Studios See Big Rise In Estimates of Losses To Movie Piracy

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May 3, 2006; Page B1

The movie industry wanted the world to know exactly how much money it loses to piracy. But now a study shows the damage is far worse than expected, giving some studio executives second thoughts about releasing the information to the public.

The Motion Picture Association of America, Hollywood's lobbying group, two years ago commissioned a detailed study that it hoped would pinpoint more precisely how much the industry loses to piracy annually.

The study, by LEK Consulting LLC, was completed last year, and people familiar with it say it reached a startling conclusion: U.S. movie studios are losing about $6.1 billion annually in global wholesale revenue to piracy, about 75% more than previous estimated losses of $3.5 billion in hard goods. On top of that, losses are coming not only from lost ticket sales, but from DVD sales that have been Hollywood's cash cow in recent years.

The MPAA froze plans to release the survey. Late yesterday, in response to questions from The Wall Street Journal, the MPAA released some information from the survey, including members' U.S. and global piracy losses. "A study this magnitude takes some work to roll out," says an MPAA spokeswoman. She says the numbers weren't far out of line with what the industry expected. For months, MPAA members...
debated whether and how to release the information. Some studios argued that making the figures public would help the industry win tougher laws and enforcement. Other studios said the figures were so bad that releasing them would hurt their stock prices and make a laughingstock of their enforcement efforts.

The result: Piracy, an issue that normally brings Hollywood studios together, was driving them apart. Although the studios eventually agreed to release parts of the information, it was only after months of infighting. Time Warner Inc.'s Warner Bros. and News Corp.'s Twentieth Century Fox fought hardest to release the information, people familiar with the matter say, while Walt Disney Co. and Viacom Inc.'s Paramount were very reluctant. General Electric Co.'s NBC Universal and Sony Corp.'s Sony Pictures fell in the middle, these people say.

The estimate showing a dramatic increase in piracy is a function of different methodology used in the report. Previously, people familiar with the matter say, the MPAA used figures based on a series of random calculations that estimated how much was lost in each country. In one market, it was calculated that for every bootleg DVD that turned up in raids, seven more existed. Thus, estimates for piracy losses ran from $280 million in China to $275 million in Russia. There was no previous estimate for the U.S. alone, but in the new survey, losses from piracy are believed to total almost $1.3 billion solely in the U.S.

The LEK report provides staggering revisions elsewhere in the world: Mexico overshadows Russia and China to rank as the world's largest market for pirated U.S. films, accounting for an estimated $483 million in lost revenue to MPAA member studios in 2005. That is up from $140 million in 2004 by old tallying procedures, according to partial data the MPAA released in February.

The new approach reduces the estimated losses in some of the world's most notorious pirate markets, even as it adds Internet-related losses for the first time. China's losses slipped to an estimated $244 million in 2005, from $280 million in 2004 under the old counting technique. Russia's estimate declined by about $10 million. These international results have also generated skepticism about whether Mexico could really be a bigger piracy market than giants like China.

The survey was conducted over 18 months in 28 countries and cost $3 million. It uses more consistent methods and incorporates consumer research for the first time -- in the form of telephone and Internet surveys and focus groups -- to derive estimated losses. In recent months, the MPAA has been fine-
tuning the totals after factoring in outside analysis and new
information, in some cases lowering the estimated losses -- for
example, the losses due to potential customers receiving illegal
copies of movies from friends.

The previous estimates didn't include the impact of free
Internet downloading, which is incorporated in the LEK report.
Another surprise involves the fast expansion of online piracy
by consumers compared to the losses stemming from
professional bootleggers who sell DVDs. Last year, according
to a person familiar with the matter, copies of movies
downloaded or received from people who had downloaded
them cost the studios $447 million in the U.S., whereas copies stemming from professional
bootleggers cost the studios $335 million. An additional $529 million in losses came from
consumers making copies of legitimate films they bought on DVD or VHS.

Critics have faulted some piracy estimates for equating each pirated DVD with a lost sale,
when many consumers would have skipped the movie altogether if they hadn't gotten a cheap
or free unauthorized version. This time, the survey specifically asked consumers how many of
their pirated movies they would have purchased in stores or seen in theaters if they didn't have
an unauthorized copy, giving studios a different picture of their true losses.

The study also shows that home video, not theatrical distribution, is the market that piracy hits
hardest, accounting for two-thirds of the studio's lost revenue. That is a big blow to the studios,
which had been counting on the lucrative DVD market to increase their bottom lines, but in
recent months have found DVD sales are slowing considerably.

The survey also bucks the assumption that piracy is a kids' activity. In Japan, one of
Hollywood's biggest foreign markets, 50% of the overall industry's losses are the result of
piracy by people ages 25 to 39.

While piracy hasn't had much of an impact on the stock prices of the big conglomerates that
own studios, that could change if investors feared DVDs would no longer generate sales at the
pace they expected, says Michael Nathanson, an analyst with Bernstein Research. "If it became
an issue, you would see a collapse in [valuation] multiples," he says.

While new data are potentially helpful in negotiating with foreign governments because they
also estimate losses to local film industries, the information is also bad news for the MPAA's
antipiracy efforts. Those have ranged from public-awareness campaigns to beefing up laws to
raids of illegal DVD plants. Dan Glickman, the organization's president for almost two years,
has made fighting piracy a priority. He joined the organization a few months after it hired John
Malcolm, a former Justice Department official, to head its world-wide antipiracy operations.

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