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Technology, Media & Telecommunications

iConsumer: Digital Consumers Altering the Value Chain

As consumers around the world continue to shift their media, communications, social and shopping activities online, the impact on the technology, media and telecommunications industries will be profound. Hundreds of billions of dollars in value are at stake. This paper describes six overarching trends in consumer digital behavior, and the impact that will be felt throughout the industry value chain

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iConsumer research overview

We launched our iConsumer research program in 2008 to understand changes in consumers digital behaviors over time, across different platforms, and across different parts of the world. Combining deep structured surveys (over 200,000 completed to date), detailed clickstream web-log data, and ad hoc observational research (in-home and in-store), we have a highly detailed and segmented view of today's digital consumer, and regularly use this longitudinal data and insight with our clients to help them refine their strategies and product and service offerings.

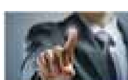
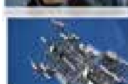
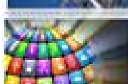
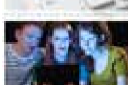
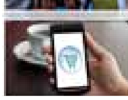
iConsumer: Digital Consumers Altering the Value Chain

Consumer behavior is rapidly changing, with "digital" activities growing rapidly in every sphere. In the US, nearly half (48%) of all the video we watch is now either "time-shifted" (using DVRs or Video-on-Demand), or "device-shifted" onto our laptop, tablet or mobile phone screens. Music is even more digital, with just over two-thirds of usage from streaming services, MP3 files, and satellite radio, leaving traditional AM/terrestrial FM radio with just 32% of usage share. Even among consumers aged 55-64, mobile phone usage has overtaken landline voice usage. These user-behavior changes have and will continue to disrupt existing industry value chains and economics, creating many opportunities and risks for stakeholders.

These shifts are supported by findings from our own primary iConsumer research, as well as, our experience working side-by-side with leaders in High Tech, Media, and Telecom (TMT) sectors. Our research tracks the cross-platform and cross-device behaviors of tens of thousands of consumers each year, in both developed and emerging markets around the globe. As we look back at findings from our fifth year of research, we see six major ongoing consumer trends that are reshaping TMT and related industries (see Exhibit 2).

EXHIBIT 1: SIX SIGNIFICANT iCONSUMER TRENDS

Top iConsumer Trends for 2012

				Share of usage 2008	Share of usage 2012
	1	**Device shift** *from PC to touch*	**PC** **Mobile** **Tablet**	**78%** **22%** **0%**	**57%** **33%** **11%**
	2	**Communications shift** *From voice to data*	Voice Email Social Other	39% 42% 15% 4%	27% 36% 26% 10%
	3	**Content shift** *From bundled to fragmented*	Mobile voice Mobile data	61% 39%	22% 78%
	4	**Social shift** *From growth to monetization*	Social Other internet	13% 87%	23% 77%
	5	**Video shift** *From programmer to user controlled*	Linear TV DVR, VOD, OTT	78% 22%	65% 35%
	6	**Retail shift** *From channel to experience*	E-commerce/ All retail	3.6%	4.9%

What is digital?

We hear the word all the time, but what do we mean here by "digital"? In the consumer device and media context, we refer to consumer-controlled interaction or cross-platform usage, rather than the specific technology layers behind a product and service.

Magazine publishers, for example, have been using digital page layout and printing techniques for decades, but we discuss "digital" in the context of how readers now are accessing those products through tablets and smart phones rather than on the printed page. Similarly, while cable broadcasters have long transmitted digital signals to digital set-top boxes, we now discuss "digital" in how consumers can watch unmanaged, Internet-based video on their main television sets from a variety of different providers.

In the consumer context, it's shorthand for all things "non-traditional" that flow from online and mobile usage.

- Device shift – from PCs to mobile/touch devices. Smart phones are fast becoming ubiquitous, with penetration about 60% in the US. Just over 30% of US Internet equipped households now have a tablet as well, and the rest of the developed world is close behind. Mobile phones and tablets now make up about 44% of all personal computing time, having nearly doubled from 2008. The implications of this shift is already being felt by multiple device manufacturers and their major retail partners.

- Communications shift – from voice to data and video. Email and telephonic voice have fallen from over 80% to about 60% of our "communications portfolio", while time spent on social networks has doubled to take over a quarter of all our communications time. And when we use our phones, only about 20% of the time is for talking (down from over 60% just 5 years ago), with the majority used for more data-centric activities such as streaming music, browsing websites and playing games. The upshot: mobile carriers in particular face challenges in re-orienting their business models to focus on data rather than voice minutes. The US market has many lessons for the rest of the world in this area.

- Content shift – from bundled to fragmented. In large part thanks to powerful search tools, the 'long tail' of media and content (whether that be text, video, classified listings, products for sale, or otherwise) is accessible to anyone. Thus some of the value in traditional "bundles" (whether newspapers, network TV stations, or big-box retailers) has been eroded. The way we use our mobile phones illustrates this well. The number of apps (typically for specific single-purposes) installed has doubled to over 30 from 2008 to 2012. Our spending on these apps is highly fragmented, however, and the growth potential still highly uncertain. Challenges abound for both content owners and marketers to reach and engage audiences that access such eclectic, fragmented media.

- **Social shift – from growth to monetization.** Social networking represents almost a quarter of all Internet time (up 10 points since 2008) and reaches over 75% of all Internet users. Yet, for the first time we have seen small declines in both total audience and levels of engagement in developed economies. This is a remarkably fast climb to maturity, given that major players like Facebook, LinkedIn, and Twitter have yet to celebrate their 10th birthdays. Facebook and LinkedIn now face the quarterly earning pressures of the public markets as well. At the same time, businesses of all shapes and sizes are now actively trying to use social media as part of their marketing efforts. Achieving real and measurable returns on these efforts will be a continuing challenge for players across the TMT spectrum.

- **Video shift – from programmed to user-driven.** Traditional live, linear television remains relatively flat on an absolute basis, but has slipped on a relative basis, and now represents just 65% of all video viewing for US consumers on their television screen, and 52% across all screens. Time-shifted DVR content, watching video on PCs and over-the-top internet video services such as Netflix, make up much of the balance. The increase in all varieties of time-, place- and device-shifting video options will continue to pressure traditional advertising-supported business models for distributors, advertisers, and content owners in the value chain.

- **Retail shift – from channel to experience.** Despite its tremendous growth and transformation of the retail landscape, e-commerce holds only about 5% of all retail sales. As connected mobile devices proliferate, their potential to transform the shopping experience (both in store and online) is the next opportunity. About half of all smart phone owners now use their devices for retail research, and though small today, we will soon see significantly more consumers using smartphones and tablets to complete their transaction as well. The combination of mobile retail and true multi-channel integration will have a transformative effect on the retail experience, and begin the era of Retail 3.0.

In upcoming articles, we'll discuss the details and dynamics of each of these shifts in greater detail. However, this summary of our recent findings make clear that the implications of these shifts will be significant for years to come.

Insights and implications

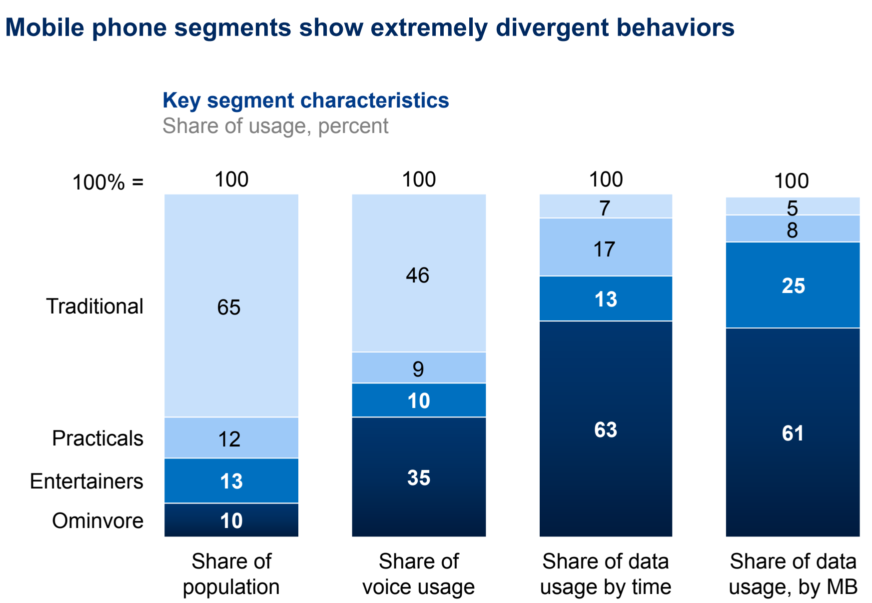
As we consider these trends and reflect on our experience working with players across the global value chain, we have several observations managers should keep in mind as they evolve their digital strategies and business plans.

1. Averages hide incredible diversity in consumer behavior, making micro-segmentation necessary

As we have seen numerous times already, conducting a simple age-based segmentation provides insight into the digital divide of different consumer needs and usage patterns. However, we would advise managers taking that segmentation several steps further to strengthen sales, operations, product development or other key customer-facing business processes. Incorporating product- and brand-specific usage, spending, attitudes and needs can allow development of far more nuanced segments. This highly segmented approach will be needed to win and maintain customer relationships.

For example Exhibit 2 illustrates how we identified four important segments among European mobile phone users: the "Traditionalists" who largely use just voice, even with their smartphones; the "Data Practicals" who use very little voice but lots of data for email, browsing, news and social communications; the "Data Entertainers" who also use little voice but are heavy video, music and game users; and the "Mobile Omnivores" who are super-users of both voice and data services. While the Omnivores and Entertainers represent just 23% of the population, they consume 45% of all voice traffic and over *85% of data traffic*. At the same time, they pay roughly same in monthly service fees as Practicals and Traditionalists, creating huge differences in customer value and cost-to-serve that may or may not be reflected in plan pricing. This has used to reshape both tariffs and customer service.

EXHIBIT 2: Segmentation of mobile phone users



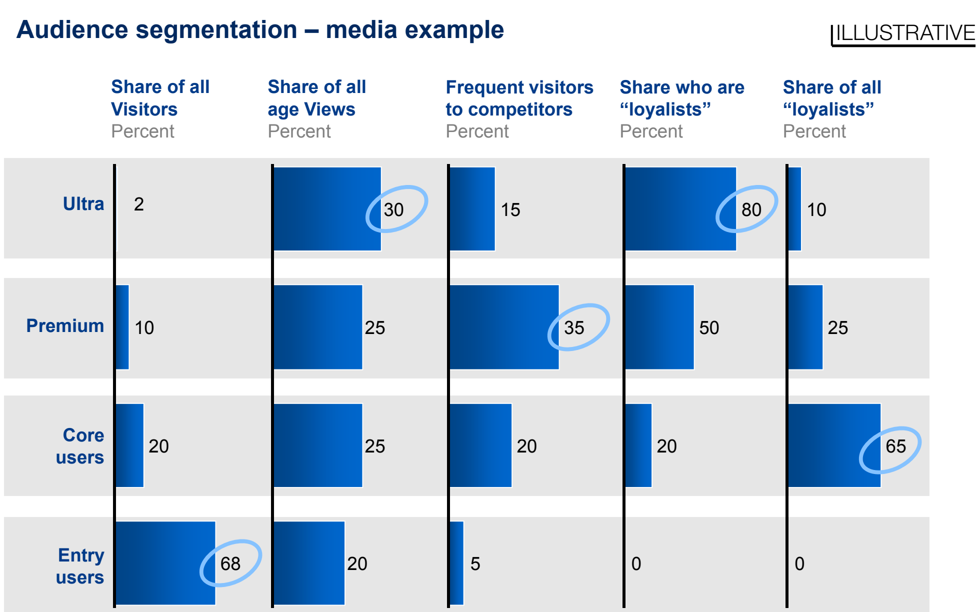
SOURCE: iConsumer 2012 (Europe)

2. Value is not equally distributed, or accurately priced

These Omnivores remind us of the familiar "80/20" rule: no matter what your business, about 80% of the value typically comes from about 20% of the customers. This general truth still holds, though the rapid digitalization of consumer behavior and freemium business models has added an interesting spin. In some cases (like social gaming or digital news subscriptions), digitalization enables an even more extreme version, where only a small percent of users might drive nearly all the revenue. Identifying these high-value users, whether they are on your site or in your store, will become a critical capability.

With one digital publishing client, for example, we found that very occasional visitors made up about 80% of audience by numbers, but less than 10% of the total page views for advertisers (See Exhibit 3). Understanding the detailed behavior of the remaining 20% of high-intensity users, for example, their use of competitive services, and their loyalty to our client's services – enabled the company to successfully introduce a tiered-access subscription model, while maintaining the overall size and breadth of the advertising audience.

EXHIBIT 3: Divergent behavior among customer segments



SOURCE: McKinsey iConsumer clickstream, US 2012

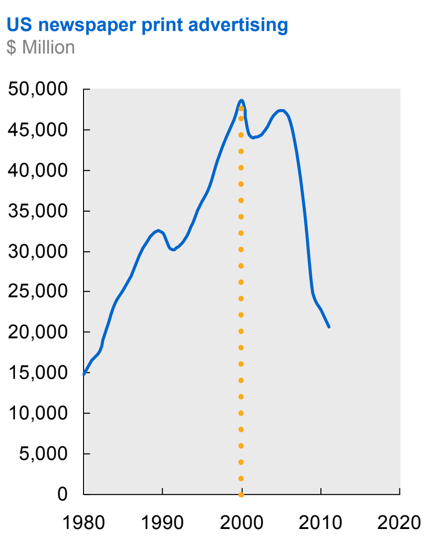
Digital marketing tools can also be immensely valuable in reaching these high-value customers with the right touch points. For example, at one mobile operator we found that its highest-spending customers disproportionately used the e-commerce channel for both sales and service. The response: we helped the operator build a set of targeted products and service offers specifically tailored to that segment. This not only lowered the company's cost to serve, it improved satisfaction with those higher-value customers who used their preferred service channels.

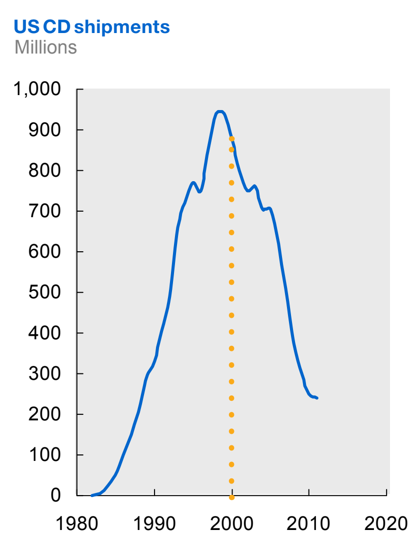
3. Structural changes (especially declines) often happen quite slowly … until they happen very quickly.

Hemingway's observation on how people go broke is as relevant today as after the Great Crash. Short-term economic and industry factors often mask long-term structural problems that lead to gradual – and then very sudden – reversals. Consider that the newspaper industry enjoyed its most profitable decade in the late '90s and early 2000's, even as online-only competitors for classified and display advertising grew in scale and market power. Similarly, the recording industry shipped a record number of CDs during the very dot-com boom that paved the way for digital music's eventual takeover (See Exhibit 4).

EXHIBIT 4: Rapid changes in market structures

Rapid turnarounds in digital media





SOURCE: NAA; RIAA; McKinsey analysis

In hindsight, these reversals can seem obvious, even predestined. Yet, in real-time, understanding and acting on the probable contours of change requires reflection and deep insight into customers' behaviors, industry dynamics and feedback loops. For example, as lower customer volumes no longer support the fixed cost base required, providers often respond by increasing prices for the remaining customers, feeding a vicious cycle and accelerating the unraveling.

We are paying close attention to consumer trends in numerous TMT industry segments signs of change (PC shipments, network television advertising, pay-TV subscriptions, OEM-installed licensed software, terrestrial radio, and physical retail for example). In many cases, we are working with management teams of leading players to reshape their business models to exploit structural changes and cushion potential shocks.

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Regardless of the industry, we believe that most organizations will need to strengthen and renew some of their core capabilities to continue to prosper in an all-digital world. This is as true for those currently on top of their industries as for laggards. Both will also need to prepare for the generational, transformative changes in the market as maturing Millennials replace retiring Baby Boomers as decision-makers for household spending (and business investments, for that matter). A few imperatives for all executives:

- Stay close to users by investing in customer insight. Customer behavior is rapidly changing, demanding strong market intelligence and customer insight functions. Innovative teams will integrate emerging digital, social and mobile tools into more traditional 'voice of the customer' processes, and effectively build feedback loops into key business functions such as product development and sales. Never before has this been easier.

- Build an edge with deep analytic skills. Especially as segments get smaller and more precise, the need to use data to optimize product development and marketing will only grow. Leading players will test and measure just about everything – and, 'big data,' systems will support and guide them.

- Make your business models more robust to reflect consumer diversity. Focus and breadth are both needed. In other words, focus on the 20% or 2% that drive the economics; and build a diversity in business models to address the remaining 80-98%.

- Ensure investments are clearly aligned with consumer shifts. Executives need to clearly communicate the 'what' and the 'why' of strategy and operations and tie it to current opportunities. However, most companies will also need to make sure legacy platforms and businesses get the management attention they deserve.

- Place a premium on and reward superb execution skills. A potential downside of 'big data' and analytics is that the analysis goes on too long and the market opportunity evaporates or is seized by a competitor. To avoid this trap top management focus needs to be on delivering the products and services that will serve and delight its customers – today and tomorrow.

As we look at these behavior shifts and the group that is leading the change, we would argue that for many big TMT players, if you can't connect with Millennials, you'll probably be out of business in ten years. But if you can't hold onto the rest of your customers, you'll be out of luck a whole lot sooner than that. It's a very interesting marketing and sales challenge for agencies and marketing directors, but an *existential challenge* for top C-level executives and strategists with a long-term value-creation agenda.

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Ewan Duncan is a Partner in the Seattle office, and leads our location there. He co-leads the firm's knowledge effort on iConsumer (which explores the evolving behavior patterns of digital consumers) and the Consumer Decision Journey (which explores the changing nature of how consumers research and buy products). Ewan works with multiple tech and telecom clients, to help them drive strategy and execution against the type of shifts outlined here.

Eric Hazan is a Partner in the Paris office, and co-leader of the European Consumer practice. Eric advises the top management of leading telecom, Internet, media, and entertainment companies in Europe on their most critical business issues. His 15 years of client work for both public and private institutions have spanned all major segments, including mobile and fixed telephony, broadband, broadcasting, TV production, consumer publishing, gaming, Internet, cable and satellite distribution, and sports.

Kevin Roche is a Knowledge Expert in the Tech, Media & Telecom practice, and manages the iConsumer service line globally. Kevin leads the design, execution, analysis and insight delivery to clients. As both a consultant and a practice expert, Kevin has worked with clients across media, telecom, retail and finance on strategy, marketing and business development challenges.

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