The Growth of the Internet and The Implications for UK TV content

An assessment by Oliver & Ohlbaum Associates for Ofcom

September 2008

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- SUMMARY
- THE STORY SO FAR
    - THE UK TV CONTENT ECOLOGY
    - THE INTERNET AND ADVERTISING
    - THE INTERNET AND VIDEO CONTENT
    - THE REVENUE CHALLENGE
    - THE LIKELY CONTRIBUTION OF THE INTERNET AND “ON DEMAND” TV

INTRODUCTION AND SUMMARY

SUMMARY

- This report has been produced as part of the second phase of Ofcom's Second Public Service Broadcasting Review. Phase one identified both challenges and opportunities that new media were bringing to PSB delivery. In this report we have assessed the existing and potential future impact of online on PSB funding as well as the potential revenues to non-linear platforms from content delivery.
- The internet currently has a largely indirect and high level impact on commercial PSB's capacity to fund originated TV content.
- Internet search advertising has provided a much more effective method for executing "response" and "transaction" based advertising campaigns (traditionally mainly print classified and direct mail campaigns). This has led to a shift of monies by advertisers (especially in the travel, telecoms, retail and finance sectors) away from display advertising (which has only been growing by 1 to 2 per cent a year in real terms over the last 5 years) into response based advertising (which has been growing by 4 to 5 per cent a year over the last 5 years largely due to internet search and online classified).
- The slow growth of all UK display advertising combined with the internet's own rising (but still small) share of display advertising (through banner ad campaigns etc), has led to relatively low growth rates across all TV advertising. Low growth across all TV advertising combined with a rising share of all TV audiences accounted for non commercial PSB channels, has helped to put commercial PSB channel revenue under significant pressure.
- There is much less evidence that the growing number of internet based TV and TV clip based services are, as yet, taking significant revenue directly away from traditional TV channels or the video on demand spin offs (i-Player, 4oD, ITV.com) of the channels. While internet clip based services providing mostly short form professional and user generated content (UGC) do account for 90 per cent of all video consumption on the internet (80 per cent of which is to YouTube), evidence from the USA suggests that most video on demand advertising flows through to long form services run by broadcasters and TV platforms. Even within sites such as YouTube, the majority of revenue for short form clips is for professional content "channels" and not for uploaded user generated material.
- However, going forward, if take-up of online video increases, and is more widely substituted for TV and becomes more prone to unauthorised and illegal use, this could damage the economics of content creation and undermine that same content's ability to earn revenue from traditional platforms.

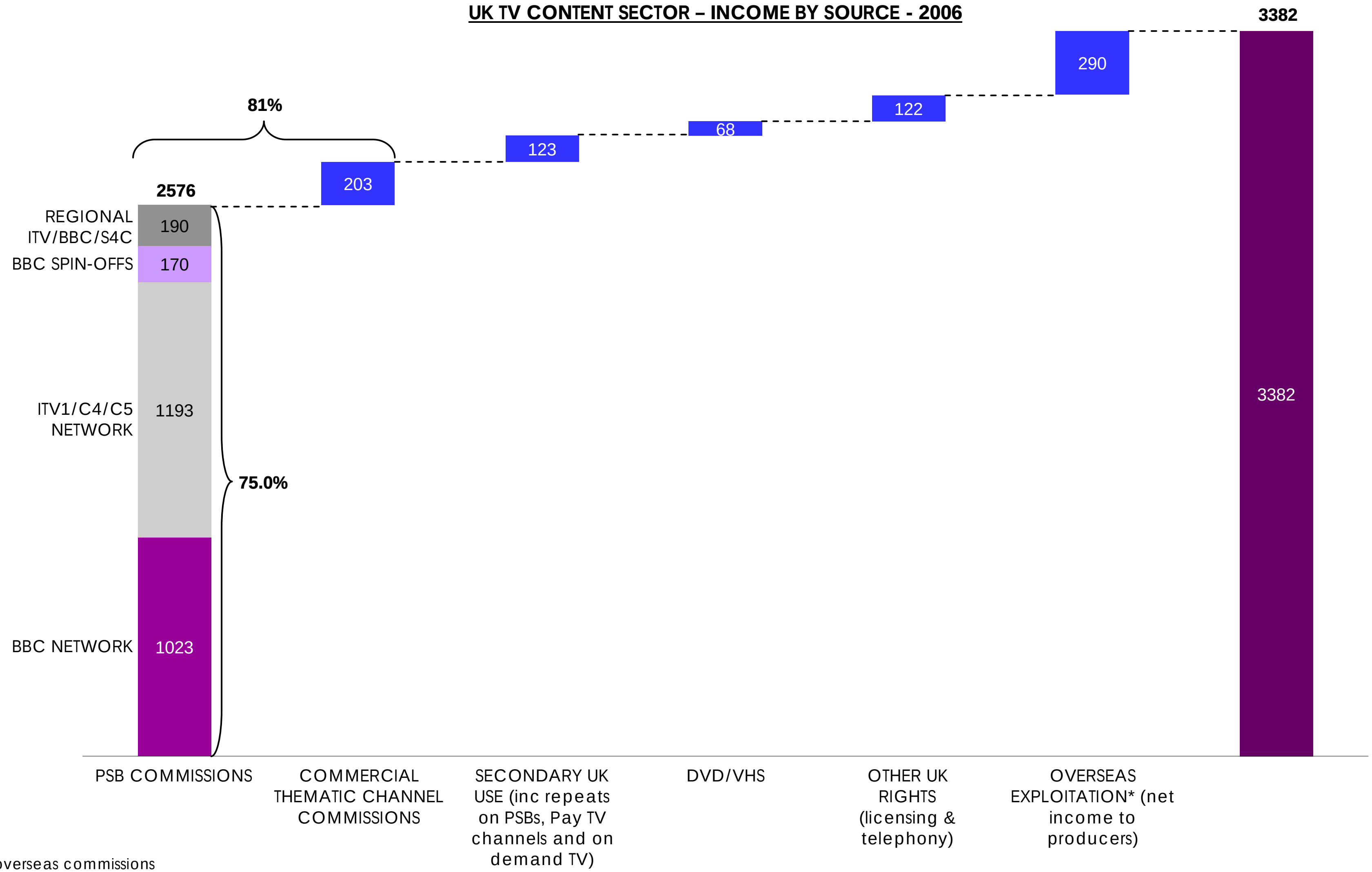
INTRODUCTION AND SUMMARY

SUMMARY

- The scenario models developed by O&O for Phase One of the Ofcom PSB review explicitly addressed the likely impact on traditional TV and content creation of growth in the internet, growth in search advertising and growth in Web 2.0 TV consumption – both on demand services of traditional broadcasters and the more YouTube type clip services.
- In particular, the Stagnation scenario was developed to reflect potential "value destruction" by the increasing use and availability of content (UGC and copyright professional material) through Web. 2.0 TV services, and the possibility that this would lead to a direct reduction in attributable UK TV related advertising (with the new services taking content consumption away from traditional services, but unable to monetize this consumption properly and unable or unwilling to invest any money they do earn in paying for content – especially new content).
- In the Stagnation scenario, the on demand TV services run by PSB broadcasters, pay TV platform providers and leading online retailers (such as Apple) are unable to make more than £200m a year in advertising by 2020 due to the wide availability of UGC and unauthorised copyright material on the internet. While the more independent internet based services do manage to recoup almost £400m in revenue by 2020 (due to their very high volumes of consumption) the exposure they give to traditional TV material seriously undermines the revenue earning potential of all TV outlets in the UK, putting significant pressure on their ability to originate content. At the same time, with so much unauthorised and UGC content available to generate viewing, the independent sites have no need to invest in new content of their own.
- In the Gradual Transformation scenario, by contrast, broadcaster and on demand TV services take a larger share of viewing than independent internet based services, and make significant revenues by 2020 (PSB on demand services plus other IPTV and TV platform based services generate £600m a year by 2020). These services are assumed to invest a greater proportion of their revenue back into either new content or the re-use rights for existing TV content, leading to a small rise in originated content spend to 2020. What keeps this content spending growth rate relatively low is the general switch of advertising revenue from display to response based outlets and television's inability to properly tap into response based advertising money as effectively as search.

THE STORY SO FAR – the UK TV content ecology – current mix of revenues

...the PSBs still provide 75% of all UK TV content sector income, and original commissions still provide over 80% of all content revenues...



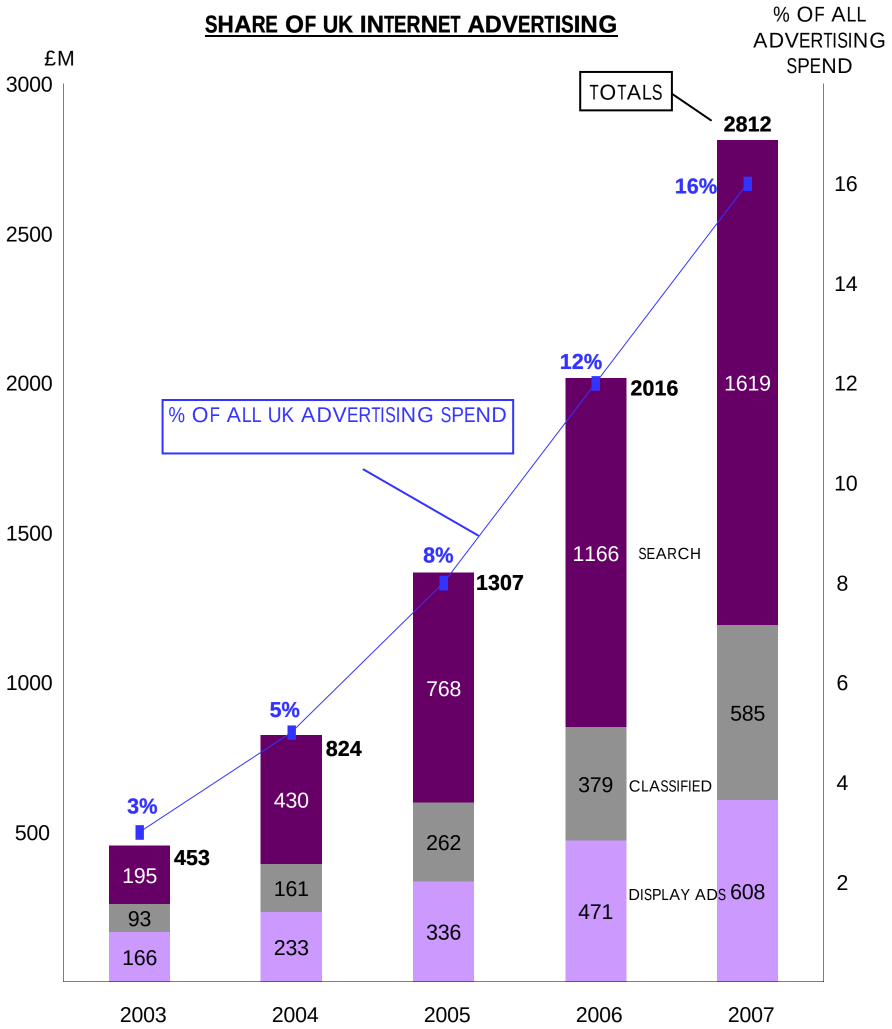
*excludes overseas commissions

SOURCE: PACT CENSUS, O&O ANALYSIS

THE STORY SO FAR – the internet and advertising – a rising economic force

…internet advertising has grown to account for 16% of all UK advertising spend…and it may well surpass TV advertising in 2009…

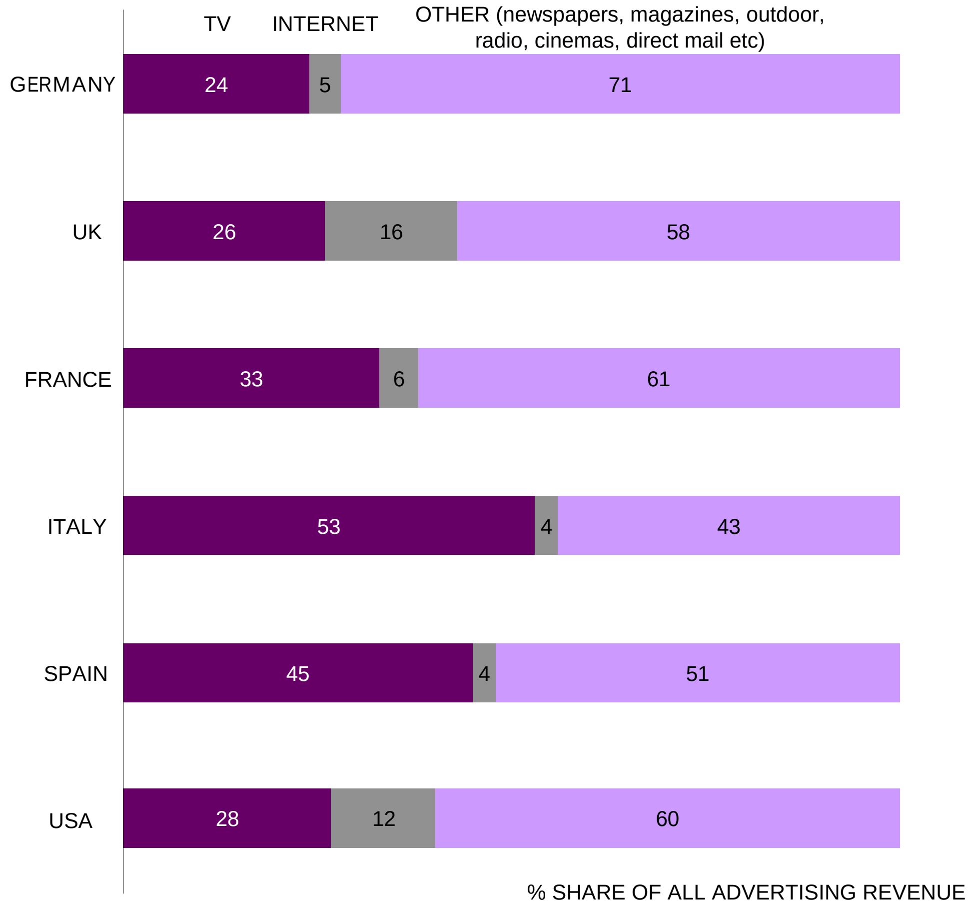
SHARE OF UK INTERNET ADVERTISING



SOURCE: ADVERTISING ASSOCIATION, O&O ANALYSIS

…the UK internet advertising market is the most advanced in the world…

ESTIMATED SHARE OF TOTAL ADVERTISING SPEND BY COUNTRY - 2007

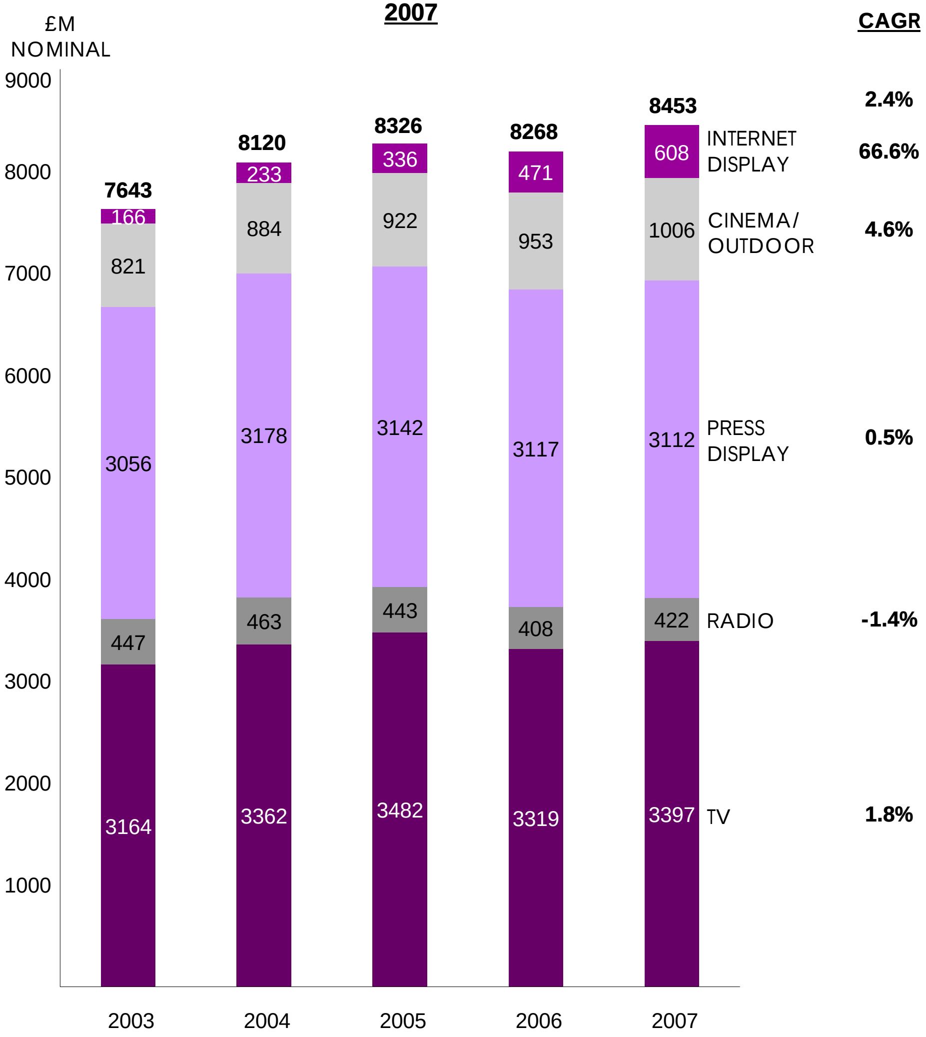


SOURCE: PWC, OBS, VERSUS SUHLER, O&O ANALYSIS

THE STORY SO FAR – the internet and advertising – still a limited role as a "display" advertising medium

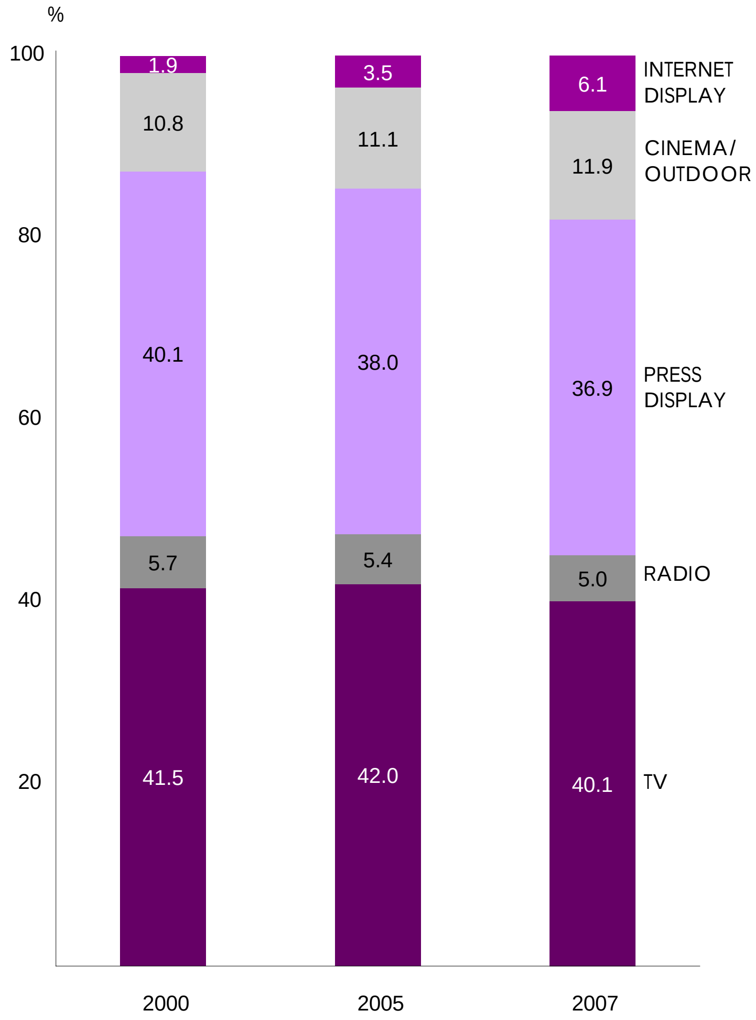
…display advertising in the UK has been growing by just 2% to 3% in nominal terms – about 0 to 1% in real terms…

UK DISPLAY NET ADVERTISING REVENUE TRENDS – 2003 TO 2007



…the internet now accounts for 6% of display advertising… just above radio…but still a long way behind TV…

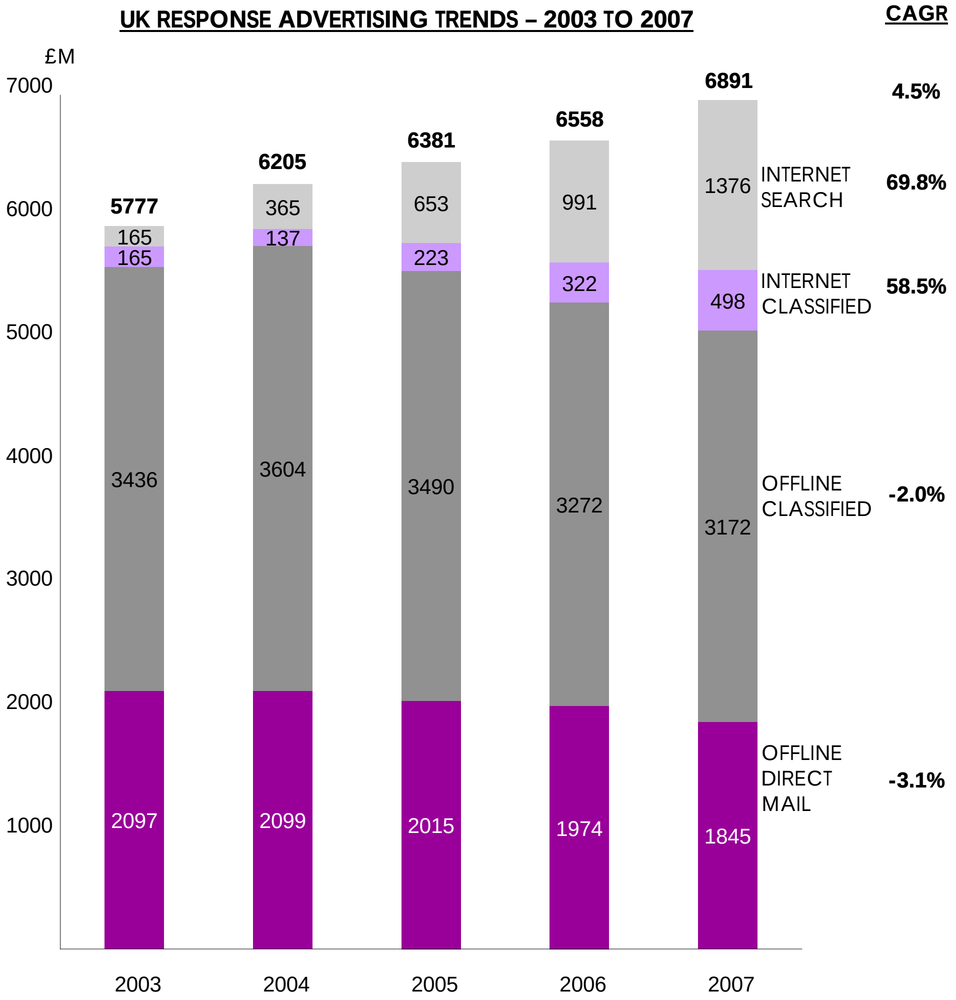
DISPLAY ADVERTISING BY MEDIUM – 2003, 2005 and 2007



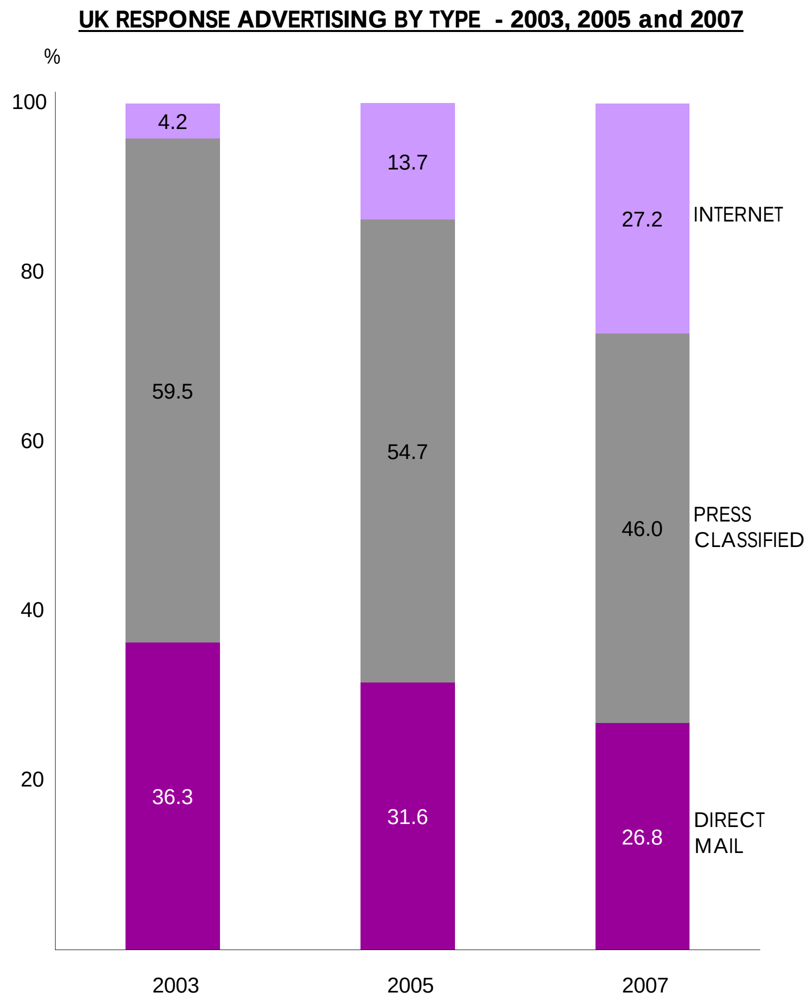
SOURCE: ADVERTISING ASSOCIATION, O&O ANALYSIS

THE STORY SO FAR – the internet and advertising – more important as a "response" advertising medium

…"response" advertising in the UK has been growing by 4.5% per year…



…the internet has been a major driver of this growth, now accounting for 27% of the "response" advertising market…

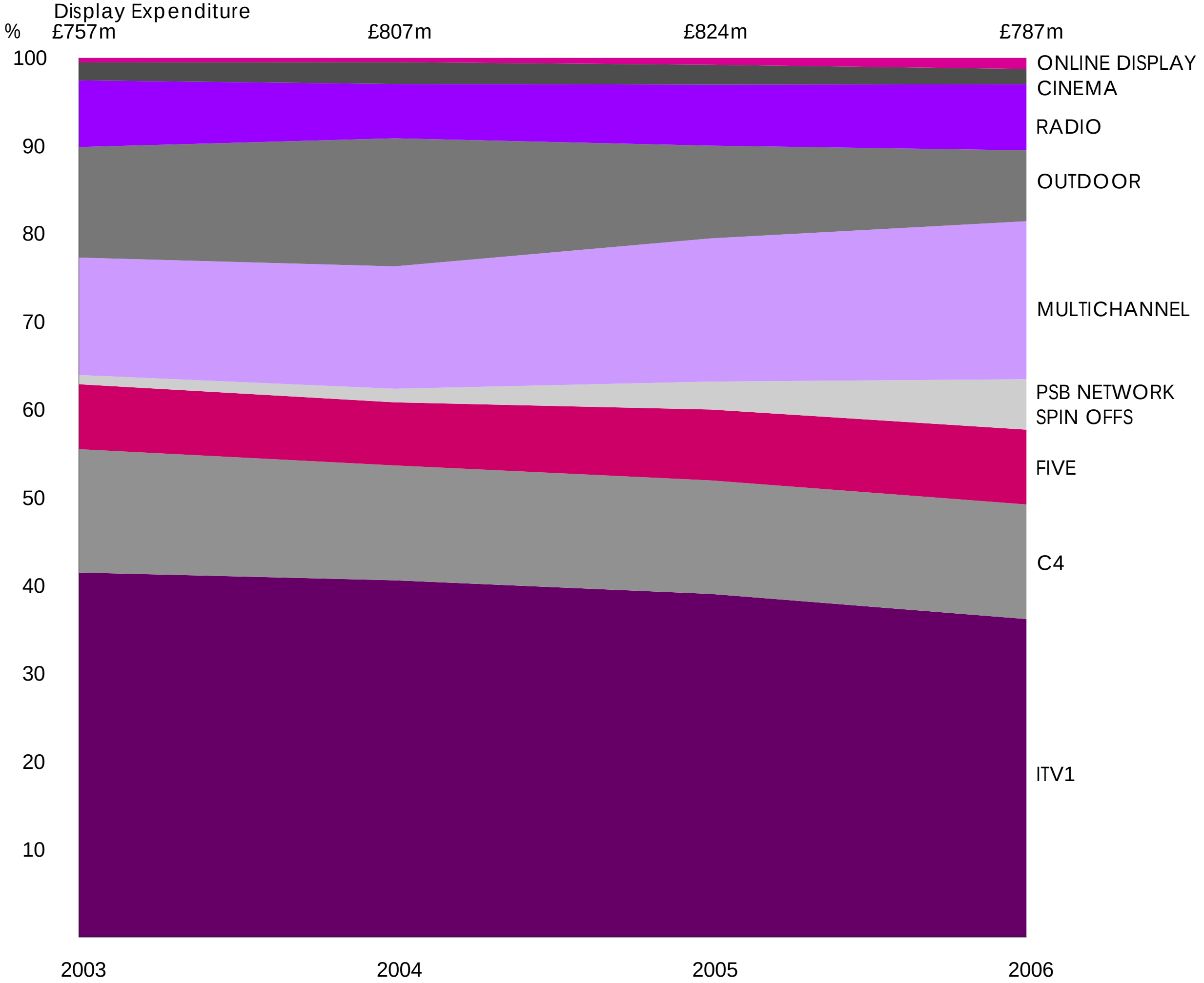


SOURCE: ADVERTISING ASSOCIATION, O&O ANALYSIS

THE STORY SO FAR – internet and advertising – no switch into internet display by top TV advertisers

…evidence from the analysis of the top ten TV advertisers spend suggests TV is still the preferred media for major fmcg brands and retailers …in these sectors there has been no significant shift of display advertising spend to new media…

SHARE OF TOP TEN TV ADVERTISERS'* DISPLAY ADVERTISING SPEND BY MEDIA, 2003-2006**



	SHARE OF SPEND		
	2003 (%)	2006 (%)	ABSOLUTE CHANGE %
PSB NETWORK SPINOFFS	1.0	5.7	+4.7
MULTICHANNEL	13.4	18.0	+4.6
FIVE	7.4	8.5	+1.1
ONLINE	0.6	1.3	+0.7
RADIO	7.6	7.5	-0.1
CINEMA	2.0	1.7	-0.3
C4	14.0	13.0	-1.0
OUTDOOR	12.6	8.1	-4.5
ITV1	41.5	36.2	-5.3

* Proctor & Gamble UK, Reckitt Benckiser, Coi Communications, Kelloggs, Loreal, Marks & Spencers, Masterfoods, Nestle, Tesco Plc, Unilever Plc

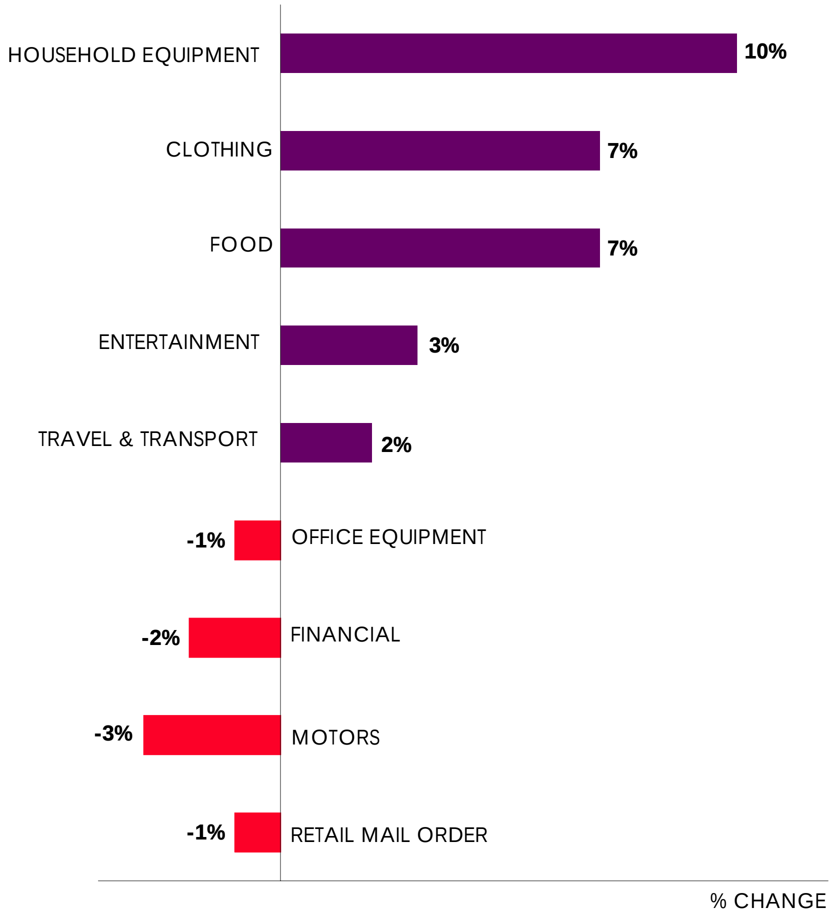
**Press and direct mail spend not included

SOURCE: NIELSEN MMS, O&O ANALYSIS

THE STORY SO FAR – internet and advertising – the move out of display (into response?)*

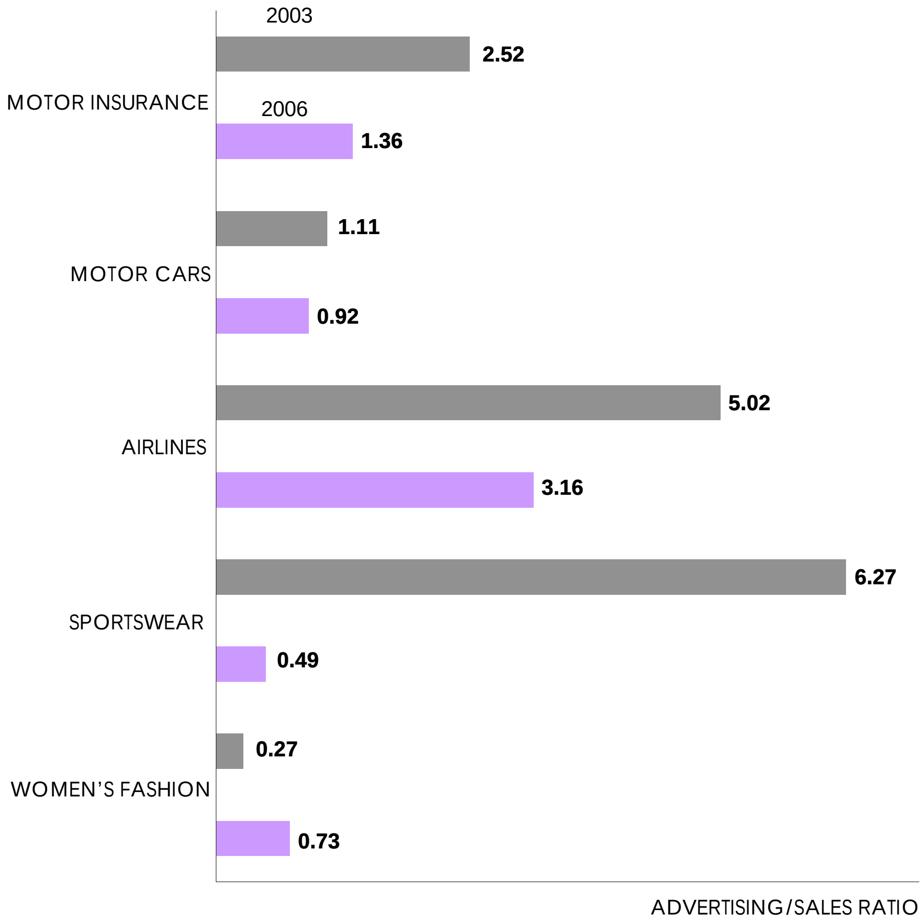
...some sectors have made a significant move out of display advertising...

% CHANGE IN ANNUAL TOTAL DISPLAY AD SPEND – 2003 TO 2007



...some sub-sectors have seen a significant reduction in their display advertising to sales ratio suggesting a move of display...

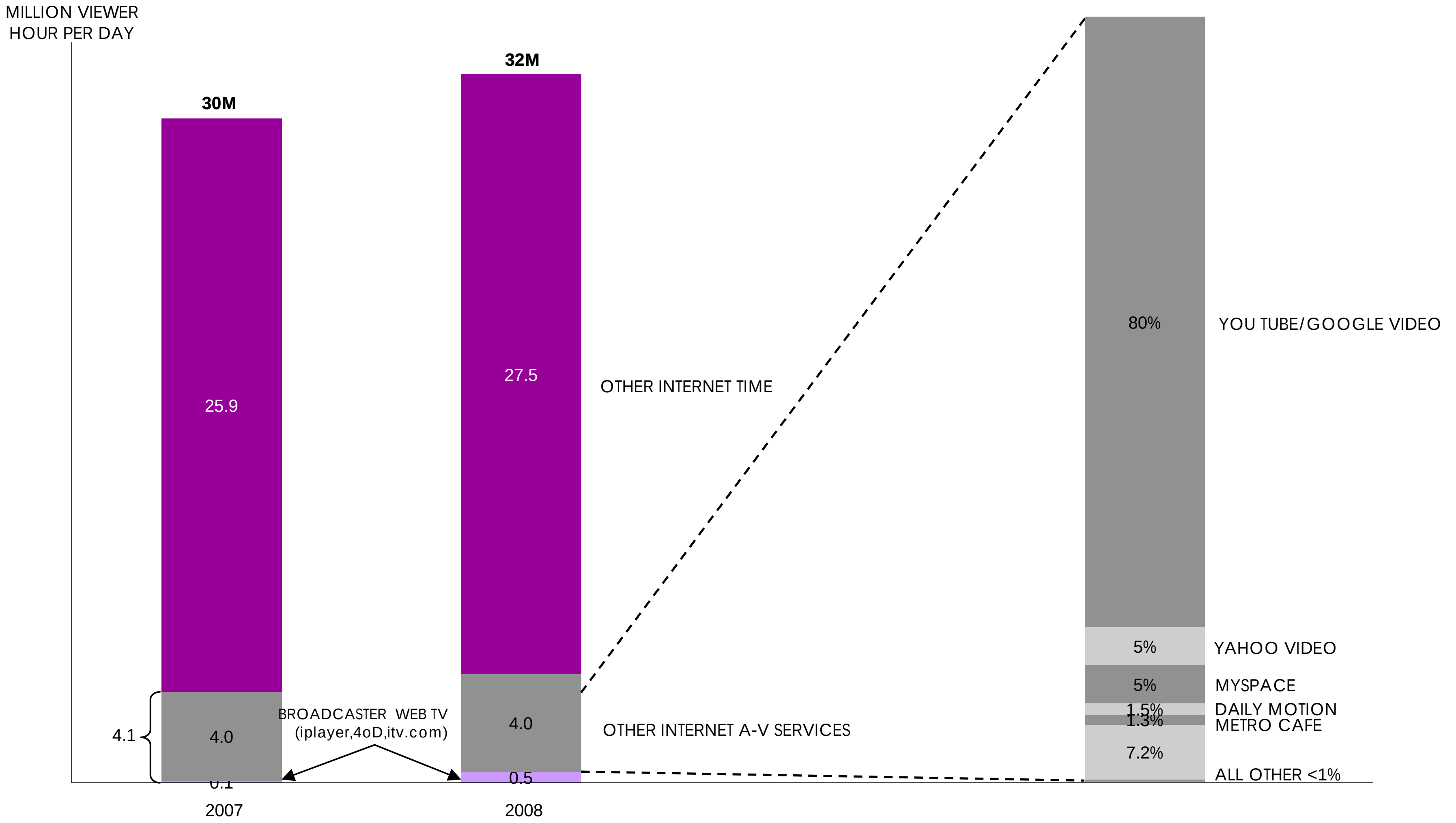
DISPLAY ADVERTISING/SALES RATIOS OF SECTOR SUB SEGMENTS – 2003 and 2006**



*there is no database of major "search/direct response" advertisers
** advertising in millions divided by total sector sales in 000s

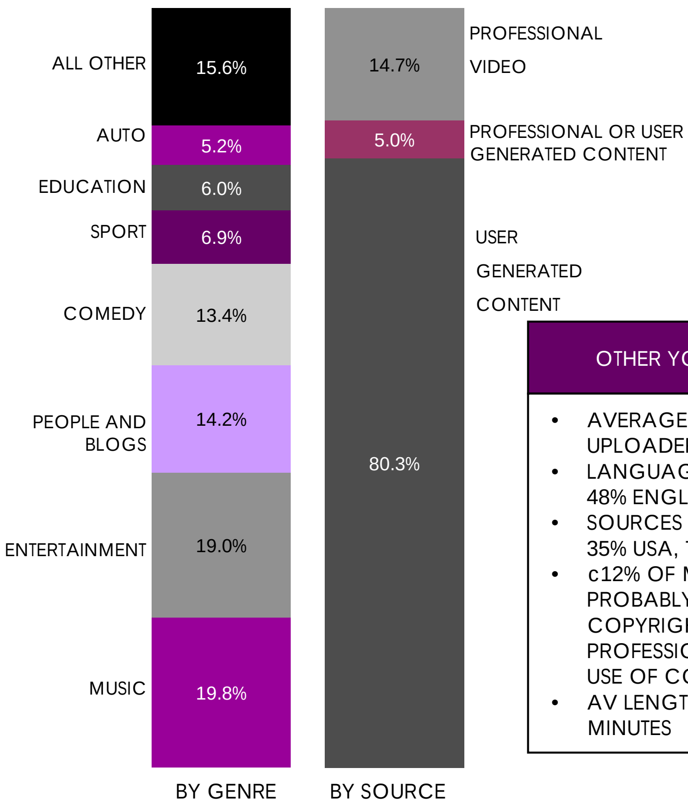
THE STORY SO FAR – the internet and video content – usage by source

…between 10% and 15% of internet time in the UK is currently spent streaming video, of which only about 20% is to broadcaster services, and 80% of the remainder is to YouTube/Google….

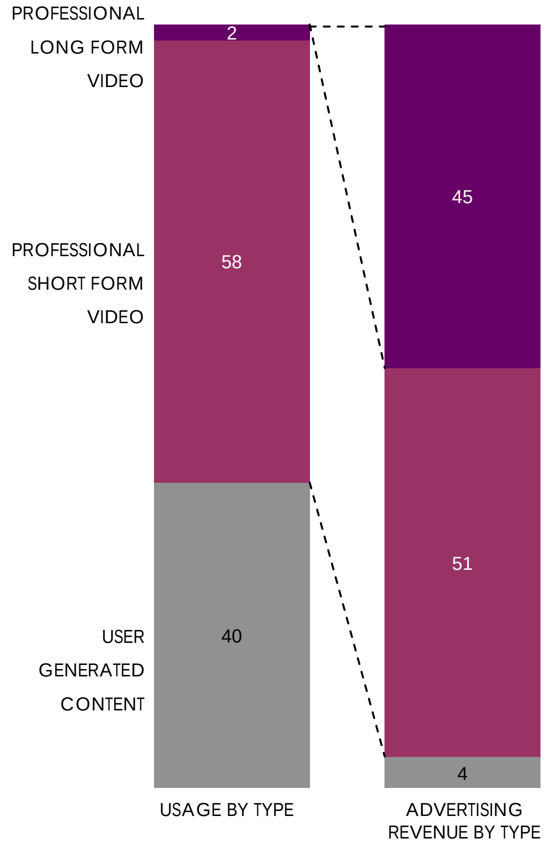


THE STORY SO FAR – the internet and video content – content available on Youtube

YOUTUBE CONTENT BY TYPE - 2008



MONETIZING ALL WEB 2.0 TV -2007/08



OTHER YOUTUBE FACTS

- AVERAGE AGE OF UPLOADER – 27
- LANGUAGE OF CONTENT – 48% ENGLISH
- SOURCES OF CONTENT – 35% USA, 7% UK
- c12% OF MARKET PROBABLY IN BREACH OF COPYRIGHT (I.E PROFESSIONAL AND UGC USE OF COPYRIGHT CLIPS)
- AV LENGTH OF STREAM 2.5 MINUTES

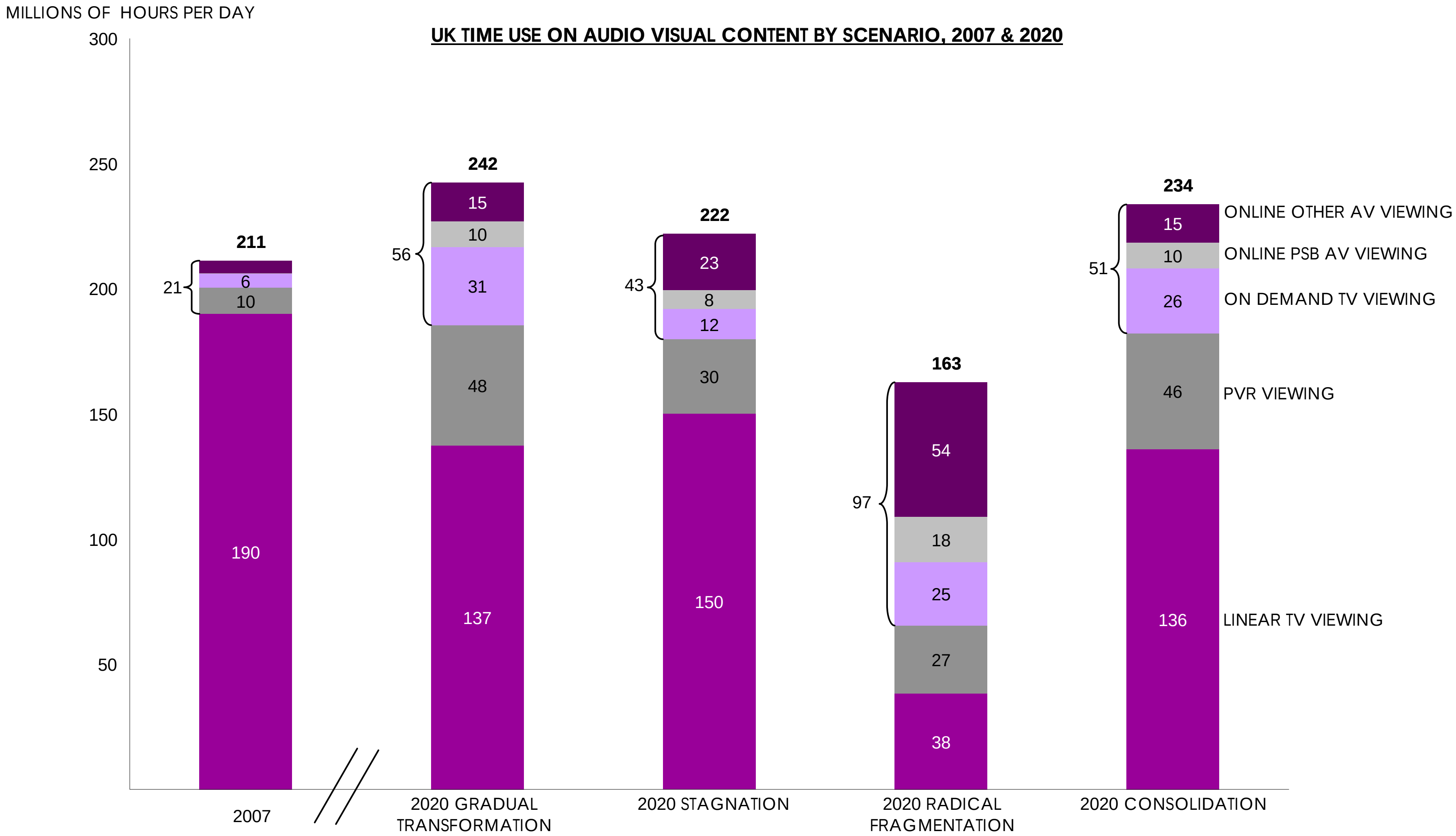
YOUTUBE STATISTICS

- TRAFFIC = 1 BILLION VIEWS PER DAY
- REVENUE - $200M
- REVENUE/000 VIEWING HOURS = $11(COMPARED TO c$100 FOR USA NETWORKS)

SOURCE: KANSAS STATE UNIVERSITY, TDG RESEARCH

FUTURE CHALLENGES – the contribution of internet – time use

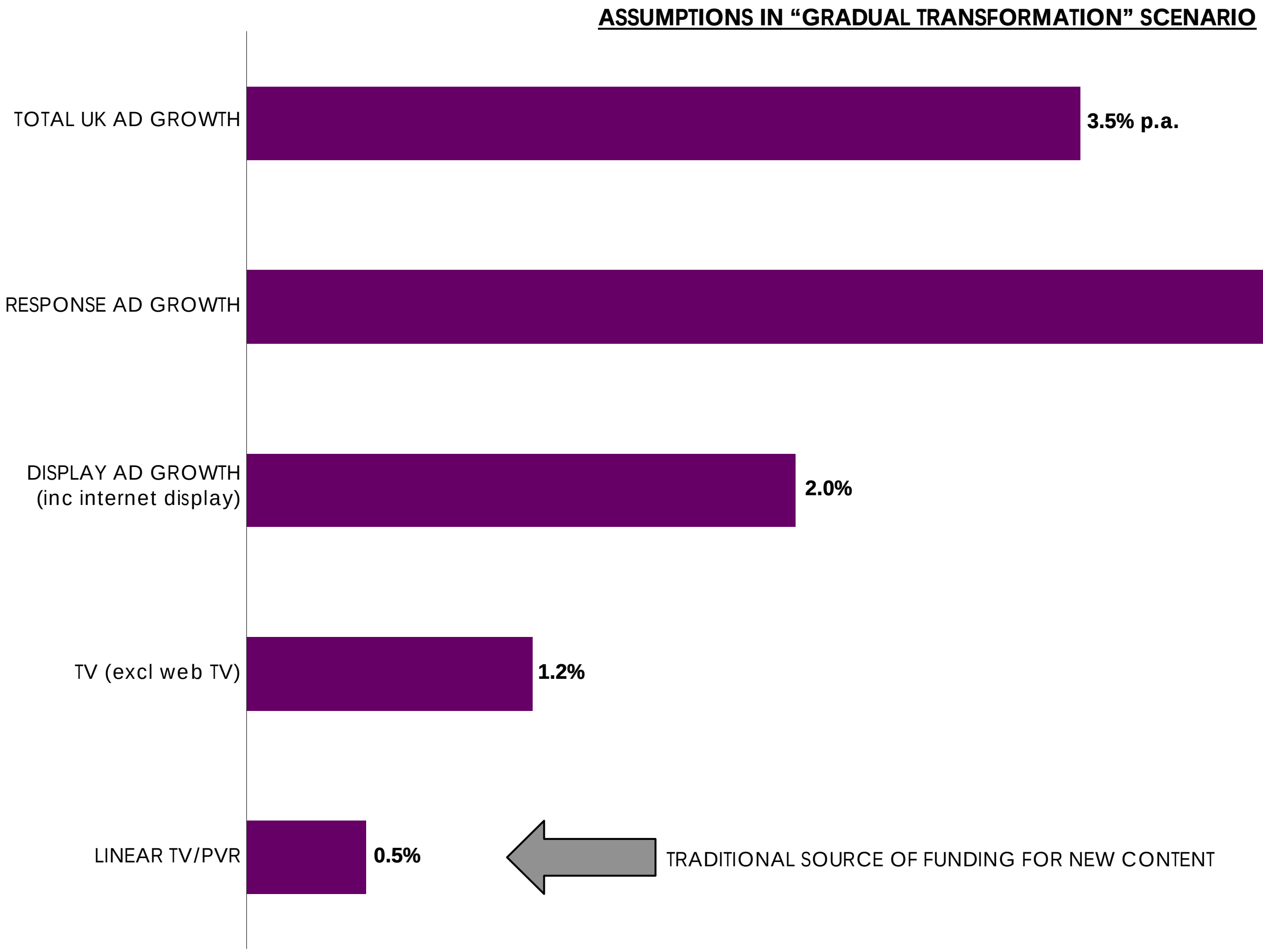
…on demand TV use, both through TV platforms and from Web based TV services, will increase under all scenarios at the expense of linear TV viewing…



SOURCE: O&O ANALYSIS

FUTURE CHALLENGES – the revenue challenge – an ongoing ad spending switch

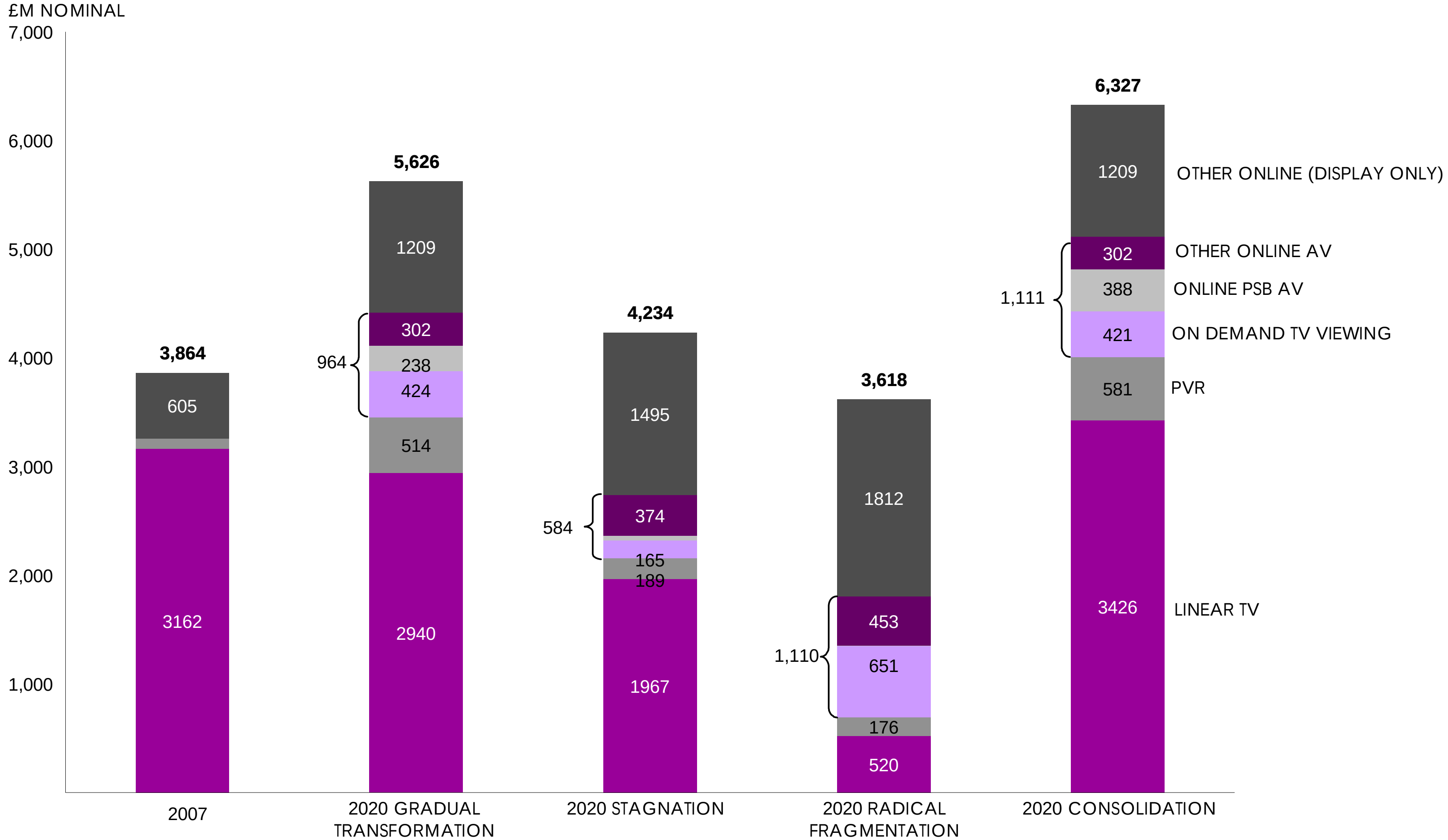
…O&O scenarios to 2020 assume continual ad market growth, switch to response advertising from display, and TV share of display falling gradually, with on demand TV increasing its share of all TV advertising…this leaves very low growth for the traditional sources of funding for new TV content in the UK even in the Gradual Transformation scenario…



FUTURE CHALLENGES – the contribution of internet – revenue

…non PSB internet AV services could be generating between £300m and £450m in display advertising revenue by 2020 which could contribute towards content spending…BUT the internet's main source of funding (response based advertising) will not be directly attributable to video….

UK ADVERTISING VALUE BY FUNCTIONALITY BY SCENARIO, 2007 & 2020



SOURCE: O&O ANALYSIS