

MONETIZING DIGITAL MEDIA

TRENDS, KEY INSIGHTS AND STRATEGIES THAT WORK



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Introduction

1. Preamble

The widespread global penetration rates of broadband Internet, smartphones and tablets have changed the consumer and enterprise landscape forever. Dramatic increases in high-speed and mobile connectivity have fuelled the creation of new and compelling interactive media platforms and user experiences, monetized through an array of schemes to respond to voracious consumer demands. There is no doubt that we have entered a golden age of content and media.

This study is concerned with the monetization of interactive digital media, that is, the methods by which companies extract value from intellectual property to generate revenues. For the purposes of this study, the authors focus primarily on games and applications, and “convergent” content that is produced as an extension, or in relation to, a television program. This study also considers stand-alone digital content, however, this examination is limited to original dramatic web series.

2. Approach and Methodology

The goals of this study are threefold:

- to undertake a review of the monetization trends, strategies and success stories of interactive digital media internationally and in Canada
- to assess the effectiveness of monetization models supporting the sector; and
- to provide market intelligence of interest to the funders of interactive digital media that could be used to support more robust monetization models.

The consultants conducted a literature review of international and national sources; interviewed nineteen industry leaders and profiled selected examples of monetization strategies being used by eight Canadian companies in order to provide lessons learned. Annex 1 includes a selected bibliography. Annex 2 provides a list of those interviewed.

3. Structure of this Report

This report is divided into six sections:

- Section A provides a general overview of the monetization of digital media;
- Section B describes the global trends for consideration in the monetization of games as well as the prevalent models being used to monetize them;
- Section C examines global trends for consideration in the monetization of convergent digital media and web series as well as the key models being used to monetize them;
- Section D presents the perspectives of stakeholders on challenges and opportunities;
- Section E profiles selected examples of the monetization of successful games and digital media; and
- Section F concludes with summary observations.

A. A General Overview of the Monetization of Digital Media

1. Preamble

In today's world, to monetize their digital content, companies must increasingly consider how to reach consumers across a growing number of distribution platforms and an array of monetization models, pricing strategies and tactics.

This section provides a general overview of the key models being used to monetize digital media content with the aim of providing a foundational basis for understanding the monetization of games, convergent media and web series discussed in the sections that follow.

2. Monetization Models

2.1 Key Monetization Models

"Monetization," the means by which companies generate revenues, is described as digital media's most intractable problem because as there is no "one size fits all" solution.¹

Monetization models are as diverse as digital media content itself and as is shown in figure 1, they can be categorized as consumer-paid models; funded models and hybrid models. While consumer-paid models refers to monetization models that extract revenues from the consumer, the funded model, as described by Forrester research, refers to intellectual property that is monetized through funding from an advertiser or third party licensor. Hybrid models involve the simultaneous use of more than one model of monetization.

Over the past two decades, new monetization models have emerged like successive waves, propelled by changing technologies and distribution platforms. With each successive "wave," the monetization landscape has increased in complexity. Monetization models developed in the 1980's to support single-player console game platforms persist today, competing with newer models associated with web-based online distribution platforms that favour social interaction, as well as mobile platforms, whose ascendancy has been driven by the rise of "free" – giving away initial access to content.

Figure 1: Key Monetization Models²

Consumer-paid models	Funded models	Hybrid models
<p><i>Subscription:</i></p> <p>Users subscribe to content for a monthly or annual fee.</p>	<p><i>Ad-supported:</i></p> <p>Content is monetized through ads, for example, banner or video ads.</p>	<p><i>Freemium:</i></p> <p>Offering a game, product or service for free, while charging a premium for advanced features, functionality or related products like virtual goods through micro-transactions. In some cases, developers combine this model with advertising.</p>

¹ Stephen McClelland, "Monetize, Monetize at a Price", *Intermedia*, Vol 39, Issue 2, May 2011, page 1.

² Adapted from Sara Rotman Epps, *Eight Models for Monetizing Digital Content*, Forrester Research, 2009.

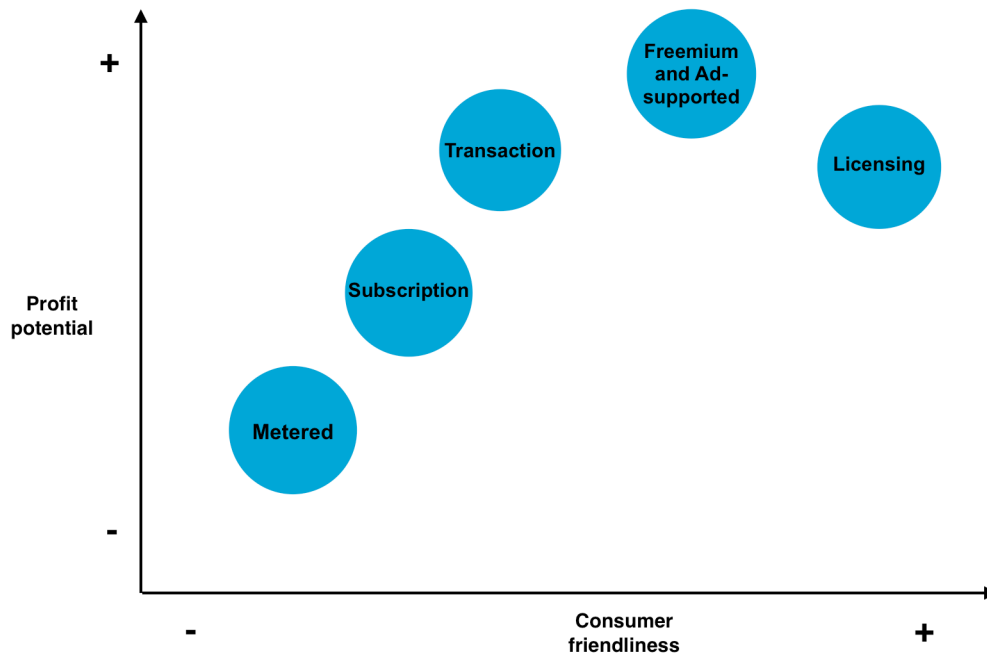
<p><i>Transaction:</i></p> <p>Unbundled pieces of content, such as a song, game or video downloads, which are sold individually.</p>	<p><i>Branded content:</i></p> <p>Content is completely funded by a brand.</p>	<p><i>Paidmium:</i></p> <p>Offering a game, product or service as a paid download, combined with charging a premium for advanced features, functionality or related products like virtual goods.</p>
<p><i>Metered (also called a Pay-wall):</i></p> <p>Content is free until a user reaches a certain threshold, such as number of articles or videos viewed or based on the amount of time viewing.</p>	<p><i>Licensing:</i></p> <p>Other businesses license the digital content (that is, the right to use the intellectual property) such as a digital video series. Syndication is a form of licensing.</p> <p>Licensing may also involve selling the right to use the intellectual property to a toy company or other manufacturer to produce and sell merchandise (also called merchandizing).</p>	
<p><i>Premium:</i></p> <p>Games or apps that must be purchased for download before they can be used.</p> <p>Premium purchases can include pre-purchases.</p>		
<p>Merchandizing – Where the owner of the IP produces merchandise to sell directly to the consumer, such as DVD's, music or ringtones.</p> <p>See also licensing.</p>		

Companies monetizing their users or audiences directly must begin by identifying the best model to encourage the consumer's willingness to pay, before they can address any of the tactical issues of user acquisition (audience development), pricing or payment models.

There are many considerations for companies to keep in mind in terms of the willingness of consumers to pay for a product or service. For example, it is vital that consumers value the content (i.e., as unique, highly relevant or scarce), particularly since they have been accustomed to getting content for free. Having pre-existing billing relationships with consumers is also said to increase willingness to pay. As discussed below, the freemium model, based on

initially giving a product away, has been identified as providing the greatest potential for profit. (See figure 2.)

Figure 2: Profit Potential and Consumer Friendliness of Monetization Models³



2.2 Video Games Industry Innovation in Monetization

The video games industry has been particularly innovative in developing new means of generating revenues. Monetization models have undergone a number of radical transformations, driven by new distribution technologies and games today are generating significant revenues in spite of consumer demand for free access to content. As one industry observer notes, “The gaming industry is one sector that is learning to play the monetization game.”⁴

As new distribution platforms have been introduced and scaled up, complex ecosystems have developed around them, including new audiences with different usage patterns.⁵ In this regard, the emergence of digital online distribution for games was profoundly disruptive, giving rise to three different game ecosystems in short succession: the browser-based web ecosystem, the Facebook-driven social ecosystem, and the mobile ecosystem supported by the iOS and Android platforms. (See figure 3.)

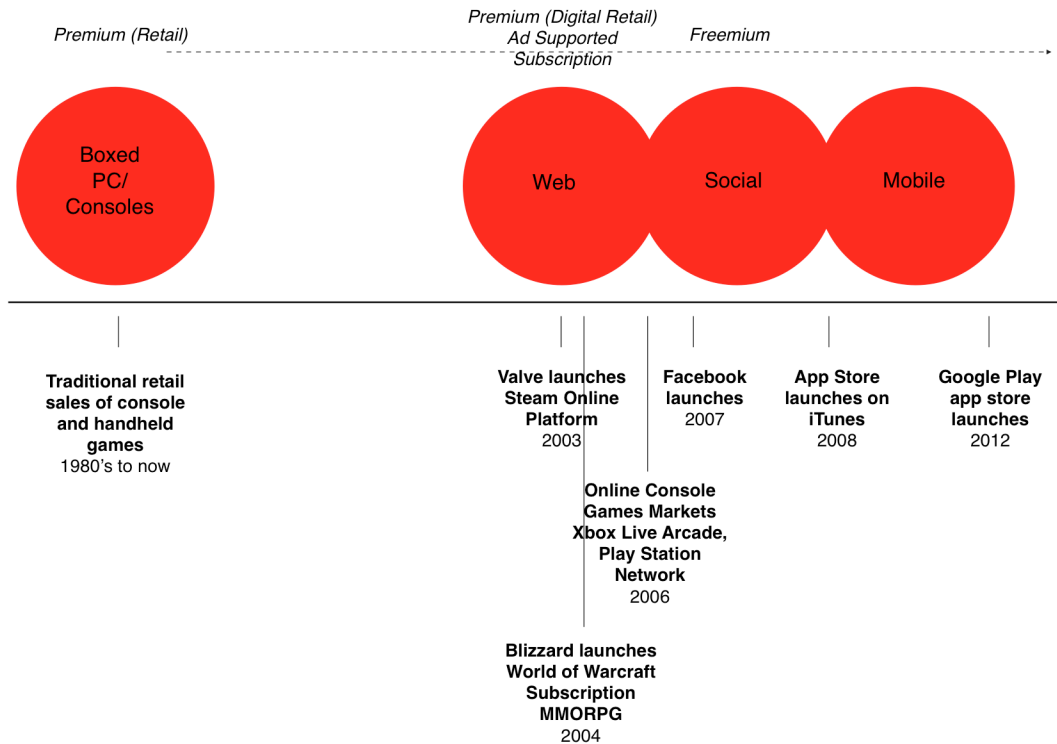
³ Figure 2 is adapted from Sarah Rotman Epps with Mark Mulligan, Erik Hood, “Eight Models for Monetizing Digital Media”, Forester Research, June 25, 2009.

⁴ Ernst and Young, *Monetizing Digital Media: Creating Value Consumers will Buy*, Ernst and Young, <http://www.ey.com/GL/en/Industries/Media---Entertainment/Monetizing-digital-media-creating-value-consumers-will-buy>, page 10.

⁵ Jan Becker, “Guest Post: Learning from the past: Patterns in the recent history of game platforms, Part 1,” *Inside Mobile Apps*, February 8, 2013.

Massive growth in smartphones and connected mobile devices has dramatically expanded opportunities to reach consumers and today represent a powerful new avenue of monetization.

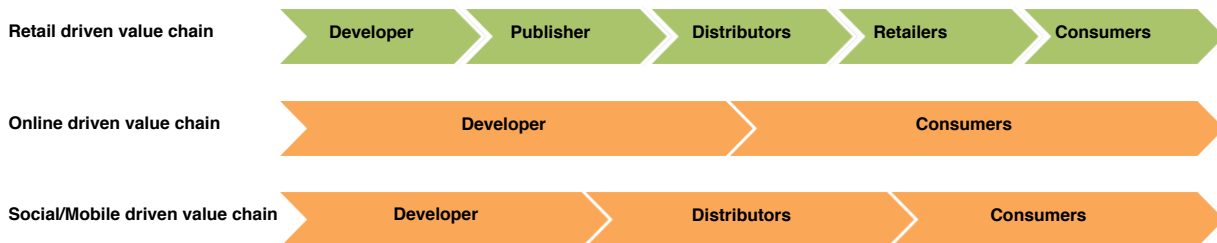
Figure 3: Evolution of Games Distribution Platforms, Ecosystems and Monetization Models



Key models being used to monetize video games today include premium (retail and digital retail); advertising supported; subscription; and hybrid variations such as freemium (free to play games supported by in-game purchases).⁶

With each successive transformation of the games ecosystem, the relationship between the consumer and the developer has changed, re-shaping the value chain, as can be seen in figure 4.

Figure 4: The Most Common Value Chains of the Gaming Industry⁷



⁶ Ryan Morel, "Choosing the Right Business Model for Your Game or App," *Adobe.com*, August 12, 2012.

⁷ *Game Development and Digital Growth*, European Game Developers Federation, 2011, page 5.

These changes in the value chain for games have implications for how developers monetize their games. With more immediate access to consumers than was possible in the traditional retail model come greater opportunities but also responsibilities to manage relationships effectively to extract the maximum lifetime value from each player. Success depends on understanding player motivations for playing and paying, and building strong and enduring relationships with them. “The customer, in short, is king. In the Internet world, this is a fact that remains abundantly clear - price or no price.”⁸

2.3 The Prominence of the Freemium Model

By far the most significant trend in the current games market is the significant growth anticipated in the mobile and PC markets as a result of the revenue generation potential of the freemium monetization model. Smartphones, tablets and the PC are growing their share of games spending while spending on dedicated console and handheld games (traditionally sold through retail channels) is going down.⁹

Revenue generation in the mobile games space is dominated by the freemium model, extending to apps in general, with revenues from free apps increasing on both the Apple App Store and Google Play.

The freemium model has also been successfully adopted by other games sectors, notably online games. For example in the massively multiplayer online (MMO) games sector, where subscriptions once comprised the main source of revenues, free-to-play and micro-transactions for virtual goods are growing and creating successful micropayment-based in-game “economies”.

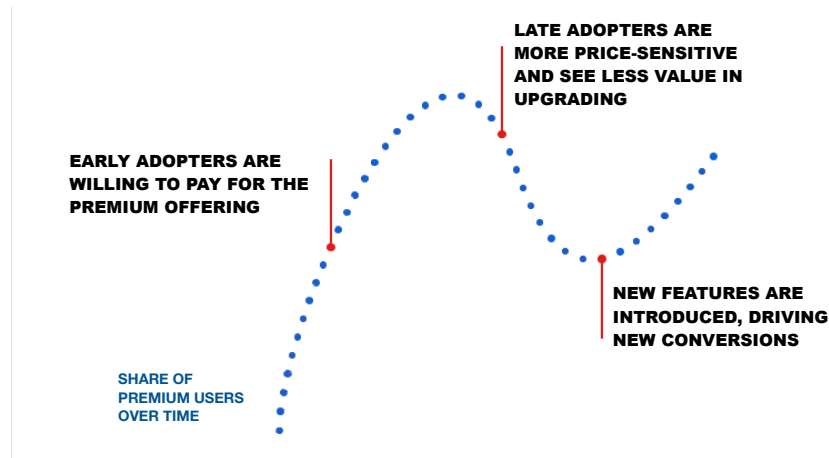
Several factors contribute to the appeal of a freemium monetization model for games. Because free features are a potent marketing tool, “the model allows a new venture to scale up and attract a user base without expending resources on costly ad campaigns or a traditional sales force.”¹⁰ Companies that launch their games on multiple platforms can take advantage of multiple opportunities.

In the freemium model, micro-transactions are an important element driving incremental revenue. Companies that are using the freemium model typically see the share of sales rise and fall and then rise again in a predictable way over time. Those that don’t account for this phenomenon risk failure. For example, early adopters are more likely to pay for premium offerings than late adopters, who are more price-sensitive. Introducing new features helps to drive more sales, and is a cornerstone of the model. (See figure 5.)

⁸ *Monetizing Digital Media: Creating Value Consumers will Buy*, Op. Cit.

⁹ *Value Exchange Advertising in Freemium Games*, IHS Technology, March 2014, page 3.

¹⁰ Vineet Kumar, Making “Freemium” Work, *Harvard Business Review*, May 2014.

Figure 5: The Freemium Model and the Life Cycle of Upgrades¹¹

The use of behavioural economics is being increasingly used to persuade consumers to purchase virtual goods through dynamic pricing, targeted at defined market segments. For example, developers iterate their pricing models in real time, such that price points change in reaction to responses by targeted users. “In the end, it is use of psychology, pricing and game mechanics that are driving monetization.”¹²

3. Summary Observations

The monetization models for digital media can be categorized as consumer-paid models, funded models and a range of hybrid models.

Generally, companies that are monetizing digital content have to consider the reality of multi-distribution platforms and the consumer’s preference for free content in the design of their monetization strategies.

The video games industry has been a leader in the adoption of various models ranging from premium, freemium, subscription, advertiser supported and hybrid models. The last decade’s transformations in distribution technologies have created complex ecosystems requiring re-thinking and reinvention of monetization strategies for this sector. The models and approaches adopted by the gaming sector show that free models complemented by micro-transactions are providing the most lucrative means of monetization. However, a deep and sophisticated understanding of consumer behavior in relation to various pricing and mechanics is necessary to optimize monetization.

¹¹ Vineet Kumar, Making “Freemium” Work, Harvard Business Review, May 2014.

¹² Interviews conducted for this study.

B. Monetizing Games: Trends and Approaches

1. Preamble

Having provided a broad context for the monetization of digital media generally in section A, we examine global trends in this section in terms of spending, pricing and payment methods in the gaming industry. This allows us to position Canada among the top countries in terms of game transactions, to identify the popularity of platforms, discuss the challenge of under pricing and the complexity of payment methods. These all impact on revenue generation for companies.

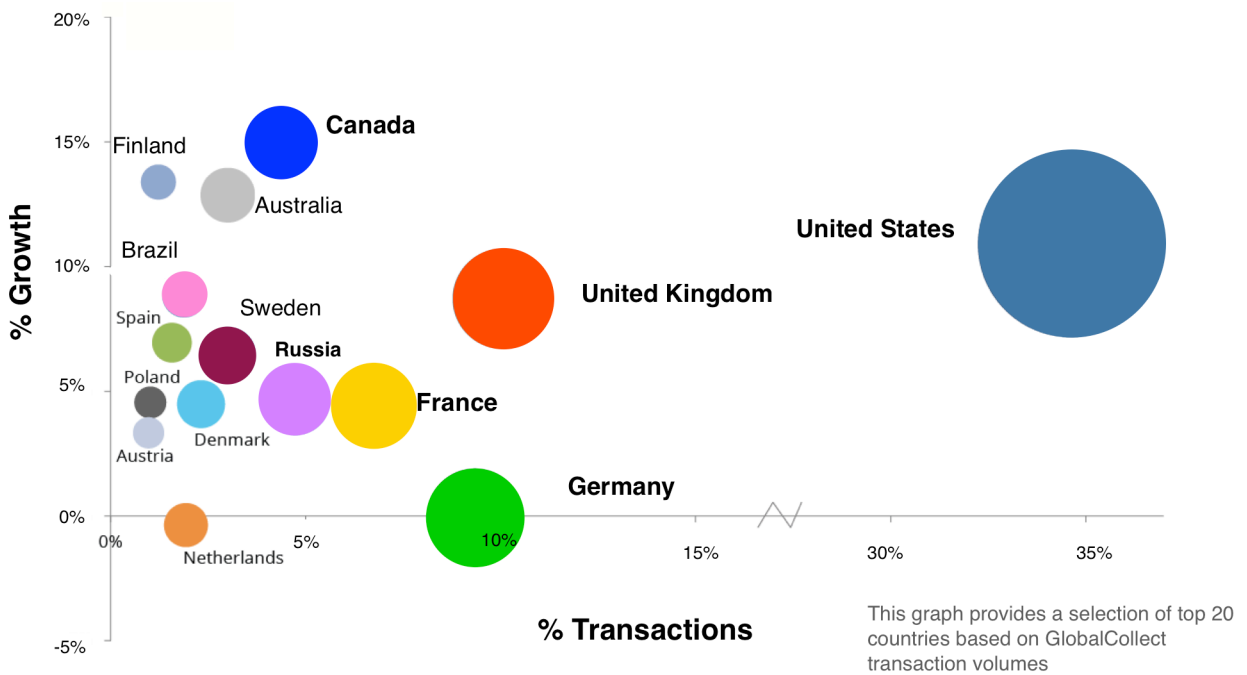
We then provide a detailed discussion of the most prevalent monetization methods currently employed in the games industry, with considerations for their use.

2. Trends to Consider for the Monetization of Games

2.1 Global Trends in Game Transactions

The U.S. market leads the western world market in terms of the number of game transactions, followed by the United Kingdom, Germany, France and Russia. Canada ranks sixth in the western world, fuelled by 14.93% growth in the total game transactions. (See figure 6.) Often used as a test bed for the United States, Canada also ranks high on iPad and iPhone spending at 6th place.

Figure 6: Leading Transactions by Country – Western Markets¹³



¹³ IBID.

The fastest growth in game transactions is occurring in Asian countries: Korea, followed by Japan and Singapore. We note that Canada is also showing strong growth. (Figure 7.)

Figure 7: Rate of Growth in Game Transactions by Country

Top Growth in Transactions	
Korea	24.13%
Japan	22.72%
Singapore	19.10%
Ireland	17.81%
New Zealand	15.53%
Canada	14.93%

When it comes to average amount spent per paying gamer, Canada is positioned in the global top 4 together with Korea, Japan and the United States.¹⁴

At the present time, only fifteen percent of the global population generates 74% of global game revenues.¹⁵ In the future, it is expected that growth will take place in markets such as Asia-Pacific and Latin America.¹⁶

One industry analyst points to the great innovation that has taken place in countries such as China, Japan and South Korea, which are said to be up to two years ahead of North America and Europe when it comes to the science of monetizing mobile games, having invented the free-to-play model of monetization. Unhampered by the old, and with the benefit of scale in terms of population size, greater innovation is expected from this region.¹⁷

2.2 Micro-Transactions are the Driving Force of Current Market Expansion

Figure 8 shows the share of revenues from differing monetization models being used to drive games revenues. The shift to free downloads supported by the monetization of premium content through micro-transactions is driving revenues and user acquisition and it is now possible to have free game experiences with millions of active users. Games with micro-transactions are currently the main driving force behind market expansion.¹⁸

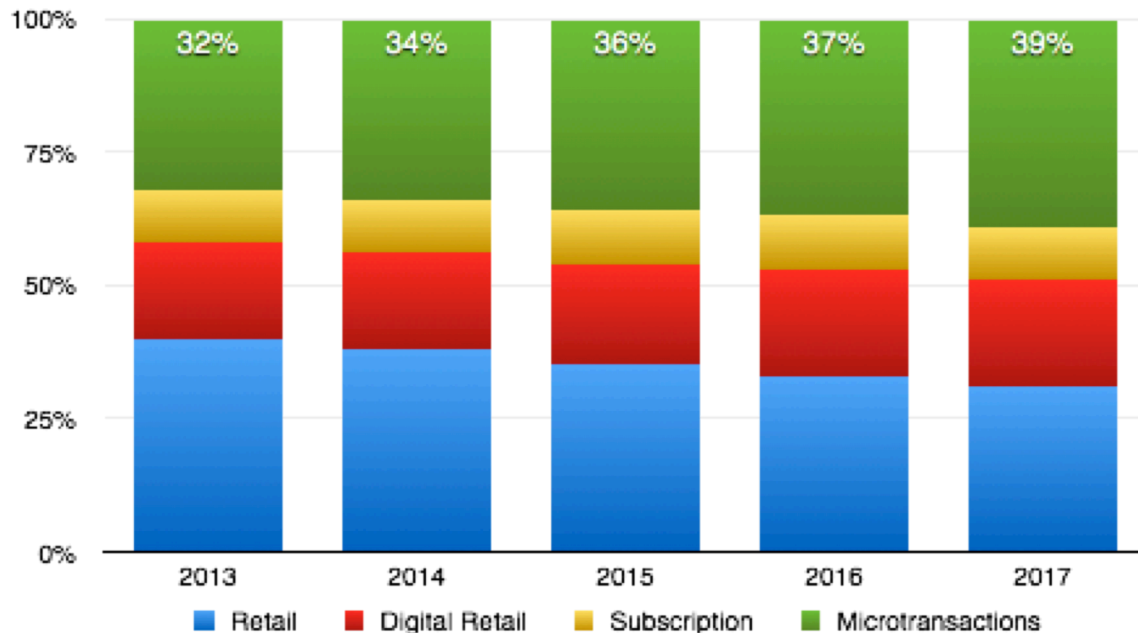
¹⁴ "The Global Games Market Report: Key Facts & Insights On the Global Games Market," *Newzoo Trend Report*, September 2013.

¹⁵ "The Global Games Market Report: Key Facts & Insights On the Global Games Market," *Newzoo Trend Report*, September 2013.

¹⁶ IBID, page 5.

¹⁷ Mike Williams, "Asian markets 'two years ahead' of West in mobile monetization," *Games Industry Biz*, October 13, 2013.

¹⁸ *Value Exchange Advertising in Freemium Games*, IHS Technology, March 2014, page 3.

Figure 8: North American Games Spend Share by Monetization Model¹⁹

2.3 The Mobile Games Market is Fuelling Micro-Transactions

The number of game transactions have increased dramatically since 2008 – 186% between 2008 and 2010 and a further 67% between 2010 and 2012.²⁰ These transactions are propelling the growth of the global video games market, which is expected to surpass \$102.9 billion dollars by 2017.²¹ The mobile games market is one of the fastest growing games sectors, expected to double to an impressive \$35.4 billion by 2017, when it will represent one-third of the entire global market for video games.²² This growth will be fuelled primarily through micro-transactions in freemium games, which are expected to represent 90% of all mobile and tablet game app revenues in 2017. (See figure 9.)

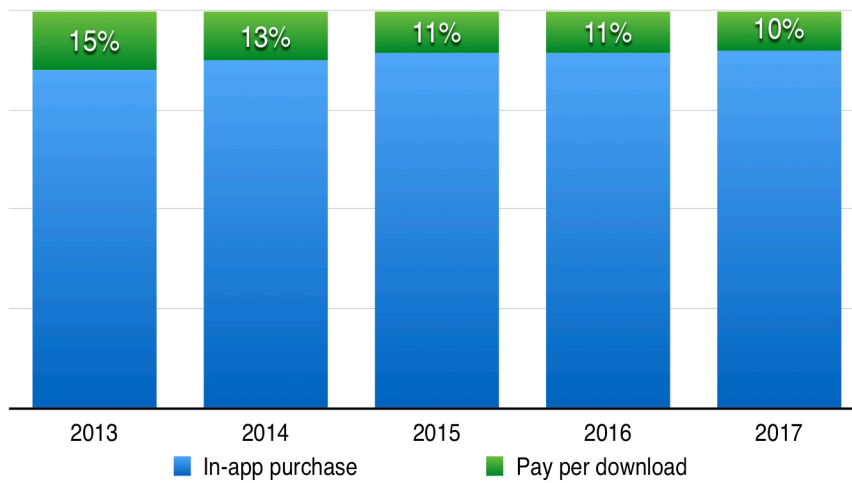
¹⁹ *Value Exchange Advertising in Freemium Games*, IHS Technology, March 2014.

²⁰ *The Shifting Games Video Landscape: Payment, Intelligence and Trends*, Global Collect, March 2013, page 4.

²¹ "The Global Games Market Report: Key Facts & Insights On the Global Games Market," *Newzoo Trend Report*, September 2013.

²² IBID.

Figure 9: Worldwide Mobile and Tablet Game App Revenue by Monetization Model



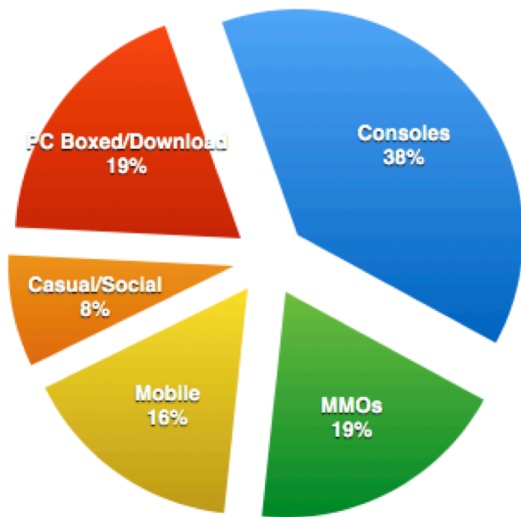
2.4. Paying Players are Spending Money Across Screens

Trends show that the vast majority of paying gamers spend money on a variety of game genres and platforms. Only five years ago, gamers played mainly on two screens: the TV (game consoles) and the PC. That number has since doubled: gamers are now spreading their budget across all screens. As game companies aim to follow their players across all screens, consumer and payment insights become increasingly important to support strategic and commercial decisions.²³

Figure 10 provides an analysis of revenues being generated by the different game market segments. Worldwide, console games account for 38% of revenues, followed by PC games and MMOs, at 19%, respectively.

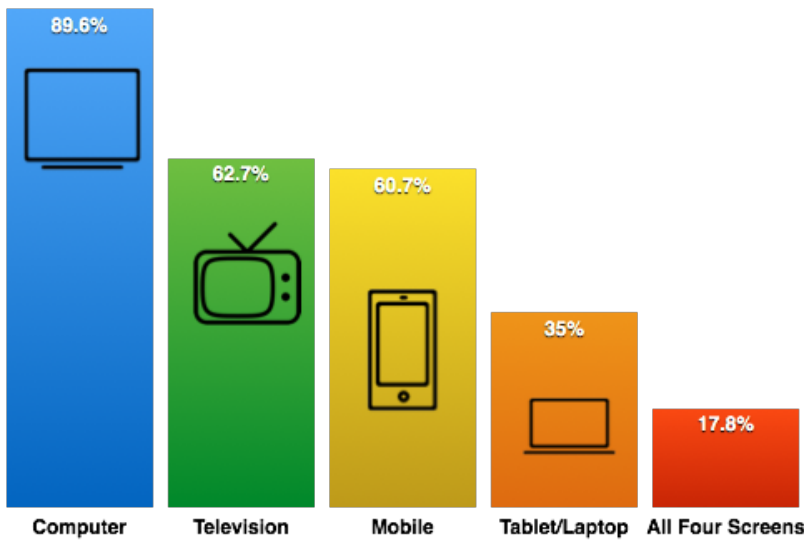
²³ Peter Warman, *Cross-Screen Impact of Free-to-Pay: Let's lean back for a moment*, Newzoo, November 2012.

Figure 10: Global Games Market by Segments²⁴



In Canada, the majority of gamers are playing on their PC, a trend fuelled by MMO games.²⁵ (See figure 11.) Almost 20% of Canadian gamers are playing across four screens: computers, TV sets, mobiles or laptops.²⁶

Figure 11: Cross-Screen Gaming in Canada²⁷



²⁴ “The Global Games Market Report: Key Facts & Insights On the Global Games Market,” *Newzoo Trend Report*, September 2013.

²⁵ Canadian Games Market Infographic, NewZoo, December 2013; 13 million of the total 15.9 million Canadian gamers play casual and social games followed by ten million who play console games. Floating screens refers to laptops and notebook computers.

²⁶ IBID.

²⁷ IBID.

2.5 Under Pricing is a Challenge

In a universe of free content choices, pricing of digital media products can be a challenge for which there are no easy solutions.

The devaluation of mobile products has directly affected pricing within free-to-play games. One industry observer notes: “The mistake that most developers make is that they under-price. The truth is that a low percentage of people are never going to buy. The mind set of the 99-cent app has encouraged developers to come in and price their lowest package at 99 cents.”²⁸ This trend has been encouraged by platform holders as a cheap application ecosystem which adds value to the devices they are trying to sell.

It has also been suggested that developers are underselling their games with the 99-cent price point. “With the excitement of a new platform there was this race to the bottom in terms of price. While developers and publishers initially saw increased downloads from a nominal game fee, this had a detrimental effect on the revenue accrued from even the best-selling games. People confused getting more exposure from having a sale with true price elasticity. It’s just very hard for any developer to make money on a paid app with a 99-cent pay point. The number of people who will buy is not going to support very many developers.”²⁹ Paid apps appearing in the top 1000 grossing apps on Apple app store and Google Play are most commonly in the \$2 to \$4 dollar range.

For premium games, piracy is an issue, and game developers need to get their pricing strategies right to discourage players from seeking out bootleg copies. At the same time, the dynamic pricing pioneered by Steam, with its weekend deals and half-price specials, has posed a significant challenge to traditional retailers’ less flexible pricing schemes. There is some concern about the potential for price erosion.

3. Monetization Models and Strategies

3.1 Freemium

In recent years, the freemium model has come to replace other monetization models as the dominant generator of revenues.³⁰

In the mobile sector, the vast majority of games that make it to Apple and Google’s top grossing charts are free-to-play, with their revenues coming entirely from micro-transactions.³¹ Industry trends show that selling virtual goods has become a major new revenue model in massively-multiplayer online games as well. This is especially true in the East Asian market, where virtual goods are now part of the value proposition.³²

The underlying rationale with free-to-play is that the bigger supply you have for one product, the bigger demand there can be for complimentary products. Employing the freemium model as a teaser to build a following is being used successfully to recruit new audiences.³³ There

²⁸ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014.

²⁹ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014.

³⁰ *The Shifting Games Video Landscape: Payment, Intelligence and Trends*, Global Collect, March 2013.

³¹ Laura Hockensen, “2013 was the year for freemium games but 2014 may not be,” *Gigaom*, December 20, 2013.

³² Juho Hamari, *Virtual Sales Goods as a Business Model*, September 6, 2010.

³³ Erik J Martin, “The Freemium Frenzy: Is this the Right Monetization Model for You?,” *eContent*, November 26, 2012.

are two criteria that companies must follow: 1) the ability to create a no-charge product that can reach a large audience; and 2) the ability to create complimentary products that can be upsold off the free product.

The goal of the free-to-play model is to break down the value proposition to such small offerings that the consumer is willing to pay for the service or good, as “an alternative to asking for \$40 or \$50 up front.”³⁴ The freemium model allows companies to exercise dynamic pricing, also called perfect price discrimination.³⁵ Using analytics, companies can base their pricing strategies dynamically, based on the maximum value that consumers are willing to assign to different virtual goods. Dynamic pricing is made possible by the “monopoly” that the developer has on all goods sold inside the game (i.e. players cannot “shop around” for better prices.) Ascertaining maximum price points is achieved largely through trial and error, based on analysis of player behaviours.

It is important to note that “people don’t buy virtual goods the same way they buy physical goods, it’s not a rational decision. The longer someone plays your game, the more likely they are to buy and the less price sensitive they become.”³⁶

The sale of virtual goods through micro-transactions involves selling some form of virtual items, or currencies to players. There are many freemium value propositions that can appeal to different types of users. Functionality (paying for virtual items, speed-ups, content, additions, upgrades, services or capabilities) is the most common value proposition used by freemium developers. Most frequently, the object sold for real money is a virtual currency, which is then exchanged for virtual items. Permanent items are the preferred purchases. The items can range from weapons and armour in online games to clothes in virtual worlds and simple two-dimensional graphical badges in social networking games. The items are used as part of gameplay and fulfil similar social and aesthetic functions as physical commodities do in consumer culture.

Industry observers point out that “while allowing and encouraging high value users to spend what they want, you really do need your non-paying players too, which seems to be a message that is getting lost in the frantic fishing for monetizable gamers. This creates the dangerous concept that non-paying users are worthless. Just because nonpaying players don’t and maybe never will create in game revenue, you can to a certain extent give them a dollar value. I am going to call this Social Value.”³⁷ Non-paying players can also be monetized through in-app advertising.

The freemium model relies on a small proportion of users making in-app purchases to succeed. In a free-to-play game, many players play without paying but an increased player base allows for alternate monetization.³⁸ It is this large base of engaged gamers that is driving revenues.

Currently between 2% and 10% of a player base in a free-to-play game will monetize. This takes into account unsuccessful free-to-play games on mobile platforms, which make up the majority of free-to-play games by volume. For successful free-to-play games – those that reach the top 100 chart on their respective platforms – this figure is between 5% and 10%, although geographic considerations also play a part. Players in Russia for example, will

³⁴ Interviews conducted for this study.

³⁵ Perfect price discrimination refers to charging the maximum possible price for each unit sold.

³⁶ Jacob Serebrin, “How to Use Data to Create Profitable Games,” *TechVibes*, November 13, 2013.

³⁷ Philip Driver, “Player Valuation for Marketing in Free to Play Games,” *Gamasutra*, March 26, 2013.

³⁸ Adrian Cook, “The Power of Free-to-Play,” *Game Developers Conference*, 2008.

monetize at a lower rate than those in more developed economies like the United Kingdom, the United States and Japan.³⁹

It must also be noted that there exists a significant spread in terms of the revenues generated by the top performing apps and their close seconds. Breakout apps can earn over \$100,000 dollars per month, and account for the majority of revenues from the freemium model. By comparison, developers earning in the 75th to 90th percentile are making up to \$10,000 dollars per month.⁴⁰

One of the considerations for developers in monetizing their games through the freemium model is the very short “lifecycle” of players. The game analytics company, Flurry, reports that games have the shortest life of all apps, and can lose up to 50% of their initial players in the first two months.⁴¹ It is important for developers to understand that the majority of free-to-play players monetize quickly, generally in the first week of playing though it varies depending on genre and platform. Those companies using the free-to-play model need to bring in some more expensive purchasable items early on to increase revenue. It is suggested by some in the industry to start prices high, and lower as needed.⁴²

Player retention provides a certain level of sustainability and security for companies. As players invest more time in a game, they are more likely to value their achievements in the game (i.e. their status or progress). This makes switching to another game or past time more costly. One approach to increased player retention is to focus the company’s energies on supporting the app full-time over the long haul, continuing to re-engage players with new features to create a more robust user base over time. Most games use social strategies to encourage user retention.

The risks associated with player drop off may also be mitigated by focusing on a portfolio of games that can appeal to a wider group of potential players. It’s important to understand the different roles that the games in the portfolio play, for example, some may be better at acquiring players, while others are better at monetizing them. The portfolio is one approach to cross-promote games and encourage players to play other games by the same developer.⁴³

3.1.1 Balance in the Game Economy

Attaining balance in the economy of a free-to-play game is considered key to successful monetization. One industry expert explained a game’s economy as follows: “A game economy is...a trade-off between resource generation, resource destruction and if the game has any sort of multiplayer feature to it – trading.”⁴⁴ Economic game mechanics are used as a tool for balancing games.

A freemium game typically involves an in-game economy that is crucial to the game’s performance in engagement, socialization and monetization. This economy is also closely relat-

³⁹ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014.

⁴⁰ Corriea, Alexa Ray, “Flappy Bird Collects 50 K Per Day in Ads,” Polygon, February 6, 2014.

⁴¹ Benjamin Hansz, “Life is Short (for Mobile Games),” *Games Industry Biz*, October 21, 2014.

⁴² Emily Greer, “Maximizing Monetization in Free to Play Games,” *GDC Online Talk*, October 24, 2012.

⁴³ Benjamin Hansz, “Life is Short (for Mobile Games),” *Games Industry Biz*, October 21, 2014.

⁴⁴ *Game Monetization: A Bright Future*, Video Games Intelligence, October 3, 2014, page 3.

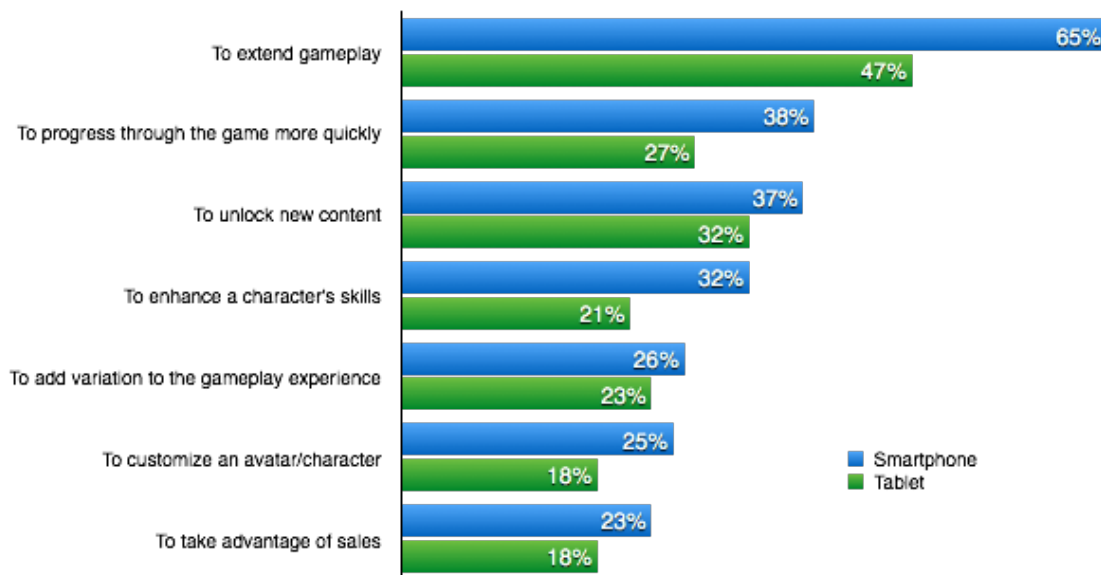
ed to the game's balance, by being positioned right in the sweet-spot where challenge and progression intersect.⁴⁵

The freemium model is sometimes seen as using micro -transactions to practice “the tactic of deprivation” such that users only have a finite number of moves or actions to take before waiting a period of time (sometimes hours) to be able to play again.⁴⁶ The biggest challenge is to make the player feel like the money he is putting in has value. As one industry analyst explains: “It’s a balancing issue around how much one pays to progress and how much skill one uses to progress.”⁴⁷

For example, in *Rise of Nations*, every time a unit - such as a Knight or Archer - is purchased, the cost of future units of the same type goes up, simulating the pressure of demand upon price. This design encourages players to diversify their armed forces, in order to maximize their civilization's buying power. By allowing the "values" of different paths and options to float during a game, designers present players with a constantly shifting landscape, extending replay-ability by guaranteeing no perfect path to victory.

We can see in figure 12 that extending gameplay motivates most in-app purchases, while special offers are motivating less than a fifth of spenders in mobile games.

Figure 12: Motivations Driving In-app Purchases⁴⁸



3.1.2 Payment Methods for Freemium Models are Evolving

Micro- payment methods to support micro-transactions are described as the weak link in the current system of payment methods. To make the micro- transaction model work more effec-

⁴⁵ Raul Aliaga Diaz, “A Practical Free-to-Play Game Economy Design,” Adrian Crook + Associates, April 29th, 2013.

⁴⁶ Laura Hockensen, “2013 was the year for freemium games but 2014 may not be,” *Gigaom*, December 20, 2013.

⁴⁷ *Game Monetization: A Bright Future*, Video Games Intelligence, October 3, 2014.

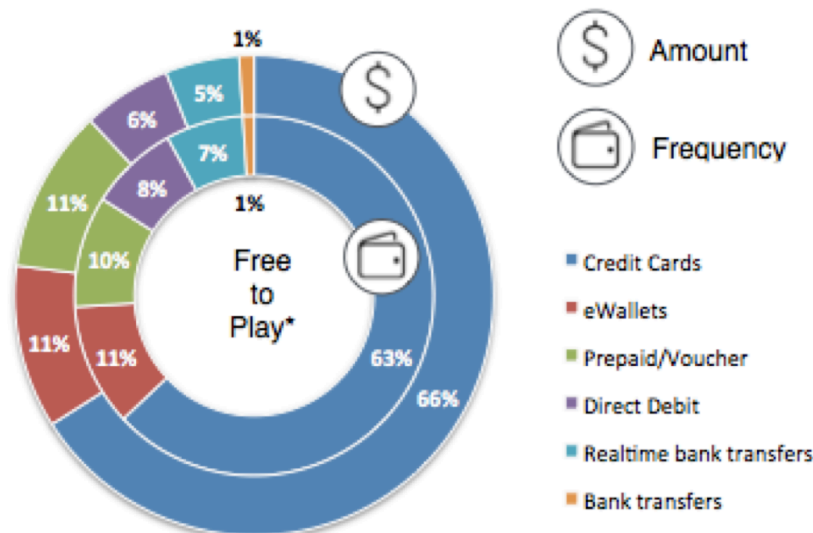
⁴⁸ *Mobile Games Market*, SuperData, August 2014.

tively, micropayment methods need to improve in three key areas: security, processing costs and ease of use.⁴⁹

On a global scale, payment methods are evolving. Approximately two-thirds of all transactions are made using credit cards and debit cards, both in terms of the number of transactions and in terms of their total value. Alternative payment methods account for approximately one-third of all transactions. (See Figure 13.)

Convenience is the overriding factor for influencing payment method choice. Although consumers still view credit cards as the payment method most typically associated with transactions, e-wallet usage continues to grow across different platform types, rising significantly for mobile phones, PCs and tablets, as these typically have an association with a particular marketplace (such as PayPal and eBay in the retail world). As the use of smartphones and tablets continues to gain traction amongst video gamers, the popularity of e-wallets will continue to rise.⁵⁰

Figure 13: Frequency of Payment Methods with Free-to-Play Games



*Free to play models (inc. F2P Subs, F2P Virtual Currencies, Item Selling, Extensions/Extra levels)

The rise of alternative payment methods is suited to youth audiences and emerging markets where access to e-commerce enabled credit and debit cards is limited.⁵¹ What are currently seen as alternative payment methods could well become the de facto methods of the future, potentially involving higher levels of integration – for example to transfer virtual currencies between players or even across different video games.

Alternative payment methods include:

⁴⁹ *Monetizing Digital Media: Creating Value Consumers will Buy*, Ernst and Young, <http://www.ey.com/GL/en/Industries/Media---Entertainment/Monetizing-digital-media--creating-value-consumers-will-buy>.

⁵⁰ *Video Games Payment Preferences*, Worldpay Whitepaper.

⁵¹ *The Shifting Games Video Landscape: Payment, Intelligence and Trends*, Global Collect, March 2013.

- Real money-based e-wallets, which operate like an in-game or on-console bank account. This model is used by the PlayStation Network, Steam and parts of the Xbox Live Marketplace.
- Points or credits-based systems, where real currency is converted into virtual currency. This model is currently used by the Xbox Live Marketplace (although is being phased out), *Second Life* (Linden Dollars), *League Of Legends* (Riot Points), *Lord Of The Rings Online* (Mithril) and *Draw Something* (Gold)
- Direct debits or direct transfers
- Cash vouchers or prepaid cards
- Mobile phone carrier billing, which appears directly on a phone bill.

It has been shown that having more than one means of paying removes friction and helps to increase willingness to pay. Adding just one alternative payment method has been shown to increase the conversion of players to payers by 14%.⁵²

3.2 Advertising

For even the most successful companies, advertising constitutes only a fraction of total revenue. A survey of video game executives conducted by Video Games Intelligence⁵³ found that companies earning at least 70% of their revenue from advertising represented only 10% of respondents, of which more than half depend entirely on advertising as their sole method of monetization.

For larger companies there is merit in adding advertising to a hybrid strategy. It has been observed that: “There are a lot of start-ups trying to fix the advertising problem. If you’re a larger company then it makes sense to have some resources for ad sales, but not for smaller games companies. I would estimate that advertising is maximum 5% of revenue for games that implement a hybrid model. Even a very large company like Zynga is reportedly earning only 10-15% of their revenue from advertising.”⁵⁴ Smaller companies seeking revenue through advertising will almost certainly need to go through a third party in order to maximize efficiency.

In free-to-play games, the opportunity for advertising is a lot smaller than is the opportunity for in-app purchases. However, advertising allows companies with freemium monetization models to cast a wider net and better monetize non-paying players, providing a more consistent revenue stream over the long run.

A recent trend towards value exchange advertising is changing the ways ads are perceived in games. In this model, players can instantly earn free sessions or in-game items in exchange for watching branded advertisements. Players who don’t want to part with their cash can still be monetized by watching video ads, for example, integrated into the game, providing a less disruptive play experience.⁵⁵ One recent study reported value exchange advertis-

⁵² David Radd, “Exclusive: A Primer on Monetization of F2P Games, [a]list daily, December 28, 2012.

⁵³ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014.

⁵⁴ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014, page 10.

⁵⁵ <http://venturebeat.com/2014/03/10/chartboost-launches-video-and-in-game-ads-to-boost-mobile-game-monetization/>

ing is generating revenues for developers while driving greater player engagement, through more hours of game play with the intent to purchase premium items.⁵⁶

Andrew Lim, CMO of CMA Megacorp, sees the attraction of advertising as very much dependent on platform. “In terms of advertising, there are some scenarios where it’s worth looking at, particularly on Android because the user base isn’t as willing to spend.”⁵⁷

Other stakeholders predict that advertising methods such as deep ad integration will be key to monetization models involving well-known brands.⁵⁸

3.3 Premium

A few years ago, a premium game would have designated a high quality, big budget game with a costly price tag. Today, premium refers to any game that must be purchased to be played, from a 99-cent download for a casual mobile game to a \$50 dollar console game.

The premium game monetization model has perhaps undergone the greatest number of transformations since the early days of single player console games in the 1980’s. Premium games have evolved to be sold digitally through online marketplaces controlled by console platform holders (i.e., Microsoft, Sony and Nintendo), as well as third party distributors. Premium games have seen significant price erosion and regardless of the platform, they may also include in-game stores seeking to extract additional value from players through in-game purchases.

Premium games exist on all platforms, and are priced according to the type of game experience being offered. While the model for games is shifting away from the premium model, there is still a significant market for high quality console games that offer an extended and deeper game experience.

In general, the premium model is seen to be successful in the following scenarios:

- When there is a strong demand for the product, particularly niche areas;
- There already exists a strong brand and trust has been established with users such that they are willing to pay;
- There is not a lot of competition that will almost certainly drive the price down;
- Reach is not important as it will be much smaller because of the existence of a “pay gate”;
- There are no ongoing feature or content costs that can drive up the average cost of supporting a user to levels higher than what the user paid for the product.⁵⁹

As they proceed through the path to purchase, players of premium games seek different information – for example assets released by the company pre-launch, tips for advancing

⁵⁶ <http://www.macrumors.com/2014/03/31/ios-users-prefer-freemium-games/>

⁵⁷ *Game Monetization: Choosing A Strategy that Works*, Video Games Intelligence, October 22, 2014, page 11.

⁵⁸ Interviews conducted for this study.

⁵⁹ “Premium versus Freemium versus Subscription,” Lattice Labs Blog, September 13, 2013.

through the game shared at the time of the launch, and downloadable content extensions post-launch. In addition, players are increasingly seeking ongoing engagement.

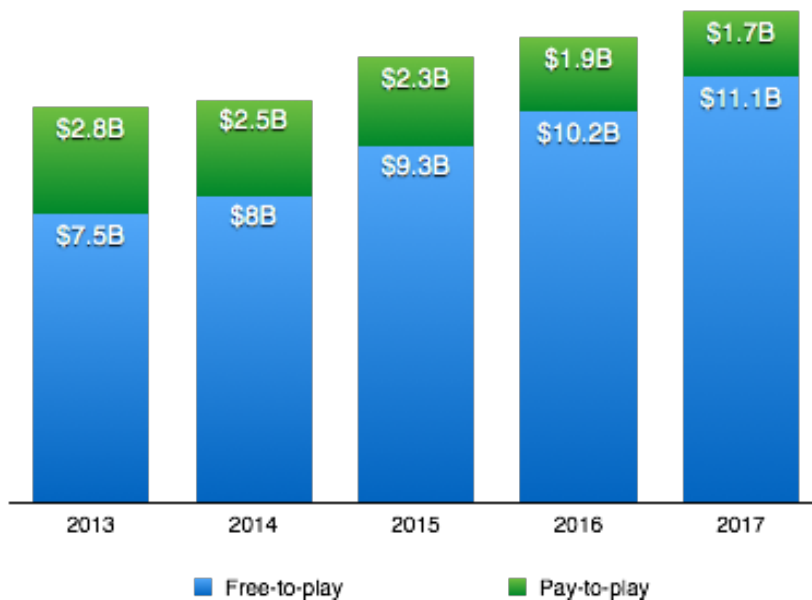
Pre-purchase options are one way that companies are incentivizing the sale of premium games. For example, Steam's Early Access program allows players to access games in their beta (incomplete) versions and to provide feedback to developers as they continue to develop the final version of the game. This model can also provide developers with funding to complete their game.⁶⁰

3.4 Subscription

The concept of paying a regular, flat fee for access to a game first got its start in the mid-eighties,⁶¹ when many companies invested in the development, marketing and release of signature games. With the proliferation of mobile devices and as free-to-play games became more common, online gamers became less willing to pay a recurring monthly expense.⁶² *World of Warcraft*, is today the most successful remaining subscription-based game, though even its player base has fallen from its peak of twelve million subscribers in 2010, to about 7.6 million today.⁶³ By comparison, formerly successful subscription games like *Star Wars: The Old Republic* by Electronic Arts, are now offered on a free-to-play basis after the number of subscribers decreased dramatically.

Figure 14 shows the increasing worldwide importance of revenues from the free-to-play monetization model for MMO games and decline in revenues from pay-to-play models.

Figure 14: Revenues for MMO Games: Free-to-play versus Pay-to-play⁶⁴



⁶⁰ Steam website: http://store.steampowered.com/earlyaccessfaq/?snr=1_200_200_Early+Access.

⁶¹ Orland, Kyle, "Good Riddance: the death of online gaming's monthly subscription model," *Ars Technica*, August 1, 2012.

⁶² Chapman, Lizette, "Online Gaming Shuns Subscription Model Spawning by 'World of Warcraft' Free-to-Play Becomes the Rule for Gazillion Entertainment and Other Startups," *The Wall Street Journal*, May 2, 2014.

⁶³ IBID.

⁶⁴ *2014 MMO Games Market*, SuperData Research, 2014.

As the games market shifts to the free-to-play monetization model, many pay-to-play MMOs have opted to hybridize their monetization models to include free-to-play models of game-play.

In today's environment, it would be difficult for a game such as *World of Warcraft*, using a subscription model of monetization, to reach the same level of subscribers. Its current dominance is due to the game's multi-year head start and strong network effects. Subscription games have typically relied on a blockbuster launch to attract a critical mass of subscribers and create a community entailing significant upfront game development and marketing costs. This makes the model far riskier today in a market where competition comes from a plethora of less expensive free-to-play games that are being developed in stages, scaling up gradually as their popularity with players grows.

Other factors also drive costs of subscription games. Monthly subscriptions incentivize players to rush through content as quickly as possible so that they will not have to pay again the next month. As a consequence, keeping players engaged requires a steady release of content, which is expensive to produce, and gobbled up in just a month's time.

Other industry observers are of the view that the subscription model can be a robust and even first-best revenue model, under certain conditions.⁶⁵ However, subscriptions prevent game companies from being able to price discriminate – that is, everyone pays the same price for access, rather than being charged for how much they value that access.

4. Summary Observations

Both the rise of revenues generated by the games market and the increasing number of people playing games are positive developments for companies that are monetizing in this space.

Canada ranks sixth among the countries with the most transactions for game purchases. On a country-by-country basis, Canada is ranked in the global top four when it comes to average amount spent per paying gamer together with Korea, Japan and the United States.⁶⁶

The mobile games market is one of the fastest growing segments of the video games market, largely propelled by micro-transactions.⁶⁷

The rise of cross-screen gaming impacts on the monetization strategies of companies particularly in their consideration of which screen or screens to develop for as well as the need to acquire a deep understanding of the purchasing behaviour of consumers on different screens. The majority of Canadians continue to play games on their PC, while almost 20% are now playing across four separate screens.

Games companies have a number of established monetization models to consider, some of them tied to specific types of games. With the rise of mobile and the ensuing race to the bottom of the pricing scale, it is clear that freemium has become the key monetization route with

⁶⁵ Isaac Knowles, "A Measured Defence of the Subscription Model," *Gamasutra*, September 17, 2013.

⁶⁶ Canadian Games Market Infographic, NewZoo, December 2013.

⁶⁷ *Portable Gaming Spotlight: 2013 Review*, App Annie, February 2014.

games being offered for free and monetized via micro-transactions, a trend that has extended to other game platforms, largely supplanting the subscription model of digital PC games.

The large volume of free and low cost mobile products has directly impacted the prices that can be obtained for games on other platforms, where prices for game have also fallen. This presents a challenge for companies monetizing their products. The wide availability of free games has vastly driven user acquisition and it is now possible to have free games experiences with millions of active users. It is expected that this will continue to be the main driving force behind market expansion in the coming years. To be successful, companies must acquire and retain vast numbers of players.

A critical mass of game players is necessary to support analytics-driven development, and to monetize a free to play game profitably. Only a small percentage of players will become payers. Successful companies recognize the value of non-paying players to support their promotion and acquisition efforts through the power of word of mouth, as well as their value to advertisers.

Monetization in free-to-play games is linked to player retention, as the longer people play a game, the more likely they are to spend money in it. Player retention depends on successfully interpreting user demands and providing refreshes and upgrades to a game in keeping with what players want. Game designers must be skillful in designing their game so as to create an optimum economy that balances resource generation, resource destruction, and for social games, trading. Given the short lifecycle of players of free-to-play games, companies need to introduce more expensive items early on to maximize their revenues.

On a global scale, payment methods are evolving because of the freemium model. Half of all transactions are made using credit cards and debit cards, with the remaining payments made through alternative methods. The rise of alternative methods may open the door to access to a greater pool of potential consumers.

Advertising models have evolved from unpopular promotions that interrupted game play to advertising experiences seamlessly integrated to game experiences, such as value exchange ads that leverage in-game player motivations to attract eyeballs. Some believe that well-known brands using deep product integration will be key to monetizing games in the future.

Premium games have seen significant price erosion but there is still a market for high quality games offering a deeper game experience over an extended period.

The pricing limitations and prohibitive start-up costs of subscription-based games are making it more difficult to monetize games through this model.

C. Monetizing Digital Media: Trends and Approaches

1. Preamble

In this section, we examine the key trends that are helping to maximize revenues for digital media content. These include the use of a 360-degree content approach by companies, integration of second screen experiences and the shift from browsers to mobile for viewing videos.

We then provide a description of the monetization models and strategies being used by companies.

2. Trends to Consider for the Monetizing of Convergent Digital Media

2.1 A 360-Degree Content Approach to Maximize an Array of Monetization Methods

Producers of convergent properties, particularly children's properties, are taking a 360-degree content approach to maximize the monetization potential of their original properties.

Companies embracing this approach begin at the earliest stages of concept development to shape content decisions according to the potential of various platforms or types of content to generate consumer value and returns through multiple forms of expression and distribution channels. The approach seeks to optimize 360-degree user experiences, engaging consumers where they live online.

These companies are using a range of monetization models adapted for online content, mobile apps, and interactive games based on consumer desire to interact with their property. Monetizing also extends to exploiting opportunities for third party licensing or merchandise. In most cases, the linear television component of the property is leveraged for its ability to support brand building and discoverability and associated properties may be deployed to coincide with particular television events.

Ideally, content related to the brand rolls out over an extended period of time, increasing opportunities for deeper and more engaged user experiences and increased sales.

Digital extensions of convergent digital media may also serve to encourage sales of television properties by making them more attractive in a highly competitive international market. As producers interviewed for this report noted, the digital extensions are often included in the overall license fee for the television property, as marketing assets.

2.2 Second Screen Experiences Can Generate Revenues

Second screen viewing combines opportunities for engagement with the potential for generating new revenues.

The latest industry data reveals that 35% of Canadian and 84% of U.S. mobile device owners are watching television with a second screen in hand.⁶⁸ Audiences are said to be using their second screens to deepen their engagement with the programs they are watching, from searching for information on characters and plot lines, to research and purchasing products and services they see advertised.

Some broadcasters have experimented with their own Social TV apps to boost their ad revenues through “companion ads.” One example is Fox Now, a series of second-screen apps developed by Fox Broadcasting, in the U.S., on which viewers could have access to exclusive companion content and companion advertisements and could chat with each other.⁶⁹

Third party app developers with broad distribution such as Shazam or ConnectTV offer other opportunities to leverage second-screen viewing to monetize content, by syndicating second-screen content and companion ads.⁷⁰

A Canadian study notes that broadcasters who implement second screen strategies could potentially see their advertising exposure increase tenfold, greatly increasing their value to advertisers.⁷¹ The user experience of social TV is considered a critical element for monetization, to attract and retain audiences.

In addition to social experiences provided by second-screen apps, major social networking companies Twitter and Facebook have introduced their own programs to monetize the social TV chatter on their services.

Sixty percent of TV chatter on Facebook is said to take place during program airings, 80% of it originating from mobile devices and primarily aimed at entertainment programming. Discussions on Twitter are considered even more important,⁷² with an estimated one million Americans discussing television programs on Twitter each day, broadcasting their tweets to a total of 11 million readers.⁷³ In Canada, 40% of Canadian adults are said to tweet about TV programs.⁷⁴

Following the experience of its Social TV ad program, Twitter Amplify, earlier this year Twitter announced the acquisition of two European start-ups with a view to helping advertisers and broadcasters take advantage of conversations around television content on Twitter.⁷⁵ For its part, Facebook launched its own social TV program, Chatter, in partnership with social media

⁶⁸ *Fast Friends: How Brands are Capturing the Attention of Social TV Audiences*, Nielsen, September 15, 2014. Source for Canadian data: MTM.

⁶⁹ Ryan Lawler, “With Help From Watchwith, Fox Syncs Social TV content with Second-Screen Apps Shazam, Voggle, ConnectTV, and NextGuide,” *TechCrunch*, February 26, 2013.

⁷⁰ Chris Smith, “Where’s the money in social TV and second screening?” *The Guardian*, August 9, 2013; Tom Cheredar, “TV industry-backed second screen app ConnectTV raises \$1.4 million,” *Venture Beat*, June 26, 2013.

⁷¹ *The Second Screen and Television: Benefits and Impacts*, Evolumedia Group, March 7, 2013.

⁷² Jeff Bercovici, “Who rules the second screen: Facebook or Twitter?,” *Forbes*, February 12, 2014. See also *Watching With Friends: How TV Drives Conversation on Facebook*, Second Sync, February 2014.

⁷³ *Social TV and the New Digital Consumer*, Nielsen, February 15, 2014.

⁷⁴ Source: MTM.

⁷⁵ Seth Fiegerman, “Twitter Expands Social TV Efforts with Two Acquisitions,” *Mashable*, March 31, 2014.

television analytics company SecondSync. The service will provide advertisers with detailed information on Social television data on Facebook.⁷⁶

It is clear from these developments that opportunities exist to monetize television viewing on a range of platforms. A recent study by metrics company Nielsen found a high overlap between people who tweet about TV and those who tweet about brands, who in turn have a high level of influence, amplifying marketing messages throughout their social networks.⁷⁷ As marketers seek to engage viewers through social networks, it will be important for brands and broadcasters to understand how these viewers engage with their content.⁷⁸

2.3 Shift from Browsers to Mobile for Viewing Videos

Some producers of convergent digital media have in some cases been able to monetize their digital assets in the online video market. An interesting recent development is the monetization of web series. Some companies interviewed for this report are experimenting with monetizing original dramatic series.

Online video viewing in the U.S. market has grown 43% in the past year, to set a record of 38.2 billion views. Canadians are said to view more online video. According to Comscore, 74% of Canadians watch online videos, and spend 1,769 minutes per month watching them, compared to 1,237 minutes spent by American viewers.⁷⁹

In particular, viewing of online video is sharply increasing on mobile devices, with upwards of 26% of online video views now on a mobile device - up 57% over 2013 in the U.S. market. Online video viewing on smartphones is now more popular than tablet viewing. Industry metrics company Comscore calls mobile “the single most important change in the media landscape since the invention of the Internet.”⁸⁰

In Canada, Canadians are said to be rapidly increasing their consumption of online video and authenticated television (TV Everywhere) via mobile devices, with a 50% increase in viewers who watch videos online almost everyday between 2012 and 2013. Three out of four Canadians are said to own smart phones, a higher rate than in the U.S. or other developed countries.⁸¹

As companies develop streaming video apps, they are increasingly interested in finding advertisers through which to monetize their video streams. Advertising views for online video in the U.S. market have increased by 25.8% in the same year and digital ad spends are expected to overtake television advertising expenditures by 2016.⁸² In Canada, online video ad spending is projected to grow to over \$360 million in 2016.⁸³ These trends point to opportuni-

⁷⁶ John Abbruzzese, “Facebook Steps Onto Twitter’s TV Data Turf,” *Mashable*, January 30, 2014.,

⁷⁷ *Connecting with Social Brand Ambassadors*, Nielsen, July 14, 2014.

⁷⁸ *Fast Friends: How Brands are Capturing the Attention of Social TV Audiences*, Nielsen, September 15, 2014

⁷⁹ *Canada Digital Future in Focus 2014*, Comscore Inc., 2014.

⁸⁰ *U.S. Digital Future in Focus 2014*, Comscore Inc., 2014.

⁸¹ *Canada Digital Future in Focus 2014*, Comscore Inc., 2014.

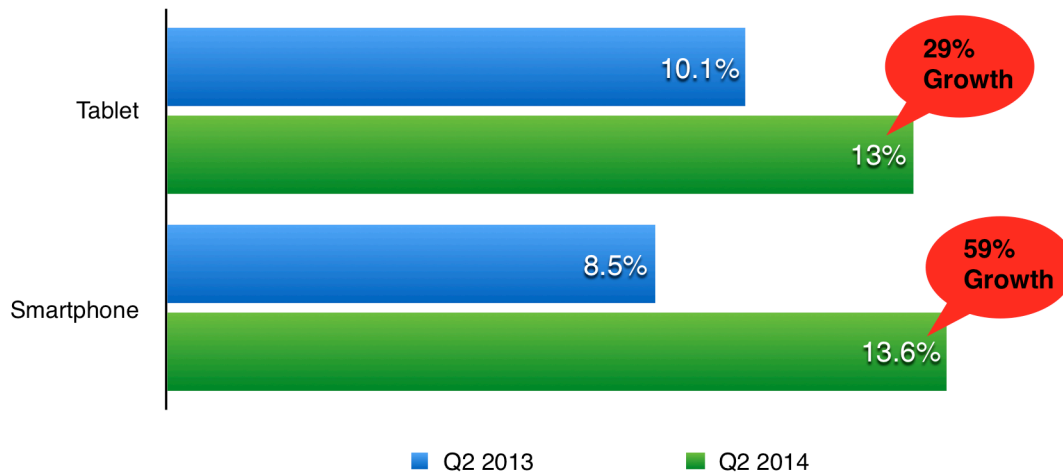
⁸² Tim Peterson, “Digital to Overtake TV Ad Spending in Two Years, Says Forrester,” *Ad Age*, November 4, 2014.

⁸³ *A Breakthrough Year: Digital Video 2013*, Brightroll Canada Video Advertising Report for IAB Canada, 2013.

ties for producers, though the challenge will be to ensure that ads are properly tracked and engagement measured to meet the needs of advertisers.⁸⁴

Figure 15 shows the growth in online video on tablets and smartphones in the U.S. market.

Figure 15: Increase in viewing of online video, by mobile platform (U.S. market)⁸⁵



Online TV (authenticated TV Everywhere services) viewing has shifted away from browser-based access to a wider variety of devices, including apps, with Android apps realizing a 28% increase over 2013.⁸⁶ (See figure 16.)

These trends are impacting on the monetization strategies of companies as they experiment with content on mobile platforms. Advertisers are increasingly interested in cross-platform advertising, particularly integrating mobile advertising. A recent survey in the U.S. found that 80% of advertisers are experimenting with mobile in their campaigns and intend to continue to invest in them in the coming year.⁸⁷ In Canada, it is expected that in three years, mobile screens will become the most important screen for multi-screen ad campaigns.⁸⁸

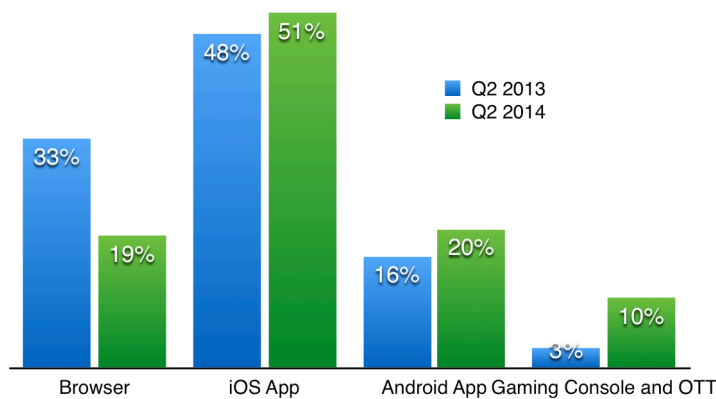
⁸⁴ *U.S. Digital Video Benchmark: Adobe Digital Index Q2 2014*, Adobe, 2014.

⁸⁵ *U.S. Digital Video Benchmark: Adobe Digital Index Q2 2014*, Adobe, 2014.

⁸⁶ *U.S. Digital Video Benchmark: Adobe Digital Index Q2 2014*, Adobe, 2014.

⁸⁷ *The Mobile Tipping Point*, Nielsen, 2014.

⁸⁸ *Optimizing Integrated Multi-Screen Campaigns: Survey Research Benchmarks and Trends*, Nielsen and IAB Canada, 2014.

Figure 16: Increase in viewing of TV Everywhere, by platform⁸⁹

3. Monetization Models and Strategies

3.1 Licensing and Merchandizing

Licensing and merchandizing currently represent the most important means of monetizing convergent digital media content as well as original web series. Producers of convergent content are monetizing their intellectual property (IP) through licensing, for example, to broadcasters or manufacturers of merchandise (such as toys or apparel). Licensing is also being pursued with third party app developers, including for interactive digital books for the educational and children's markets.

One producer interviewed explained how his company approaches the development of new story ideas with a well-thought out commercial approach to launching properties, including interactive development, merchandizing and brand planning to maximize licensing opportunities. "We really try to think about what our audience will ultimately expect once a new show launches...Our strategy is to make sure we have thought through what it will take to deliver on their love of the property, and we try to choose properties that can naturally evolve that core story across multiple touch points."⁹⁰

Web series are being licensed to online content aggregators and broadcasters. Some content aggregators, such as Amazon Prime Instant Video, are licensing original series they commissioned to provide Amazon Prime users with an enhanced experience. Some Canadian producers interviewed for this study have been successful in licensing their content to Hulu. However, overall these licensing deals are said to be rare for Canadian producers and the licenses are small. In some cases, the licensing is based on a revenue sharing arrangement.

One producer interviewed for the study was successful in licensing a convergent web series to a different broadcaster (other than the commissioning broadcaster). The company is now exploring producing stand-alone original web series to create a potential new revenue stream.

⁸⁹ U.S. Digital Video Benchmark: Adobe Digital Index Q2 2014, Adobe, 2014.

⁹⁰ Interviews conducted for this study.

One means of extracting value from web series is to repurpose the content in newly edited versions for licensing as feature films or television half hours. Producers indicate that to the extent possible, it is preferable to provide potential buyers access to their content in a range of formats (i.e., as television programs, web episodes and feature films) in order to appeal to different types of broadcasters or aggregators, and to provide these with both traditional content and web series with which to experiment. In this regard, one company has noted the importance of planning the eventual TV play at the development stage of a new web series, both from a business and creative perspective.

The sale of merchandise, such as songs, ringtones, DVDs or other items, provide a further avenue of monetization for some properties. The web series *Hailey Hacks* produced by Story2oh generated significant revenues from a range of monetization channels, including giving away teaser content and selling the longer form episodes, affiliate marketing relationships, merchandizing and pre-roll advertising.⁹¹

3.2 Advertising and Brand Sponsorships

A study conducted on the web series sector in Ontario found that in order to monetize their content, 70% of original web series creators drew on advertising - the most common monetization model. Sponsorships were second, with 43% of web series creators reporting that they worked with sponsors in 2013.⁹²

It is said to be very challenging to attract a brand sponsor for original web series and that it is often easier to find opportunities for product placement.

To succeed with brand sponsorship, producers must demonstrate audience engagement with their content. As noted in one study, “Established niches or communities of interest are required for successful web series. Given the move in advertising to hyper-targeted advertisements, knowing how to interact effectively with one’s niche viewership is critical...This “niche” approach and access to detailed analytics is perceived by many web series creators to be a key success factor in building audiences,”⁹³ which are of interest to brands.

Jonas Diamond, CEO of digital media producer iThentic, notes that, “Brands like Red Bull, GE, or Intel are becoming viable publishers of content, and are creating major platforms for driving audiences. As such, brands may become an increasingly important partner for web series producers looking for distribution.”⁹⁴

The introduction of content partner channels on Hulu and the ability for content brands to monetize their audiences through YouTube has changed the world of online platforms. “Handing over your audience management to YouTube, or to a YouTube aggregator like Machinima or Maker Studios, means losing control over that audience. But, owning 1% of a bil-

⁹¹ *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014

⁹² *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014

⁹³ *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014, page 28.

⁹⁴ *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014

lion dollar business is still better than 100% of a zero dollar business.”⁹⁵ Needless to say, more popular video content with a greater number of views garners higher ad revenues.⁹⁶

3.3 Monetizing Convergent Apps - Premium and Hybrid Models

Apps have become a significant new means of monetizing convergent IP through a variety of hybrid monetization models. These include premium models and freemium models with either in-app purchases or advertising or some combination of these.

In some cases, apps are being monetized through the premium model based on the strength of the brand. These may include video viewing or game apps. Freemium games developed as convergent digital content by companies interviewed for this report are seen as a means to build viable, sustained revenue streams whose growth is potentially unhampered by the limitations of the television business model.

Advertising provides another means of monetizing users of free-to-play games associated with television content. Some companies are experimenting with advertising based on user behaviour, rewarding in-app spenders with fewer ads. Others are trying pre-roll ads for in-app video content. Advertising may comprise up to 30% of app-related revenues. Apps are also being monetized through a mix of in-app purchases and advertising revenues.

Some producers interviewed for this study have also begun experimenting with pre-roll ads to monetize video content in their apps.

A number of challenges face companies developing apps for children, where there is a need to create safe play and learning environments, free from exploitative methods.⁹⁷ Developers choosing to monetize freemium apps through in-app purchases must be cautious to respect the balance of privacy and security required of them while finding opportunities to monetize their apps. For example, selling consumable items such as in-game currency is not advised, though there is said to be room for acquiring new content such as expansion packs, where payment is not related to game play and where parents permissions are required to obtain payment.

Developers choosing to monetize their apps through premium sales often struggle to find their audience.⁹⁸ As one industry veteran notes, “the bottom line is that it's extremely difficult to build a successful kids' mobile game with an upfront price. The vast majority of games in the App Store are free with [in-app purchases].”⁹⁹ It is instructive to note that even the highly successful children's app developer Toca Boca finds it difficult to monetize through the paid add model. “There is a very small head and a very, very long tail. And the angle at which the head drops to the tail is very steep.”¹⁰⁰

⁹⁵ Jonas Diamond entry, *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014.

⁹⁶ *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014.

⁹⁷ *An Ethical Framework for marketing and monetizing digital content media for a 'self-published' children's/youth audience*, Kids Media Centre, July 2013.

⁹⁸ “Toca Boca refines its craft after 40m downloads of its apps for kids,” The Guardian Apps Blog, 2014.

⁹⁹ Michael Acton Smith OBE, CEO and creative director at Mind Candy, quoted in Richard Stanton, “Selling Candy to Babies,” *Polygon*, April 3, 2014.

¹⁰⁰ Bjorn Jeffery, Chief Executive, Toca Boca, quoted in “Toca Boca refines its craft after 40m downloads of its apps for kids,” The Guardian Apps Blog, 2014. Toca Boca recently partnered with Toronto-based conver-

Bjorn Jeffery, Toca Boca's chief executive, notes that most problems are related to discoverability, as "sheer amount of things that come out is overwhelming for developers, but also for parents."¹⁰¹ Indeed, one of the key challenges that producers in the children's space face is the intense competition from other well established brands. Apps are more likely to be downloaded by viewers seeking extended engagement with their favourite TV shows.

4. Summary Observations

Companies have been making digital extensions of television programs for many years but there are now new revenue opportunities thanks to the app economy, the rise of social TV and second screen experiences and advertising opportunities for online video.

The successful deployment of 360-degree content approaches by producers of convergent properties provides important lessons in monetizing convergent content. On the other hand, trends in social TV and online and mobile video underscore the potential for monetizing content through advertising revenues. While multi-platform advertising campaigns are still in their early days, advertisers intend to continue to increase their investments in them.

Monetization models for convergent digital media include licensing and merchandizing, product integration and brand sponsorships and freemium, premium and hybrid monetization models for convergent apps.

There is also potential to monetize online video, including original and convergent content, through in-app advertising.

gent production company Zinc Roe Productions to form a new company called Sago Sago. (Bjorn Jeffries, "Toca Boca Acquires zinc Roe Tickle Tap App Series and Development Team," March 6, 2013, Toca Boca press release.)

¹⁰¹ Bjorn Jeffery, Chief Executive, Toca Boca, quoted in "Toca Boca refines its craft after 40m downloads of its apps for kids," The Guardian Apps Blog, 2014.

D. Perspectives from Stakeholders: Challenges and Opportunities

1. Preamble

This section presents the perspectives of stakeholders interviewed for this study on the challenges and opportunities in monetizing interactive digital media content.

2. Challenges and Opportunities in Monetizing Games

2.1 Creating Viable Games as Services

The concept of games as a service first emerged with MMO games.¹⁰² This model marked a major shift in how games are developed and monetized.

Stakeholders for this study point out that in order to create viable games-as-services, they must be designed to be long-lasting. Developers are often working with limited budgets and the challenge is to determine the most efficient way to extend the experience of a game. One company points out: “Some companies launch a game and they may get great metrics but nothing happens after a month because no one thought about how the experience was going to extend beyond that. The challenge is the vision and scope of the game. Creating games that have rich potential is really difficult.”¹⁰³

Trends have shown that consumers are willing to play continuously and want access to games that are, in principle, free. Ideally, their game continuously improves and expands, as developers continue to update and upgrade the game experience based on player feedback.¹⁰⁴

The design of games has evolved from single story lines with very limited player. As it was pointed out, “Now when we launch a game, we launch content systems. For example, players can upgrade their equipment to make them better players so that they can progress through the game.”¹⁰⁵ Content must be thought of in a way that can be continuously updated for extended periods of time to build small incremental ways that people can spend money.

Indeed, a number of developers interviewed for this study noted that the real development work for a free-to-play game begins once the game is live and has a user base. One stakeholder described a game at this stage as “a living thing.”

2.2 Building and Understanding Your Base of Users

Analytics – real time quantitative data gathered from players using a game - is critical to successful monetization.

¹⁰² Chernyak, Ulyana, “Understanding” Games as a Service” for Game Development,” *Gamasutra*, October 13, 2014.

¹⁰³ Interviews conducted for this study.

¹⁰⁴ *The Bigger Picture: Key Facts and Trends on the Ever Changing Market Global Games Market*, Newzoo, 2012.

¹⁰⁵ Interviews conducted for this study.

The use of data analytics is perceived to be increasingly important in the monetization efforts of a company because it is important to understand the reasons why sections of a game or characters are not enticing players. The challenge becomes how to map the growth of what is influencing the players.

The greater the number of users of a game, the more reliable are the analytics in identifying trends. One company put the minimum number of daily active users at 10,000 to have a sufficiently large set of data from which to study behaviour patterns across the entire price point curve. In interviews conducted for this study, independent game developers point out that attaining a critical mass of players is one of their biggest challenges, largely due to smaller marketing budgets that make it difficult to compete on the same scale with larger companies. Soft launches in markets where acquiring new users is less expensive allowing companies to observe what is working and what isn't.

One industry observer points out that the best way to acquire customers is by word of mouth: "You want to try to figure out how to make players include their friends. So you design a game where it's better if you do it together. For example, in *World of Warcraft* they designed an overlapping skill buff system. In general...the metric is that five people playing together are each, individually, 20% more productive. You design it so instead of 10 points an hour individually, a group of five gets 60 points together."¹⁰⁶

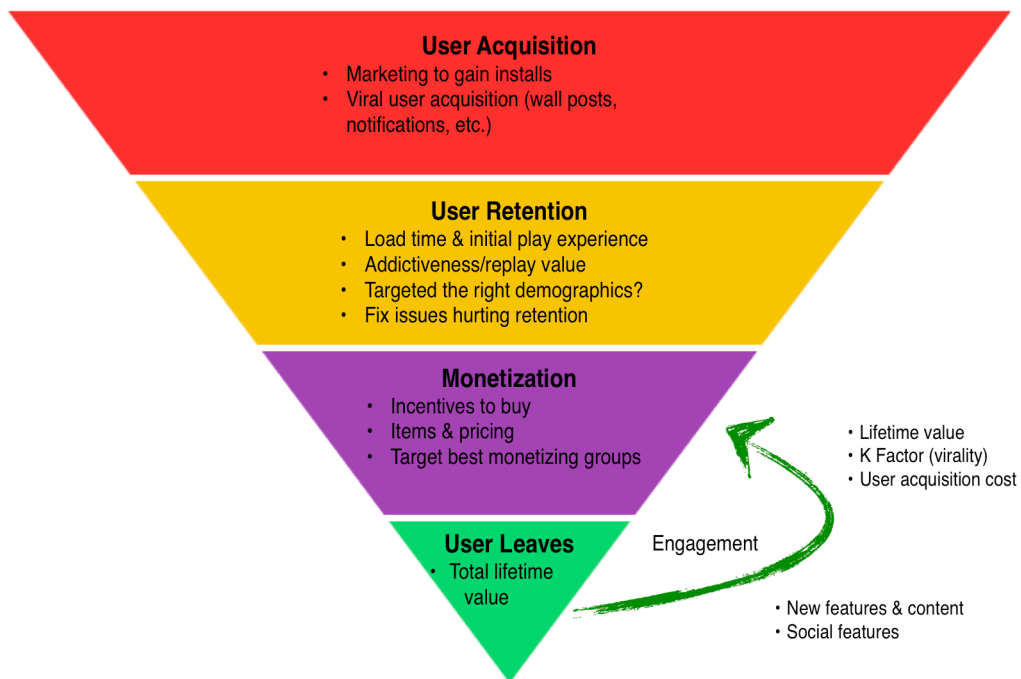
An important development has been getting featured in the Apple App Store, which is said to be worth on average, 200,000 installs (downloads). Getting featured on Twitch.tv is said to be worth 10,000 installs. In addition, word of mouth promotion should generate between half and three-quarters of new users.

With analytics, developers generate user profiles to help them understand what sort of actions the user is taking, what the first time user experience funnel looks like, and where friction points are in the game. As it is explained by one company: "When users play a game, it is important to nudge them to complete specific event chains (called funnels) which guide them towards coming back later, making viral posts, getting deeper into gameplay, or monetizing. This can be done by creating specific event chains triggered at natural points in the gameplay. As you operate your game, you can gauge the performance of these funnels at driving users towards retention, engagement, virality, and ultimately monetization. Over time you want to test to tweak your funnels via testing to be as effective as possible towards achieving their goals."¹⁰⁷ (See figure 17.) The data will allow companies to make modifications.

Developers also rely on a range of different metrics, such as daily and monthly actives, and a three-months range in order to assess if the game will have a rich community. The use of analytics is essential because it not only helps companies determine where they stand in the market relative to other games but also because it assists in making decisions on where to spend marketing dollars. Analytics helps companies assess if their referrals are coming from other users or from a specific ad network or Facebook stream posts or social media.

¹⁰⁶ *Game Monetization: A Bright Future*, Video Games Intelligence, October 3, 2014.

¹⁰⁷ "Breaking Into Social Gaming - A Must-Read Guide to Entering the Facebook Game Space," *Social Times*, August 26, 2011.

Figure 17: The Analytics Funnel and Monetization¹⁰⁸

One company notes: “Releasing your title is important and we have been fortunate that some of our games are still around after four and five years. Keeping up that level of innovation is challenging. Early on we recognized that we are building communities of players that are engaging with these products. So having that feedback loop for them to be able to talk to us and to feel that we are listening to their concerns is important.”¹⁰⁹

Another stakeholder noted that with respect to qualitative data, the simplest way to gather information is to “go to where your players are and have conversations with them. Engage your community wherever they currently are. If they don't have a place to talk then you should set up forums. Find any way that you can to engage with your community and then track the actions they actually do through the data to understand how their behaviours match their actions.”¹¹⁰

2.3 Discoverability

Discoverability is a challenge that has implications for monetization.

One industry analyst has stated, “Like any other industry, hits and discovery in the digital games industry will increasingly be driven by the marketing spend on the game. “The naïve

¹⁰⁸ “Breaking Into Social Gaming - A Must-Read Guide to Entering the Facebook Game Space,” *Social Times*, August 26, 2011.

¹⁰⁹ Interviews conducted for this study.

¹¹⁰ Interviews conducted for this study.

notion that by putting free to play awesome games into the ecosystem, they will get lucky and go viral is over.”¹¹¹

The crowded marketplace now demands that companies select the right distribution model and spend significant resources for their games to get discovered. The choice of promotional partners is key to dealing with the discoverability challenge. Many companies note that being promoted by Apple is important but not a guarantee of success. One company explained that, “If we get promoted by Apple, our game will stay high in the charts for a week, but then the game will get pushed out by other companies who have the money to spend on big marketing.”¹¹²

Some Canadian independent developers are showing great success in breaking through the noise in the PC/console game market, with marketing strategies linked to strong relationships with platform holders. For Cappybara Games, opportunities to be featured by the console companies, such as through ads on the Xbox Live dashboard, are very important to discoverability. “In all cases, getting your game discovered is the biggest challenge, on Steam, on the App Store, on consoles, on toaster ovens. It's all a challenge to get that prime space. Those big...banners are important. They matter a lot more than people are willing to admit.”¹¹³

From the perspective of Cappybara Games, the opportunity exists in bringing a game to multiple devices, or consoles, or platforms. Its most recent game, *Super T.I.M.E. Force*, launched exclusively for the Xbox 360 and Xbox One, and on Steam for PC a few months later, re-branded as *Super T.I.M.E. Force Ultra*. At the same time, being featured is not enough on its own. The question of discoverability is a broader one for the company, linked to quality.¹¹⁴

One company references the importance of having the name recognition of a publisher attached to their game: “There are thousands and thousands of games coming out every year. The amount of effort to cut through, and to have the name recognition of the publisher associated with your production can really open doors and consumer awareness. We are not trying to build a brand for our company. We don't expect consumers to know us and be waiting for our next game. We are fine with people being excited that our publisher will be launching this game.”¹¹⁵

One stakeholder explained that success may depend on having an existing following of fans: “Top spot games on Steam became hits because they had an existing following.” Among the strategies being used on digital store fronts like Steam or the App Store include the following: getting featured in the top games; reaching YouTube audiences via live streaming or and working with YouTube personalities. YouTube is perceived to be one of the biggest touch points for the discovery of games.

A number of stakeholders were excited by the potential for HTML 5 to disrupt existing models of monetization. They point out that HTML 5 will eventually become the dominant means for providing a seamless experience across-platforms, effectively bypassing app stores and oth-

¹¹¹ *Gamerista 2014: Scenarios for the Future of Gaming*, Gamerista: Digital Video Games Research & Development, February 11, 2014.

¹¹² Interviews conducted for this study.

¹¹³ Brendan Sinclair, “When players speak, “sometimes you just have to eat that” - Cappy Games”, *Games Industry Biz*, May 28, 2014.

¹¹⁴ Brendan Sinclair, “When players speak, “sometimes you just have to eat that” - Cappy Games”, *Games Industry Biz*, May 28, 2014.

¹¹⁵ Interviews conducted for this study.

er intermediaries. According to one industry analyst, strong brands or games have the potential to transcend platforms. "The biggest leverage area is strong cross-platform plays. Think games like *Angry Birds* and *Minecraft*."¹¹⁶

2.4 Accessing International Markets

International markets provide opportunities to monetize games by expanding the player base. While new markets provide considerable new populations to reach, one stakeholder noted that it is necessary to adjust pricing in regions with less spending power. It was also explained that different price points and types of content work better in different parts of the world.¹¹⁷

Some companies interviewed for this study are looking to the Asian market for growth because of the size of the market combined with its high penetration rate of smart phones. One stakeholder explained that opportunities exist to license or co-develop games with overseas partners.¹¹⁸ Canadian companies partnering with distributors in China note the importance of having a significant presence on app stores for Android devices in order to generate sufficient revenues. China, Korea and Japan were mentioned as having substantial mobile markets that require this type of significant presence. Others pointed out that they are more focused on English-language countries including the United States, Australia, United Kingdom, New Zealand, as well as European countries. Some companies said they are beginning to generate sales on mobile platforms in Eastern Europe and Latin America.¹¹⁹

2.5 The Importance of Pricing

For premium publishers, setting appropriate prices is a key consideration. Premium games have seen significant price erosion since the explosion of digital distribution and freemium games.

One game developer noted that, "when we start working on a game we have a price point in mind but we never lock it down until we finish the game. We seek to balance what we think the game is worth with what the market will accept. There are price points that simply are too much or too little depending on the platform." Another company observed that, "some people think that six or seven hours of game play is plenty for \$20, while some think it should be more. One has to find that sweet spot otherwise even if the quality is good, people are going to pass."¹²⁰

Some developers, are confident that the market will continue to support current price points. "I definitely think times have shifted...There are more great smaller, downloadable games. Transistor at \$20? No one even thinks twice. And \$20 used to be like, 'No way an independent game can be \$20. That's crazy!' And now it's pretty common, pretty accepted, pretty comfortable. And deservedly so."¹²¹

¹¹⁶ David Cole, cited in James Brightmans, "Console declines delay \$100 billion mark for industry to 2019 – DFC, *Games Industry Biz*, October 21, 2014.

¹¹⁷ Interviews conducted for this study.

¹¹⁸ Interviews conducted for this study.

¹¹⁹ Interviews conducted for this study.

¹²⁰ Interviews conducted for this study.

¹²¹ Brendan Sinclair, "When players speak, "sometimes you just have to eat that" - Capy Games", *Games Industry Biz*, May 28, 2014.

3. Challenges and Opportunities in Monetizing Digital Media

3.1 Extended and Deepened Engagement and Use of Analytics is Key

According to stakeholders interviewed for this study, creating opportunities for extended and deepened engagement is key to monetizing digital media brand extensions of television properties. One company noted that it took two years of consistent audience building and engagement strategies to monetize their app to the level of a sustainable business. Skillful analysis of user analytics are of great importance in this regard.

One company indicated that licensed merchandizing deals, which could account for up to 25% of overall revenues for some of its convergent projects, are an important driver of engagement.

Audience engagement is said to be a constant focus for web series creators. Social media is an important tool to help producers find and engage with their audiences. Facebook and Twitter are the most widely used social media by web series creators.¹²²

One of the key lessons learned with respect to monetization is the need for continuous new content launches in order to drive engagement. Indeed, one company noted the need to produce a sufficient volume of online web episodes as it takes time to build an audience and to keep them engaged and coming back for more.

As in the freemium mobile games sector overall, mobile game developers in the convergent digital media sector require significant numbers of users to derive sufficient revenues. While the average number of users who pay may be as high as 5%, in some cases, companies noted that fewer than 1% of all users may be making any in-app purchases. A larger user-base is needed as well to provide meaningful information and data on how users are interacting and engaging with the app in order to drive more efficient ongoing development and maximize the conversion of players into payers.

As a television property is sold in foreign markets, the increased visibility may provide new opportunities to expand the app's user base and at a lower cost per acquisition, notably in markets in Asia, Russia or Latin America.

3.2 Monetizing Original Web Series Online is Still a Challenge

Creators of original web series are innovating in largely uncharted waters, where financing and revenue models are still emerging. By being responsive to the type of content that resonates with viewers online, and keeping its budgets low, one producer has found a niche for professionally produced productions that are attracting the interest of audiences, advertisers and broadcasters. The company says it is learning from its experiences and is well positioned to take advantage of new opportunities emerging in this space.

After having successfully licensed a convergent web series, one company interviewed for the study is experimenting with its own content channel on YouTube with productions funded through brand sponsorship. To scale up their production, the company is looking to the U.S. advertising market due to the small size and lack of sufficient financing available through the Canadian advertising market.

¹²² *Industry Profile of the Independent Web Series Creators of Ontario*, Independent Web Series Creators of Canada, May 30, 2014, figure 19.

Producers also noted that license fees for online video content are much lower than for the television market, making it challenging to produce for this space without some other form of financing.

One company has a variety of online channel partners with their own built-in audiences, and is monetizing its content through a variety of licensing deals. It was pointed out that it is important to geo-gate access to its online web properties in order to maximize the revenue potential of sales across multiple territories, much like in the television model.

3.3 Advertising Spends for Online Video Series Are Lower Than Television Spends

Pointing to the lack of maturity of the market to support higher budget professional video productions, stakeholders note that at present monetization in the online video space is limited, primarily because of the low valuation of online audiences. This is making the online space riskier to exploit.

Content aggregators such as certain channels on YouTube provide access to built-in audiences that are said to be more attractive to advertisers. It was pointed out that the model that has monetized best on these portals is low budget, direct to camera video featuring individual personalities, favouring a lower cost per thousand (CPM) to advertisers. On the other hand, Hulu, which distributes mostly commercial film and television, was said to attract a higher CPM. However, it is important to reiterate that revenues for the time being are very low.

4. Summary Observations

Among the challenges facing companies in their monetization efforts are attaining critical mass, building communities and the critical need to integrate analytics to provide viable games as services and optimize monetization. The trend towards games as services is expected to continue and game experiences must be conceived in ways that motivate all players to keep coming back to the game, and paying players to make incremental purchases.

Pricing is a key consideration for premium publishers, with some confident that the market will sustain current pricing models.

Some companies are looking to Asia and other markets with high rates of smartphone use to fuel their growth.

Licensing is an important monetization model for convergent digital media and original web series, though license fees from online aggregators and broadcasters for web series are low, requiring producers to keep their production budgets low.

Producers of convergent media and web series point to the need to engage with their audiences to support monetization. Analytics provide powerful tools for understanding their audiences. At the same time, the revenue models for web series are still being developed and monetizing web series is still a challenge. Advertising and brand sponsorships are seen as having important potential for the monetization of web series, though the valuing of online audiences is low due to the lack of maturity of the market.

E. Canadian Success Stories and Lessons Learned in Monetization

1. Preamble

This section profiles nine successfully monetized games and digital media content. While these examples do not in any way represent the gamut of what is being done in the interactive digital media industry, there are lessons to be learned in monetization methods being used.

Figure 18 below lists the examples examined in this section including the title, type of digital media product, monetization method used and the company.

Figure 18: Summary of Selected Examples

Title	Content	Monetization	Company
Forces of War/Mighty Monsters	Mobile game	Freemium	Uken Games
Mega Jump/Storm Casters	Mobile game	Freemium, Paidmium	Get Set Games
Warframe	Downloadable PC/Console game	Freemium	Digital Extremes
Outlast	Downloadable PC/Console game	Paid	Red Barrels Games
Super T.I.M.E. Force	Downloadable PC/Console game	Paid	Capybara Games
Slugterra	Digital extension of a television property	Syndication, Freemium	Nerd Corps Entertainment
Dino Dan	Digital extension of a television property	Syndication, Freemium	Sinking Ship Entertainment
Guidestones	Original web series	Syndication, Product integration (advertising)	iThentic
McLaren's Workshop	Mobile App	Freemium	National Film Board of Canada

2. Games

2.1 Forces of War and Crime Inc.

Ontario-based Uken Games develops freemium games and was an early entrant in cross-platform games, which allow users to continue playing the same game as they move from device to device. The company's games can run on iPhone, iPad, Android and BlackBerry platforms, as well as on Facebook.¹²³ To do this efficiently, Uken Games spent two years building out a reliable and scalable internal infrastructure to facilitate cross-platform development, building its own internal services around authentication, payments, notifications and deep analytics. "For the most part, we collect all actions within the games. Any click, or any action, or view, we're collecting that data. If we're putting out a new feature, there are certain

¹²³ Frank Condon, "Canada's Young Entrepreneur of the Year, 2012," Profit Guide.com, December 5, 2012.

KPI's [key performance indicators] that we measure. Things like retention, things like engagement, time spent on the app; we measure a before and after effect of that."¹²⁴

The investment has paid off as the company taps into a much larger, more deeply engaged audience. *Forces of War*, which was released in 2010, boasts over 20 million players worldwide according to the Google Play app store. *Crime Inc.*, which was released a year later, has 10 million players. Overall, the entire suite of nine games launched by the company since 2009 has an installed base of over 25 million users and over one million monthly active users. As Chris Ye notes, "Many of our players will play on both a mobile device and Facebook resulting in a much more engaged player. Those are the exact players we're searching for."¹²⁵ The company has been profitable since 2010.



To create strong user retention, Uken Games has focused on social interaction between gamers. Built-in forums, profile walls and chat features help create a deeper, more compelling game experience. In the words of company founder Chris Ye, "You want to create an environment in a game where people get more value playing with other people. That creates a lot of stickiness that would be hard to create just through the game itself."¹²⁶

2.2 Mega Jump and Storm Casters

Get Set Games, based in Ontario, initially launched *Mega Jump* as a 99-cent download in May 2010 and hit the top ten chart in several countries. To maintain the initial level of sales, the company made the game available for free a few months later, in August of the same year, and quickly achieved a million downloads. The free version of the game hit the top of the charts in over 20 countries, and with the addition of in-app purchases, the company has since earned millions from this game alone.¹²⁷



With the follow up freemium hits, *Mega Run* and *Mega Jump 2*, the company has since achieved over 50 million downloads on Apple and Android mobile devices for its suite of games. Given the difficulty of breaking through on the app stores, the company pays attention to the quality of its games, understanding that marketing alone is not sufficient. "One thing that we consistently try to do is work on the quality of our titles. The care and craft that goes into making a game is one of

¹²⁴ Herbert Lui, "How to Stay Hyper-Competitive: Secrets from Uken Games," *Techvibes*, August 8, 2012.

¹²⁵ Tom Worthington, "RIM's helpful hand makes BlackBerry a good base for developers, says Uken Games," *Pocket Gamer.biz*, May 3rd, 2012.

¹²⁶ IBID.

¹²⁷ Company co-founder Matt Coombe quoted in Brian X. Chen, "Playing at No Cost, Right Into the Hands of Mobile Game Makers," *New York Times*, March 18, 2012; Chad Sapiha, "Achieving success on iOS: Toronto-based Get Set Games doubles down on a mega hit with Mega Jump 2," in *Financial Times*, January 20, 2014.

the few things that an indie developer can control when launching a game, and this goes a very long way toward impressing new players and to possibly getting some promotion from Apple."¹²⁸

Earlier this year the company launched *Storm Casters* as a premium game with in-app purchases (also called the paidmium model).¹²⁹ The monetization model allowed the company to save time in the development process. The company also believed that taking this approach might give their game a bit of an edge in the Apple app store, judging that premium games aligned better with Apple's ideal consumer experience.

2.3 Warframe

Warframe is the first freemium title released by Ontario-based Digital Extremes. Noting that the free-to-play model was working for successful games, Digital Extremes considered that free-to-play need not be limited to casual or mobile games but could be a successful strategy to fund the development of a game for which it lacked a publisher willing to make a risky investment.

The freemium model allowed the company to take its own risks, scaling up gradually and doing away with the costs of retailers and other expenses in the traditional game value chain.

Without prior experience with free-to-play monetization, the company took a chance and developed a beta version of the game using a small in-house team, with only one level of play, and using the same universe as the company's previous release, *Dark Sector*, which they released on Steam as an experiment. Player response and interest from Sony confirmed their approach and the project went forward with further development.

The company was successful in attracting Sony to develop the game for its new PlayStation 4 console, giving the developer a competitive advantage as an early entrant to the PS4 market. The game went on to be ranked the second-most downloaded app on the Playstation 4, after Netflix and has been downloaded over two million times.¹³⁰



Implementing lessons learned from the earlier release of *Dark Sector*, the company hired a slew of customer support representatives to support their monetization efforts by supporting players and capturing their feedback. "The difference with *Warframe* is we hired customer support representatives. We hired marketing people. We hired people who speak different languages so our Russian players, and our Japanese players, and our German players can have people talking to them on our forums. We are taking responsibility for the game from top to bottom."¹³¹

¹²⁸ Chad Sapieha, "Achieving success on iOS: Toronto-based Get Set Games doubles down on a mega hit with Mega Jump 2," in *Financial Times*, January 20, 2014.

¹²⁹ Carter Dotson, "'Storm Casters' Review – Hacking and Slashing and Never Stopping," in *Touch Arcade*, July 2, 2014.

¹³⁰ Colin Campbell, "*Warframe* is PS4's second most-downloaded app; more free-to-play planned," *Polygon*, April 30, 2014.

¹³¹ Brendan Sinclair, "*Warframe* dev: Mid-size developers dying off," *Games Industry Biz*, June 21, 2013.

The success of the game has given the company a new lease on life. In July of 2014 Digital Extremes announced that it had entered into an agreement in principle to be acquired by Chinese MMO (massively multiplayer online) game company Perfect World.¹³²

2.4 *Outlast*

Outlast, the breakout premium hit by Quebec-based Red Barrels Games, was first released on Valve's online sales platform Steam in September 2013, immediately attracting attention and garnering over 2 million downloads by November of the same year, essentially earning back its initial investment.¹³³ The game was also released for the PS4 and Xbox One platforms. Player feedback informed the development of the game's console version. As one company founder remarked, "Making a DLC [downloadable content] was always part of the plan. We had a few ideas and planted seeds here and there so we could have as much options as possible. But it wasn't until the game was shipped and we had the players' feedback that we decided exactly what the DLC would be."¹³⁴ It was still among the top 20 downloads on PS4 a year later in September 2014.¹³⁵



The product's monetization strategy is linked to exploiting a niche genre, horror, which was mostly being kept alive by independent studios at the time of the game's development, as well as to delivering AAA game mechanics in a PC and DLC game at an affordable price.¹³⁶

With new platforms lowering the barriers to entry, the competition is getting tougher, especially for smaller, independent studios with fewer resources for marketing. To compensate, Red Barrels Games leveraged social marketing to promote the game. The game received significant exposure on YouTube, featured on Let's Play videos by YouTube personalities. One of these, PewDiePie, has garnered over 7.4 million views of his Let's Play video of *Outlast* game play. The company encouraged more YouTubers to create their own Let's Play videos, giving them permission to monetize them, and in some cases reaching out to them to encourage them to play the game.

The company also leveraged mainstream publicity opportunities to further promote the game to a mass audience, reportedly paying \$30,000 to have the game played and enthusiastically endorsed by Conan O'Brien on late-night television.

¹³² "Warframe Dev Set to be Acquired by MMO Company Perfect World and a Chicken Meat Supplier," Gamespot, July 6, 2014; Matthew Handrahan, "Digital Extremes to be acquired by Perfect World," *Games industry biz*, July 4, 2014.

¹³³ Brandan Sinclair, "Don't think of going indie as romantic, says Outlast dev," *Games Industry Biz*, November 7, 2013. See also Michael Carusi, "How Great Products Sell Themselves: The Red Barrels Case Study," Blogpost, November 21, 2013.

¹³⁴ "Red Barrels: An Interview with David Chateaufneuf and Philippe Morin," FogKnight Blog on N4G, <http://n4g.com/user/blogpost/indiemonth/528242>.

¹³⁵ Maxime Chiasson, "Here are the PlayStation Store's Top Downloads for September," *Gamer Headlines*, October 9, 2014. See also Red Barrels press release, "Outlast: Whistleblower Coming to Terrify You Again on May 6," April 29, 2014, Red Barrels website, <http://www.redbarrelsgames.com>.

¹³⁶ *Outlast* retails for \$20 or less.

2.5 Super T.I.M.E. Force

Super T.I.M.E. Force from Ontario developer Capybara Games launched exclusively for the Xbox 360 and Xbox One, and on Steam for PC a few months later rebranded *Super T.I.M.E. Force Ultra* (STFU). The game's revenue model is paid downloads, currently retailing for \$17.00 per download on Steam. The company also bundles STF and STFU with its sound track for a total of \$22.00 on Steam.



With the ever-increasing number of games available for sale online and on game consoles, discoverability is becoming more and more of a challenge for developers of premium games. New platforms provide an edge for early entrants, but as more games appear them, discoverability becomes a more difficult challenge, particularly for independent game developers.

The popularity of platforms follows a cycle of rapid changes, making it challenging for companies with development times of up to a year or more to keep up. As Nathan Vella points out, "it used to be if you could get a game on Xbox Live Arcade, awesome. Then it shifted - if you can get a game featured on Steam, you've got a good chance. Now boom, that's shifted as well."¹³⁷ As the company sees it, the opportunity [lies] in bringing a game to multiple devices, or consoles, or platforms.

Capybara values its partnerships with platform holders, recognizing the importance of the promotion offered by platforms such as Steam, XBOX One to its success and sees potential for monetization by deploying its games on multiple platforms. At the same time, the question of discoverability is a broader one for the company linked to the quality of their games, which increases the chances of success and sustainability. The company has been lauded with numerous prestigious awards that recognize the company's creative innovation, and considers its creative excellence to be very important to successfully monetizing their games.

3. Digital Media

3.1 Slugterra

British-Columbia-based Nerd Corps Entertainment takes a 360-degree content approach to exploiting its property, *Slugterra*, a series of digital extensions of the television property also produced by the company. The television, web and iOS properties support brand building, and are being monetized through syndication (licensing deals), and freemium apps integrating in-app advertising and in-app purchases. “

The Emmy-winning action/comedy television series and website *Slugterra* airs on Disney XD and broadcast TV in over 170 countries. The company's suite of online games, *Battle for Slugterra*, *Slug Run* and *Slugslinger Duel* have garnered over 20.7 million game plays on *Slugterra.com* and third party websites.¹³⁸

¹³⁷ IBID.

¹³⁸ Boylan, Juli, "Nerd Corps Profile, Let's Slug it out!" interview with Ken Faier, President of Nerd Corps Entertainment, Head of Global Consumer Products," in *Licensing Today Worldwide*, October 2013.



The Slugterra apps were originally created to support the brand and provide a secondary stream of revenues. The games drive engagement with the brand and an engaged fan base makes it easier to attract licensing partners. Internationally, Nerd Corps has signed agents and licensees to help support the toy roll out and global merchandizing and licensing of the brand. The company currently has over 50 licensing deals in Europe, Latin America, Russia, China, South Africa, Turkey and Israel.

The property extends to a trilogy of movies: *Slugterra: Ghoul from Beyond* (a TV movie and DVD release), *Slugterra: Return of the Elementals* (which had a limited theatrical release in North America), and *Slugterra: Return of the Shane Gang* (which contains the first five episodes in the series). The movies are intended to create tent pole moments to engage existing fans and create excitement to reach new ones. They are also available to broadcasters as half-hour episodes.

The key to creating a successful brand is understanding how your show will translate into a fantasy play pattern. For this, the company brought in consultants to help understand the play patterns and then creative talent to help drive the play pattern and fantasy play and the sustainability of the property.

Once launched, timing is key – to be in the market at a certain time to coordinate the licensing support. The company points to the importance of getting the property in the right time slot, with the right ratings, on the right networks, as well as aligning broadcasts with the release of merchandise to support their licensees and create a win for everyone involved.

3.2 *Dino Dan*

In developing *Dino Dan*, the Ontario-based Sinking Ship Entertainment began by securing all of the property's underlying rights in order to successfully monetize its brand across a range of productions. *Dino Dan* is an award-winning television property produced by Sinking Ship Entertainment airing on TVO Kids in Canada, and Nick Jr. in Australia and the U.S. and over 100 countries worldwide. It had the most watched debut when it launched on Nick Jr, with over 753,000 young viewers.¹³⁹

In addition to the television property, Sinking Ship Entertainment determines the most appropriate digital properties to extend beyond the show.¹⁴⁰ Digital extensions of this 360-degree content help sell the television property, while the apps are also creating new revenue streams for the producer. At the same time, tying apps to television properties increases their visibility and provides opportunities to create high quality content.



Dino Dan apps are being made available as freemium and premium games.

¹³⁹ "Sinking Ship Entertainment Picks Ruckus Media Group for DINO DAN Storybook Apps," *Business Wire*, February 9, 2012.

¹⁴⁰ Blair Powers, Producer and Partner, Interactive at Sinking Ship Entertainment, quoted in Etan Vlessing, "Secure and protect digital content rights, indie producers warned at iLunch 9," *Playback*, March 1, 2011.

The company is generating additional revenues through licensing, for example a licensed toy line, which is integrated with the digital extensions. Toys and DVDs ship with codes that unlock digital content, which in some cases cross promotes other apps of the same brand. Licensed products include dinosaur excavation kits, prehistoric play-sets, fossil replica kits, action figures, *Dino Dan* outdoor adventure gear and DVDs. The release of apps and merchandise is timed to television premieres to take advantage of cross promotion opportunities.

The company sees the educational content in its products as serving to enhance the overall entertainment value of the brand. With respect to *Dino Dan*, the company tried not to underestimate the audience's knowledge about dinosaurs. In tests with preschoolers and kindergarten children, the company discovered a high level of intrinsic knowledge about dinosaurs, able to name several species. The company worked with museums from the beginning, notably the Royal Tyrell Museum in Alberta, to provide an authentic experience.

3.3 Guidestones

This award-winning original scripted web series of 50 3-minute episodes produced by Ontario-based iThentic, features elements of transmedia and ARG (augmented reality game) storytelling. The show is monetized through integrated product advertising, a revenue sharing licensing deal with Hulu, and licensed merchandise being sold on iTunes.



With a \$300,000 cash budget for the first season and \$400,000 for the second, financing for digital series is significantly lower than what is available for television. License fees from broadcasters are much lower for digital content than they are for television or film. For this reason, the producers designed their season 2 episodes with a view to repurposing for broadcast. As noted by the

show's director, Jay Ferguson, "While the industry is shifting in many ways and changing, it's still hard to finance and monetize content that's just only playing online...we don't really have public funding systems set up for this kind of digital content," and brands are not as heavily involved in funding digital content in Canada as they are in the U.S.¹⁴¹

Original web series can be particularly challenging with respect to engaging viewers and convincing them to come back and watch additional episodes. The solution for the producers of *Guidestones* was to engage viewers through a transmedia experience featuring elements of ARG storytelling, combined with a subscription model of push notifications sent via email to invite viewers to watch new episodes.

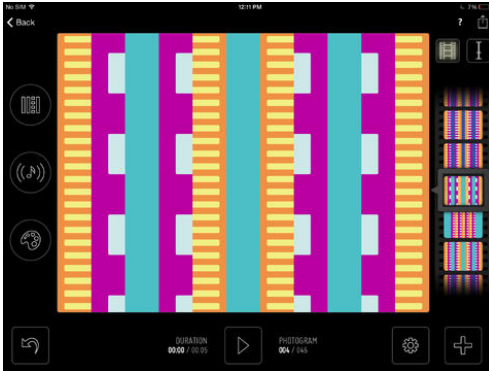
Season Two of the series, *Guidestones: Sunflower Noir*, features 18 10-minute episodes, to be compiled into six half-hour television shows, and a 3-hour feature film that screened earlier this summer in Toronto, to allow for more opportunities for monetizing the series.

Producer/distributor Portfolio recently announced it has acquired the international rights to seven digital titles produced by iThentic, including *Guidestones*, noting the availability of the show in multiple formats offers a lot of flexibility to both traditional and digital platforms.

¹⁴¹ Jay Ferguson, cited in "Digital original series like 'Blue' and 'Guidestones' picking up steam," CTV.ca, July 30, 2014.

3.4 McLaren's Workshop

Produced by the National Film Board of Canada, *McLaren's Workshop* provides an interesting example of an app associated with the films of Norman McLaren. This freemium app created for the iPad allows users to create their own films with animation techniques used by McLaren. The app contains three workshops (programs) approximating the techniques used by McLaren: paper cut-out animation, based on the film *Le Merle*; scratching-on-film based on *Blinkity Blank*; and synthetic sound based on the film *Synchrony*. The cut-out workshop is free, while the other two are sold as in-app purchases.



Beyond the filmmaking activity, the app also includes 51 films by the celebrated Canadian filmmaker and 11 documentaries about the artist. Appealing to a niche market of animation enthusiasts and those with an interest in Canadian film, the app has been hailed as “forward to a new way of learning animation history in the 21st century, in which understanding a filmmaker’s work isn’t done through passive activities like reading a book or watching a film, but rather by making films of one’s own.”¹⁴²

The launch strategy involved a collaboration between the NFB, Vimeo, and renowned animation filmmakers, David O’Reilly, Don Hertzfeldt, Regina Pessoa, and Koji Yamamura. The filmmakers used the app to create short films. These were shared on the Vimeo platform and made available to the public during a 30-day period. Vimeo also produced short tutorials that contributed the app’s success.

The app has been downloaded close to 100,000 times, and generated modest revenues. A new version of the app released 6 months after initial release stimulated an increase in in-app purchases as the new release allowed users to try the scratch on film and synthetic sound workshops.¹⁴³

¹⁴² Amid Amidi, “NFB’s Free McLaren’s Workshop iPad App is a Must-Download,” *Cartoon Brew*, June 7, 2013.

¹⁴³ Source: National Film Board of Canada.

F. Concluding Observations: Looking to the Future

New platforms, new consoles and the near global ubiquity of mobile devices will continue to drive the future of gaming.

As one industry analyst describes it, “Gaming is in the midst of migrating towards complete digital distribution through full downloads and now cloud based on-demand streaming.”¹⁴⁴ The user-base of console games is shifting to new game platforms. A segment of hardcore gamers has migrated back to the PC and more compelling game experiences on tablets and mobile are attracting casual gamers. Five billion mobile phones, three billion PCs and an anticipated one billion tablets are creating vast new market opportunities. The mobile games market is predicted to overtake that of consoles by 2015, to be the most lucrative in the industry, fuelled by freemium monetization strategies and tactics. As one analyst notes, “The public is on the browser and on mobile devices. That’s where you have to reach them.”¹⁴⁵

At the same time, the convergence of advancements in cloud computing and hardware development are leading the way for a new paradigm shift in the way games are monetized. Cloud gaming has become a reality, bringing on-demand gaming to players and the promise of a Matrix-like shared experience of persistent game universes.¹⁴⁶ The extinction of the \$60 dollar packaged game seems almost inevitable as games are increasingly being played on any device.

As the ecosystem shifts, monetization models continue to evolve. For example, some companies such as Electronic Arts, are finding new ways to extract value and monetize their legacy content through their own subscription service, EA Access.¹⁴⁷

From the game developers’ point of view, the proliferation of games devices has made the creation of cross-platform games even more complex, increasing costs and reducing control on the software. Mitigating this trend is the move to a cloud-centred environment, which has the potential to lower production costs.

As the ecosystem evolves, analytics will continue to play a key role in understanding user behaviours and companies will continue to need to adapt their monetization models to adapt their monetization models. The only thing certain about the way forward is that the future is uncertain. As Boyd Multerer, Xbox’s Director of Development, sums it up, “There’s so much change, going so fast, I can’t predict what it’s going to be.”¹⁴⁸

As free-to-play has become the primary model in the mobile games ecosystem, developers need a strong understanding of how they will get their games discovered and how they will monetize them. Increasingly these questions need to be considered at the design stage. Companies developing new products would greatly benefit from having access to industry

¹⁴⁴ *The Gaming Sector: New Categories Take Centre Stage*, Digital Capital Advisors, September 2014, page 5.

¹⁴⁵ Trip Hawkins, quoted in *Cloud Gaming Europe 2014 – Industry Leaders’ Thoughts*, Whitepaper, Video Games Intelligence, 2014.

¹⁴⁶ Matt Buchanan, “The Future of Video Games: A Box and a Cloud,” in *The New Yorker*, May 23, 2013.

¹⁴⁷ *The Gaming Sector: New Categories Take Centre Stage*, Digital Capital Advisors, September 2014, page 6.

¹⁴⁸ Matt Buchanan, “The Future of Video Games: A Box and a Cloud,” in *The New Yorker*, May 23, 2013.

expertise on marketing and monetization, for example through bootcamps, industry conferences and business accelerators. Companies could also benefit from having access to research on the lessons learned by others in the industry.

Convergent digital media content producers will need to heed these changes as they continue to engage with the games sector.

The rapid expansion of the mobile market holds many of the same opportunities and challenges. Discoverability will continue to require innovative solutions to break through the noise of over a million apps, a number that will continue to rise as analysts foresee continued growth in the sector for some years to come.

For producers of web series, the profound fragmentation of this marketplace will require lower production expenditures for quite some time for companies to be profitable. Licensing opportunities will likely continue to evolve, but the fees commanded will remain low as compared to broadcast licenses. Recognized brands will continue to be key to discoverability and audience building to attract advertisers and brand sponsors as these experiment with multi-platform ad campaigns. Developers will also benefit from multi-channel networks that aggregate audiences as a means of monetizing their content through advertisers while assuming less risk.

The significant expansion of mobile video viewing hold promise for monetizing streamed video. Mobile video offers the possibility of improved measurement and more targeted curation of content, providing added value to advertisers and more revenues for content creators. In the meantime, experimentation is key to build experience, audiences and brands in this emerging market.

As digital platforms continue to emerge, media fragmentation will accelerate, forcing content producers to re-think the content experience to find the best platforms and formats to engage with consumers from the dual perspectives of content and monetization. Producers who can access funding to develop web series will benefit from risk taking and experimentation in this emerging market.

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Annex 3: Glossary

Ad supported: typically includes banner advertising; video ads; offer walls; and interstitials.

Banner advertising: Banner ads enable developers to display small advertisements throughout an app, or on specific screens.

Cloud gaming: is a type of online gaming that allows direct and on-demand streaming of games onto computers, consoles and mobile devices, similar to video on demand, through the use of a thin client, in which the actual game is stored on the operator's or game company's server and is streamed directly to computers accessing the server through the client. The server is the system that is running the processing needs. The controls and button presses from the user are transmitted directly to the server, where they are recorded, and the server then sends back the game's response to the input controls.

Free-to-Play/Freemium: Offering a game, product or service (such as software, web services or other) free of charge while charging a premium for advanced features, functionality, or related products like virtual goods and services.

HTML 5: is a core technology markup language of the Internet used for structuring and presenting content for the World Wide Web. HTML5 technologies well suited for creating browser based games, HTML5 is an open technology and only requires a simple text editor to code in. By using HTML5, a developer can target a wider array of devices and gadgets without having to specifically port a game to each different platform.

Hybrid: Monetization model that combines any number of different business models together (premium, free to play micro-transaction, advertising, episodic, subscription, etc).

Interstitials: Interstitial advertising, like video, enables developers to show full screen ads at natural break points in a game or app. In most cases, these ads market other third-party applications.

Merchandising: Intellectual property is licensed to a toy company or other manufacturer to produce and sell merchandise, or the owner of the IP produces merchandise to sell directly to the consumer, such as DVD's, music or ringtones.

Metered (also called a soft paywall): Content is free until a user reaches a certain threshold, such as number of articles or videos viewed or based on the amount of time viewing.

MMO games: Acronym for Massively Multiplayer Online game, characterized by a large, persistent world) that is used by large groups (typically thousands or more) of players simultaneously. Also short for MMORPG (Massively-Multiplayer Online Role-Playing Game). MMOs usually involve a free download and recurring monthly fee for gameplay.

Offer walls: Offer walls are typically used in freemium games and apps. They enable developers to provide users with free items, like currency, in exchange for taking an action such as: signing up for a free Netflix trial, liking an app or product on Facebook, and other related tasks.

Pay-to-Play/Subscription: Offering a game, product, or service (such as software, web services or other) for a set price over a defined time period. Discounts are granted for longer subscription periods and access is blocked when payment discontinues.

Paidmium: A type of hybrid monetization model where a game, product or service is offered as a paid download, combined with charging a premium for advanced features, functionality or related products like virtual goods.

Premium: Defined as charging for an app or game. Premium was the predominant model early in the app store and it is used by some of the biggest names in the market like Angry Birds, Doodle Jump, and Cut the Rope.

Pre-Sale or pre-purchase: This model lets fans fund the development of a title, by pre-paying either the totality or a portion of the cost of a game. Some developers offer fans the opportunity to participate in the final development of a game as beta testers in exchange for pre-payment.

Subscription: Users subscribe to content for a monthly or annual fee.

Steam: is an internet-based digital distribution multiplayer (a digital storefront) and social networking platform developed by Valve Corporation. Steam provides the user with installation and automatic updating of games on multiple computers, and community features such as friends' lists and groups, cloud saving, and in-game voice and chat functionality. Steam also offers the Early Access program, which allows users to pre-pay for games in their beta phase and contribute feedback for their final development.

Transaction: A monetization model whereby unbundled pieces of content, such as a song, game or video downloads, are sold individually.

Value exchange advertising: allows advertisers to subsidize premium content, virtual goods or game play in exchange for players interacting with a marketer's brand in the course of their game play session. Value exchange ads can be many things including, but not limited to, long form video, custom mini-games, and branded in-game content. In some contexts, value exchange advertising is traded for points or other in-game items when users agree to watch advertisements during gameplay. This is said to lead to greater retention because of the ad's integration into game play.

Video ads: Video ads enable developers to show short (15-30 second) videos during natural breaks in an app.

Virtual Goods: In-game items or game-related services, such as a virtual currency that enable or enhance game play.

Whales: Top spending users who typically generate bulk of revenue.

Sources: *Making the Switch: Adopting the Free-to-Play Revenue Model*, Global Collect; *Game Balance Concepts, Level 10: Final Boss*, September 8, 2010; Ryan Morel, *Choosing the Right Business Model for Your Game or App*, August 12, 2012; *Wikipedia*; Jeremy Liew, "29 business models for games," (based on talk by David Perry, CCO of Acclaim Games Inc.), Lightning Speed Venture Partners (lsvp.com), July 2, 2008.

