* is then preparing a future nodal network based on the model of *Apple music store* but for movies. The Asian consumer electronics manufacturer *Creative* has already agreed to use *Microsoft* operating system called *Windows Mobile for Portable Media Center* for its generation of multimedia jukebox called *Creative Zen Portable Media Center* released in June 2004. *Microsoft* has understood that these various expertise will be needed to provide customers with the experience they are looking for. Consumers may have a bad experience if one part of their experience environment is not compatible with the other. It is all about adopting a consumer centric approach and focusing an experience, not an product.

The configuration of the experience environment described above may evolve as new standards and new technologies will appear : for instance the spreading of 3rd generation mobile phones allowing large broadband trans-

fers and web surfing may be a new deal. In Japan where mobile phones allow broadband transfers, e-mails, instant messaging services and allow to browse a "simplified internet" called I-mode, mobile phone operators have become nodal companies : A telling example of this configuration is the alliance created in February 2004 called "ubiquitous Open Platform". Fourteen firms have signed this alliance to create common standards for electronic devices' access to the internet. This partnership will reduce costs with a single shared standard among the industry. Electronic devices will not have to be compatible with several technologies at the same time. Satoshi Ishiyama, Vice President of *NTT*, the leading Japanese phone operator, is managing the alliance. The other members are *KDDI* (competitors of *NTT*), *Hitachi, Matsushita Electric Industrial, Matsushita Electric Works, Mitsubishi Electric, NEC, Pioneer, Sanyo, Sharp, Sony, Sony Communications Network et Toshiba,* and *Nifty* (leading ISP in Japan). This alliance is preparing a nodal network structure including ISP, several mobile phone operators, networks operators, and consumer electronic manufacturers. All these partners have Experience Synergies since they may be included at some point in the same experience environment. Therefore they all HAVE TO be compatible with one another in order not to break the experience environment.

Devices, software or companies that propose made-to-measure experiences will always be in a good position to become nodal companies. There will always be people reluctant to interact with companies, but young people who will be adult very soon will require interactions. The PCs or in the future the mobile phones may replace the TV set in the leaving room. Partly because they offer more personalized experiences than television, and also because they are part of the same experience environment. *Dell* for instance is manufacturing computer monitors that can also be flat TV sets[105]. *Microsoft* initiatives with the *Windows Media Center* are building bridges between PC and TV. In France, three ISPs are offering cable TV and traditional TV channels on PC through simple internet cable connection. *Sony* is also building bridge between the two environment because the new *PS2* transforms the TV into a PC by allowing to record programs on a 250Go hard drive and to burn them thanks to the DVD-RW burner included in the *PS2*. The design of new computers and computer screens are well suited for an exposure in the leaving room. The boundaries between the two worlds are progressively

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[105] Source : Kevin Maney for USAToday, *Dell to dive into consumer electronics market*, September 25, 2003

erased because of Experience Synergies between this various entertainment products.

3.2. Co-Creation of Value is also at the crux of the cooperation between companies

3.2.1. The entertainment industry and consumer electronics manufacturers Co-Create Value together

This two sectors have been considered separately for too long. Today they have been brought together by new consumption habits. When taking a consumer-centric view, it appears that this two industries are tied in the same experience environment. But their core products and expertise are totally different. Therefore there are no industrial synergies, but alliances make sense.

When unified in a nodal network, these two sectors create value for each other. The picture industry and home theater manufacturers are a telling example : Special effects are becoming more and more common in movies today. The increased budget of recent blockbusters helps to make movies that are more and more spectacular, gorgeous, visually moving. HDTV, flat screens, home theater devices, or the DVD format would not have taken-off that rapidly if blockbusters were not so visually advanced. The score of most movies are so refined that an audio quality close to CD quality is almost necessary to fully enjoy it. Hence the development of Surround sound at home. The reverse statement is also true : by lowering the price of flat TV, DVD-players and home theater devices, the hi-tech industry is fostering the sales of DVDs.

The video game industry is also creating huge value for PC manufacturers. First new gaming consoles such as the *X-Box* or the *PS2* are offering high quality graphics that almost require large TV screen to really enjoy them. In addition, by developing games that are more and more avid for performance, the gaming industry is driving the renewal of PCs every two years on average. By setting up a minimum configuration that increases continuously with each new games, the gaming industry is indirectly forcing consumers to buy new computers. Today computers bought two years ago are barely meeting the minimum configuration needed to decently run recent games. The reverse statement is also true : by increasing the performances of graphic cards for instance, the hi-tech industry is trans-

forming the sequels of a successful game into a brand new games totally improved. PC manufacturers and video games publishers are in the same experience environment, and therefore they Co-Create Value. This concept is true between companies and consumers, but also between consumers and consumers, and between companies and companies. The nodal network configuration is similar to the configuration of the "network of the network": on the internet, clients may become servers, and servers may become clients. There are mutual benefits from any interaction.

3.2.2. Cooperation between the mobile phone industry and entertainment content providers is valuable for both actors

In order to anticipate what could be the future of the mobile phone industry in the U.S and Europe for instance, one could observe what has happened in Japan with the 3rd generation of mobile services available since the end of 1999. The number of sites on *I-mode* has soared, as explained by Takeshi Natsuno, one of the founder of the I-mode : by the end of 1999, only 67 companies had created an *I-mode* site. By the end of October 2000, *DoCoMo* counted 1200 official *I-mode* sites offering services from 665 companies. In addition, 28,000 "voluntary sites" have been created by individuals. Along with the increase in subscribers, the *I-mode* attracted more and more content providers, which attracted more and more subscribers…

DoCoMo's success is based on a deep understanding of the links between entertainment and new technologies. *DoCoMo* has taken into account the experience environment as a whole to bring together sectors that may not seems to be complementary at first sight. The example of restaurant reservation is a good illustration of it : the *I-mode* user finds a restaurant in the I-mode restaurant guide. Screens in I-mode have a "phone to" function. Therefore all what the user has to do is press the "phone to" button to dial it and make a reservation. That is not possible on a personal computer : it takes a mobile phone (a device that combines access to the internet with voice communication functions). The consequence is that *I-mode* subscribers uses their mobile for voice communication 20 % more than the non-subscribers. This idea could not have been possible without adopting a consumer-centric view, and realizing that it would be neat to make reservation once a restaurant is found : Experience Synergies made it happen.

The rise of *I-mode* and the increase quality of content had impact on the manufacturers of mobile phones because it has generated replacement de-

mand. When new services are made available, new mobile phones capable of utilizing the new functions are needed. For instance *Bandai* started a new service that consisted in sending out cartoon characters over *I-mode*. This was only compatible with one type of mobile phone from *Matsushita*. But the success was immediate. This new services has generated the obligation for mobile phones to be able to display downloaded visuals from *Bandai* site. This process is similar to the boom of new ring tones parallel to the development of mobile phones with multichord sound generators. Value is Co-Created between content providers, mobile operators and mobile phone manufacturers : the development of one service, one offer, one technology drive sales for the group as a whole since splits between sectors do not exist in the experience environment of consumers.

More original mutual benefits have emerged such as the linking of *I-Mode* with *Playstation* to play some specific games indifferently on the two platforms. This alliance between *NTT DoCoMo* and *Sony Computer Entertainment Inc*. is a win-win situation as explained by Takeshi Natsuno : "as in the case of car navigation systems, the immensely larger TV screen provided another opportunity to compensate for the limitations of the I-mode display (…) Naturally, there were benefits for *PlayStation*. An alliance with I-mode would expand the time available to play *PlayStation* games beyond time spent at home." By linking mobile phones to the *PlayStation*, we can imagine new types of interaction such as receiving on the mobile phone a code or a key that unlock an hidden character of the *PlayStation* game for instance. Opportunities for transforming any standard copy of a game into a personalized and immediately adaptable experience are huge.

3.2.3. Other nodal network configurations offer Experience Synergies to the entertainment industry

If some source of profits seems to decline for the entertainment industry such as the one coming from distribution activities, other configuration and partnerships offer new profits. When adopting a consumer-centric approach, the problem of music swapping on the internet brings more value than it destroys. At least when the necessary adaptations are made to derive value. Those who download the most are maybe the most active fans of an artist. Profits coming from concerts and live production have been following the same trend as the development of P2P networks over the last few years. Part of the money that is not spent on CD is spent on concerts. And concerts are the best way to create emotional links between fans and the artist. Through

P2P expansion, the best artists have seen their public increasing and the activity of fans soaring. Today Music Majors do not derive a lot of money from concerts[106], according to Eric Tong Cuong, Head *EMI Music France*, but maybe new type of cooperative work would rebalance the profits coming from concerts.

If music fans are changing their consumption habits, an adjusted experience environment may be proposed : When setting up online activities, a lot of companies need to add entertaining content to create traffic on their websites. An alliance between two different sectors such as food and entertainment reveals that business boundaries have been reshaped : if *Pepsi* wants to get traffic, they have to constantly provide new content to consumers. And *Pepsi* are ready to pay for the content whereas most consumers are looking for free fun on the internet. Hence if money cannot directly come from final consumers, why not partnering with other stakeholders in the same experience environment to derive value indirectly ?

A similar starting point is tried by *Sony* : *Sony* is thinking about developing a strategy for its online music store called *Connect* and its MP3 players that make the most of the evolving musical experience environment. Jay Samit, general manager of *Connect* interviewed by the *Wired magazine*, is giving the example of a new type of cooperation : "The example would be, you go to a specific retailer, like a bar or coffee shop, at a specific time and content is made available to you for free and delivered straight to your Wi-Fi-(enabled) device. The bar or coffee shop would now pay Sony Connect and we, in turn, would pay the artists." He added that *Sony* is working on developing Wi-Fi devices, handy for selling music to hipsters who hang out at cafes and university campuses, and for some cities[107]. This type of strategy shows the flexibility and opportunities offered by a network of economic partners. The starting point is always the consumer to define economic links based on Experience Synergies.

The video games industry is also looking for new partnerships that co-create value : The video game industry has been benefiting from an exchange of expertise with the Music industry and the Picture industry over

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[106] Source : Eric Tong Cuong, Head of EMI Music France, in an interview with *Le Monde*, October 3, 2003
[107] Source : Kate Dean, *Music Gadgets Get Smaller, Sexier,* http://www.wired.com, January 19, 2004

the last few years[108]. Until recently, music that goes along with video games was created partly by the video game team project itself, not as skilled as professionals. Now the most successful games are featuring music from professional bands such as *Rage Against the Machine* in gaming franchise like *Tony Hawk*'s skateboarding games. Mark MacDonald, executive editor of *Electronic Gaming Monthly*, pointed to *Electronic Arts*' hit, *Def Jam Vendetta*, a wrestling game with hip-hop overtones based on licenses from the *Def Jam record label*, as one sign of games' increasing "crossover power". He also pointed to games such as the current bestseller, *True Crime: Streets of LA*, which features rap star Snoop Dogg as well as voice-overs by actors including Christopher Walken and Quentin Tarantino movie veteran Michael Madsen[109]. This "crossover power" mentioned by Mark MacDonald refers to the extended experience environment handled with new partnerships to compose a nodal network.

According to John Hayase, project manager at *EA games* for *Tiger Wood 2004*, the music industry has understood that during games, players are totally emerged in the virtual world. Listening to the same song every hour during the game will have at least a huge marketing impact. Some CDs that regroup the music of a particular games have even been released with success. In recent games such as *SSX3* on *Xbox*, the title of the song and the name of the artists appear on the screen while playing the game, a bit like an *MTV show*. Famous music songs from *Placebo, N.E.R.D, Fatboy Slim* or the *Chemical Brothers* are part of the musical environment of *SSX3* game. In games like *GTA3*, players can choose to listen to a specific type of radio (such as Rn'B, rock, rap…) while playing the game. John Hayase explained during a lecture at the University of Michigan business school last year that there is a whole group of people at *Electronic Arts* doing nothing but signing music bands or sports rights or movie licences.[110] They have understood that music is part of the experience environment of video games. Consumers are not bothered by the "industrial" split between the two sectors. This split

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[108] Source : John Hayase, Director of Development of Tiger Woods PGA TOUR 2004 at Electronic Arts, during a lecture at the University of Michigan Business School, October 1, 2003
[109] Source : Suneel Ratan, *What Gamers Want : Year in Review*, Wired magazine, http://www.wired.com/news/games/0,2101,61682,00.html, December 23, 2003
[110] Source : John Hayase, Director of Development of Tiger Woods PGA TOUR 2004 at Electronic Arts, during a lecture at the University of Michigan Business School, October 1, 2003

only exists when adopting a firm-centric approach, inadequate to deliver maximal value to consumers, and maximum profit for the company.

The video game industry is also capitalizing on the expertise of the Picture industry. For instance the latest game from *Atari Driver3*, to be released in May 2004, has benefited from the expertise of the directors Tony and Ridley Scott : *Atari* has signed an agreement with *Ridley Scott Associates* to realise three shorts clips of one minute around the universe of *Driver3* to promote the game. These clips are three parts of a short story called *Run the Gauntlet.* Six teasers of 30 seconds each will also be release to create the buzz around the clips and ultimately the game. In addition to these type of initiatives, action movie actors are bringing their expertise in fighting scenes to add some realism to video games. Expertise is shared between stakeholders of the same experience environment.

Lastly TV channels are also part of the experience environment of video games. They are fully integrated into the experience network of video games through specialized TV programs related to games. The exchange of expertise has become common. The broadcast network *UPN* has entered the game market with *Game Over*, a prime-time, computer-generated program set to begin by March 2004 according to *wired.com*. The half-hour comedy, which features the voice of Lucy Liu, takes place within a video game universe in which race car drivers and archeologists come home after a long day at work and deal with life in the suburbs and raising kids. David Sacks, executive producer at *Game Over,* explains that "The thing that excites me most about video games today, and I've been playing since the days of Pong, is that visually, games are entertaining just to watch. We have a big-screen TV in the office and there's always someone playing the latest game on it. You can't help but stop and watch the games these days." Games can be passively experienced as any TV programs.

Fox, another broadcast network, appears to be taking a hard look at game-related programming. According to *wired.com*, the network signed a deal with *The Sims* creator Will Wright that gives *Fox* the first opportunity to purchase original TV projects currently in development. Although the deal is not specifically for game-based content, it is the first door opened to video game creators looking to shift to network television production[111]. A

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[111] Source : John Gaudiosi, *TV Execs Go Gaga Over Gaming*,
http://www.wired.com/news/business/0,1367,61627,00.html, December 17, 2003

cross-fertilization has taken momentum between the gaming, TV, picture and music industry. Simply because these four sectors are part of the same experience environment called "Entertainment". The entertainment industry will generate more and more alliances between this four sectors in the future to meet the demand for increasingly complex and advanced experience environments.

3.3. The threat was brought by The Internet and the New technologies, but they represent the biggest opportunities for future Co-Creation of Value

3.3.1. Artists, Consumers, Music Majors and ISP together : AIR, AOL and Virgin Music France initiative

Until recently, the Music and Movie industry have been arguing that Internet Service Providers (ISP) have benefited unilaterally from the spread of copyrighted content on the internet and the advent of P2P networks. Therefore they claim a right to earn some royalties on broadband subscriptions. This solution is firm-centric and do not encourage to further cooperation between ISPs and the entertainment industry. However since the beginning of 2004, the situation is evolving on both sides, and the entertainment industry starts considering the internet as the drive for future growth. The success of *Apple iTunes* has shown that a lot of money could be made online, for the benefit of everybody. This was a first step toward Co-Creation of value, between the hi-tech and the music sector, with consumers co-opted in the *Apple Music Store* type of functioning.

A second step has been realized in March 2004. The French Music group *AIR,* the ISP *AOL* and *Virgin Music France* (owned by *EMI France*) have created a new type of interactive concerts online. Called "Interactive Web-show", this event is exclusively for *AOL On Demand* services customers. The music group AIR has given a four-hour live concert broadcasted on *AOL On Demand* : therefore this concert can be viewed at any time on demand using the streaming technology. At the same time, viewers have the possibility to choose from which point of view they want to watch the concert or add personalized backgrounds or their own pictures to the scene. Hence consumers can individualized their experience at any time. *AOL* benefits from the expertise of *Virgin Music France* in broadcasting concerts. *AIR* and *Virgin Music France* gain access to an additional paying audience online.

Viewers will then have the opportunity to create their own video clips based on the video of the concert. Fans of *AIR* are invited to create a video clip for each of three specific titles of the album *Talkie Walkie* performed during the live concert. Several tools are at the disposal of the viewers such as animation, special effects, transitions, different views of the same live action, numerous pictures and additional video clips of the artists. Of course these bootlegs can be shared legally with anybody.

Lastly web surfers are invited to reward the five best "homebrew" video clips. *AIR* has announced a "surprise" for the winning video clip, maybe a contract to realize the next video clip of the group. Consumers have been co-opted to promote the music group by diffusing their own video clips of the concert on the net, to their friends, on P2P networks, without any legal restrictions. *AOL* generates additional traffic on its site by hosting the competition. And *AIR* and *Sony Music France* may use the winning video clip for "official" purpose.

This initiative is the sign that mentalities are evolving. According to Gwenaëlle Mordelet, VP Business Development-Entertainment Opportunities at *AOL, "*We [AOL] want, in cooperation with Music Majors, to create new forms of promotion of artists and to bring additional interests and bonus by using interactive and innovative methods brought by the internet." So ISP can create value for Music Majors by offering new tools coming from the internet and the New technologies. Christophe Palatre, VP Marketing at *Virgin Music France* adds that "by offering this concept [of Interactive Webshow] Virgin Music wants to get closer to artists, while setting up innovative methods of promotion"[112]. This successful initiative will give birth to similar actions in the future. Co-Creation is taking off.

3.3.2. New technological formats are under experimentation to protect Intellectual Properties and boost Co-Creation of Value

In the past, the software industry could resist piracy and co-opt consumers by creating the shareware format. Thanks to this format, consumers could experience most products legally before buying them, or buying another version of the software. Which solution do people have today to

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[112] Source : Jérôme bouteiller, *AOL et Virgin Music testent un nouveau format promotionnel musical*, http://www.neteconomie.com, and also Max Verbatim, *AOL et Virgin lancent le Web Show interactif*, http://www.silicon.fr, February 28, 2004

experience a movie before buying it ? How can they promote it, and there-fore co-create value, if they do not have access to it ? Access is key in the Co-Creation business model to interact in the development of a personalized product at different stages of its conception. So to Co-Create value, the entertainment industry may have to find a solution similar to what the software industry did. The biggest problem of the entertainment industry today is the non protection of copyrighted content online through easy transfer of ownership : with P2P networks, access equals ownership. So the entertainment industry has more or less decided to ban any access to P2P network, making Co-Creation more difficult. By adopting a format similar to the shareware format, not only would the entertainment industry promote its content by diffusing it without any restriction, and also would make money from customers willing to transform limited access into full ownership.

Solutions are under study to ease access without ownership and therefore Co-Creation of value. For instance the software editor *Adobe* has announced that the future version of its successful software *Acrobat Reader* will include advanced copyright management features. The *Acrobat Reader* format is widespread on the net to exchange electronic documents such as e-books for instance. By the end of 2004, users will have the opportunity to trace the diffusion of their content, to limit the use in time, and to remotely unlock any protection.

As far as video are concerned, the boom of streaming technologies enable access without ownership. In 2003, 7.8 billions of hours of video have been officially streamed online, which represent an increase by 104 %. *Real Networks, ESPN*, *AOL* and *Yahoo !* accounts for a vast majority of the streaming market. Musical video clips represent 33 % of the content streamed, news 28 % and sport 17 % according to *AccuStream iMedia Research*.[113] The Entertainment industry largely benefits from this trend that illustrates the fact that "On Demand" access to entertaining content is highly valuable.

The development of a new generation of mobile devices such as multimedia jukebox, PDA, laptop, or mobile phones offer access to content. But this access is limited in capacity, time and space. Except if users already own the content copied from a computer for instance. This is one of the reasons why people look for downloading content online rather than streaming

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[113] Source : AccuStream iMedia Research annual report, quoted by silicon.fr

it : to access content anywhere at any time, they HAVE TO own it. Would file-swapping be that spread if people do not need to own content at first to access it on the go in a second time ? In the future, new technologies will make ownership, and therefore uncontrolled file-swapping obsolete, are at least unnecessary :

- With the development of third generation mobile phones and advanced multimedia services such as high quality video streaming, content will really be available at anytime, anywhere

- With the advent of Wifi connections and hotspots around the world, people will be able to stream content really everywhere

- More and more wireless devices such as PDA, multimedia jukebox, watches, camcorders will be internet-ready, and will offer streaming possibility

Many scientists explain that within 10 years, the internet will be comparable to electricity. Any device will be provided with the internet, the same way they are provided with energy. So access to servers and therefore entertainment content will have no more spatial or quality limitation. It will no longer be an issue. And therefore owning entertainment content will no longer be necessary to access it wherever and whenever consumers want. Accessibility is far more controllable than ownership, and it enables Co-Creation of value.

We can even imagine in the very long term, and this is my own personal view, that individuals will no longer own digital content, which will make file-swapping and the spreading of protected content impossible. The reason is that as long as access is granted at anytime, anywhere, it will not change the experience of entertainment products for consumers. Is ownership different from an unlimited access at anytime and anywhere ? We can also imagine remotely controlled and personalized access to content. *NTT Docomo* is experimenting a similar type of functioning with *Sony Entertainment* : *Sony* can communicate with a *Playstation 2* connected to an *I-mode* mobile phone : then digital keys can be sent on the mobile phone to unlock the access to a level or a special character of a game on *PS2*. Access is remotely controlled and individualized experiences are created[114].

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[114] Source : Takeshi Natsuno, *I-mode Strategy*, Wiley edition

Another initiative may pave the way for a new management of Intellectual Property (IP) : *Nintendo* is experimenting a new device and a new distribution method to address the gigantic Chinese market : IP is hardly respected in China and piracy is very common. Nine games out of ten sold in official retail stores are faked copies. So how can *Nintendo* support the idea of addressing the Chinese market and being profitable at the same time ?

First Nintendo decided to make extra money on games already profitable. So they decided to adapt successful games coming from the Nintendo 64 gaming platform, rather than the new GameCube console. Therefore games' prices are really low and affordable, even for the Chinese market. The gaming console is called the *iQue,* which means "the toy of gods" and costs $60. It is an advanced joypad to plug onto the TV set. It features a 64 Mo "flashable" memory card to store several games. Games have no physical support : when one wants to buy a new game, one goes to an *iQue Depot* (a simple terminal hosted by most supermarkets) with its memory card, and loads the new game directly on its card for an average of $5. At the same time terminals deliver a key to unlock the protected game. In the future, it will be possible to buy and directly load games from the internet on to the memory card.

The business model used in China by *Nintendo* is different from the usual one since only already-profitable games are sold, cheaper, and no physical inventory is needed for games. In the future, the internet will enable to further decrease distribution costs. *Nintendo* with this business model co-creates value with consumers : Consumers in the future will support the cost of the distribution of games by paying ISP to access the downloading platform of the *iQue* online. We can also assume that very rapidly a community of active fans will develop their own games to be downloaded. But what if the operating System of the *iQue* is hacked in the future and people can download games without paying on the internet ? *Nintendo* has a created an Operating System (OS) for its joypad called UOS for Updateable Operating System. Therefore an update of the *iQue* may be realized in *iQue Depot* in the future. Releasing an update enables for instance to continuously repair the flaws or weaknesses in the OS used to hack the machine. Updated and therefore "fixed" OS may be mandatory for instance to play new games. Therefore hackers would be counter-hacked. This feature will be adopted for the OS of the *Microsoft Xbox2* too.

Solutions are under experimentations to protect Intellectual Property and content owners. New technologies are creating additional opportunities of development for the entertainment industry rather than being responsible for currently sloping financial results. It is all about interpreting signs and being flexible enough to build on them.

Conclusion

Several signs show that the internet and the New Technologies offer interesting growth prospects for the entertainment industry. Even if at first sight the internet and the new technologies are a threat for future profits : According to Jana Monroe, assistant director of the FBI's Cyber Division, the four industries : music, movies, software and video games suffer $23 billion losses each year because of piracy.[115] One may consider this fact as a source of even bigger losses in the future. Or a huge opportunity if the so-called "pirates" are co-opted to Co-Create valuable Experiences.

Who are pirates or hackers ? People who make new things from old, people who notes an error and build on it, so people who creates better products. And in an industry where creation, and even more creation of better products is highly valuable, hackers are of the highest value for the entertainment industry. Hackers are consumers that reconstruct the products of the entertainment industry to adapt them to their own needs. They individualize products for them and for other consumers. And this personalization can be valuable also for companies when managed legally and fully integrated into a business model. Hackers would then be called "most active consumers". Claiming that they are source of losses today is true, since most firms consider that they have the monopoly of value creation as explained by Professors C.K Prahalad and Ramaswamy[116]. Hackers are outside the value creation process, so the value they create is in competition with the value created by the entertainment industry.

The Museo Nacional Centro de Arte Reina in Spain has even dedicated an exhibit to hackers in February 2004. Its name is "Hackers : The Art of Abstraction". It explores the connections between hackers, artists and anyone engaged in any kind of creative work as reported by Wired Magazine.

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[115] Source : Katie Dean, *RIAA's new seal of disapproval*, http://www.wired.com, February 19, 2004
[116] Source : C.K Prahalad and Venkatram Ramaswamy, *The future of Competition : Co-Creating Unique Value with Customers*, Harvard Business School Press, 2004

According to Jenny Marketou who has co-organized the show, "Culture is only a big, endless plagiarism in which nobody invents anything. People only rework, and this reworking happens collectively ; nobody creates anything alone."[117] Hackers are at the heart of the Co-Creation process.

Hackers are mastering new technologies. They challenge the status quo and help to improve services offered to consumers. They are lead users. They are a great source of learning since they fill their needs by adapting products themselves. But their needs are not different from the ones of other consumers probably less skilled. Understanding hackers, lead users and new technologies is more efficient than any market study.

The entertainment industry should not be afraid of what hackers and other various stakeholders like to call a "revolution". Revolutions in history usually end up with a reallocation of the roles of everybody. Consumers are claiming a part in the value creation process. The Entertainment industry has now the tools to understand this claim. It has also been provided with the basics to start building a profitable business model out of it. Kaleb Kain, who works for StartNow.com[118], has studied twenty years of file-swapping : His conclusions are not mentioning the Co-Creation model as a way to explain this revolution. However, his final ideas are very similar to the one proposed by Prahalad and Ramaswamy. They have interpreted signs and defined concepts to rationally explain the current revolution. They have putted names on changes that nobody can deny. The onus now is on the entertainment industry to catch opportunities highlighted by the new paradigm of Co-Creation.

The conclusions of Kaleb Kain about the current revolution also mention that opportunities are there for the taking : "Peer-to-peer file trading is just the beginning of the revolution. The question is : will the software, music, and movie industries be willing to adapt and profit ? The software industry has taken measures to provide the consumer with what they want. Most software creators provide the user with full demos and reward their consum-

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[117] Source : Michelle Delio, *Every Bit Is a Work of Art*, http://www.wired.com, February 27, 2004

[118] Kaleb Kain is an editor for StartNow.com, a web portal. He is working with high traffic websites to promote the future of P2P networking. On February 1st 2004 Superbowl Sunday, he has released The Great File Trading Survey on Warez.com and other P2P sites. This survey gathers data to show the file trading practices of the world and eliminate any myths. Results are available for the entertainment industry to view. Email : kaleb@warez.com

ers with discounted upgrades. The music industry is actually beginning to get the picture. The growing success of satellite delivered, commercial-free, music channels such as Sirius proves that consumers are willing to pay a monthly fee for portability and a wide range of choices. Labels are starting to package bonus CDs and DVDs within new releases to give the consumer more than he can find online. The movie industry has learned early to package bonus features within DVDs to ensure that people will continue to buy them. However, after 20 years, the trading of warez continues. The Pandora's box of P2P networking is opened and cannot be closed. People will always choose online innovations that provide them with the content they want and the privacy they need. How the money is made and where it goes is not their concern. Industry must let the user become a consumer, not force them to be one."

The current revolution is a claim for a new equilibrium and more balanced roles between companies and consumers. Consumers have been empowered by the internet and the New Technologies. They ask for their part in the process of creation of value. An understood revolution is easier to handle and should end-up in a win-win situation for every participant. But it takes companies to give up a firm-centric approach and adopt a consumer-centric point of view to see future opportunities. One thing for sure, dialogue, better than blocked positions and conflicts, will transform an unstable revolution into a prosperous era. By the way, dialogue is one block of the co-creation of value, isn't it ?

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