

# Mediatique

## **Future models for the delivery of public service broadcasting**

A report for Ofcom in support of its review of the future of  
PSB

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## **Executive Summary**

- Public Service Broadcasting ('PSB') is facing the most severe challenge of its long history. Changes in technology, consumer behaviour and business models may very soon render the current funding model unsustainable.
- The PSB 'compact' used to be relatively straightforward, obliging PSBs collectively to fulfil certain statutory purposes and individually to meet a set of service-specific requirements (including bespoke quotas for original UK content, regional programmes, news and current affairs), in exchange for a range of service-specific benefits including access to spectrum, prominence in TV guides and – for the BBC – public money. In so doing, the PSBs helped sustain flourishing, globally renowned creative industries.
- The compact worked well when TV was widely consumed and the PSBs played the leading role in TV. Ten years ago, broadcast TV was the pre-eminent means by which consumers received their audio-visual services, and most of the viewing was to scheduled television. Today, just 50% of daily viewing in the UK is to 'live' broadcast TV.
- Consumers now have many other options, including subscription and ad-funded services delivered over the internet directly to TVs and other connected devices by 'streamers' such as Netflix, Amazon, Disney+ and Google's YouTube. This has meant the emergence of new gatekeepers, often focussed on collecting consumer data and selling products and services, using TV content as an incentive to engage.
- Revenue pressures on the UK's PSBs, whether funded publicly (the BBC, S4C) or commercially (ITV, STV, Channel 4, Channel 5), have been rising as a consequence of these changes, with direct impact on their ability to fund original UK content at their former levels.
- Since 2008, PSB expenditure on first run origination has declined by £500m a year in real terms, and increased commitment to such content by non-PSBs (Sky, Discovery, more recently Netflix) has not been enough (nor sufficiently multi-genre and universally available) to compensate.
- Throughout the Covid-19 pandemic, evidence has been mounting of an acceleration in these viewing and expenditure trends. The PSBs all announced further deep further cuts in content spend (partially reversed subsequently), as they attempted to navigate the short-term impact of the pandemic and resultant lockdowns.
- For the purpose of this report, we have focused mainly on the genres that might typically be deemed PSB and not normally profitable for commercial providers, such as children's, arts, formal education, regional news and ethics genres. In addition, we have considered UK content origination as the principal proxy for PSB outcomes. What we see as the critical elements of PSB – broadly, universal availability of original UK content, regional programming and local news – are under threat. If PSB is to be safeguarded, reform will be necessary.
- This is the context in which Ofcom's current consultation on PSB – entitled *Small Screen: Big Debate* – is being conducted. Mediatique was asked by Ofcom to contribute to a consideration of market dynamics over the next five years, analysis of likely outcomes in the event that no changes are made to the way PSB is regulated, and a review of options for reform in response to trends in technology, consumer behaviour and business models.
- To inform our contribution, we undertook desk research and conducted in-house financial modelling; we also held confidential interviews with a range of stakeholders active in UK media and communications industries.

### ***Stakeholder consensus on PSB objectives***

- We identified several areas which are core to PSB objectives going forward and which are widely supported by the stakeholders we interviewed:
  - Sustaining production of content in 'market failure' genres<sup>1</sup> (e.g., kids, arts, culture) and categories (e.g., Nations and Regions, including indigenous-language content);
  - Promoting UK origination across multiple genres, and ensuring breadth and depth in content output;
  - Making content available that appeals to multiple tastes and preferences – targeting many audiences;

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<sup>1</sup> Defined as commercially unviable content that would not be made absent regulatory intervention of some kind.

- Ensuring content is made that sets a quality benchmark; and
  - Fomenting creative skills and promoting the appeal of UK productions in international markets.
- Stakeholders disagree, however, on some aspects of PSB, with views tending to follow understandable patterns depending on the identity and category of the respondent. Areas of divergence include whether PSB content needs to be available for ‘free’ and the degree to which non-PSB companies (including, e.g., pay TV channel operators and global streaming companies) provide content that should be defined as ‘public service.’
  - Divergence in views is also discernible in relation to future funding models, particularly whether the licence fee should be reformed (as to quantum and collection mechanism), the prospect for direct and indirect taxation, the case for extending tax credits and the need (or otherwise) for a level playing field in the regulation of broadcasters and digital operators. For the avoidance of doubt, the concept of public funding for PSB, and some form of universal fee, continues to have widespread stakeholder support.<sup>2</sup>

### ***The challenges arising from recent market trends and their impact on PSB***

- Viewing of traditional broadcast TV (upon which the PSB compact is still reliant) is declining, driven by technological innovation (e.g., faster broadband speeds and adoption of devices on which to view content, such as smart TVs, streaming sticks) and changes to consumer behaviour (notably in viewing/usage and willingness to pay). Both TV and radio are being affected by the emergence of new platforms aimed at curating services, including via smart TVs and home assistants that may not confer prominence to PSB content.
- Commercial revenues associated with PSB (TV advertising, sponsorship and, indirectly, traditional pay TV subscriptions) are flat or declining (a trend exacerbated by the impact of the Covid-19 lockdown); meanwhile, the justification for a universal licence fee, given reduced broadcast viewing/listening and growing competition from Subscription Video on Demand (‘SVOD’) and other digital services, is being eroded. The fastest growing revenue segments are SVOD and Advertiser-funded Video on Demand (‘AVOD’), dominated by new entrants.
- PSBs (and other broadcasters with UK distribution) have sought to mitigate viewing and revenue weakness by offering their own on-demand services; however, these have not compensated for the decline in traditional engagement and face much greater competition from multiple providers in the online and connected TV space.
- Revenue pressures on the PSBs have had a direct and material effect on their expenditure on original UK content. The production hiatus in 2020 saw further deductions in expenditure by the PSBs (and others), which will take some time to restore. Meanwhile, there has been marked underlying inflation in the cost of key genres, including drama, comedy and high-end factual, driven by intense competition for talent and programmes.
- In the short term, the Covid-19 crisis is likely to lead to further revenue weakness for the PSBs (including the BBC<sup>3</sup>) and higher costs directly related to Covid-19 security as production resumes. Commissioning broadcasters are also seeking to reduce overall programming expenditure through changes in their content mix, focussing on cheaper content that is less lucrative to suppliers.

### ***Absent changes to the compact or strategic shifts by market participants, what are the likely trends to 2024?***

- The challenges facing traditional broadcasting generally, and PSBs specifically, show no signs of abating. The period to 2024 will be characterised by increased competition for viewer and listener attention, driven in particular by the growing appeal of content and services provided and promoted by large, global players on multiple devices. These gatekeepers are incentivised to favour their own content (or auction access and prominence to the highest bidder), thereby disadvantaging domestic providers in particular. PSBs will see further erosion in their ability to promote content and collect consumer data.
- Meanwhile, renewed market consolidation is likely, involving production, distribution and platform operators – evident both in mergers and acquisitions to achieve scale and diversification and in closures and other instances of rationalisation. Larger production and distribution entities are likely to continue to acquire smaller,

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<sup>2</sup> An extensive summary of the anonymised views of stakeholders can be found in an Annex to this report.

<sup>3</sup> The BBC is facing both licence fee pressures (fewer households paying the licence fee) and commercial under-performance (declines in revenues at BBC Studios in line with the production hiatus following the Covid-19 pandemic and acute revenue weakness in key commercial segments where BBCS is exposed, such as traditional pay TV and advertising.

cash-constrained brands, particularly those overwhelmed by Covid-19 financial challenges. There is particular potential for larger-scale mergers and acquisition activity involving financially robust digital players and challenged 'traditional' media companies.

- While these pressures mount, the ability of traditional sectors to generate revenues will be further diminished. The expectation for both the licence fee and traditional TV advertising (the critical underpinning of PSB origination expenditure) is for flat revenues at best, with traditional pay TV income poised to decline further. SVOD revenues are expected to grow. Commercial PSB 'core' revenues will drop at a faster rate than new forms of income (e.g., ad-funded broadcaster VOD) can compensate, even as certain key costs (including for content and IP distribution) rise. Meanwhile, pressures on the BBC will intensify, requiring it to reduce costs further.
- As the financial position of the PSBs worsens, we expect to see significant pressure on the funding available for PSB content and, concomitantly, lower expenditure by PSBs on first-run UK origination. Absent changes to the strategies of multichannel operators and SVOD providers, the declines in PSB contributions to a full range of PSB content will not be offset by increased commitment from non-PSBs. This is likely to be the case even if co-productions between PSBs and non-PSBs are aggressively pursued, as these are far more likely to be in commercially viable genres. Moreover, co-productions inevitably dilute the commercial returns from programmes in ancillary windows and markets, reducing financial returns to the PSBs. The knock-on impact to the external supply sector (still very reliant on PSBs for first-run commissions) will be considerable.

#### ***What options might be considered to improve PSB sustainability?***

- Informed by our research and extensive engagement with stakeholders, we consider whether changes to existing rules and models could mitigate some of the pressures on the PSB system and enhance sustainability.<sup>4</sup>
- The options are aimed at addressing the challenges that we identify in sections 3 and 4 of our report, namely: declining linear audiences; reduced 'traditional' TV revenues; intensifying pressures on the licence fee and the concomitant impact of these trends on levels of UK content expenditure.
- The specific issues identified, which any reform would seek to address, include: the lack of affordable access/prominence via online/digital platforms for PSB providers – particularly to ensure engagement with younger audiences; limited (and worsening) bargaining power in relation to distributors (and lack of a level playing field between broadcasters and 'digital natives'<sup>5</sup>); a reduction in PSB content output owing to revenue challenges; significant content inflation in key genres and in upstream distribution costs; and a constrained regulatory environment for linear advertising (reducing advertising income).
- We consider options within three categories.
- Under '**Strategy**' we outline a number of approaches the PSBs might adopt (indeed, may already be adopting) – around, for example, collaboration to aggregate on-demand distribution (a single sign-in, combined search and navigation, data sharing) and to ensure improved bargaining position *vis-à-vis* digital platforms. PSBs may also rationalise their operations (reducing the number of services and reducing costs). There may even be scope to cooperate more fundamentally on a plan to accelerate the transition from broadcast to IP over time, reducing costs substantially by phasing out terrestrial and satellite distribution.
- In '**Compact**' terms, we concentrate on regulatory reform in key areas such as advertising minutage (for commercial PSBs) and the terms of trade applied to contractual relationships with external content producers (for all PSBs). We also review potential changes to the prominence regime including extending protections currently applied to linear EPGs to include digital on-demand platforms as well.
- We also assess changes to the '**Public funding**' of PSB, including the way in which the BBC, specifically, is funded; this includes analysis of both advertising and subscription as potential models for the BBC, in whole or in part. We also consider: direct funding of PSB by government; a 'contestable' licence fee open to applicants other

<sup>4</sup> For the avoidance of doubt, one extreme 'solution' would be to abandon any PSB intervention at all – no licence fee, no licence obligations for commercially funded PSBs, no regulatory framework. In this case, the outcomes are left to the market (including global players such as Netflix, Google and Apple). As our analysis will show, PSB (using original UK content investment as a proxy) would not be sustained absent regulation, with severe implications for audiences, competition and the UK media ecology; stakeholders, moreover, do not support such a radical approach.

<sup>5</sup> Defined as companies with no traditional revenue income to protect: includes SVOD, AVOD and social media.

than the BBC; the creation of content funding levies applied to digital providers and pay TV operators; and the expansion of tax credit regimes (already in use for selected genres).

- We conclude that the most viable options for sustaining PSB outcomes are those that extend elements of the existing PSB compact across the PSBs’ on-demand services and augment their bargaining power, including by permitting greater collective action. This might include regulatory reform to ensure that PSBs are given privileged access to IP and broadcast networks and prominence for all their services on multiple devices.
- The extended use of tax credits and the creation of new funding models appear viable. By contrast, the concept of a subscription-funded BBC or a service partially supported advertising would lead to a reduction in funding, placing into jeopardy some of the fundamental objectives of PSB. Direct funding from general taxation may prove untenable politically given budgetary restraints; moreover, it raises important accountability issues.
- A summary of our assessment of the options, including the degree to which each addresses the challenges identified and whether stakeholders are supportive, is provided below. This is abridged from a more detailed table at the end of Section 5: Future models for PSB, where we summarise options; provide examples; review positives and negatives of each (impact, achievability, feasibility); detail the degree to which the options address the key challenges to PSB we identify and the extent of stakeholder support.

Option	Issues addressed	Stakeholder support	Viability
<b>Category: 1 (Strategy)</b>			
Changes to strategy	1, 2	High	•
Cooperation and collaboration	1, 2, 3	High	••
Consolidation and rationalisation	2, 3	High	•
<b>Category: 2 (Compact)</b>			
Liberalisation of PSB advertising restrictions	3, 4	Mixed	•
Changes to Terms of Trade	3	Mixed	•
Extension of PSB prominence to non-linear	1, 2, 3	Mixed	•••
Right of access for PSB non-linear services	1, 2, 3	Mixed	•••
Protection of attribution for PSB services	2	Mixed	•••
Right to compensation for commercial PSB activities	1, 2, 3	Mixed	•••
<b>Category: 3 (Public funding)</b>			
Reform of licence fee	None	Mixed	•
Top slicing of licence fee	None	Mixed	•
Abolition of licence fee (shift to commercial BBC)	None	Low	•
Direct funding of PSB	2	Low	••
Indirect funding of PSB	2	High	•••

- Below we include a key for the four key challenges facing PSBs as surfaced in our analysis; if the number is included in the ‘Issues addressed’ column this is indicative of the option’s ability or otherwise to enable the relevant challenge to be met.

1)	Lack of affordable access/prominence in digital for PSBs – particularly to ensure engagement with younger audiences – and limited, worsening bargaining power in relation to platforms
2)	Reduction in PSB content output owing to revenue challenges
3)	Significant content inflation in key genres and across distribution (upstream); and
4)	A constrained regulatory environment for linear advertising (reducing advertising income)

## 1. Introduction

- 1.1 Mediatique has been asked by Ofcom to contribute to a consideration of how the Public Service Broadcasting ('PSB') compact may need to evolve in response to changes in technology, consumer behaviour and business models over the next five years.
- 1.2 To inform our work, we undertook desk research involving review of various documents (e.g., from Ofcom, the BBC, commercial PSBs, third-party analysis) and conducted in-house financial modelling; in addition, we held confidential interviews with a range of PSB and non-PSB stakeholders active in the UK media and communications industries, to gauge where there might be consensus and where there is evidence of contention and disagreement. The results of these interviews are incorporated throughout the present document, and views are summarised at greater length in an Annex to this report.<sup>6</sup>
- 1.3 Our work forms part of Ofcom's review of the future of PSB, which comes at a time of complex change in the media industries, with significant potential impact on the PSB compact and its sustainability. Ofcom is now asking very fundamental questions about the compact, including what PSB objectives should be set, how they should be delivered and funded, and what regulatory and policy tools may be needed in the future. At the same time, Ofcom is examining the role of UK broadcasting, and the PSB channels, in the success of the wider creative economy.<sup>7</sup>

### Regulatory oversight and the current PSB compact

- 1.4 PSB is delivered by means of the Communications Act (2003), the Royal Charter and Framework Agreement between the Government and the BBC and within the terms of the licences issued to the commercial PSBs by Ofcom. In addition to regular (statutory) reviews of PSB<sup>8</sup>, Ofcom also oversees the delivery of Channel 4's commitments and remit in its annual Statement of Media Content Policy (as introduced in the Digital Economy Act, 2010<sup>9</sup>) and in multi-year reviews (the most recent of which was published in 2020 and covered the period 2014-18<sup>10</sup>).
- 1.5 Since 2010, and the Digital Economy Act, Ofcom has also been specifically tasked with considering the contributions of other 'media services' to PSB outcomes, including TV and radio broadcasters (e.g., multichannel groups and commercial radio companies) and online providers (where editorial control is exerted). While not technically PSB, programming provided by these players can contribute to the diversity and plurality of the content market.
- 1.6 The context in which the PSB compact operates has undergone significant changes over the years during which audio-visual content and services have been regulated by Ofcom – notably the transition from analogue to digital transmission, the issuance of the latest licences by Ofcom to commercial PSBs (for 10

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<sup>6</sup> We interviewed senior management at 20 industry stakeholders including broadcasters, platforms and industry groups and covered the current state of the market and future trends, the role of PSB and in particular the definition of PSB content and delivery, various options to reform funding models and the potential impact from each, and the role of regulation in an evolving media landscape. See Mediatique, *Future models for the delivery of Public Service Broadcasting – a summary of industry stakeholder interviews: an annex to a Report for Ofcom in support of its review of Public Service Broadcasting*.

<sup>7</sup> The Department for Digital, Culture, Media and Sport Select Committee is also [engaged in reviewing the future of PSB](#) and was taking evidence and calling for submissions as this report for Ofcom was being written. In November 2020, an Advisory Panel to support the Government's strategic review of PSB was announced; the [terms of reference](#) are described in the press release issued on the Advisory Panel.

<sup>8</sup> The [latest five-year review](#) was published in February 2020 and informs Ofcom's consideration of the future of PSB.

<sup>9</sup> See the [Digital Economy Act](#).

<sup>10</sup> See the [most recent review](#). Channel 4 is required to broadcast "a broad range of high-quality and diverse programming which demonstrates innovation, appeals to the tastes and interests of a culturally diverse society, includes programmes of an educational nature, and exhibits a distinctive character." In addition to statutory obligations for the main channel, Channel 4 is also responsible for delivering a range of media content on its other services to meet its remit to be distinctive and innovative.

years from 2015-2024) and the decision, as part of the most recent renewal of the BBC's Charter (in 2016), to disband the BBC Trust and to subject the BBC to regulatory oversight by Ofcom.<sup>11</sup>

- 1.7 The current system for the delivery of PSB in the UK is based on a balance between the rights and obligations of key institutions – the BBC and commercially funded PSBs<sup>12</sup> – and reflects the historically critical importance of access to scarce public airwaves. In exchange for privileged access to these airwaves and prominent positions on TV channel guides (and, in the case of the BBC, to public funding), PSB channels undertook to produce and distribute high-quality original UK content, regional programmes and impartial news; in so doing, the PSBs provided depth and breadth of content (in a wide range of genres appealing to different tastes and needs) on a universally available basis, while at the same time contributing to the UK's creative industries.
- 1.8 The value of the regulatory assets within the PSB compact (spectrum and prominence) have declined over time, in line with the reduced share of total audio-visual content consumption that is delivered via broadcast TV. Declines in the value of these assets have been recognised through changes over time to PSB undertakings, but PSBs may find it challenging to meet even these reduced obligations as the trends disfavouring broadcast TV persist.

#### The current review of the future of PSB

- 1.9 As noted by Ofcom in previous reports and reviews, and as underlined again in the documents issued for the current forward-looking exercise, the PSB compact has come under increasing pressure, linked to innovations in technology, shifts in consumer behaviours and at times rapid evolution in commercial business models. Some of the changes Ofcom has observed raise fundamental questions not just around how PSB objectives can be met but more fundamentally what constitutes 'PSB' in an era when consumers have access to extensive amounts of content from all around the world, often for free.
- 1.10 As a consequence, Ofcom has launched an extensive consultation process, entitled *Small Screen: Big Debate*<sup>13</sup>, looking at "what the PSB system should deliver in the future, how it should be delivered and what legislative and regulatory framework might be needed."
  - To help frame that debate, Ofcom has published a number of analyses and extensive data from recent years (focussing in particular on the period 2014-18) charting audience behaviours, the take-up of new technologies and trends in relation to expenditure by broadcasters and others on (*inter alia*) UK original content, by genre. It is also undertaking extensive research among UK audiences to determine what they (both as consumers and as citizens) want and expect from public-service media.
  - Ofcom is also consulting stakeholders, including the PSBs themselves, non-PSB broadcasters and other media companies. Ofcom has made it clear that it wants "to stimulate new ideas on the future of PSB, with its stated purpose to provoke a national conversation involving viewers, the broadcasting industry, Parliament, and regulators about how the benefits of PSB might be assured for the future."
  - Based on its workstreams and engagement with consumer-citizens and stakeholders, Ofcom intends to consult on its conclusions before providing its recommendations to Government for any subsequent action.

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<sup>11</sup> Ofcom reviews how it regulates the BBC at least once a year and reports annually on whether and how the BBC meets its performance undertakings as set out in the BBC's operating licence.

<sup>12</sup> The main channels of ITV, STV, Channel 4, S4C and Channel 5 are designated as PSB for the purposes of the Act (i.e., excluding the 'diginets' such as E4, More4, ITV2, ITV3, etc.).

<sup>13</sup> See Ofcom's [Small Screen: Big Debate](#).

1.11 The timing of this process is subject to change, owing to the intercession of the Covid-19 crisis. Original plans to hold a number of roundtables and other meetings in Spring 2020 were disrupted as the lockdown was imposed, and initial expectations of a final report in time for Summer 2020 were deemed impractical. Moreover, the impact on broadcasters and others of the pandemic and its aftermath has been acute and may indeed fundamentally affect the medium-term outlook for PSB and its practitioners, in ways difficult to determine. We understand that Ofcom has engaged further with stakeholders throughout 2020 and will consult formally on its findings by the end of the year, with the process continuing into 2021.

#### Mediatique's contribution

- 1.12 Ofcom commissioned us to provide three workstreams (summarised in the remaining four sections of the present report). In the **first module** (presented in section 2), we provide a summary – as informed by statutory requirements, recent formal reviews (of PSB, Channel 4's Statement of Media Content Policy and the BBC's Operating Licence), Ofcom's own analysis and the views of stakeholders – of the key constituents of PSB in 2020.
- 1.13 We then provide, in a **second module** (presented in sections 3 and 4), a review of the intensifying challenges confronting PSB – including the impact of improving network delivery, take-up of connected devices, shifting audience behaviours (especially among younger demographics) and evolving business models of key providers and new entrants alike – and how these are likely to change over time.
- In section 3, we provide an analysis of sector developments in viewing, usage, revenues and expenditure across the UK media over recent years, and what impact these have had on key attributes of PSB, including expenditure on original UK content. In section 4, we provide a view of how the market will develop between now and 2024, absent any changes to regulation, focussing on the role of broadcasting, the evolution of pay TV, the growth of subscription video on demand ('SVOD') and the relationship between PSBs and third parties (e.g., platform operators and other distributors). We chart, in particular, the impact on original content expenditure and the effects upstream, including on the independent production sector.
  - In our analysis of both current dynamics and likely future developments, we also briefly touch on the audio sector, covering trends around the displacement of radio by other audio services such as podcasting and music streaming and how this is likely to evolve over the next five years. This element is included given the BBC's role in radio and the importance of the BBC, commercial and community radio in sustaining news and local programming, delivered via a range of audio services.
- 1.14 In the **third module** (presented in section 5), we propose a number of options to sustain the delivery of PSB in the future, ranging from approaches close to the *status quo* (implying evolution and self-help measures such as restructuring, consolidation and partnership) up to and including radical transformation (involving significant changes in the scale, scope and even identity of key PSB players, alterations to business models and reform of funding mechanisms). We evaluate each option in light of their pros, cons and impediments (including requirements for regulatory or policy change) and conclude with an assessment of whether and how well the options contribute to addressing the challenges to PSB identified in our report.
- 1.15 Published separately to this report is an annex in which we summarise our findings from an extensive set of discussions with stakeholders, covering such areas as the degree of consensus on definitions of PSB; views on funding options and models for the future; and insights from market participants about the medium-term evolution of relevant markets absent changes to the regulatory compact. In these discussions, we have explored stakeholder views on the sustainability of PSB, their recommendations for changes to the compact and insights into the advantages and disadvantages of different options and models.

## 2. Principles and objectives of PSB: toward a consensus view

2.1 The Communications Act (2003) sets out the PSB purposes and objectives. The BBC, ITV, STV, Channel 4, S4C and Channel 5 are all PSB providers, but some channels in the portfolio of commercial PSB providers are fully commercial and have no public remit.<sup>14</sup>

### PSB definitions and objectives

2.2 Based on the statutory principles enshrined in the Act, Ofcom's own definitions<sup>15</sup>, the extent of current terms and conditions across the PSB landscape and our discussions with a range of stakeholders, we have distilled here the key points that help serve to define PSB – now, and for the medium term. Readers are advised to consult the Annex to this report, where views expressed by a range of stakeholders are summarised, compared and contrasted.

2.3 We have identified a number of objectives core to a consensus definition of PSB and with which all stakeholders we interviewed agreed, including:

- Sustaining production of content in market failure genres (e.g., kids, arts, culture) and categories (e.g., Nations and Regions, including indigenous-language content);
- Promoting UK origination across multiple genres, and ensuring breadth and depth in content output;
- Making content available that appeals to multiple tastes and preferences – targeting many audiences;
- Ensuring content is made that sets a quality benchmark; and
- Fomenting skills in the UK's creative industries and promoting the appeal of UK production resources in international markets.

2.4 However, there were a number of objectives on which stakeholders taking part in our audit of views disagreed – and the variations in comments tend to follow understandable patterns depending on the identity and category of the respondent.

- The PSBs themselves consider that a core PSB characteristic is that content is available universally, free at the point of consumption. This, by definition, excludes pay TV channels from securing PSB status – and some stakeholders (including those with pay TV operations) argued that the availability of content behind a pay wall should not be grounds for excluding such content from a definition of public service.<sup>16</sup>
- There were also differences of opinion on whether the PSB system should be based on current institutions or another organising principle. Again, the differences expressed here were broadly along institutional lines, with existing PSB institutions strongly in favour of retaining the current institutional delivery mechanisms of PSB and other stakeholders profoundly of the view that the content outcomes, rather than the institutional source, should be central to definitions of PSB. PSBs, themselves, pointed to the importance of brand (including the power of the brand historically) as a key factor in sustaining the PSB compact.

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<sup>14</sup> See Appendix for background information on the PSB system and institutions, and Ofcom's role in regulating PSB.

<sup>15</sup> Ofcom has in the past (e.g., in its first PSB Review in 2004) provided a number of 'purposes' and 'characteristics' of PSB; it should be noted that these have not been emphasised in the current review. In its [PSB Tracker](#) (currently suspended owing to the Covid-19 pandemic), it has however routinely asked respondents to consider a range of statements regarding the purposes and characteristics of PSB content, and whether and the degree to which channels have delivered on these.

<sup>16</sup> [Sky has publicly questioned the PSB status of ITV and Channel 5](#), arguing that they do not deliver value equal to their benefits as designated PSBs. Sky also argues that multichannels provide produce content with clear PSB attributes. Even some PSBs said to us privately that the existence of the BBC and multiple other PSBs may not be sustainable. Whether for tactical or other reasons, Sky recently announced it was transitioning Sky Arts to a free-to-air' basis, including via broadcast on Freeview; this is one answer to the question as to whether content produced by non-PSBs might have the characteristics of PSB (high quality, original content, universally available, and for 'free').

- All interviewees accepted the importance of PSB to the independent production sector, although there continue to be questions raised about the bargaining position of larger indies. Some interviewees from among broadcasters noted that the terms of trade are no longer fit for purpose with regard to the bigger, increasingly globally focussed players in the sector able and aiming to negotiate different terms with broadcasters, particularly around the sharing of rights and the ability to supply international SVOD platforms. Suppliers, for their part, continue to portray the large PSBs as ‘gatekeepers’ with market power. These views tended to settle along traditional fault lines – with domestic broadcasters routinely fearful of the growing strength of internationally owned, globally focussed external suppliers.
- While there was widespread support for the role that the PSB compact plays in ensuring the production and wide availability of news, particularly local news, a number of interlocutors (including pay TV operators, SVOD operators and social media companies) argued that the news ecology was enriched by suppliers beyond PSBs and that this should be more openly acknowledged in the context of any reform of PSB that might be envisaged. This might include, for example, consideration of the contribution of digital providers to news when policy makers and regulators consider any changes to funding models and content regulation regimes.

- 2.5 There was consensus arising from our stakeholder engagement that the PSB compact needs updating if it is to be relevant in the future. Key areas of consensus include: the need to ensure that PSB rights and obligations extend to digital/IP platforms (i.e., away from the connection to terrestrial spectrum); and greater transparency on access and prominence (although not necessarily to extend privileges in this regard to legacy PSB institutions).
- 2.6 It should be noted, however, that some stakeholders continue to emphasise the role that broadcast (particularly Freeview) plays in providing PSB to mainstream UK households, which they believe may be placed at risk if a new PSB compact is redrawn exclusively on the basis of IP or digital means of delivery.<sup>17</sup>
- 2.7 On access and prominence, there was considerable agreement among those outside the group of global SVOD and online video providers that rules should be consistent across broadcast and IP (the idea of a ‘level playing field’ also emerged in relation to editorial standards, data capture and taxation). New entrants (SVOD players, social media platforms) argued, however, that prominence in the non-linear environment should not be introduced in a way that would stifle innovation (in search, navigation and discovery) or counter the interests and preferences of consumers themselves (who may prefer multiple sources of content and ease of access to them).
- 2.8 There was also criticism from outside the PSB institutions around the practicalities of extending prominence to non-linear players that may well feature extensive content that is not ‘PSB’ (for example, catch-up content from non-PSB channels in the commercial PSB family). Some respondents argued that PSB content should itself be prominently featured on players if these are to be given valuable preference in relation to access and prominence on connected platforms.
- 2.9 In summary, from our review of the PSB framework and stakeholder opinions, we think it is possible to propose a foundational set of principles that are 1) consistent with the broad thrust of the purposes of PSB set out in the Act; 2) in line with Ofcom’s latest determination of PSB purposes and characteristics (as

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<sup>17</sup> It should be noted that two multiplex licences – one, awarded to ITV and Channel 4 (‘Digital 3&4’) and one now owned by ITV plc (‘SDN’) – expire in 2022, and the Government will consider whether and how to renew these (no mechanism currently exists for automatic renewal). The Digital 3&4 multiplex carries the main channel of ITV throughout the regions of England and Wales, as well as STV and Channel 4’s main service and it is Mediatique’s assumption (not necessarily shared by Ofcom) that this licence will at the very least carry on until the ITV and Channel 4 operating licences are next subject to renewal at the end of 2024, and probably beyond. The renewal (or even re-advertising) of the SDN multiplex licence may be subject to different terms, given its commercial nature and ownership. The Government will not have reached a decision in time for any conclusions to be incorporated into the present analysis.

represented by the list of questions put to respondents in the PSB Tracker around high quality, breadth and depth of genres, innovation, commitment to news and regional issues and trustworthiness); and 3) subscribed to by all key categories of stakeholder. However, we underline that these agreed definitions are not necessarily linked to the perpetuation of the current institutional framework for delivery or to the concept that availability must be 'free' at the point of delivery, given the growth in the willingness of many more households to pay for access to audio-visual content. There is a clear split on these issues between the PSBs and non-PSBs, for understandable reasons.

- 2.10 We also identified a further tension within the sector on the means of ensuring delivery of those PSB purposes and characteristics where there is consensus – the degree to which the current institutional bias is too weighted toward linear, broadcast TV and not suitably fit for future purpose as consumer behaviour, technological innovation and changes in business models continue to transform media consumption outcomes. It is the direction and pace of these anticipated changes that are likely to dictate how the challenges facing the PSB compact develop over time. This is the theme of the next sections of our report.

### 3. Market dynamics and the PSB system

- 3.1 A number of market developments are creating significant challenges for the PSB institutions and the sustainability of the PSB system.
- Viewing of traditional broadcast TV (upon which the PSB compact is still reliant) is declining – driven in turn by technological innovation (e.g., faster broadband speeds and adoption of smart devices on which to view content, such as smart TVs, streaming sticks) and changes to consumer behaviour (notably in viewing/usage and willingness to pay).
  - Certain traditional revenues associated with PSB (TV advertising, sponsorship) are flat or declining; meanwhile, the justification for a universal licence fee, given reduced broadcast viewing/listening and growing competition from SVOD and online audio-video, is being eroded. The fastest growing revenue segments in recent years have been SVOD and Advertiser-funded VOD ('AVOD'), where new entrants have been active. PSBs (and other broadcaster channel groups with UK distribution) have sought to mitigate viewing and revenue weakness by offering their own on-demand services, but these have not compensated for the decline in traditional engagement (and face much greater competition from multiple providers' on-demand content in the online space).
  - There has been marked inflation in the cost of key genres, including drama, comedy and high-end factual, driven by intense competition for talent and programmes. PSBs have been able to work co-operatively with SVOD streamers and other (largely US) channel groups (such as HBO) in co-productions in certain genres (e.g., high-end drama, comedy) but often at the risk of foregoing the value historically available to them in secondary (e.g., overseas) markets. This has had the effect of stretching budgets for the PSBs (less upfront investment) but at the cost of a reduction in editorial control, less brand attribution in secondary and international markets and a potential decrease in overall returns.
  - Both TV and radio are being affected by the emergence of new platforms aimed at curating services, including via smart TVs and home assistants that do not necessarily confer prominence to local providers (such as the PSBs and commercial radio stations and services). The means by which content is displayed on home screens and via smart speakers often favour content or services from providers willing to pay for access and prominence, and such arrangements are often reached at a global level (for devices in multiple markets). In these instances, global players routinely displace local providers such as the UK's PSBs or UK radio stations. In some cases, the owners of the operating systems (e.g., Amazon) seek to promote their own content directly, typically to lock in customers not only for their video content but for a range of other services (music, gaming, e-commerce).
- 3.2 The challenges facing traditional broadcasting generally, and PSBs specifically, show no signs of abating. Consumers will become ever more enabled (with technology and devices), confirming two clear trends: younger, digitally savvy audiences will grow older and take their digital behaviours with them into subsequent life phases; and older consumers will themselves begin to adopt new behaviours and indeed are already doing so.
- 3.3 As the Covid-19 pandemic hit in early 2020, and throughout the lockdown period, evidence mounted of an acceleration in these trends. While the direction of travel had already been apparent – non-linear viewing and listening in the ascendancy, at the expense of broadcast, a significant displacement of traditional pay TV by smaller bundles of pay TV channels and/or SVOD, structural pressures on TV and radio advertising – the pandemic and its aftermath acted as an accelerant. Notwithstanding a spike in TV viewing and radio listening (driven by the availability of daytime audiences at home during lock down<sup>18</sup> and consumption of broadcast news), the trend lines look inescapable. Indeed, as schedules began to thin, reflecting the impact of the

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<sup>18</sup> These gains were offset in the case of radio by a reduced availability of listeners in cars.

enforced hiatus in TV production during lockdown, a reversion to earlier trendlines was already evident for TV.

- 3.4 It is not yet clear whether the spike in SVOD subscriptions in lockdown will change the fundamental long-term outcomes or merely bring them forward.<sup>19</sup> But change is inevitable: in an era of IP delivery of services, as and when consumers choose, the competition is intensifying, and global players are securing an increasing share of consumer attention, at the expense of traditional broadcasters. This places the delivery of PSB objectives under significant strain.
- 3.5 In the remainder of this section, we review the dynamics that have led to the current scale, scope and structure of the UK audio-visual ('A/V') market, starting with enablement (broadband connectivity and device take-up) and covering the resultant relationship between platforms and PSBs, broad trends in viewing and usage, with a focus on PSB viewing, and the concomitant impact on sector revenues. We then analyse PSB expenditure trends, related to these revenue impacts, followed by a review of how market dynamics have driven corporate activity (fuelling mergers and acquisitions across the value chain). While a secondary element of our analysis, we conclude this section by providing a broad overview of trends in audio, and in particular the displacement of radio by other audio services.

Broadband connectivity and device take-up

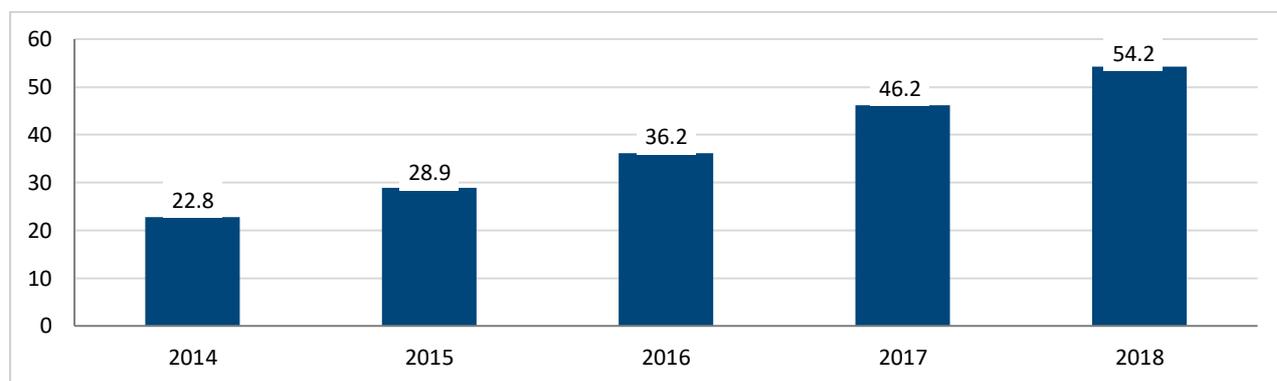
- 3.6 The catalyst for the decline in broadcast TV viewing has been the growing number of households with fixed broadband connections in the UK: 80% of UK households now have access to a fixed-broadband internet service. Broadband connectivity is even greater if mobile is included.

Figure 1: Number and % of UK homes with fixed broadband connections (2014-2018) (Ofcom Communications Market Report)<sup>20</sup>

	2014	2015	2016	2017	2018
Fixed broadband connections (m)	23.7	24.7	25.4	26.0	26.6
% of UK households w/ fixed broadband connections	73%	78%	79%	82%	80%

- 3.7 Moreover, these connections increasingly permit higher average download speeds, thus enabling a greater proportion of users to stream content, including in high-definition.

Figure 2: Average actual fixed broadband download speed, Mbit/s (2014 – 2018) (Ofcom CMR)



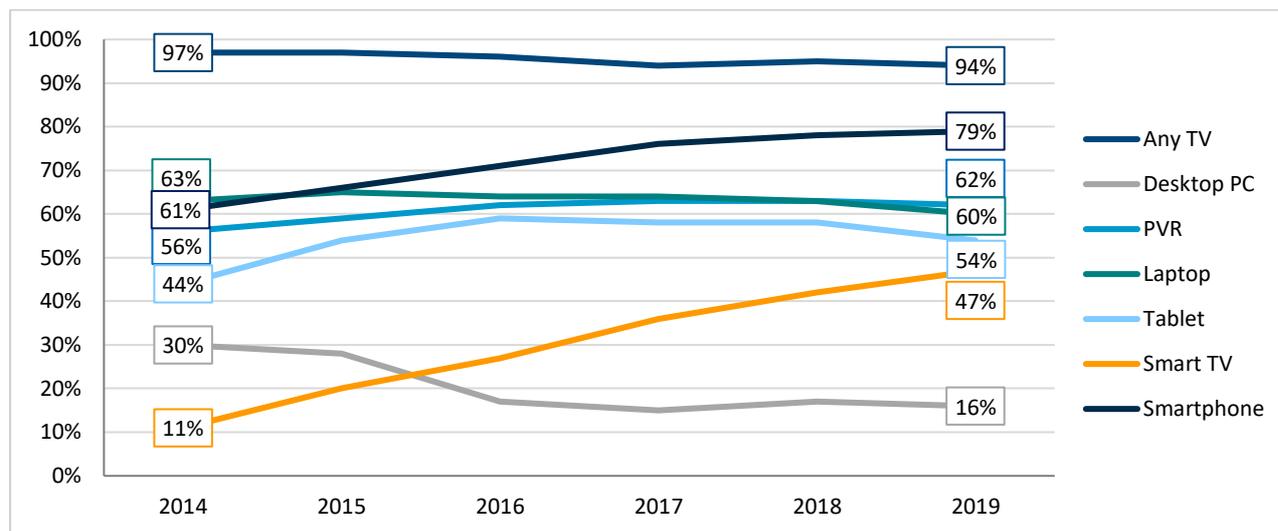
- 3.8 A consequence of increased connectivity has been the greater extent to which the delivery of audio-visual content over IP is accessible and prominently displayed on devices (e.g., TV sets) that were once dominated by broadcast TV channels, accessible via an EPG on a 'free' TV service or one provided by a pay TV operator such as Sky or Virgin.

<sup>19</sup> We provide forecasts later in this section outlining a base case for viewing, SVOD, pay TV and a range of other metrics.

<sup>20</sup> From this point onwards, we refer to the various Ofcom sources using the following shorthand: Ofcom Communications Market Report: 'Ofcom CMR'; Ofcom Media Nations: 'Ofcom MN'; Ofcom PSB Review – *Small Screen: Big Debate*: 'Ofcom PSB Review'.

3.9 A key driver of increased competition in the household has been consumer adoption of smart TVs (i.e., TVs capable of connecting to the internet natively) and the popularity of streaming sticks (‘dongles’) which enable ‘dumb’ TVs to become ‘smart’.<sup>21</sup> By the end of 2019, 47% of UK households had a smart TV, and a further 11% were using streaming sticks. While viewing on PCs, laptops, tablets and smartphones is a factor, and PVR use has long had a cannibalising impact on broadcast viewing<sup>22</sup>, it has been the colonisation of the main set in the living room for IP-delivered services that has accelerated the disintermediation of traditional linear broadcast most emphatically.<sup>23</sup>

Figure 3: Household Device Take-up, % (2014 – 2019) (Ofcom MN; PSB Review)



3.10 Pay TV providers themselves have had to adapt, with Sky offering IP-enhanced services both indirectly through off-brand proposition Now TV and directly through Sky+ and Sky Q, using hybrid satellite-IP technologies (with a clear roadmap to migrate its base to IP over time).

PSBs’ relationships with platforms

3.11 There has been a long history of friction between channels and pay TV distributors on access, prominence and compensation. However, the settlement for satellite and cable has at least been relatively transparent – with mainstream PSB channels prominently displayed on EPGs and even their players (iPlayer, ITV Hub) allocated relatively strong positions on Sky and Virgin.<sup>24</sup>

3.12 As Sky, Virgin and BT increasingly seek to offer IP-enabled propositions, and enter into deeper relationships with the global SVOD streamers themselves (e.g., Sky Ultimate TV package, which includes Netflix Basic), they thereby potentially displace smaller, local providers of services (such as the PSBs). Moreover, in households that do not subscribe to pay TV (or who ‘toggle’ to their underlying smart TVs to access on-demand content),

<sup>21</sup> Although the relevance of streaming sticks is waning as smart TVs become more commonplace, we note their importance in enabling widespread access to audio-visual content streamed over IP and rendering this behaviour habitual.

<sup>22</sup> PVRs have certainly been disruptive of broadcast viewing (and traditional advertising models owing to the prevalence of ad-skipping in PVR-equipped households). However, PVRs have tended to reinforce broadcast programme brands (on standard PVRs, consumers record programmes from broadcast schedules for viewing at a more convenient time). The availability of a huge array of content, delivered over the IP (either via a managed connection or ‘over the top’) introduces significant substitutive competition. Critically, late-generation PVRs (e.g., in Sky + and Sky Q households) are IP-enabled for streaming and ‘progressive downloading’, in addition to providing extensive in-home storage for consumer-initiated recording from a broadcast signal.

<sup>23</sup> Our focus here is on residential connections, and substitutability of broadcast by IP in the home. Mobile connectivity has a role to play here, of course (and this may be increasingly the case depending on the extent and pace of 5G roll-out and its ability to ‘carry’ TV or TV-like content in the household and on the move). In our forecast period to 2024, we assume that the ability of IP to challenge broadcast as a medium of PSB delivery will be determined by fixed-line rather than mobile connectivity.

<sup>24</sup> We return to the relationship between PSBs and platforms later in this section.

the emergence of new gatekeepers poses a growing threat to PSBs, absent changes in the legislation promoting the findability of PSB content.

- 3.13 The longstanding appeal of domestic broadcast content in the UK initially ensured that the PSBs, and their associated BVOD propositions, were a prerequisite for any comprehensive smart TV or connected device. However, as this appeal begins to wane, and heavyweight global streamers join the competition for prominence, the picture becomes more complex.
- 3.14 For new gatekeepers, controlling the operating system represents an opportunity to monopolise the sitting room experience by offering a common consumer interface across smartphones, speakers, tablets and TVs, for example. There is very likely to be a hierarchy of access on single devices, whereby the provider of the underlying operating system, a pay TV operator with its own user interface and content suppliers all vie for control of the relationship with the end user. In this scenario, the smaller content suppliers (e.g., a local TV or radio broadcaster, including the PSBs) may struggle to secure bargaining power, even though it is their content, in many cases, that consumers want to see.<sup>25</sup>
- 3.15 Further, these new entrant gatekeepers will expect to be (indeed, some already are) compensated for providing access, prominence and positioning on these platforms. The underlying operating systems and user interfaces of many smart devices (Amazon, Google and Apple) are incentivised to favour their own content (e.g., Amazon Prime Video) and/or the content of those with the means to pay for access to homepages, promoted positions within, for example, top picks and recommendations and to prominence in searches.<sup>26</sup>
- 3.16 A key currency in the trading of access and prominence is first-party data, the extremely valuable information on customer preferences and choices generated via the supply of content through connected devices. Depending on the technology, user interface and the functions of the operating system, data is collected and monetised in several ways: to inform tailored advertising, to secure and retain subscription income and to sell adjacent goods and services (e.g., e-commerce, bundled audio-visual products). These exchanges of value are increasingly occurring at global rather than local level (e.g., between large equipment manufacturers and global content aggregators such as Netflix or Disney), making it harder for the PSBs to secure traction.<sup>27</sup>
- 3.17 Of the current PSB cohort, only the BBC appears to have been able to routinely lay claim to a prominent position on the landing page of connected devices. ITV and Channel 4, for example, report difficulties in their negotiations with operators, and the smaller PSBs face a significant deficit in bargaining power.<sup>28</sup>
- 3.18 In the figure below, we highlight the different ways in which the PSB players are currently accommodated on these platforms.<sup>29</sup>

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<sup>25</sup> Ofcom has already recommended changes to ‘appropriate prominence’ rules to ensure connected devices display PSB prominently. These are already the subject of debate across the industry, as emerged in our stakeholder discussions. Many argue that PSB is already prominently displayed; moreover, it is dangerous, say some, to pre-empt consumers’ own preferences with regard to how they search for and find content (as expressed through recommendation, customisation or the personalisation that is delivered via search algorithms). The PSBs worry that platforms (pay TV and new OS providers) seek disaggregated access to PSB content where the value is attributed to the platform rather than the broadcaster. We consider ‘discoverability’ as part of our review of options around the future regulation of PSB in section 5.

<sup>26</sup> A similar dynamic is at play in the audio space, as we review below.

<sup>27</sup> Dynamics in this market are reviewed in detail [in a report by Mediatique commissioned by Ofcom](#) and published in August 2020 as part of consultation on the prominence regime.

<sup>28</sup> iNews, [ITV boss warns Amazon ‘smart TV’ sets could make UK broadcasters disappear](#), (2019).

<sup>29</sup> Several (but not all) smart TV manufacturers have reached a deal with Freeview to enable Freeview Play, ensuring that PSB players are suitably prominent; they also provide backward compatible access to players via the EPG (for catch-up from the previous seven days).

Figure 4: Relative dynamics between PSB VOD services and connected TV platforms (Mediatique)

PSB VOD Service	Description
<b>BBC iPlayer</b>	Generally seen by platforms and connected gateways as important ‘hygiene factor’ to ensure a comprehensive smart TV proposition; normally positioned in the first few ‘tiles’ on a home screen, usually sharing the privilege with Netflix, Amazon, YouTube (on Google Android devices) and – increasingly – Disney+
<b>ITV Hub</b>	Nearly always prominently displayed on connected gateways; both sides of the negotiation report friction on prominence and access, particularly in terms of revenue share (e.g., of BVOD); CE/OS players maintain that other global players are willing to pay/share more than ITV for prominence
<b>All4</b>	Less prominent on home screens; harder for Channel 4 to argue ‘must have’ status as it does not have long-tail of programme rights (as these are often traded directly by IP rights holder with other distributors)
<b>My5</b>	First of the PSB providers to lose front page prominence as a result of SVOD launches – as the smallest and last of the PSB players (when placed in contiguous order). May secure advantage from parentage (ViacomCBS) over time, depending on evolution of Pluto TV (and other services) integrated into My5 <sup>30</sup>
<b>STV Player Clic</b>	STV Player is a separate service to ITV Hub, and features content from the main ITV channel which can only be viewed on STV Player for users in Scotland. ITV Hub’s other services (ITV2, ITV3, etc., in linear and for catch-up) are available to Scottish users via the ITV Hub. S4C’s Clic is hosted by iPlayer, as well as having its own online portal and app.

Viewing and usage trends in an era of increased connectivity

3.19 The growth of SVOD services, which occupy prominent positions on connected devices, has been the most important contributor to the downward pressures on broadcast TV viewing since 2014: in 2019, SVOD penetration reached more than half of all UK households, just six years after being tracked by BARB for the first time. Netflix is the dominant service, now in over 12m households.<sup>31</sup> In that time, live TV viewing has declined to just 53% of all A/V viewing tracked by Ofcom, from 85%.

<sup>30</sup> Providers of connected TV operating systems (‘OS’) have innovated recently by introducing different means of ‘listing’ tiles on front pages of their propositions – through adding a row above the legacy row of tiles allowing users to explore content availability in different ways. However, the appearance of a given tile in a prominent position continues to be of ‘tradeable’ value to OS providers, and this will advantage content suppliers with higher willingness to pay, ability to trade at global level across the value chain (content, data, technology) and/or with corporate ownership links with the OS provider (e.g., Apple, Google). By definition, this is likely to disadvantage domestically oriented content suppliers, including the services of the PSBs that are not currently protected by prominence rules.

<sup>31</sup> The impact of the Covid-19 induced lockdown has been significant in terms of SVOD penetration in the UK – Netflix and Amazon remain market leaders, but subscribers of the timely new entrant Disney+ have grown at the fastest rate over the period: by mid-2020 we estimate that Disney+ had c.3m subscribers. This is in line with survey data published by Ofcom in Media Nations 2020. BARB is not currently reporting new data on SVOD, owing to the lockdown.

Figure 5: SVOD households in the UK, m (2014-2019) (Mediatique; BARB)

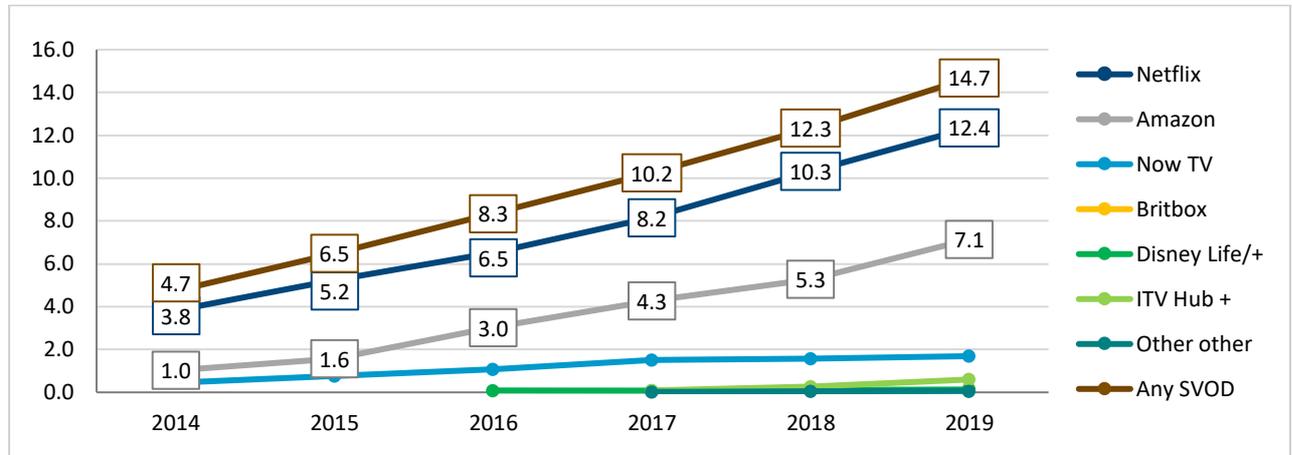
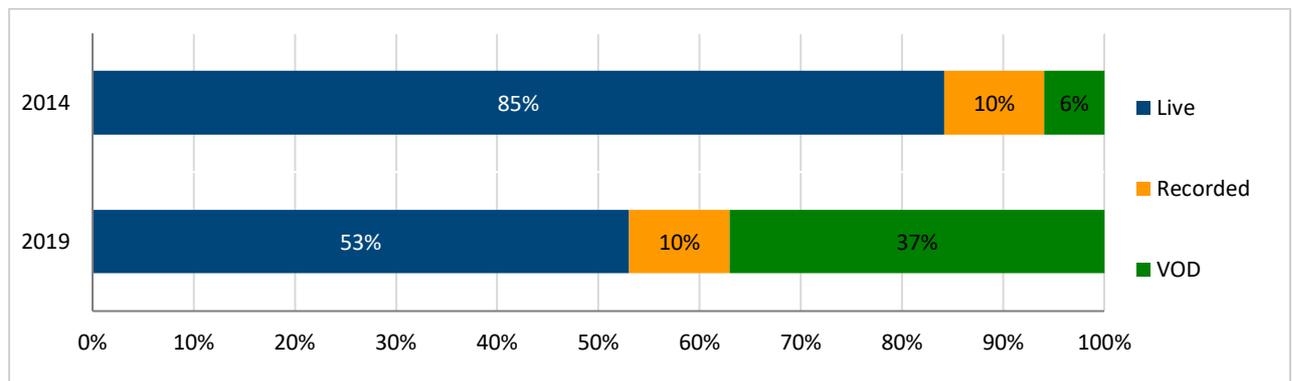
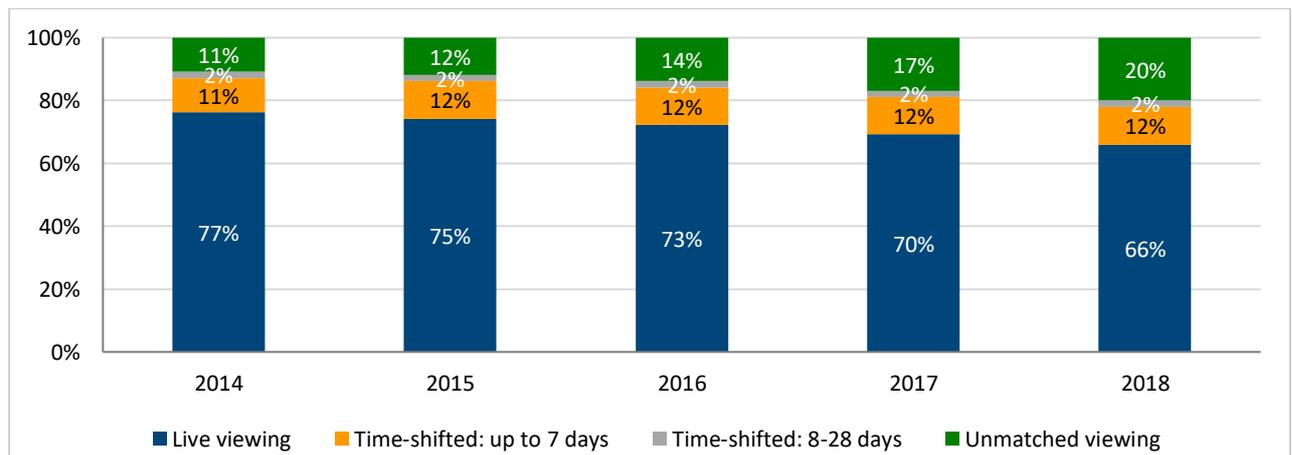


Figure 6: Share of total video viewing by category, % (2014-2019) (Ofcom MN)<sup>32</sup>



3.20 SVOD providers do not routinely publish viewing figures for their services. BARB tracks total viewing (on TV screens) of broadcast content versus viewing of PVR and catch up, and also what BARB calls ‘unmatched’ viewing (a blend of PVR playback +28 days; SVOD; YouTube; DVDs; gaming, and ‘idle’ time using the EPG). While not exhaustive (it does not account for viewing on smartphones and tablets), the BARB metric does underline the degree to which broadcast TV is in decline.

Figure 7: Live, time-shifted and unmatched share of viewing, % (2014 – 2018) (Ofcom MN; BARB)



3.21 Declines in linear viewing are more marked among younger demographics, suggesting future outcomes will be even starker. As viewers age, they are unlikely to wholly abandon their current digital behaviours even if

<sup>32</sup> Starting with Ofcom’s Media Nations 2019 report, it published VOD data with more granularity than it did five years ago. For the purposes of the chart we have used a historical version of this chart from 2014 and the latest breakdown from Media Nations 2020.

there may be some re-balancing of viewing across different categories in later life stages. At the same time, older viewers themselves are showing signs of altering their consumption patterns over time.<sup>33</sup>

**Figure 8: Total broadcast TV minutes, (broadcast + 7 days), by demographic (2010 vs. 2019) (Ofcom MN)**

	2010	2019	Change (%)
All Adults (4+)	242	183	-24%
Aged 4-15	150.6	64.1	-57%
Aged 16-24	168.7	69.9	-59%
Aged 25-34	198.6	104.3	-47%
Aged 35-44	234.3	140.1	-40%
Aged 45-54	269.2	207.1	-23%
Aged 55-64	311	274.3	-12%
Aged 65-74	342.3	328	-4%
75+	338	349.1	3%

3.22 The impacts of consumer enablement and shifts in behaviour on the TV market have been observable for many decades. But since 2012, there has been a discernible change to the rate of decline in the reach of PSB channels, and this is largely driven by the growing penetration of connected devices and the adoption of SVOD services. As we illustrate in the figure below, BBC One’s CAGR decline in weekly reach accelerated from just -0.1% in the period 2008-2012, to -2.8% in the period 2012-2019.

**Figure 9: CAGR decline in weekly reach of five main PSB channels, % (2008 – 2019) (Ofcom PSB Review)**

	BBC One	ITV	BBC Two	Channel 4	Channel 5
2008 – 2012	-0.1%	-1.9%	-2.6%	-2.6%	-1.1%
2012 – 2019	-2.8%	-3.2%	-3.4%	-3.8%	-3.4%

Erosion of traditional revenue streams in favour of new business models

3.23 Declines in broadcast TV viewing have directly affected traditional revenue categories including TV advertising, the primary revenue source for the commercially funded PSBs; meanwhile, the licence fee allocated to TV has also been declining (subjected to freezes and the need to meet additional commitments such as local TV and S4C).

**Figure 10: Traditional revenue categories decline, £m, 2018 prices (2014 - 2018) (Ofcom PSB Review)**

	2014	2015	2016	2017	2018	CAGR
Advertising	4,100	4,358	4,329	4,062	3,900	-1.2%
Public funding	2,896	2,770	2,677	2,557	2,462	-4.0%
Sponsorship	220	219	223	220	221	0.1%
Subscriber income	3,843	4,206	4,323	4,253	4,075	1.5%
Total	11,059	11,553	11,552	11,092	10,658	-0.9%

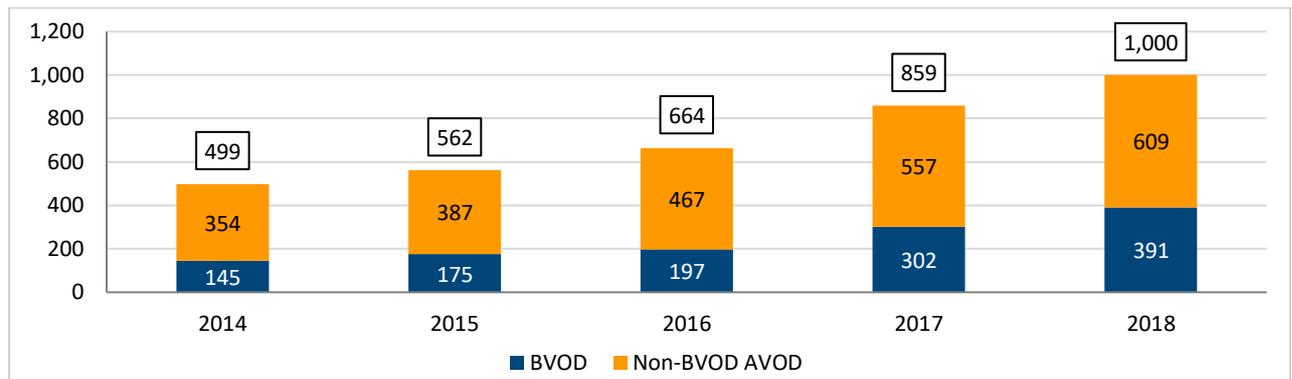
3.24 The revenues that underpin the delivery of PSB content (the licence fee, TV advertising and sponsorship) have been particularly weak. However, even traditional pay TV revenues have been under pressure as consumers shift to cheaper packages and to SVOD. The decline in pay TV revenues has had an impact on PSBs – both directly through downward pressures on affiliate fees paid to commercially funded PSBs ITV and Channel 4 (e.g., for ITV Encore, HD variants of the mainstream commercial PSB channels) and indirectly via

<sup>33</sup> We return to the implications for the future of these trendlines at the end of this section.

the reductions paid by Sky and Virgin for the UKTV channels. Owned by BBC Studios<sup>34</sup>, these are not PSB services, but help fund the dividend stream that flows through to the BBC.

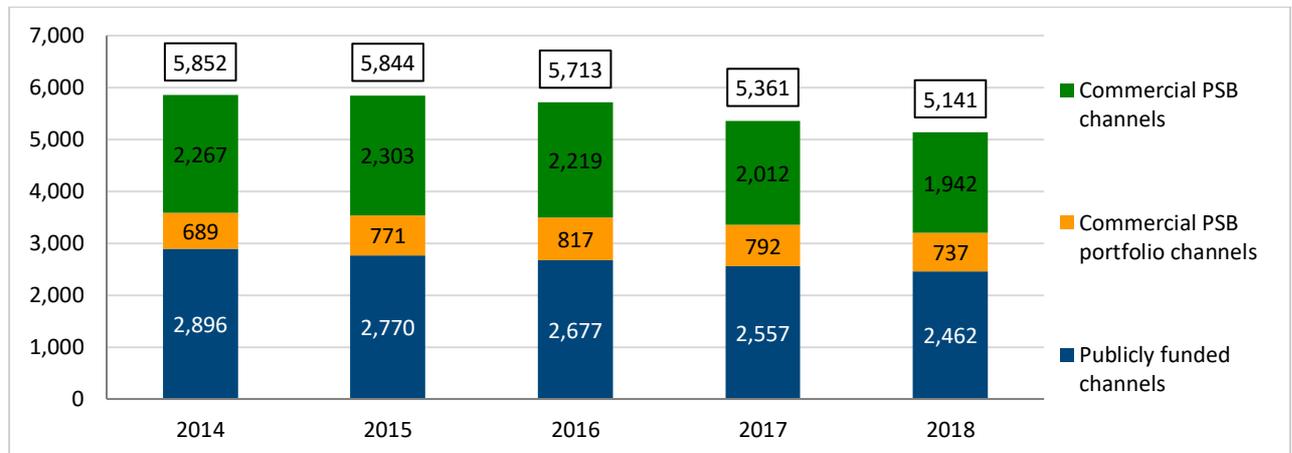
3.25 Offsetting these downward trends has been the growth in new revenue streams, notably SVOD and AVOD, including YouTube and the Broadcaster VOD ('BVOD') services from ITV, Channel 4, Channel 5, Sky and others. The commercial PSB broadcasters have sought to develop these alternative revenue streams by launching their own VOD portals (ITV Hub, All4, My5) or subscription services (e.g., BritBox); however, this has not to date been enough to offset pressures in core revenue categories.

Figure 11: Online video revenue, by source, £m, 2018 prices (2014-2018) (Ofcom PSB Review; Mediatique)<sup>35</sup>



3.26 The overall trendline for PSB funding is thus starkly negative – Ofcom itself confirms the significant pressures on those revenues directly related to the funding of PSB, as we summarise below.

Figure 12: PSB revenue, by source, £m, 2018 prices (2014-2018) (Ofcom PSB Review)



Challenges to PSB genres<sup>36</sup>

3.27 Revenue pressures on the PSBs have had a direct and material effect on their expenditure on original UK content. In the ten years since 2008, PSB network spend on first-run UK originations<sup>37</sup> has declined at a CAGR of -2% and the PSBs spent £500m less in real terms in 2018 than they spent, collectively, in 2008.

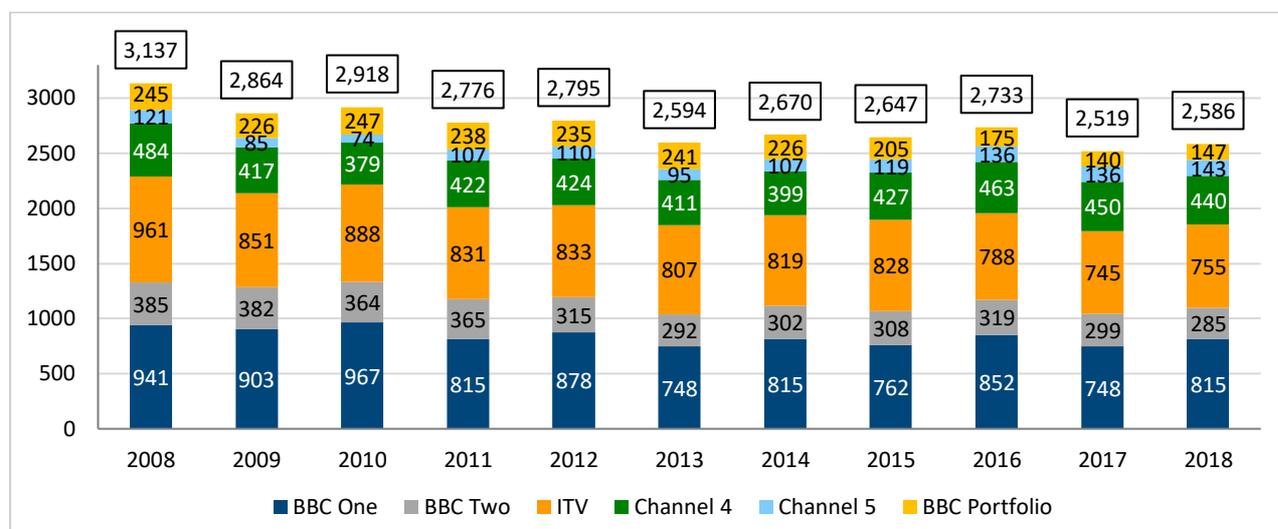
<sup>34</sup> UKTV had been a 50/50 joint venture between the BBC’s commercial arm and Flextech, then Virgin Media, then Scripps. Following the purchase of Scripps by Discovery, BBC Studios and Discovery agreed a deal by which the BBC took 100% of certain channels in the portfolio (Drama, Dave, W, Alibi, Gold, Yesterday and Eden).

<sup>35</sup> Ofcom has published revenue figures for online video advertising in Media Nations 2020: non-BVOD AVOD revenues for the year stood at £641m, whilst BVOD revenues were £452m. However, in the absence of complete revenue data for the next figure, we have elected not to include 2019 here so that the two charts are directly comparable.

<sup>36</sup> Mediatique defines these as genres that might typically be deemed PSB and not normally profitable for commercial providers: children’s, arts, formal education, regional news and ethics genres.

<sup>37</sup> While there are no first-run UK origination requirements in the commercial PSB licences, we use this metric as a proxy for tracking PSB outcomes.

Figure 13: PSB network spend on first-run UK originations, £m, 2018 prices (2008-2018) (Ofcom PSB Review)



3.28 Multichannel groups such as Sky and Discovery, as well as new entrants Netflix and Amazon, have increased their commitment to UK origination in recent years. However, multichannel expenditure, as Ofcom points out, is heavily weighted toward sport (in the four years post-2014, spend in the category increased by about £1.2bn to reach £3.2bn<sup>38</sup> in 2018); investment in drama and comedy has increased, *albeit* from a very low base. Similarly, SVOD streamers tend to invest in a limited number of genres, notably drama and comedy. Moreover, content created by pay TV channel groups or global SVOD players is routinely distributed (at least initially) behind a pay wall and is not available (as is PSB content) free at the point of delivery.

Figure 14: Multichannel spend on first-run content, by genre (all), £m, 2018 prices (2014-2018) (Ofcom PSB Review)<sup>39</sup>

Category	2014	2015	2016	2017	2018	CAGR
Arts & Classical Music	9.01	13.58	10.90	9.15	11.01	5%
Children’s	14.36	16.06	11.14	9.44	4.10	-27%
Comedy	0.92	6.69	3.91	11.85	11.37	87%
Current Affairs <sup>40</sup>	0.00	0.00	0.24	0.29	0.37	24%
Drama	38.62	96.03	88.60	118.29	126.11	34%
Entertainment	98.46	117.15	113.55	122.04	151.11	11%
Factual	50.60	61.68	48.78	60.41	78.86	12%
News	70.11	71.45	78.51	67.39	70.41	0%
Other <sup>41</sup>	0	0.07	0.02	0.03	0.06	101%
Sport	2,069.06	2,325.10	2,836.34	3,150.34	3,225.76	12%

3.29 In this context, dramatically reduced PSB revenue, and consequently lower spend on first-run UK originated content, has had a particular impact on genres that might typically be deemed PSB and not normally profitable for commercial providers: children’s, arts, formal education, regional news and ethics genres. Expenditure in most of these genres has declined since 2008.

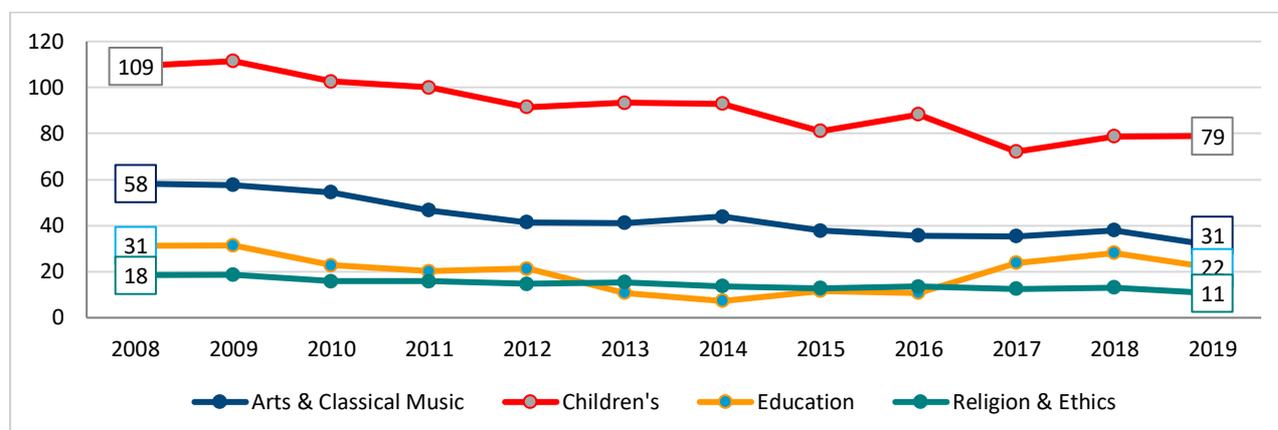
<sup>38</sup> [Small Screen: Big Debate](#): ‘Multichannel spend on first-run content’, (2014-2018).

<sup>39</sup> Pact does not publish the SVODs’ spend by genre. UK commissioning income from international SVODs (including Netflix and Amazon Prime) increased by 87% in the year from 2017 to 2018, reaching £280m; a significant portion of this was likely allocated to a limited range of genres most popular on these services: drama, comedy and factual.

<sup>40</sup> CAGR refers to period 2016-2018 from when investment was first recorded.

<sup>41</sup> CAGR refers to period 2015-2018 from when investment was first recorded.

Figure 15: PSB network spend on first-run content, by genre, £m, 2018 prices (2008-2019) (Ofcom MN)<sup>42</sup>



3.30 Meanwhile, in critical PSB genres such as children’s, news and arts, multichannel spend has been modest, according to Ofcom’s own figures, and expenditure in these three categories has actually declined in real terms in the five years from 2014, as the data in Figure 15 shows.

3.31 A secondary effect of the global streamers’ entry to the UK market has been a significant impact on PSB content expenditure (i.e., inflationary pressures on talent costs, both in front of and behind the camera). As evidenced below, there have been particularly marked rises in feature films, comedy and sport.<sup>43</sup> The ‘flat’ trend in drama is misleading, as only the PSB expenditure is tracked and not trends in production costs. A number of factors (high-end drama tax credits, deficit funding by large suppliers and an increase in co-productions, notably involving global SVOD players and US channel groups such as HBO) mask the significant inflation on costs per hour reported by market participants.<sup>44</sup>

Figure 16: PSB TV expenditure per hour, by genre (first-run origination), £, (2016 vs. 2019) (Ofcom MN; Mediatique)

Category	2016	2019	CAGR
Arts & Classical Music	126,323	127,324	0.3%
Children’s	131,098	123,399	-2.0%
Comedy	518,670	548,904	1.9%
Drama	765,678	761,838	-0.2%
Education <sup>45</sup>	289,811	350,823	6.6%
Entertainment	186,298	183,953	-0.4%
Factual	95,282	95,252	0.0%
Feature Films	875,208	1,178,889	10.4%
News & Current Affairs	17,872	18,453	1.1%

<sup>42</sup> In [Ofcom’s Media Nations Report](#) published in 2020, it did not restate PSB network spend on first-run content by genre for the trailing period; we include 2019 data here as indicative of the continued decline in funding for market failure genres typically associated with PSB.

<sup>43</sup> These three categories are among those most likely to be affected by global streamers’ entrance to the UK market: 75% of Netflix’s content offering in 2019 (according to data reported by Ofcom) was in just two genres – drama and comedy. The equivalent figure for Amazon Prime Video was 68%; secondarily it is also assuming a more competitive role in bidding for rights to broadcast live UK sport: from 2019, it will show 20 English Premier League football matches as part of a three-year agreement.

<sup>44</sup> Participants also report higher prices for secondary content, directly associated with the entry into the TV market of new players such as Netflix and their recent efforts to provide both global and ‘local’ content in markets such as Germany, France and the UK.

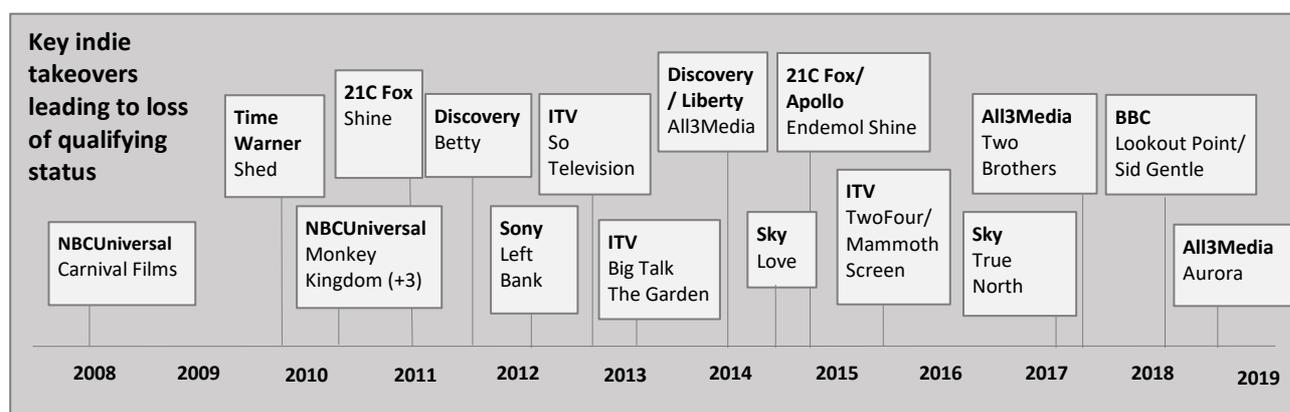
<sup>45</sup> Although expenditure per hour of ‘Education’ content grew significantly over the period, this cannot be attributed to market entry by global streamers. Spend in the genre doubled over the period but this was from a small base and across very few hours, resulting in a high but misleading CAGR.

Category	2016	2019	CAGR
Religion & Ethics	112,808	105,535	-2.2%
Soaps	352,503	362,746	1.0%
Sports	176,716	200,113	4.2%

Corporate restructuring in response to market dynamics

3.32 Increased market entry and content cost inflation have fuelled market consolidation, driven by both legacy global media and communications companies (e.g., NBC-Universal & Comcast; Time Warner & AT&T) and also domestic players. On the latter front, this is perhaps most evident in the production sector, where merger and acquisition activity has been driven by US acquirors and by domestic players such as ITV.

Figure 17: Timeline of indie M&A activity, (2008-2019) (Mediatique)

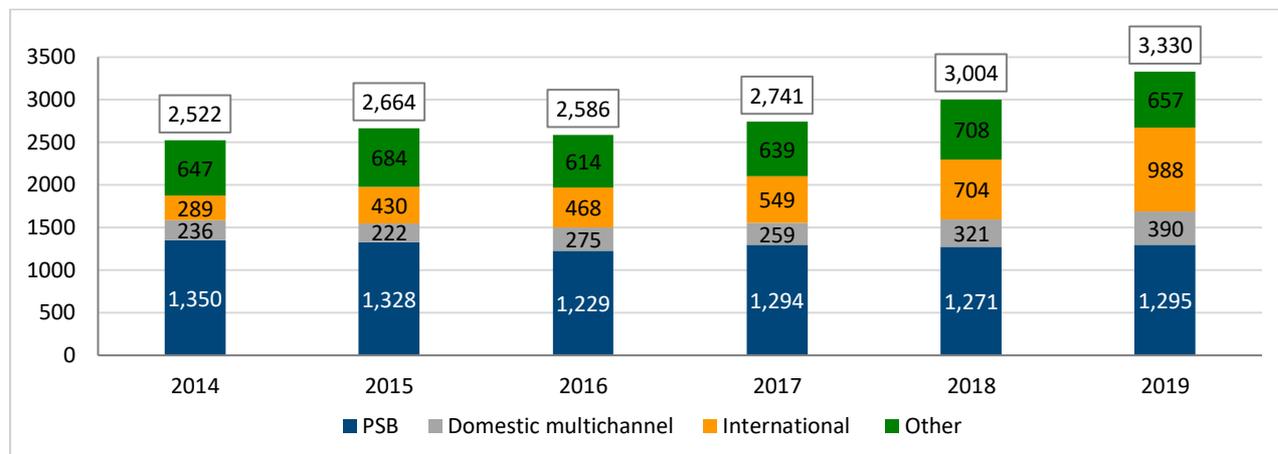


3.33 A net effect of sector consolidation has been an altering of the composition of external supplier revenue; whilst income generated for the UK independent sector is higher overall than in 2014 (reaching just over £3.3bn in 2019), revenue has increasingly been generated internationally, with reliance on the PSBs reduced.<sup>46</sup> Assuming that PSB content expenditure continues to decline in line with associated revenue pressures, it is likely that PSBs will lose bargaining position vis-à-vis large, global suppliers.<sup>47</sup>

<sup>46</sup> Covid-19 will undoubtedly have an impact on production revenue in 2020. Also significant will be the impact of the pandemic on broadcast/publishing schedules, both in the short and medium term.

<sup>47</sup> The relationship between qualifying independents and broadcasters is subject to specific regulations governing terms of trade and commitment to production by broadcast hours.

Figure 18: Total UK independent production revenue, £m (2014-2019) (Pact)



Audio market trends

- 3.34 The audio market in the UK has also been characterised by an erosion of linear broadcast radio by a range of new services enabled by connectivity (particularly via mobile). Initially, music was the key arena of disruption, with the growth of first music downloads and then music streaming; more recently, other formats, including speech, have increased in popularity, with the growing maturity of the podcasting market.
- 3.35 Radio remains a cornerstone of audio listening, both in the home and in the car; it continues to reach all key demographics; and it is particularly strong among older listeners. However, younger age groups evince declining reach and significantly lower average listening as they turn to streaming (and more recently podcasts), as well as online clips.

Figure 19: Radio reach, all radio (2014-2019) (Ofcom PSB Review)

Category	2014	2015	2016	2017	2018	2019	CAGR
15-24	87.6%	83.4%	83.8%	83.2%	83.0%	80.1%	-1.8%
25-34	87.5%	85.9%	85.1%	85.1%	87.1%	84.8%	-0.6%
35-44	92.9%	91.0%	91.6%	90.0%	92.5%	91.2%	-0.4%
45-54	94.0%	93.7%	94.1%	94.2%	93.7%	95.3%	0.3%
55-64	93.5%	92.4%	93.0%	93.4%	94.8%	93.9%	0.1%
65+	87.7%	89.6%	88.3%	89.5%	90.2%	90.1%	0.5%
Adults 15+	90.3%	89.3%	89.3%	89.3%	90.2%	89.4%	-0.2%

Figure 20: Average radio hours per listener, all radio (2014-2019) (Ofcom PSB Review)

Category	2014	2015	2016	2017	2018	2019	CAGR
15-24	15.55	14.99	13.98	13.79	12.73	12.78	-4%
25-34	17.91	17.77	17.25	17.07	16.92	16.50	0%
35-44	21.24	20.35	19.89	19.78	20.02	19.83	-1%
45-54	23.36	23.19	23.15	23.46	22.80	23.00	0%
55-64	23.95	25.01	23.95	25.21	24.54	24.70	1%
65+	25.85	24.76	25.65	25.32	25.12	25.07	-1%
Adults 15+	21.54	21.29	21.05	21.22	20.84	20.90	-1%

- 3.36 As in the case of TV, new patterns of audio consumption are the result of increased broadband and device take-up, which enable changes in consumer behaviour. Emblematic of the trends is the increase in take-up

and use of smart speakers, which are used not just to access broadcast radio but a range of (competing) services such as podcasts, music streaming and catch-up audio.

- 3.37 At the same time, there have been changes to business models that have had implications for consumer behaviour. For example, streaming services such as Spotify are aiming to attract older audiences (e.g., by offering speech formats) even as traditional providers (the BBC and commercial radio) adopt non-linear models of content and distribution (e.g., the BBC's launch and aggressive promotion of BBC Sounds in part to enable non-linear consumption for audiences less likely to listen to broadcast radio).
- 3.38 Depending on these trends, the degree to which broadcast over audio (whether AM/FM or via Digital Audio Broadcasting) is wholly displaced by the internet (fixed and mobile) is likely to affect commercial revenues for UK radio companies over the medium term. Analogue and digital radio favours incumbent broadcasters, whereas IP enablement places these broadcasters in a much more crowded and fragmented environment. IP environments also confer greater advantage in particular to those with a gatekeeper role in mobile and smart assistants (e.g., Amazon, Google and Apple).
- 3.39 These impacts are particularly observable in households. By contrast, usage in cars remains relatively robust for radio generally (analogue or digital), owing to lower levels of connectivity in cars, the popularity of breakfast and drivetime radio shows (including news and traffic bulletins), the difficulty of operating connected devices while driving and mobile network black spots.
- 3.40 We look at the likely future trends in the next section, where we lay out our base case for the period to 2024.

#### 4. Forecasts of market developments to 2024

- 4.1 In our analysis thus far, we have focussed on the pressures that have been building around the PSB model – on viewing, revenues, and original content expenditure. These pressures are acute and show no signs of abating.
- 4.2 The impacts are felt downstream (on viewing and revenue outcomes) and upstream (competition for talent and formats). The PSBs are also struggling to secure prominence via emerging connected gateways controlled by large, well-funded players (which themselves may be competing for content and audiences).
- 4.3 In this section, we provide our forecast for the A/V market over the next five years.
- 4.4 We have established our counter-factual ('CF') forecast to 2024 to consider how the PSBs will fare over time in the absence of meaningful changes to the PSB compact, and against which to evaluate the future funding options that we lay out in section 5.<sup>48</sup>
- 4.5 We construct the CF by examining first the anticipated shifts in consumer behaviour (around broadband connectivity, device take-up, adoption of services and viewing/usage) and how this will affect revenues. The objective is to track the impact on UK content origination (as a principal proxy for PSB outcomes).<sup>49</sup> Although not central to our analysis, we also provide, below the sections detailing our core A/V analysis, a forecast for the audio markets as well. Finally, we summarise our key conclusions on future developments.
- 4.6 A key assumption in our CF model is that younger demographics will maintain/sustain digital behaviours as they age (take-up, viewing/usage, willingness to pay), but the pace of future behavioural change will moderate to reflect the near universality of digital behaviours among younger users today; and that older demographics will adopt more digital behaviours in the aggregate over time, at a rate faster than pure extrapolation would suggest, reflecting late adoption among these older demographics.<sup>50</sup>

##### Connectivity, devices, platforms and the consumption of video services

- 4.7 We assume that UK broadband penetration has reached near maturity in the UK, and absent any (unlikely) contributions from mobile broadband and/or 5G in the short term, the likely developments to internet connectivity between now and the end of the forecasted period will come in the form of improved network speeds which will in turn enable further use of a growing range of smart devices.
- 4.8 We expect that 64% of UK households will have a smart TV by 2024, up from 47% in 2019; smartphone penetration will grow to 82% from 79%, whilst streaming sticks/boxes (or 'dongles', devices that enable dumb TVs to become connected to the internet) will decline as internet connectivity in TV sets becomes native to hardware. The take-up of such devices reflects changes in demographics (a slightly ageing population, but further acceptance among older demographics of the advantages of connected TVs in particular).

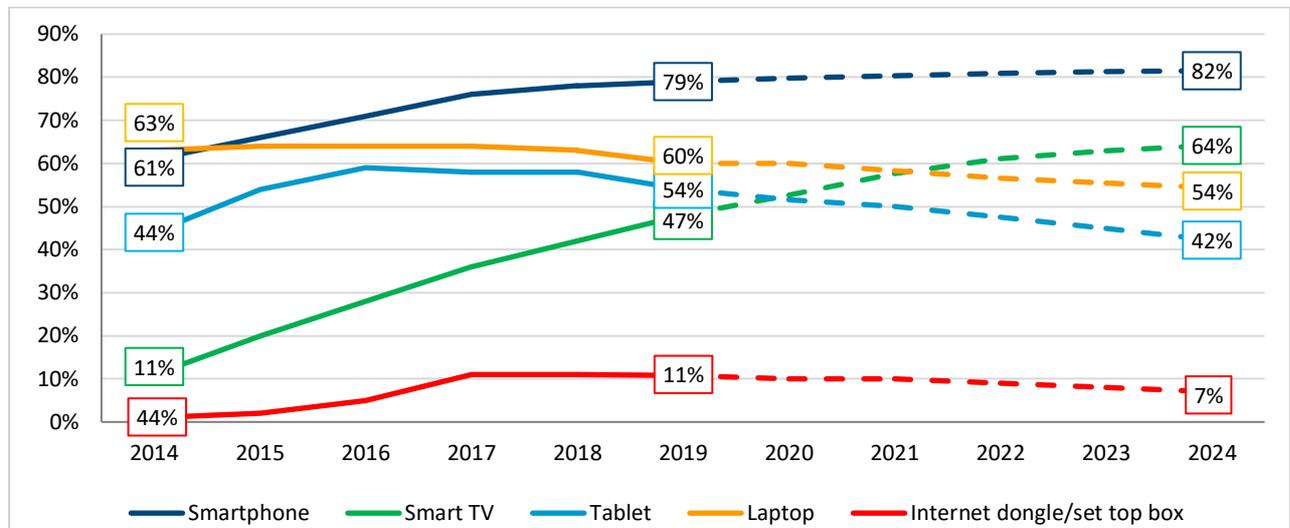
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<sup>48</sup> The forecast period coincides with remainder of the terms of the operating licences for ITV, STV and Channel 4. As mentioned elsewhere in this report, the multiplex licence held by ITV and Channel 4 in their role as commercial PSBs expire in 2022; we assume for the purposes of our work that these licences are rolled over at least to coincide with the operating licence terms, and very possibly beyond. A range of options for the treatment of multiplex licences are likely to be considered by Government and are beyond our current scope.

<sup>49</sup> In order to produce this counter-factual analysis, we have referred to data included in Ofcom's published five-year review of Public Service Broadcasting: [Small Screen: Big Debate](#). Some of the datasets which contribute to this review include an extra year (i.e., the data runs to 2019, rather than 2018); we have referenced this where appropriate.

<sup>50</sup> In all the forecasts that follow, we have incorporated the 'Covid-19 effect' in 2020 (around device take-up, SVOD adoption, pay TV, viewing, etc.). As we noted at the outset of our report, we observe that the pandemic and its aftermath are likely to have accelerated certain relevant behaviours but not changed the structural dynamics nor the direction of travel.

Figure 21: Smart device take up, various, % (2014 – 2024) (Ofcom PSB Review; CMR & Mediatique)<sup>51</sup>



N.b. dotted lines post-2019 represent Mediatique forecasted growth rates; Note that we track smart speakers and home assistants, which continue to grow in this period, but are expected to be largely confined to audio usage or integrated into the functioning of a smart TV.

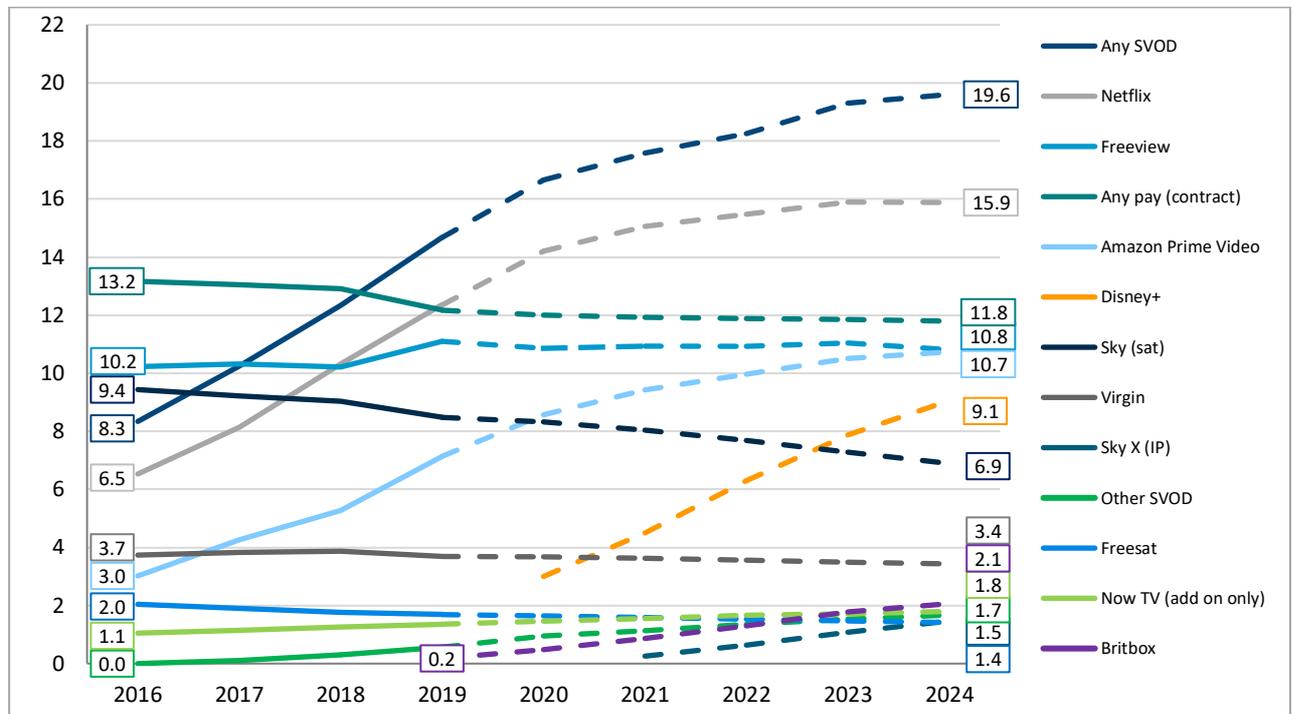
- 4.9 We have also considered the implications of evolving consumer preferences on TV platforms (pay, free) and SVOD take-up over the short-medium term. We expect traditional pay TV to decline as consumers increasingly switch to cheaper pay TV packages, free TV (e.g., Freeview) or no TV at all (e.g., VOD-only homes). The presence of Covid-19 and the subsequent cancellation of live sport broadcasts, often a significant determining factor for those who choose traditional pay TV, has accelerated this trend further.
- 4.10 Likewise for SVOD, Covid-19 has been an accelerant to a trend already observable: high rates of subscriber acquisition. However, although we expect further growth in this category in the period to 2024, we do not expect it to be exponential. When the UK’s lockdown period concludes, it is likely that all streamers will encounter higher churn rates than usual, and it is assumed by many, not least by Netflix itself<sup>52</sup>, that subscribers acquired during the UK’s lockdown period are, at least in part, subscribers that would have joined eventually rather than not at all. In effect, these subscribers have been brought forward from future periods.<sup>53</sup>
- 4.11 The spike in the spring of 2020 in SVOD subscriptions (and indeed in the use of broadcast VOD services such as iPlayer, ITV Hub and All4) is nonetheless striking. It may be too early to say whether or not the growth has longer-term impacts, over and above those already identified in our model. For example, has the lockdown habituated older TV viewers to consume significantly more content on a non-linear basis (via BVOD and SVOD) than we had been predicting, thus leading to an acceleration in digital adoption sufficient to require a change our five-year projections for SVOD households? Given that we had assumed growth in 2020 in line with a range of industry estimates on Covid-related consumption, and had set an ambitious target for SVOD ‘any subscribers’ of 20m households by 2024 (up from 14.7m just before lock down), we have maintained our projections at this stage.

<sup>51</sup> Ofcom data on smart devices is provided for a six-year period (2014-2019) and thus Mediatique forecasted growth rates begin subsequent to this period.

<sup>52</sup> “[We’ve had an increase in subscribers in March \[2020\] that’s essentially a pull-forward of the rest of the year.](#)” – Netflix chief executive Reed Hastings to investors commenting on first quarter performance.

<sup>53</sup> In its [Media Nations report published in 2020](#), Ofcom identified estimated that around 23% of online adults said they had added a SVOD subscription in their household during lock down, for a growth of c6m additional subscriptions in the period. We estimate that that Disney+, which launched in late March 2020 just as lockdown began, delivered around 3m of these, with the rest spread across Netflix, Amazon, Now TV and others. Ofcom’s survey suggested that around 95% of Disney subscribers were already taking an SVOD service. Our forecasts are consistent with the results of Ofcom’s survey for mid 2020.

Figure 22: Platform take-up over time, m (2016 – 2024) (Ofcom, BARB, Mediatique)<sup>54,55,56</sup>



N.b. dotted lines post-2019 represent Mediatique forecasted growth rates; 'Freeview' includes Freeview; Freeview Play and YouView households.

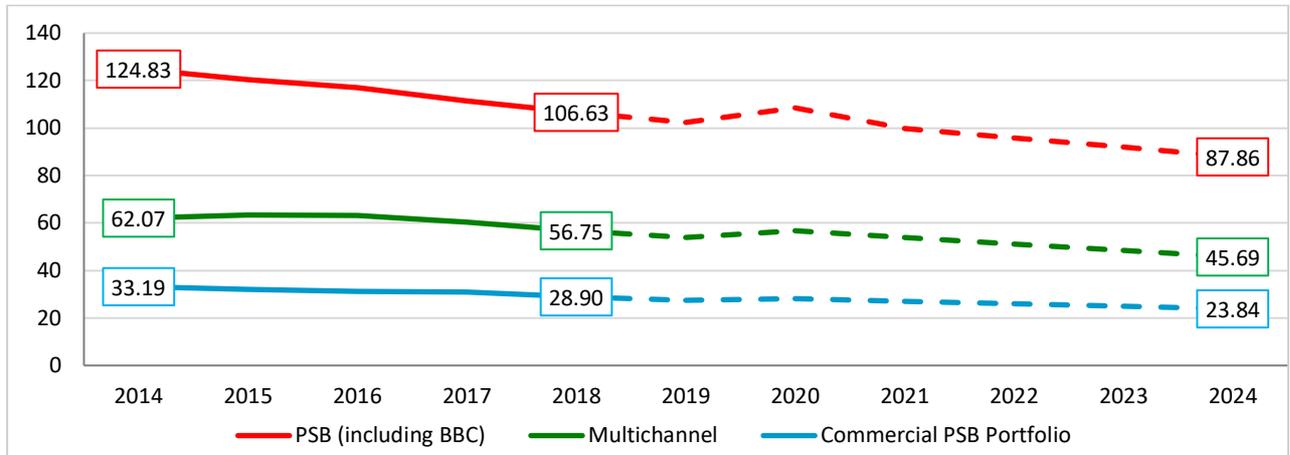
4.12 PSB outcomes are not directly discernible from changes in smart device take up, pay TV subscription trends and SVOD adoption rates; these are more evident in daily minutes of TV viewing. Using the connectivity and take-up forecasts above, we infer the daily minutes of TV viewing for all individuals by channel group: PSB, multichannel and commercial PSB portfolio (diginets). Despite an uplift in 2020 accounting for Covid-19 related increases to TV content viewing (principally driven by daytime TV and news broadcasts), the consequence of connected device penetration is an increasingly competitive viewing environment, enabling a range of viewing on TV sets and devices, including SVOD, AVOD, short form (alongside increases in time spent with games consoles).

<sup>54</sup> Freeview forecast includes smart TV households with DTT tuners; households taking BT TV and TalkTalk via YouView (equipped with a DTT tuner); and Freeview Play households. There is a chance that an IP-only variant of Freeview will be launched over the model period, although nothing has been confirmed at this stage – if an IP-only proposition does emerge, it will likely appear on connected hardware ('sticks') and apps first, given it normally takes considerable time for such innovations to be incorporated into TV set operating systems. Such interim devices would be included in 'Internet dongle/set top box' category in Figure 21. We have accounted for a small shift from DTT to IP (in BT and TalkTalk homes) for 'broadcast' of 'free to view' channels. This is captured in the trendline; a significant number of IP-only households is unlikely in the short to medium term (i.e., during the current licence term for DTT).

<sup>55</sup> 'Other SVOD' includes subscribers from both Apple TV+ and ITV+.

<sup>56</sup> Growth attributed to Sky X (Sky's 'big bundle' service distributed exclusively over IP) will take substitutive share from existing pay propositions when launched in 2021. We assume its introduction will reinforce distinct market dynamics between 'largely free' and 'largely pay' - it is likely that the majority of Sky X growth will represent household migration from other 'big bundle' propositions (e.g., 'legacy' Sky & cable households) that are already high-ARPU and where consumers are not averse to long contract lengths. Similarly, we do not expect significant migration in the forecast period from 'free' TV heartland (e.g., Freeview Play and connected TVs still relying on a DTT tuner).

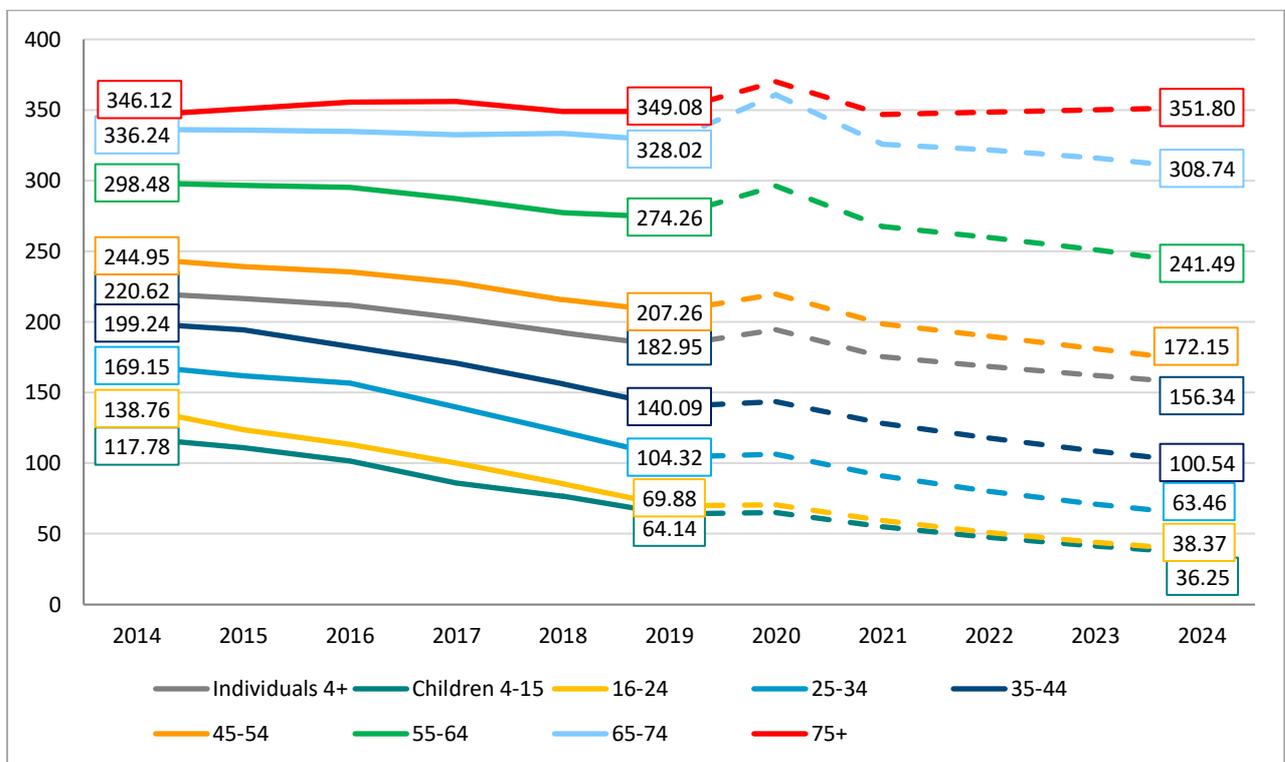
Figure 23: Average daily minutes of TV, by channel group (2014 – 2024) (Ofcom PSB Review; Mediatique)



N.b. dotted lines post-2018 represent Mediatique forecasted growth rates.

4.13 These outcomes exhibit greater significance when presented by demographic: we expect every demographic under the age of 75 to reduce its broadcast viewing, whilst the remaining group will view slightly more. The eventual decline in viewing is particularly stark for the youngest generations (e.g., the under-25s).<sup>57</sup>

Figure 24: Average daily minutes of TV viewing, by demographic (2014 – 2024) (Ofcom MN & Mediatique)<sup>58</sup>



N.b. dotted lines post-2019 represent Mediatique forecasted growth rates.

4.14 We turn now to trends in relation specifically to non-broadcast content consumption. Clearly, these have direct implications for PSBs in the short to medium term, as the PSBs, through their BVOD propositions, are seeking to offset weakness in traditional NAR by generating potentially high-premium digital advertising revenue to compensate. In this market segment, they risk not only accelerating the pace of disintermediation

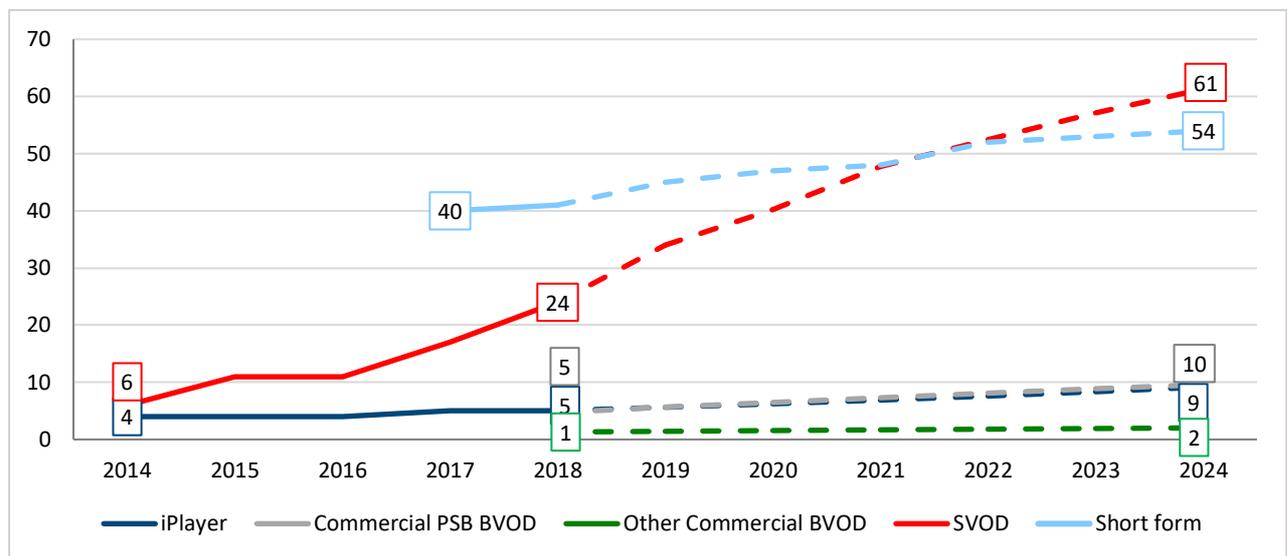
<sup>57</sup> It is important to state that these demographics are far from monolithic; among these age groups are heavy and light users of the TV set, and some who do not view broadcast TV at all. Other factors, including class and geography may also play a role. These projections, therefore, are indicative, and should not be taken to reflect behaviours of all individuals in a cohort.

<sup>58</sup> Ofcom uses BARB data as its source to inform historic daily minutes of TV viewing per person, this measurement is the current industry standard and includes both live viewing and time-shifted viewing up to 7 days.

of broadcast, but also must compete directly with other online players (for share of leisure time and in many instances for revenues), including those (notably YouTube) with no legacy advertising revenues to protect.

4.15 Below we have forecast average minutes of viewing<sup>59</sup>, adjusted for enablement and behavioural patterns, via different propositions (iPlayer, commercial BVOD<sup>60</sup>, SVOD<sup>61</sup> and short form). We note that iPlayer remains very competitive against the aggregation of ITV Hub, All4, my5, UKTV Player, Sky On Demand, Pluto TV, etc., despite the amount of competing content available on these commercial services and the prospect of new ad-funded services launching in the UK (e.g. Discovery, Disney). This will be further underpinned by the upgrades to the iPlayer made possible by the extension of its rights windows in many instances – to 12 months from 30 days – and a significantly richer offering of content on demand without having to wait for a terrestrial showing.

Figure 25: Viewing minutes by platform, per individual, per day (2014 – 2024) (Mediatique)



N.b. dotted lines post-2018 represent Mediatique forecasted growth rates.

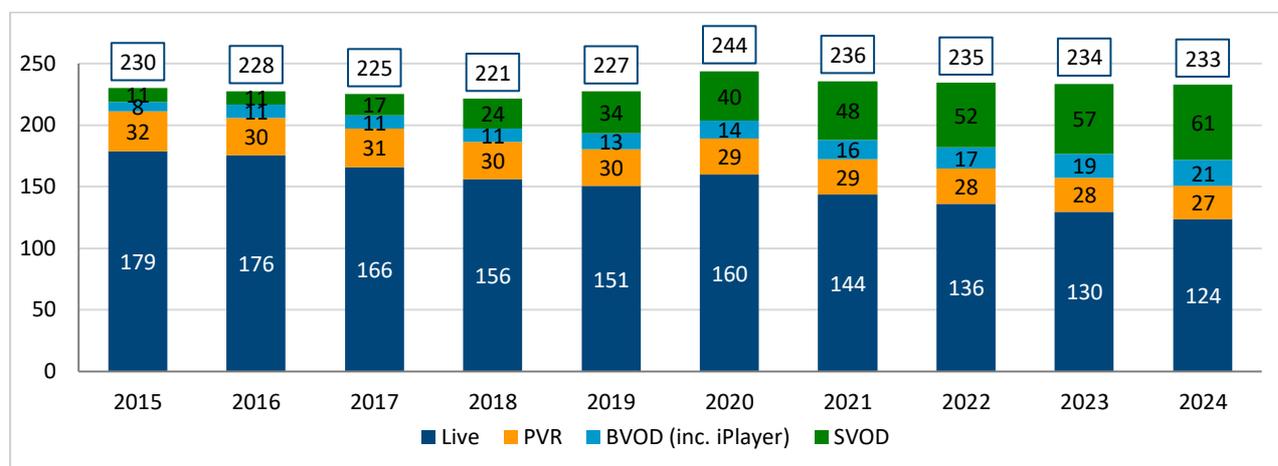
- 4.16 In addition to the iPlayer upgrade, these forecasts also reflect the prospect of other new entrants joining the AVOD long form market (e.g., Discovery). Certainly the viewing to PSB players in lockdown suggested potentially growing demand for ‘free’ (and/or ad-funded) propositions alongside SVOD.
- 4.17 Collating all these strands of analysis, we are able to forecast total long-form viewing minutes by type. As evidenced below, live viewing will continue to be eroded by increased viewing of VOD; PVR viewing will likewise decline, although only modestly (sustained by the centrality of PVRs in pay TV offerings over the medium term).

<sup>59</sup> In practice, as reported by Ofcom’s Media Nations survey conducted in mid-2020, there has been a discernible rise in viewing to BVOD and non-BVOD AVOD propositions over the Covid-19 induced lockdown period (alongside a comparable peak registered by the SVOD cohort). However, it is unlikely that these new peaks will define a revised trajectory.

<sup>60</sup> An average of ITV Hub, All4, my5, Sky On Demand and other broadcaster players. According to our model assumptions, 81% of commercial BVOD viewing is currently ascribed to the commercially funded PSB players.

<sup>61</sup> A blended figure across e.g., Netflix, Amazon, Disney+, BritBox, etc.

Figure 26: Total long-form viewing by type, in minutes (2015 – 2024) (Mediatique)



Revenue outcomes as a result of viewing/usage trends

4.18 The objective of making these projections is to be able to forecast the revenues generated across the A/V value chain and thus establish the level of revenues likely to be available to underwrite expenditure on PSB content over the medium term. Our sector-wide revenue forecasts for the CF are summarised in the Figure below.

Figure 27: CAGR Revenue growth (2014 – 2024) (Ofcom PSB Review; Mediatique)

Category	2014 (£m)	CAGR 2014 – 2018	2018 (£m)	CAGR 2018 – 2024	2024 (£m)
Pay TV <sup>62</sup>	6,294	0.3%	6,365	-3.1%	5,261
Licence Fee (TV allocation)	2,896	-4.0%	2,462	0.2%	2,487
NAR (nominal terms from 2018) <sup>63</sup>	4,100	-1.2%	3,900	-0.5%	3,778
NAR (real terms from 2018) <sup>64</sup>	4,100	-1.2%	3,900	-2.1%	3,427
SVOD	352	32.3%	1,075	20.2%	3,246
BVOD <sup>65</sup>	145	28.1%	391	12%	772
Non-BVOD AVOD <sup>66</sup>	354	14.5%	609	9.2%	1,034
<b>Total (incl. nominal NAR 2024)</b>	<b>14,141</b>	<b>1.1%</b>	<b>14,802</b>	<b>1.7%</b>	<b>16,578</b>

<sup>62</sup> We refer to pay TV subscription fees as the income accruing to Sky UK, Virgin Media, BT TV and TalkTalk TV as per the methodology adopted by Ofcom. The figure excludes linear NAR attributable to multichannels; production revenues attributable to pay TV operators; revenue derived from DVD sales; satellite/box or other installation fees; broadband and telephony charges; and revenues from PPV and EST (DTO & DTR). Our forecasts assume declines in ‘full fat’ pay TV subscriptions in favour of smaller bundles (at lower revenues per household) and outright cancellations.

<sup>63</sup> Our forecasts for NAR refer exclusively to linear NAR and reflect the slump endured in 2020 and subsequent years of partial recovery in 2021 and 2022; they are informed by regular conversations with industry bodies and stakeholders and predicated on the assumption that the combination of Covid-induced impacts on behaviour, digital adoption, and structural weaknesses already observed will preclude NAR from again reaching its pre-Covid-19 levels at any point within our five-year forecast period. We assume that key broadcasters continue to charge of premium to deliver even a declining number of TV viewers, in the absence of substitutes. Over the longer term, digital providers may convince advertisers to shift more expenditure to online propositions in line with consumer behaviour.

<sup>64</sup> In order to reach a real-terms NAR forecast for 2024 (i.e., calculating the value of 2024 NAR in 2018 terms by accounting for forecasted inflation in the period), we have used forecasted [GDP deflators as published by Gov.uk](#) and applied these to our nominal forecasts.

<sup>65</sup> All revenues generated by PSB VOD propositions *and* the revenues generated by channel group VOD propositions (e.g., Sky Go and on demand).

<sup>66</sup> The dominant player in this category is YouTube, although it also encompasses Twitch, Daily Motion etc.

- There are multiple factors causing the decline of pay TV revenue including subscriber migration to cheaper pay TV packages and free TV services. The rate of decline has been exacerbated by Covid-19: we estimate that pay TV providers' subscriber revenue loss (after offering to 'pause' subscriptions in the absence of live sport broadcasts during the period) will have led to a c£230m net loss in 2020 (after accounting for savings in production and rights costs), even before existing structural weaknesses in the category are considered.
- The expectation for both the licence fee and NAR is for flat revenues at best in the forecast period. Covid-19 has had a huge impact on advertising in the second quarter of 2020, although declines moderated in the third quarter. Despite a relatively fast predicted recovery in advertising in 2021/2022, the extent of the drop in 2020 is such that we do not expect NAR to recover to the levels we have seen historically at any time in our forecast period.<sup>67</sup>
- The licence fee too will be significantly weakened: from August 2020, the BBC will fund a free licence for over 75s in receipt of Pension Credit. The BBC is facing both licence fee pressures (fewer households paying the licence fee) and commercial under-performance (declines in revenues at BBC Studios in line with the production hiatus following the Covid-19 pandemic and lower receipts in key market segments such as pay TV channel affiliate fees and advertising). This is likely to severely limit contributions from BBC Commercial Holdings to the BBC in the financial year 2020/21.<sup>68</sup>
- We expect SVOD revenues to grow considerably, although the curve will necessarily flatten as the market reaches maturity.<sup>69</sup> In our projections, we have factored in an increase in SVOD stacking<sup>70</sup>, price increases (at the risk of losing subscribers), as well as changes to the ratios of free trials and password sharing. The ARPU versus churn issue is especially relevant for Netflix which may seek to raise prices significantly to act as counterweight to a high cash burn (spent on commissioning original content) and the ambitious valuation expectations of investors. Both BVOD and other AVOD (overwhelmingly YouTube currently) will enjoy the net benefit of increased VOD viewing.

4.19 These revenue projections<sup>71</sup> have direct implications for our view of expenditure on original first-run UK content across key market segments (PSB, commercial PSB, multichannel and SVOD) as the proportion of revenue invested in original content varies by market segment. Our analysis suggests that increased revenue weakness for PSBs will restrict their ability to fund original UK content in a variety of genres, and these genres would almost certainly not be served in the same way by SVODs or multichannels absent regulation dictating so.<sup>72</sup>

<sup>67</sup> Despite projecting a relatively quick recovery in the years 2021/2022, we assume that NAR will resume from a base that is significantly smaller than previous years; moreover, the structural weaknesses in the market will return to the fore after two years of relative recovery. ITV and Channel 4 are reporting advertising declines, year on year, of around 10-12% annualised for 2020, including BVOD and NAR.

<sup>68</sup> The commercial contribution to the BBC in 2019/20 (in the form of investment in programming and dividends) was a record £276m. Of this, around £65m was in the form of a cash dividend from BBC Studios, unlikely to be repeated in 2020/21.

<sup>69</sup> Our forecasts are broadly consistent with those of other analysts: most recently [PwC published a global forecast for SVOD revenues](#) implying a doubling from 2019 to 2024, reaching \$86bn, but predicted subscriber 'fatigue' and consolidation in the number of propositions. Given the relative maturity of the US market, this forecast implies even faster growth outside the US.

<sup>70</sup> We forecast a rise in the number of SVOD subscriptions taken by each SVOD household from 1.5 at the end of 2019 to 2.13 by the end of 2024. Ofcom estimated that the 'stacking' ratio had reached around 1.7 in mid-2020, during the lockdown. Our forecast for 2020 full year is 1.68.

<sup>71</sup> Pay TV revenues in this context refers exclusively to: subscriptions, advertising (including BVOD) and production. We have excluded other income, such as betting, gaming and installations. Likewise, for commercial PSB, we include NAR and BVOD advertising (excluding product placement, teleshopping) and production income (adjusted for 'internal' supply – e.g., content commissioned by ITV from ITV Studios).

<sup>72</sup> For example, through digital content funding levies or taxes.

- 4.20 To calculate the outputs, we reviewed the ratio of first-run expenditure to revenues characterising key market segments over a five-year period (2014-2018): PSB, commercial PSB, multichannel, and SVOD. Assuming no change to the most recent ratio of revenue and expenditure, we applied this ratio to the revenue forecasts of each segment.
- 4.21 There is, of course, no assurance that the lower propensity of multichannels and SVOD players such as Netflix and Amazon to spend on UK origination when compared to PSBs will remain stable or that ITV, for example, may not elect to spend less on content than it has traditionally done at a time when its revenues were more robust. There are reasons to suppose, however, that these ratios will hold over time. First, they are in line with historical behaviours. Second, there is clear evidence of genre preferences among multichannel and SVOD providers that do not extend to 'market failure' content.

**Figure 28: Forecast revenues & expenditure on first-run UK-originated content, £m, nominal (2019-2024) (Mediatique)**

<b>BBC – Ratio of revenue/spend: 51%</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>
Forecast BBC licence fee revenue <sup>73</sup>	2,543	2,588	2,500	2,494	2,490	2,488
Forecast BBC spend on first-run UK content	1,289	1,312	1,267	1,264	1,262	1,261
<b>Commercial PSB – Ratio of revenue/spend: 31%</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>
Forecast relevant commercial PSB revenue <sup>74</sup>	4,305	3,991	4,402	4,717	4,854	5,006
NAR attributable to commercial PSB & portfolio	2,549	2,138	2,390	2,518	2,457	2,397
Forecast spend on first-run UK content	1,341	1,243	1,371	1,469	1,512	1,559
<b>Pay TV – Ratio of revenue/spend: 6%</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>
Forecast relevant pay TV revenue	7,928	7,500	7,313	7,130	6,952	6,778
Forecast spend on first-run UK content	441	418	408	398	388	378
<b>SVOD – Ratio of revenue/spend: 26%</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>
Forecast SVOD revenues	1,373	1,800	2,226	2,583	2,933	3,246
Forecast spend on first-run UK content	357	468	579	672	763	844
<b>Forecast total first-run UK content spend</b>	<b>3,428</b>	<b>3,438</b>	<b>3,625</b>	<b>3,803</b>	<b>3,925</b>	<b>4,042</b>

4.22 On this basis, by using a combined figure for forecast PSB expenditure on first-run UK content, freezing the genre allocation and then assuming the same percentage ratios of first-run expenditure from the last relevant year, we can project in real terms<sup>75</sup> what the implications of declining expenditure are on market failure genres within PSB content categories.

**Figure 29: Forecast PSB expenditure, by genre (real terms) (2018 – 2024) (Mediatique)**

<b>Category</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>
Arts & Classical Music	38	39	38	37	34	32	29
Children’s	79	80	79	76	71	66	60
Comedy	98	100	98	94	89	82	75
Current Affairs	86	87	86	82	78	72	65
Drama	261	265	260	250	236	219	198
Education	28	29	28	27	26	24	21
Entertainment	414	421	413	398	376	347	315
Factual entertainment	187	190	187	180	170	157	143
Feature films	30	30	30	29	27	25	23

<sup>73</sup> Ofcom published ‘public funding’ revenues as part of its [Small Screen: Big Debate](#) workstream (i.e., the allocation of BBC Licence Fee attributed to TV). Our forecast is predicated on this allocation, with the overall quantum adjusted over time to take into account the latest settlement and the decision by the BBC that only those households where at least one occupant is receiving Pension Credit will be eligible for a free licence). BBC Studios also contributes significantly to content budgets in order to secure income from commercial markets after the relevant initial broadcast window.

<sup>74</sup> We have defined ‘relevant commercial PSB revenue’: NAR (attributable to both commercial PSBs and their respective portfolios); income attributable to commercial PSB non-advertising activities (i.e., revenue from content production and sales); external supply balancing factor (i.e., cost of internal supply to and from ITV plc) and commercial PSB share of BVOD revenue.

<sup>75</sup>As earlier in the report, in order to reach a real-terms PSB expenditure forecast for 2024 (i.e., calculating the value of 2024 PSB expenditure in 2018 terms by accounting for forecasted inflation in the period), we have used [GDP deflators as published by Gov.uk](#) and applied these to our nominal forecasts.

Category	2018	2019	2020	2021	2022	2023	2024
General factual	164	167	164	158	149	138	125
News	250	254	250	240	227	210	190
Religion & ethics	13	13	13	13	12	11	10
Soaps	262	266	262	252	238	220	200
Specialist factual	188	191	188	181	171	158	143
Sport	488	497	488	470	443	410	372
<b>Total:</b>	<b>2,586</b>	<b>2,630</b>	<b>2,583</b>	<b>2,486</b>	<b>2,346</b>	<b>2,171</b>	<b>1,970</b>

4.23 Despite this already stark illustration of declines in expenditure by PSBs on first-run original content, there are reasons to believe that the outcome would be in fact materially worse for certain genres.

- This is in effect a ‘best case’ scenario, particularly in the context of distressed PSB type genres: as revenues decline, and broadcasters seek to shave costs in line, they will continue to be incentivised to spend disproportionately on popular genres (drama; entertainment; factual entertainment) to maintain audiences, reducing to a bare regulatory minimum their expenditure on specialist genres, regions programming and local/regional news – in the aggregate and on a per hour basis. There will be no incentive to make more than the regulatorily imposed number of hours in ‘pure’ PSB genres (where quotas exist) or to spend more than the bare minimum per hour.

Consumption of music and audio services

4.24 The audio market is subject to the same primary drivers of change we have identified – take-up of connected devices, technology innovation, new market entry and changes to consumer behaviour. We expect an aggregate decline in the consumption of broadcast radio over the next five years, despite the growing importance of DAB (which favours traditional broadcast media) in the distribution mix. A key driver of this is the take-up of smart speakers<sup>76</sup>, where navigation (usually voice controlled) is dominated by global providers (Amazon and Apple).<sup>77</sup>

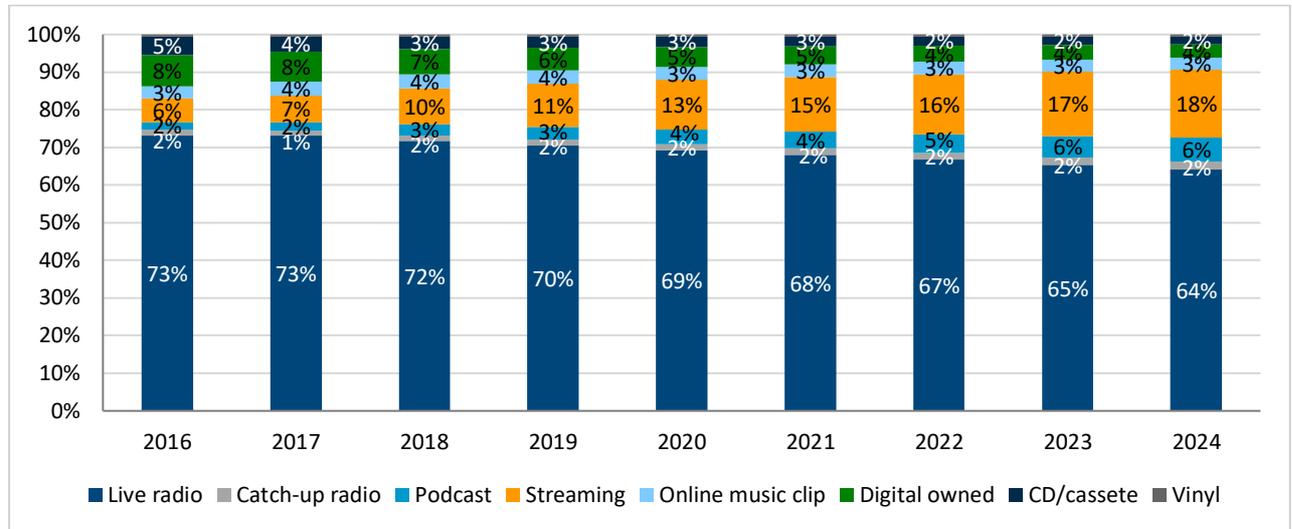
4.25 Players seek to enable households to use these devices inter-operably in a bid to colonise all activity (e-commerce, internet search, audio and A/V content access): in other words, in tandem with TVs, hardware, and their associated operating software, the aim is to become the single point of consumer interface, generally with single billing, personalisation and data capture mechanisms.

4.26 The nature of interaction with these devices (voice-assisted/voice enabled) encourages changes to habits in the way content is delivered, in turn affecting content consumption trends.

<sup>76</sup> Smart speakers are currently in around 20% of UK households. We forecast this to rise to 38% by the end of 2024.

<sup>77</sup> The BBC has announced a beta trial of its own voice-enabled search engine, which is specifically targeted at reducing reliance on the global gatekeepers in audio.

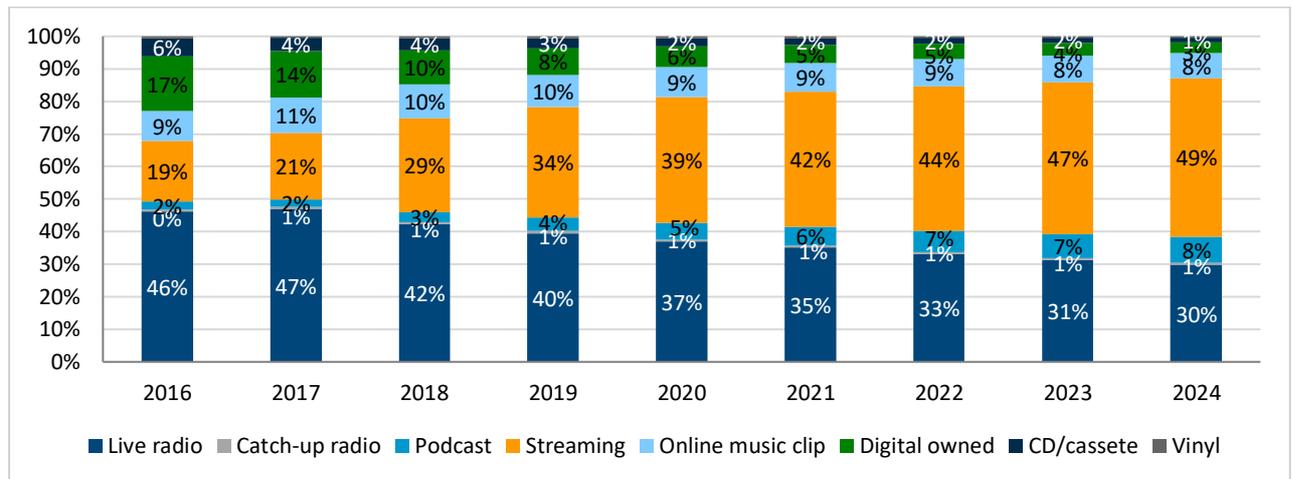
Figure 30: Market share, adults 15+, all audio, (2016-2024) (Mediatique)



N.b. graphs included post-2019 represent Mediatique forecasted market shares.

4.27 The impact is likely to be marked even among older demographics, which have been resistant to the appeal of non-linear (given that younger listeners have already significantly displaced radio listening with other audio categories). But the relentless decline in broadcast radio listening among the youngest tracked demographic will continue, as shown in the Figure below.

Figure 31: Market share, adults 15-24, all audio, (2016-2024) (Mediatique)



N.b. graphs included post-2019 represent Mediatique forecasted market shares.

Conclusions from our CF forecast and analysis

- The period to 2024 will be characterised by increased competition for viewer and listener attention, driven in particular by the growing appeal of content and services provided and promoted by large, global players on multiple devices. Further market consolidation is likely, involving production, distribution and platform operators – evident both in mergers and acquisitions to achieve scale and diversification and closures and other instances of rationalisation. Larger production and distribution entities are likely to continue to acquire smaller brands (particularly those overwhelmed by the financial challenges of Covid-19). There is also potential for larger-scale mergers and acquisition activity involving financially robust digital players and challenged ‘traditional’ media companies, given the discrepancies in revenues and market capitalisation of the digital giants (Amazon, Apple, Facebook, Google) and legacy operators (US studios, domestic broadcasters).

- 4.28 Compounding these trends, PSBs are likely to suffer from declining bargaining power with a range of the gatekeepers, especially around the ability to promote and cross-promote content and collect consumer data<sup>78</sup>. Simply put, many gatekeepers will be incentivised to make their own content prominent and discoverable, and/or will auction prominence to the highest bidder. In an increasingly transactional world for platform access and prominence, the PSBs are disadvantaged.
- 4.29 While these pressures mount, the ability of traditional sectors to generate revenues will continue to erode. Whether in the form of traditional linear advertising, legacy pay TV affiliate fees or sponsorship, commercial PSB core revenues are expected to decline at a faster rate than new forms of income can compensate, even as certain key costs (including for content and IP distribution) rise. Meanwhile, current assumptions about the BBC licence fee (the need to fund at least some over 75s licences from late 2020), coupled with Covid-related reductions in commercial dividends from BBC Studios, will require the BBC to re-double efforts to reduce costs.<sup>79</sup>
- 4.30 As the financial position of the PSBs worsens, we expect to see significant pressure on the funding available for PSB content. Absent changes to the strategies of multichannel operators and SVOD providers, the declines in PSB contributions to PSB content will not be offset by increased commitment from non-PSBs. This will be the case even where the BBC and commercial PSBs continue to seek co-production deals with these other content players, given that the resultant programmes are likely to be in a limited number of commercial genres (not those PSB genres most at risk). A clear additional risk is that co-productions lead to a decline in PSB control over rights in secondary windows and markets, reducing further their financial returns.
- 4.31 We therefore expect to see further downward pressures on overall UK content origination. This will be particularly the case in distressed genres where there is less commercial incentive to invest, and where new entrants have shown themselves uninterested. Audiences of niche content or those in the Nations or Regions are likely to be particularly affected.
- 4.32 Market outcomes will also have an impact on external suppliers – most heavily falling on the smaller independent players without well-capitalised shareholders or critical-mass businesses embracing both production and distribution. The effect will be a real-terms drop in expenditure on key genres of original content in the UK (a declining but still foundational contributor to the success of the independent sector), with implications for creativity, innovation and international trade. The impact in the Nations and Regions might be even more drastic – notably in the ability of the system to sustain out-of-London undertakings, the relative lack of commercial alternatives in the regions and a strengthening of the already firm trend favouring production within Greater London.<sup>80</sup>
- 4.33 The more integrated, international producers within the external supply sector will benefit from increased investments from the SVOD players over time. However, these commissioners typically seek to reach global deals for all rights in all windows and are not required to abide by domestic Terms of Trade. There is a risk, over time, that the UK market bifurcates between the SVOD-oriented suppliers and those continuing to work

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<sup>78</sup> Data, alongside unmediated access to end users, are critical to ensuring the ability of all PSBs to tailor content and services and to avoid disaggregation and to maintain brand attribution (which in turn sustains broad loyalty and ensure licence fee payers recognise the value of the licence). We explore this in more detail in the following section.

<sup>79</sup> The BBC confirmed in its [Annual Report for Commercial Holdings](#) that “...looking forward this crisis will significantly affect the Group’s ability to deliver revenue in 2020/21, requiring preservation of cash and a tight rein on costs.”

<sup>80</sup> Netflix recently [committed to taking permanent space at Shepperton Studios](#) while Sky is working with sister company NBC-Universal to [build new studio facilities at Elstree](#). Both are within the M25.

with the domestic broadcasters, with the former increasingly taking on the characteristics of ‘producers for hire’, as is the US model.<sup>81</sup>

- 4.34 The UK PSBs will continue to respond to these trends. Where possible, we would expect to see re-structuring, consolidation and collaboration as answers to the challenges of the medium term. In particular, we would anticipate action from the PSBs to ensure a number of key strategic imperatives are met, around access (the availability of their content on multiple devices and networks), prominence (singly or collectively ensuring discoverability), attribution (making clear the brands responsible for key content) and ability to collect data (transparently and fairly). However, more aggressive action might be needed, up to and including cuts in services (for example, closing channels, migrating certain output to online only). Some responses can be enacted with no change in the underlying PSB compact and others would require shifts in Government policy – e.g., to reform existing funding models or create new ones.
- 4.35 In considering what the medium-term future of PSB might look like, we have been asked to provide an analysis of options to inform the strategies and policies that Ofcom might recommend for reform of the PSB compact, and to set out the advantages and disadvantages of each. This is the subject of Section 5.

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<sup>81</sup> There are already signs that global streamers are eschewing joint productions with domestic broadcasters in order to ensure global rights can be exploited in early windows; even where co-pros continue, rights sharing is increasingly favouring the streamer over the domestic production partner.

## 5. Future models for PSB delivery

- 5.1 Our analysis confirms that developments in UK media markets will place increasing pressure on the PSBs’ ability to extract value from regulatory assets and deliver PSB objectives on a sustainable basis. We were tasked with identifying whether changes to existing models or new funding models could mitigate some of the pressures on the PSB system and sustain the PSB compact over the medium term.<sup>82</sup>
- 5.2 We have considered a range of options and models within three categories:
- **1) Changes to strategy, cooperation and rationalisation** – including collaboration among the PSB institutions and changes to strategy;
  - **2) Changes to the current PSB compact** – including changes to rules governing the PSBs (advertising restrictions, Terms of Trade) and changes to the regime covering access, aggregation, prominence and brand attribution; and
  - **3) Changes to the funding models of PSB institutions** – including changes to the licence fee model, new funding models for the BBC, and new sources of direct and indirect public funding.
- 5.3 In identifying these options, we have considered models in other territories, as well as taking into account emerging suggestions from the public debate; we have also included suggestions from interviewees in our extensive primary research. We have sought to provide a relatively wide menu of funding models; by definition, this covers options that may be impractical or insufficiently impactful. There are a number of overlapping principles and implications in each of these three categories; a combination of approaches is likely the best way of securing a sustainable outcome for future PSB provision.
- 5.4 There are multiple options for policy makers to consider in seeking to protect future PSB delivery, as we illustrate below. Some of the options relate to the funding and sustainability of current institutions, which include changes to existing models. We have also evaluated new models for PSB content from institutions outside the current PSB compact, including the distribution of existing or new funding. Some options will require significant change in the nature and scope of regulation or public intervention.

Figure 32: Options matrix for future models of PSB provision (Mediatique)

		Change to regulations and systems	
		Evolutionary change	Wholesale change
Change to institutions and licensed players	New institutions	<ul style="list-style-type: none"> <li>▪ Recognition of PSB delivery by non-PSBs (e.g., Sky, Discovery)</li> <li>▪ Sharing of licence fee</li> <li>▪ Extension of tax reliefs to wider institutional base</li> </ul>	<ul style="list-style-type: none"> <li>▪ Contestable fund (from direct taxation)</li> <li>▪ Extension of PSB regime to commercial radio</li> </ul>
	Existing institutions	<ul style="list-style-type: none"> <li>▪ Changes to PSB players’ strategies</li> <li>▪ Cooperation and consolidation among PSB institutions</li> <li>▪ Changes to licence fee collection / scope</li> </ul>	<ul style="list-style-type: none"> <li>▪ Updating of PSB compact (e.g., change to definition of regulatory assets)</li> <li>▪ Changes to ad minutage and Terms of Trade regulations</li> <li>▪ A commercial BBC</li> </ul>

- 5.5 In this section, we include a comparative assessment of each PSB model on the following basis:
- How would each option work in practice?

<sup>82</sup> For the avoidance of doubt, one extreme ‘solution’ would be to abandon any PSB intervention at all – no licence fee, no licence obligations for commercially funded PSBs, no regulatory framework. In this case, the outcomes are left to the market (including global players such as Netflix, Google and Apple). As our preceding analysis has shown, PSB (using original UK content investment as a proxy) would not survive absent regulation, with severe implications for audiences and competition; stakeholders, moreover, do not support such a radical approach.

- How successful would each option be in delivering and sustaining PSB objectives as we defined them in Section 2?
- What are the pros and cons of each option? Are there trade-offs and impacts?
- How practicable is each option? What (regulatory) changes would be required to enact each option?

5.6 We have set out a discursive overview of each option within the relevant categories; at the end of each subsection we have summarised our evaluation of each set of options.

#### Changes to strategy, cooperation and rationalisation options

5.7 There is flexibility within the PSB system for all PSBs to mitigate challenges to their content funding models without specific changes to the PSB compact. We have considered three main options here – changes to strategy, cooperation and consolidation.

#### *Changes to PSB strategies*

5.8 The existing PSBs might seek to re-structure their overall activities to place the institutions on a more sustainable financial footing – this might include, for example reducing the number of services they offer, placing more content behind a pay wall, or agreeing exclusivity deals with certain distribution partners.

5.9 Such changes in strategy would build on a long history of innovation at the PSBs which has included launching pay channels, building sales and distribution capabilities, and more recently introducing direct to consumer propositions such as ITV Hub+, All4+ and BritBox. The commercial PSBs have significant room to innovate, short of any change to the core PSB compact governing their main channels; even the BBC has leeway – indeed more so following the most recent Framework Agreement, where it is permitted to explore a subscription-based distribution model in its home market.<sup>83</sup> The scope both for cost savings and revenue enhancement may be considerable in these areas; however, such re-structuring will not directly address the funding and commercial pressures facing the PSB compact specifically.

5.10 The PSBs might seek to secure greater control over content supply, including investing further in in-house production or ownership of production entities – in the case of Channel 4, this would require a change in regulation.<sup>84</sup> Such an approach would see the PSBs reduce their reliance on external supply with implications for the scale and innovation of the UK independent production sector. There are also material risks that consolidation would occur among established production entities making content in commercially attractive genres; this would do little to help protect production in certain distressed PSB genres such as arts, music or religion.

#### *Cooperation among the PSBs*

5.11 Many of the challenges facing domestic broadcasters relate to scale and the difficulties of securing bargaining power against larger global operators. Global content aggregators are able to wield significant influence on local platforms to secure prominence and increasingly sign global deals with hardware manufacturers and companies providing operating systems. Moreover, some providers of operating systems (e.g., Apple and Amazon) themselves have invested in commissioning and aggregating content and may favour their own services rather than those of local providers (including the on-demand players of the PSBs).

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<sup>83</sup> See the [most recent framework agreement](#) which states “The BBC may provide a subscription service, and may develop, test and pilot such a service, with the approval of the appropriate Minister.”

<sup>84</sup> Channel’s 4 status as a publisher-broadcaster, and key client of independent producers, would need to be changed. Under section 295 of the [Communications Act \(2003\)](#), Ofcom has some latitude in determining whether Channel 4 can produce its own TV programmes. “The regulatory regime for Channel 4 includes a condition requiring C4C not to be involved, except to such extent as OFCOM may allow, in the making of programmes to be broadcast on Channel 4.” It is also likely that Channel 4 itself, and UK Government Investments, would need to favour the change.

- 5.12 The current competitive environment throws up particular challenges for smaller PSB providers including S4C and STV which struggle to secure terms with commercial platforms for the carriage of their non-linear services. Even the larger PSBs – such as Channel 4 and Channel 5 – risk being side-lined when competing with well-funded integrated content aggregators such as Amazon or Apple or with global streaming companies such as Netflix and Disney+. The benefits of plurality that derive from having multiple licensed institutions are at risk when PSB providers lack sufficient negotiating power in a globalising marketplace.
- 5.13 An evident solution here would be for the PSBs to work together in key areas to secure greater bargaining power and mitigate some of the competitive pressures arising from the emergence of larger global aggregators. There was general agreement among all relevant stakeholders interviewed for this report that closer cooperation among the PSBs could be highly valuable; some interviewees believed it was essential. We have identified a number of main areas in which such cooperation might be beneficial.
- PSB institutions could seek to negotiate collectively when seeking commercial terms for access, prominence (where subject to commercial agreement) or revenue sharing with third-party platforms. Such an outcome would provide additional negotiating strength to the PSB system; it would also provide protection to smaller PSBs, which may not be considered relevant or important to certain aggregators but which are nevertheless important contributors to PSB outcomes (particularly distinctiveness and plurality).
  - PSB institutions could consider creating shared consumer propositions that harness the collective appeal of their content to attract a wider PSB audience and to optimise time spent within a PSB environment. The most relevant example would be a shared on-demand PSB player (mooted by some of our primary sources) with a single sign-in, a single PSB brand and access to all PSB content.<sup>85</sup> Versions of this have been tested in the past – for example, Project Kangaroo (a proposed video-on-demand joint venture between BBC, ITV and Channel 4) which was prohibited on competition grounds by the Competition Commission (now the Competition and Markets Authority) in 2009– and the BBC and ITV have recently launched BritBox as a shared SVOD service.
  - The commercial PSBs could also work together in digital, online advertising sales – in theory, creating a single airtime sales house to manage and sell on-demand inventory. This is a complex option as each PSB’s commercial inventory is typically cross-marketed across spot, non-linear, sponsorship, product placement and other advertising initiatives. The competition policy issues that would arise from a joint PSB sales house offering all these products could render it inadmissible. The PSBs could consider creating a shared digital sales house for their on-demand inventory only, providing a single route to market for PSB BVOD inventory – but again, this would require complex de-coupling of linear and non-linear advertising propositions.
  - PSB institutions could also consider greater cooperation to secure services from suppliers, including in technology, distribution and content. Such an approach could yield material economies of scale and allow the sharing of risks in research, development and investment. Our interviews suggested that the most viable area for joint approaches would be in infrastructure and delivery, including developing joint technology stacks and pooled buying of distribution (including transponder capacity, transmission services, cloud services, content delivery networks, data centres). Enhancing such common approaches might be co-operation on research and development in areas such as search and voice controls. Some of this is indeed already being discussed.<sup>86</sup>

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<sup>85</sup> The PSBs already cooperate in various joint ventures including Freeview (including Freeview Play), Freesat and YouView, although these ventures still enable each institution to have control over the branding and interface of its underlying services. The BBC and commercial radio also cooperate via RadioPlayer (a joint venture of the BBC, Global, Bauer and Radio Centre).

<sup>86</sup> Although commercially sensitive.

- The PSBs might come together to create a formal IPTV proposition for all PSB channels and service delivery, agreeing a roadmap for the transition over time from broadcast to IP.<sup>87</sup>
- The PSBs are already facing competitive and inflationary pressures in securing content, rights and talent, as global SVOD players have increased their investments in UK production in high-end genres. In turn, this has encouraged the PSBs to partner with these same competing content aggregators in the co-funding and co-production of content – including Netflix and Amazon. A PSB-centric approach might see the PSBs co-fund content together, ensuring that risks and rewards can be shared within the PSB system without any external leaking of value. The approach would also address the clear trend toward the allocation of rights to the benefit of the global streaming partner rather than the domestic broadcaster, in line with funding contributions. There are of course execution issues with direct competitors commissioning content together, including sharing of access within the primary broadcast and subsequent windows. Such an approach would also have implications for plurality of viewpoints and approach within the PSB system.
- The PSBs might also consider the sharing of production resources in specific areas such as news, where newsgathering or distribution costs could be pooled, particularly in local areas where costs are likely to be high. The BBC is currently providing local news bulletins to local commercial and community radio stations which have been unable to produce their own content during the Covid-19 restrictions – this is a useful precedent for considering future cooperation, although there are implications for plurality if the same content is distributed across multiple outlets.

5.14 The practicalities of securing cooperation may be challenging for institutions that continue to compete for audiences, talent, rights and resources. The PSBs have different commercial and creative incentives that can prevent close cooperation and agreement on how best to tackle market challenges. There are also differences in culture, managerial style and decision-making processes that can hinder joint approaches. We would expect to see inevitable disagreements over control and direction, the merging of PSB brands and the determination of shareholdings or inputs.

5.15 Current competition policy may also raise significant obstacles to formalised cooperation in areas where the PSBs might be seen to be acting in concert or in a way that would inhibit market outcomes among competing broadcasters or content suppliers. The strongest objections are likely to arise upstream (sourcing of content) and downstream (customer acquisition, advertising sales). The Competition Commission's blocking of Project Kangaroo remains an important precedent in the PSBs' approach. Since then, Ofcom itself has encouraged the PSBs to collaborate more formally, including a direct call to collaborate on distribution.<sup>88</sup> Nevertheless, there is significant uncertainty as to possible competition challenges that will continue to have a chilling effect on the PSBs' willingness to consider investments in joint ventures.

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<sup>87</sup> There is prospect for such a plan to be co-ordinated, with the roll-out by BT and others of full fibre to premises in the UK (in essence to make public service media a foundational element of a new universal service obligation – 'USO' – that might extend to health, education and other Government services). Elements of how this is funded, including the degree to which it might serve to assist in the delivery of the Government's wider ambitions for broadband connectivity, would be outside the scope of a re-regulation of PSB *per se*. Ofcom would also need to consider how the current spectrum licensing arrangements, and in particular DTT spectrum awarded to PSBs, would need to be restructured. As noted elsewhere in this report, the Government is consulting on the terms under which two multiplexes – Digital 3&4 and SDN – might be treated when they expire in 2022. In Mediatique's view, any fundamental change to the multiplex licence under which the mainstream Channel 3 and Channel 4 services are delivered is extremely unlikely before the current ITV and Channel 4 operating licences expire in 2024.

<sup>88</sup> [\*Riding the waves of change: how British TV can be stronger together\*](#) – speech by Sharon White to the Freeview/Digital UK conference (2018).

*Consolidation and rationalisation*

- 5.16 Cooperation in the forms we outline above will go some way to improving the collective strengths of PSB institutions; this could be augmented by more formalised corporate actions that consolidate strengths under a more limited number of institutions.
- 5.17 The PSBs have been involved in multiple corporate actions over the years – including the consolidation of ITV licences, a number of changes in corporate ownership of Channel 5 (most recently, Viacom’s acquisition in 2014 and the subsequent merger of Viacom and CBS in 2019), and investments in independent production companies by ITV, BBC Studios and Channel 4. These deals are largely driven by a desire for greater scale, diversification and control over content supply – and in particular the ability to unlock the margin advantage conferred by a combination of content production and distribution.
- 5.18 There is scope for the PSBs to secure more of these benefits by further corporate activity, as we suggest below – these are intended as illustrative examples of ways to increase scale and influence and are not an exhaustive list.
- The acquisition of STV by ITV (plc) would complete consolidation of the ITV network; while such a move would not be transformational for ITV (plc), it would provide significant protection to STV which has struggled to secure carriage of its services on platforms that deem it unnecessary or do not wish to deal with rights issues relating to the nations.
  - ITV itself has long been seen as an acquisition target for a large US studio or media conglomerate seeking a foothold in the UK market and access to ITV’s production business. Depending on the acquirer, such a move might place ITV on a more secure financial footing within a larger diversified business. However, such a move would necessarily change the outlook of ITV senior management and potentially place at risk future commitments to PSB delivery.
  - Channel 4 Sales already represents airtime sales for UKTV (owned in turn by BBC Studios), and there could be scope for greater formal partnership between Channel 4 and BBCS, combining valuable skillsets and enabling cost savings across a range of activities (e.g., newsgathering, production, channel brands, and distribution).
  - Recent licence fee settlements will see S4C’s public funding sourced entirely from the licence fee from 2022 onwards, while keeping S4C as an independent entity. This solution falls short of the BBC taking on creative and organisational responsibility for S4C, and thus ensures plurality of service provision in Wales without requiring the BBC to run a commercial organisation. There may be scope for further sharing of resources in Wales between S4C and the BBC to improve the former’s financial position.
  - A specific corporate event is the privatisation of Channel 4, which has long been on the list of certain policy makers as a means of securing a more sustainable future for the channel. There are multiple options here, including Channel 4 being sold to another commercial organisation or remaining independent, but with a more commercial focus; such an outcome would necessarily require some reduction in its obligations and a watering down of its remit (certainly its customary remit – i.e., those elements where Channel 4 has chosen itself to emphasise public-service objectives and attributes).
- 5.19 As with all corporate activity, there are execution risks involved and transformational deals would involve the use of considerable risk capital that may not be available in the current economic climate. There are also significant risks to plurality in cases where the PSBs themselves consolidate. In a broader sense, a system that encourages the PSBs to compete aggressively with global broadcasters, studios and on-demand players may ultimately distort incentives to deliver PSB objectives if PSBs become too focussed on chasing large audiences or competing in specific genres that are commercially attractive. In particular, the maintenance of first-run original UK content might be jeopardised.

Summary of options – changes to strategy, cooperation and rationalisation

5.20 We set out below a summary of our evaluation of options in this category.

Option	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution
<b>Changes to strategy</b> (e.g., aggressive expansion in SVOD, exclusive arrangements with distributors, closure of channels/services)	Self-help options can place the PSBs on more sustainable financial footing – although by themselves do not improve incentives to invest specifically in PSB content or genres	The most valuable approaches here are likely to see greater experimentation with pay/SVOD models, or exclusive arrangements which are not in tune with PSB objectives; closure of services risks reducing reach, viewing/usage and undercutting PSB outcomes
<b>Cooperation and collaboration</b> (e.g., jointly launching a PSB Player, creating a joint digital sales house, co-operating on virtual CDNs)	Scale is increasingly important where global giants (platforms and content aggregators) are increasingly influential  Working together can improve the PSBs’ collective bargaining position, reduce costs and secure synergies	Implications for plurality and diversity if PSBs cooperate too closely  Competition issues may prevent close cooperation particularly upstream (sourcing of content) and downstream (advertising sales, customer acquisition)  Divergent incentives may also prevent workable collaboration
<b>Consolidation and rationalisation</b> (e.g., ITV-STV merger; BBCS-C4 combination)	Formalised tie-ups would protect smaller PSBs, and give greater scale to the PSB players (depending on nature of consolidation)	Implications for plurality if number of PSB institutions is reduced  Potential risk to nations/regions if smaller PSBs lose influence (e.g., S4C, STV)

Changes to the PSB compact and regulation

5.21 The PSBs gain access to valuable regulatory assets in return for commitments to deliver PSB content. As we concluded in our previous sections, this system was created for a linear environment where broadcast channels and standardised EPGs are the primary means of discovery and consumption; however, as a result of changes to consumer behaviour and broadcasting outcomes, the value of these regulatory assets is declining. The system can only continue to deliver PSB objectives if the rights afforded to PSB institutions are worth more than or are equal to the costs of delivering these objectives. By necessity therefore, if the future of PSB is to be sustained, then the PSB compact must be updated to account for changes in the media landscape and to re-establish the balance of value between the regulatory rights and responsibilities.

5.22 It is of course possible to maintain parity in the PSB compact by reducing the obligations on the PSB institutions – by, for example, reducing commitments by genre, or to original content, regional content or programmes made by independent producers. However, any diminution in commitment will raise different questions about what the overall objectives of public policy should be. A more fruitful approach to sustain PSB delivery would be to increase the value of PSB status or to offset declines in the value of the current compact. It would be for policy makers to assess whether the value of regulatory assets in any revised PSB compact were commensurate with obligations placed upon PSB providers; it might be, for example, that there is scope to increase the requirements on PSBs if the value of regulatory assets is deemed to have increased sufficiency beyond current obligations.

5.23 We have therefore considered the extent to which changes to specific PSB regulations (restrictions on advertising at the commercial PSBs, and Terms of Trade) and changes to the scope of regulatory assets can ensure that value is retained and perhaps increased in the PSB compact. All relevant stakeholders agreed that changes to existing regulations would be required in order to protect PSB provision over time, but some questioned whether PSB definitions and status were too tightly defined and too narrowly applied to a limited number of institutions. There was an acceptance among most players that certain changes to the PSB compact (including in instances where platforms were obliged to promote or protect PSB content) would face serious opposition from some parties.

*Changes to advertising rules (commercial PSBs only)*

- 5.24 The commercial PSBs are subject to tighter restrictions on the scale of advertising inventory than other broadcasters:
- Non-PSBs are limited to an average of 9 minutes/hour of advertising per day, and a maximum of 12 minutes in any given hour; and
  - PSBs are limited to 7 minutes/hour, and 8 minutes/hour in peak.<sup>89</sup>
- 5.25 The limits on PSB minutage are an additional restriction on the commercial PSBs. Nevertheless, there is a longstanding debate over the impact of harmonising minutage; Ofcom's previous analysis of these regulations suggests that the impact of equalising the PSBs' limit cannot be predicted with any certainty.<sup>90</sup> There is a risk that levelling up, for example, would materially increase the number of commercial impacts, reduce prices and ultimately lead to net revenue declines. Most market participants believe that the ultimate market outcome is at best uncertain.<sup>91</sup>
- 5.26 Once the UK leaves the European Union, UK policy makers will no longer be subject to European minutage constraints and could (theoretically) have the power to forego any restrictions on minutage at all. Such a move would give the commercial PSBs greater flexibility to compete with other advertising media but is likely to create considerable short-term uncertainty for planners and sales houses where advertising agreements continue to be based on forward projections of market share.
- 5.27 ITV itself is subject to further restrictions on advertising sales through the CRR mechanism<sup>92</sup> which limits ITV's pricing power in the TV advertising market. A removal of this restriction would give ITV greater commercial freedom in its dealings with agencies and allow for greater cross-selling of inventory across all its media properties. As with changes to minutage, the overall impacts of such a change are potentially uncertain; it is likely to be the case, however, that any financial benefits that accrue to ITV would be at the expense of other broadcasters (including the other commercial PSBs), as they compete for share of agency budgets.<sup>93</sup>
- 5.28 Commercial broadcasters (including the commercial PSBs) are also subject regulations over the use of sponsorship and product placement, including requirements for broadcasters to retain editorial control and to ensure that any commercial messages are editorially justified. A more liberal approach to commercial messaging might allow the commercial PSBs to secure incremental revenues from advertisers, albeit at the risk of compromising editorial purity.
- 5.29 Over the medium term, the liberalisation of various regulations and restrictions that affect the commercial PSBs would give these institutions greater flexibility and control over their commercial strategies. The key challenge is to assess whether such changes would lead to greater investment in TV advertising by agencies and advertisers; if abolishing rules on minutage or CRR does not lead to incremental investment, then any share gains secured by the commercial PSBs will be at the expense of other broadcasters.

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<sup>89</sup> See the [Code on the Scheduling of Television Advertising](#) report here.

<sup>90</sup> See the Ofcom report [Regarding the quantity of advertising on television](#) here.

<sup>91</sup> We did not find any support for a change in the current regulations among any stakeholders in our primary research.

<sup>92</sup> Contract rights renewal is a regulatory remedy imposed on ITV following the merger of Carlton and Granada (the primary ITV network licence holders whose merger created ITV plc).

<sup>93</sup> We did not find significant support from our primary sources for a change to CRR in current market conditions. ITV has publicly stated that a review of CRR would be "diversionary" and create a "regulatory mire" – Carolyn McCall, 2019 ITV results call.

*Changes to Terms of trade (all PSBs)*

- 5.30 PSBs are subject to Terms of Trade<sup>94</sup> with independent producers which limit the basis on which they can exploit rights sourced from qualifying external suppliers. These terms ensure that ownership of intellectual property ultimately resides with the producer; revenues secured from rights exploitation outside the primary window(s) must be shared between commissioner and producer, or they accrue entirely to the producer. These terms cement important policy goals including promoting the UK's production sector and protecting small independent producers who would be unable to negotiate fair terms with the PSBs who wield greater bargaining power. However, these terms are specific to the PSBs and there is no obligation on competing broadcasters (e.g., Sky, Discovery) or other players (e.g., Netflix, Amazon) to protect the residual intellectual property rights of commissioned producers.
- 5.31 Increasingly, non-PSBs are seeking to secure greater rights ownership across multiple windows, following the US model whereby suppliers are effectively producers for hire. In this light, the PSBs are at an increasing disadvantage when it comes to securing commissioned content, as they are unable to secure rights to non-broadcast and non-catch-up windows without payment or value sharing. The BBC recently agreed terms with Pact<sup>95</sup> under which it has the catch-up rights to commissioned content for up to 12 months (compared to 30 days currently), and this has allowed iPlayer to be fundamentally upgraded. However, the competition for content in the primary window is increasingly competitive and new entrants are prepared to pay significantly more than the PSBs.
- 5.32 Of course, there are strong incentives among producers to deal with the PSBs rather than others as commercial deals with the former will protect underlying intellectual property rights. Nevertheless, this is another example of where the PSBs do not operate on a level-playing field with other providers. Levelling the playing field would have trade-offs, however:
- Applying Terms of Trade to any organisation that commissioned content from a qualifying supplier would provide the UK production sector with greater control over their rights and revenue generation; although there are risks that non-PSB providers would look elsewhere to secure content if they were able to secure better terms (e.g., in-house production, international production). In addition, this would not lead to incremental value to the PSBs themselves.
  - Removing the obligation for the PSBs to sign Terms of Trade with production companies would certainly give the PSBs access to greater value in non-broadcast rights windows. However, this would remove protections afforded to the UK production sector with implications for financial sustainability and the dynamism and attractiveness of the sector.
  - There is scope for policy makers to take a more targeted approach within these two book-ended options, reconciling the need to protect the independent production sector with a less restrictive PSB regime. For example, Terms of Trade could be applied only to productions made by companies below a certain size that would be deemed worthy of greater regulatory protection. The production sector would likely resist this strongly, and there may be conflicting incentives for production companies that would otherwise seek to secure scale.

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<sup>94</sup> The legal requirement for PSB providers is limited to having in place codes of practice securing the high-level outcomes prescribed in s.285(3) of the Act, in the manner described in Ofcom guidelines on commissioning. Programmes commissioned specifically for VOD, but not linear broadcast, are not subject to the Terms of Trade. Moreover, the requirement for Terms of Trade only applies to commissions for PSB channels, and not to the commercial PSB providers' portfolio channels.

<sup>95</sup> Producers Alliance for Cinema and Television, which represents the interests of external suppliers of A/V content in the UK.

*Changes to the regime covering access, aggregation, prominence and brand attribution (all PSBs)*

- 5.33 An area of potential value in a reformed PSB compact is around the relationship between PSBs and third-party distributors, both for the BBC and for the commercial PSBs – although there are necessarily differences between the two categories.
- 5.34 The key regulatory assets of the PSB compact for all PSBs are access to near-universal DTT spectrum<sup>96</sup> and the right for their channels to be appropriately prominent on TV platforms. The BBC secures these benefits in addition to its privileged access to proceeds from the licence fee.

**Figure 33: The historical context for EPG prominence and carriage of PSB services (Mediatique)**

Until the rollout of multichannel TV from the late 1980s, spectrum and prominence were highly valuable. Implicitly, this value included the ability of PSBs to maintain control over aggregation, given that nearly all viewing was done ‘live’ on a channel where the schedule was controlled by the channel operator. The application of guaranteed prominence on third-party TV platforms (effectively satellite and cable), coupled with a ‘must-offer, must-carry’ regime, ensured that PSB linear services were accessible in all TV households, prominently.<sup>97</sup>

Even the growth of PVR use (which threatened the control channels had over aggregation by enabling on demand viewing of disaggregated content) did not unduly diminish the value of access and prominence. Most PVR viewing was of PSB content on major TV platforms, and while ad-skipping was an issue for commercial PSBs, the problem was manageable. No payments were made by any pay TV operator to PSB channels for carriage – indeed, for some time Sky actually charged the PSBs for technical platform services.

The prominence and must-offer/must-carry rules element of the compact did not extend, however, to the commercial PSB multichannels (diginets), HD simulcast channels nor – after the launch of on-demand players from the PSBs in the late 2000s – to the iPlayer and the ITV/STV, Channel 4 and Channel 5 variants. These were the subject of commercial negotiations between distributors (e.g., pay TV operators) and the PSBs.

In recent years, commercial PSBs (with the tacit support of the BBC) have been arguing for a change to the regulatory regime to support their ability to demand ‘re-transmission’ fees from pay TV platforms even for their licenced PSB channels. Pay TV platforms resisted, arguing that the prominence of mainstream channels on all platforms already conferred enough value.

- 5.35 As we have seen, the questions of access and prominence have become more complicated with the emergence of new platforms exercising control over user interfaces (including smart TVs and their associated operating systems) and more pressing given the declining share of total viewing delivered via linear channels (including those of the PSBs). The value of EPG prominence continues to decline as viewers are able to discover and select content via many new access points – including search, recommendations, favourites and promoted content. Moreover, access to these new devices is increasingly informed by negotiations at international level (between global operators and suppliers) and reflect dynamics not just in TV but in a range of other markets too, including gaming, music, e-commerce and social media, in ways that disfavour national broadcasters.
- 5.36 Ofcom has already taken steps to recommend changes to the policy framework that would see prominence rules extended to cover, initially, the positioning of the PSB on-demand players and content on connected TVs and other in-home devices (such as set-top boxes and streaming sticks). But prominence for PSB content

<sup>96</sup>As noted earlier, the multiplex licence for ITV and Channel 4 (Digital 3&4) as well as the licence for the multiplex originally carrying Channel 5 (SDN, owned by ITV), both expire in 2022, two years before the current commercial PSB operating licences are set to be renewed. The government will be considering whether and how to treat these licences, and this might afford the opportunity to address elements of the regulatory compact. It is Mediatique’s assumption (not necessarily shared by Ofcom) that the current multiplex licences through which ITV, STV and Channel 4 deliver their PSB channels will be extended at least to match the terms of the current ITV and Channel 4 operating licences. A more extensive renewal period – perhaps out to 2030 or even beyond for all PSB and commercial multiplexes – may also be agreed, depending on the degree to which PSB delivery (and its reliance on access to spectrum) is deemed foundational to Government policy are of course possible. The timing of any decision from Government precludes us from incorporating any such options into the present analysis.

<sup>97</sup>The ‘must carry’ rules applying to cable operators were never activated, owing to the exemption from Copyright legislation enjoyed by cable operators. This was the case until the relevant section of the Act, s73, was abolished in 2017.

on these connected devices is only one part of an emerging set of tradeable rights associated with the role new platforms and legacy providers alike are playing with regard to content aggregation: including the rights of access, prominence, brand attribution and aggregation. We deal with each of these below.

- 5.37 Issues of access and prominence also have an impact on audio services, including the BBC's radio stations and other on-demand audio content and the radio stations of commercial players, which – although not PSB – contribute to PSB outcomes and are provided access to spectrum. It may be that policy makers should consider extending non-linear prominence and other regulatory benefits to the BBC and commercial radio's output – particularly in the context of the emerging gatekeeper role played by voice-controlled smart speakers. Many of these devices share common ownership (and technological specifications) with platform operators – Amazon, Google, Apple – and represent similar threats to legacy audio providers seeking reach and relevance among UK audiences.

#### *Prominence of non-linear services*

- 5.38 Prominence of channels, services and content will continue to be a key driver of viewing outcomes for audiences. Extending the prominence of PSB institutions beyond linear EPGs to all digital platforms would extend that value of regulatory assets within the PSB compact and align the delivery of PSB objectives with changes in consumer behaviour. Ofcom is already recommending a policy along these lines, starting with a requirement to make PSB discoverable on connected TVs and other similar devices; the change will require Government action, however.<sup>98</sup>
- 5.39 The objective here would be to ensure that PSB content remained easy to find for viewers on linear and non-linear platforms. In practice, the extension of prominence to non-linear would involve two main interventions:
- Giving protection to PSB players so that they are prominent and easy to find on the homepage of platform EPGs; and
  - Enabling viewers to discover and find PSB content through recommendations and search – including, for example, giving PSB content priority in searches or surfacing similar content from the PSBs when viewers look for a specific title.
- 5.40 Granting prominence to the commercial PSB players would require them to be given PSB status, even though they increasingly contain content that might not be classified as PSB under the existing regime – for example, ITV Player will contain content that was originally broadcast on non-PSB channels (ITV2, ITV Be et al). The PSBs might seek to mitigate such concerns by ensuring that the core PSB elements (e.g., news, current affairs, children's) were made prominent within the players themselves. Policy makers would need to consider whether the extension of prominence should impose additional obligations on the PSBs.
- 5.41 There are numerous practical, strategy and financial implications to such intervention, as it would impose significant opportunity costs on platforms, which might otherwise seek to promote their own services or those of content providers that are willing to pay for prominence. Platform operators argue that the imposition of prominence for non-linear services would also stifle innovation. Nevertheless, to the extent that the creation and consumption of PSB content is a public policy objective, then such content should be discoverable by viewers even if this requires intervention.

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<sup>98</sup> See Ofcom's [Review of prominence for public service broadcasting](#) here.

*Right of inclusion of PSB services*

- 5.42 PSB services can only be made prominent on a platform if PSBs can access platforms in the first place. If the relevant services are not available on highly-penetrated platforms, then audiences will not be able to find them easily and PSB objectives are harder to meet.
- 5.43 The availability of the core linear PSB services is covered by must-offer/must-carry rules, but no such obligations exist for the commercial PSB diginets or for non-linear services. At present, the PSBs undertake commercial negotiations with platforms and TV manufacturers to secure carriage for non-linear services (see Figure 33). Commercial negotiations can be complex and carriage can involve significant development costs for both PSBs and platforms. Large PSBs like the BBC have significant bargaining power as well as internal technology resources and support, although even they can struggle to agree terms. Smaller PSBs like STV or S4C find it more difficult to secure traction with platforms and have no guarantee that their on-demand services will be carried.
- 5.44 An updated PSB compact could impose a universality obligation on the PSBs' linear and non-linear services – in effect, mandating platforms to carry the on-demand players (and associated on-demand content) of the PSBs. In turn, this would require that the PSBs' on-demand players be given PSB status.<sup>99</sup> Ofcom has already recognised that this structure would require a backstop mechanism in the event that commercial PSBs elect to invoke their rights of inclusion but were unable to meet a commercial settlement with platforms.<sup>100</sup> We assume that the BBC would always default to a backstop position, as it cannot (easily) trade value.
- 5.45 Here again, there would be arguments around what constitutes PSB content on commercial PSB players – such content may not have been originally broadcast on the licensed PSB channel and may not contribute to the attributes of public service, and yet would be guaranteed access (and potentially prominence) at the expense of other services of higher commercial utility to distribution platforms. Platforms may also incur significant costs if they are forced to carry an expanded list of PSB services – including development costs and opportunity costs; this is particularly true for the smaller PSBs where the relative potential benefits to the platform may not be evident and where regionalisation may impose specific additional costs.

*Guarantees of attribution and protection from disaggregation*

- 5.46 One of the benefits of an institutional PSB system is the ability to aggregate diverse genres and content characteristics under a single service or brand, enabling viewers to find content that they might otherwise not gravitate toward. The benefits of such serendipity extend beyond linear channels as the PSBs all aggregate content in on-demand windows via their players. However, the ability to search for content through advanced platform navigation, and to be served content on demand, threatens the link between the PSBs' brands and the content that they make. This threat of disaggregation may intensify if pay TV operators and new connected gateways successfully abrogate the ability to identify and serve PSB content themselves (as some – including Sky and Virgin – currently aim to do).
- 5.47 There are of course consumer benefits arising from the ability to search for content and having access to libraries of content from different providers in a single place. The prohibition of disaggregation would have

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<sup>99</sup> There is also the option for the commercial PSBs' diginets to be given PSB status and thus afforded access and prominence. Such a move would be challenging to justify in terms of content as much of the content available on these channels is acquired or repeated and not necessarily PSB; it would, however, provide additional scale and value to the PSB compact. This would likely raise significant opposition from platforms who would need to make EPG real estate available to many additional channels from ITV, Channel 4 and Channel 5. It would also still be rooted in the linear world and would do little to mitigate longer term pressures on PSB delivery.

<sup>100</sup> "If there were an availability obligation, for it to be effective, we think it would require a backstop mechanism to determine terms if commercial negotiations fail", as described in Ofcom's [Review of prominence for public service broadcasting](#).

significant implications for consumer utility and innovation, but policy makers might seek to reconcile the benefits of consumer functionality with the need to protect PSB institutions from disaggregation.

- 5.48 To sustain value in the PSB system, the PSBs might be offered protections from the loss of attribution for specific programmes. For example, platforms could be obliged to make clear the source of any content discovered and watched via a disaggregated search – thus ensuring that viewers are aware that content has been sourced from a PSB. There is scope for different approaches here, including stronger rights of attribution for certain types of content in PSB genres. A more interventionist option would prohibit platforms from separating a PSB’s programme from its player – hence, the selection of any PSB programme that is surfaced via search or a listing would take the viewer to the underlying on-demand player (e.g., the iPlayer) where content can be played within the PSB environment. There would be trade-offs for the platforms here, as they would lose a degree of control over the audience journey and may argue that their platforms are being usurped by the PSBs.

#### *Sharing of value between commercial PSBs and platforms*

- 5.49 When the Copyright exemption for cable was abolished in 2017, commercial PSBs argued that cable operators (and indeed other pay TV players) should have to pay for the right to ‘re-transmit’ their mainstream channels. The Government of the day stated that commercial PSBs were already “fairly compensated” for carriage of the licensed PSB services via the PSB compact and said it did not expect any net payments between platforms and PSBs for carriage of linear channels.<sup>101</sup>

- 5.50 Since then, there has been a range of (confidential) negotiations involving pay TV platforms and PSBs, on the terms under which a range of services (HD channels, diginets, players) might be carried. In very recent periods, these discussions have also included the terms under which the IP streaming rights to the mainstream PSB channels might be awarded.

- Neither side of the ‘carriage’ bargain is in any doubt that real value is generated for both. Platforms benefit from the ability to provide popular PSB content in their pay TV offerings, which assists in locking in subscribers. The PSBs gain reach and (for commercial PSBs) incremental advertising revenues.<sup>102</sup> For this reason, value is already being traded – for the HD channels, for the commercial diginets, and for the on-demand players (Sky waived platform fees for the PSB channels in notional exchange for the right to carry the early variations of the catch-up TV services of the PSBs).
- Sky and Virgin have insisted, however, that the mainstream PSB channels should not be part of any commercial compensation, as they are subject to must offer/must carry and are automatically given prominence that would otherwise be commercially valuable to a third party. PSBs have countered that the value accruing to pay TV platforms of having access to PSB channels and services is significant. Were these services to be withheld from a given pay TV platform, at least some subscribers would migrate to a platform where the services were still available.

- 5.51 Policy makers could take the view that the PSBs could unlock incremental value by giving them the freedom to seek compensation for the carriage of their services – linear and non-linear. Indeed, Ofcom, in its 2015 report, said that “reform of regulation, which may affect the flow of funds between platforms and broadcasters...could provide additional funding to commercial PSBs,” although it concluded that reform

<sup>101</sup> DCMS, [The balance of payments between television platforms and public service broadcasters consultation report](#) (2016). The carriage of PSB channels via satellite have always been complicated by the fact that satellite platforms such as Sky do not ‘re-transmit’ channels; rather, the channels are broadcast on satellite capacity secured from the satellite operator (e.g., SES-Astra). Sky’s role is to provide incorporation of the channel signals to permit a channel number to be assigned on the EPG and for the content to be recorded for playback (via a PVR or streamed ‘over the top’.)

<sup>102</sup> [Work on the dynamics of potential payment flows](#) was provided to DCMS by Mediatique in 2012.

would be complicated and there was no certainty that revenues flowing to the PSBs would be spent on PSB content.<sup>103</sup>

5.52 Taking this to its fullest extent, this revised compact could apply to all commercial PSB channels and on-demand players given PSB status, encompassing access (effectively a default must-offer/must-carry), prominence, and protection against disaggregation. Policy makers might consider constructing a regime that would permit the PSBs to invoke their right to be carried, unmediated and prominently displayed on linear and non-linear platforms and when consumers search for content on relevant platforms. This would provide a backstop protection for the PSBs, and the commercial PSBs could seek to forego these protections and seek commercial agreements with platforms.

5.53 In the event that the commercial PSBs elect to negotiate commercial terms with platforms, they may agree to concede control around the availability of their content in return for compensation.<sup>104</sup> That might come in the form of cash or in kind – for example, in return for access to consumer data generated by the platform operators.

- Data, alongside unmediated access to end users, are critical to ensuring the ability of all PSBs to tailor content and services and to avoid disaggregation and to maintain brand attribution (which in turn sustains broad loyalty and ensures licence fee payers recognise the value of the licence).
- The commercial PSBs, as they look to transition to new models of digital advertising, require transparent access to first-party data if they are to fully benefit from the premium such tailored advertising delivers. This is not always available to them; nor are they in a strong position to bargain with global players, whose own content and services are likely to be favoured and whose business models are based in many cases on charging significant fees to suppliers for the privilege of access and prominence within user interfaces.

5.54 There would need to be guarantees that any additional revenue flows to the commercial PSBs were translated into investment in PSB content. Opponents have long argued that it may be difficult to ensure that commercially funded, shareholder-owned companies (ITV and Channel 5 specifically) do not divert incremental revenues to dividends. As a counter to this (as we have argued earlier), historical trends suggest that £1 of incremental revenue accruing to PSBs is far more likely to generate UK origination expenditure. Moreover, the profits generated by new entrants in the connected gateways space are already less likely to generate tax or other benefits for the general UK economy, notwithstanding arguments about the future of PSB.

*Summary of options – changes to the PSB compact and regulation*

5.55 We set out below a summary of our evaluation of options in this category.

Option	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution
<b>Liberalisation of PSB advertising restrictions (e.g., abolition/reform of CRR system)</b>	Uncertainty as to market outcomes if PSB restrictions are equalised (or ad restrictions removed entirely)  Some scope for incremental investment from liberalised sponsorship regime or potential for greater PSB ad sales cooperation	An improved financial position for the commercial PSBs is likely to be at the expense of other commercial broadcasters  Appetite for short-term disruption from an ad sales review is limited among stakeholders

<sup>103</sup> See the Ofcom report on [Public Service Broadcasting in the Internet Age](#).

<sup>104</sup> Various calculations have been made in recent years, suggesting as much as £200m in annualised value would be realised if ITV and Channel 4 were to be able to negotiate carriage for their mainstream PSB channels on legacy pay TV platforms. If the PSBs are permitted to negotiate collectively, the value generated is likely to be considerably higher. This would not include the value of the PSB players nor any payments from new-entrant connected gateways (e.g., smart TVs, streaming devices).

Option	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution
<b>Changes to Terms of Trade (e.g., remove requirement to share rights with suppliers)</b>	A less restrictive rights position for the PSBs would level the playing field when competing with global players or non-PSBs – with potential for incremental value retention in secondary windows	Improving the PSBs’ rights position may directly leech value from the UK production sector Too prescriptive an approach (e.g., company size criteria) may distort incentives for the production sector
<b>Extension of PSB prominence to non-linear (e.g., requiring smart devices to carry PSB players prominently on home page)</b>	Enables easier discovery of PSB content, and updates the PSB compact in line with market developments	Platforms will argue that imposed prominence stifles innovation and imposes opportunity costs by disfavouring their own services or those of other commercial players Affording prominence to all content on PSB’s non-linear content may promote content that is not necessarily PSB
<b>Right of access for PSB non-linear services (e.g., create a ‘must carry’ obligation on all platforms)</b>	Secures reach for PSB services, and protects smaller PSBs from being ignored or facing significant imbalance in negotiations	Platforms may incur additional costs if forced to carry all PSB services/content
<b>Protection of attribution for PSB services (e.g., ensure content from PSBs cannot be ‘unbundled’ by platforms/operators)</b>	Maintains link between PSB brands and underlying content Mitigates threat of misattribution and promotes long-term value of PSB brands	Intervention may stifle consumer benefits from highly-functional search/navigation
<b>Right to compensation for commercial PSB services (‘backstop’ requirement for platforms/operators to compensate if terms cannot be commercially agreed)</b>	Allows the PSBs the freedom to seek compensation for the carriage of their services – and provide additional funding	Without prescription, there may be no guarantees that any additional value secured by the PSBs is invested in PSB content

Changes to public funding models

*Licence fee reform*

5.56 The licence fee represents the major source of funding for PSB content in the UK, with all the BBC’s activities across TV, radio and online defined as PSB services. The BBC also generates value from commercial operations including in TV production, content and format sales, consumer products, studios and post-production and global news. The licence fee generated £3.7bn of revenues for the BBC in the 2019 financial year ending March, and together with all other revenue sources, the BBC’s total income in 2019 was £4.9bn.

**Figure 34: BBC total revenues, by source, 2018, 2019 (BBC)**

£m	Licence fee income	Grants, rental and other PSB income	BBC studios and other commercial	Group adjustments <sup>105</sup>	Total BBC income
<b>2019</b>	£3,690m	£327m	£1,372m	- £500m	<b>£4,889m</b>
<b>2018</b>	£3,830m	£301m	£1,395m	- £464m	<b>£5,062m</b>

5.57 The licence fee is a compulsory levy on anyone who:

- Watches or record programmes as they are being broadcast on TV, on any channel;

<sup>105</sup> Includes adjustments for internal financial flows between BBC Studios and BBC PSB group.

- Watches or streams programmes live on an online TV service (e.g., ITV Hub, YouTube, Now TV); or
- Downloads or watches any BBC programmes on iPlayer.

5.58 These rules were updated in 2016 in light of changes to consumer behaviour and growth in on-demand video on connected devices. These apply to any device that a household uses, including TVs, computers, laptops, mobile phones, tablets or other digital devices.

5.59 There are many voices calling for a reform of the licence fee – some argue that a universal obligation to pay a fixed fee is regressive.<sup>106</sup> The Government is currently running a consultation seeking views on whether and how to decriminalise licence fee evasion.<sup>107</sup> Other collection methods are possible, including a voluntary payment model, direct government grant, or collection via council tax (and linked to income or wealth). There is also a case for the licence fee to be set by an independent body, away from political interference. These options relate to the mechanism of collection, and do not touch on the scale and sustainability of the BBC’s income; as such, any change to the method of licence fee collection does not affect the delivery of PSB objectives other than to the extent that it leads to changes in the BBC’s income. There are no calls for the BBC’s public income to be increased. The debate over the future of the BBC among policy makers is focussed on reducing licence fee income or sharing it among others.

5.60 Arguments around the future of the BBC are also informed by changes to public service funding models in other territories. There is a growing list of countries that have made significant changes to licence fee funding in recent years including the replacement of licence fees by direct government grants, universal household charges or a greater reliance on commercial income (e.g., Belgium, Cyprus, Denmark, Finland, Hungary, Iceland, Israel, Netherlands, Norway, Romania, Sweden and Switzerland). However, it is still the case that licence fees remain a primary source of funding for public service broadcasters in other major media markets including France, Germany, Ireland and Italy. Even in territories where licence fees have been abolished, they have largely been replaced by direct taxpayer funding and grants from government rather than fully commercial models.

*Sharing of licence fee funds (contestable licence fee)*

5.61 One structural option for the funding of PSB content would be to distribute licence fee proceeds among other PSBs in return for delivering PSB obligations. So-called ‘top-slicing’ has long been advocated by critics of the BBC and has also been a feature of recent licence fee settlements which have seen the BBC responsible for funding an increasing number of external media activities.

5.62 The licence fee now provides direct funding to many non-BBC services that would otherwise require other public intervention via direct taxation or grants – this includes S4C, local TV, BBC Monitoring and the World Service. This is evidential of commercial and public policy pressures on investment in media services, although does provide a precedent for sharing the proceeds of the licence fee with other providers that supply PSB content or services.

**Figure 35: BBC expenditure on other services, including non-BBC services (BBC, Mediatique)**

Service	2018 spend	2019 spend	Notes
<b>S4C – service spend</b>	£26m	£22m	S4C’s public funding will be provided entirely through the licence fee from 2022/23 onwards
<b>Monitoring</b>	£6m	£6m	Funded from the licence fee from 2013/14

<sup>106</sup> From 1 August 2020, over 75s will be required to pay the licence, which was previously free for this age group. Only those households receiving Pension Credit will be subsidised.

<sup>107</sup> See the [DCMS consultation on decriminalising TV licence evasion](#).

Service	2018 spend	2019 spend	Notes
World service	£227m	£234m	BBC funding only; additional funding is secured via Government grant
Other services – S4C, broadband roll-out, local TV	£160m	£94m	A scheme whereby the BBC purchased news content from local channels is set to end in July 2020

- 5.63 Licence fee funds could be shared with the commercial PSBs or be open to a wider set of providers that could bid for funding. Such an outcome could promote plurality in the system and reduce the exposure of commercial PSB provision to cyclical shocks. Some primary sources suggested to us that this might also force the BBC to be more focussed on the delivery of its own objectives and to operate more efficiently. However, recipients of licence-fee funding risk getting pulled into the political debates and the search for greater accountability that the BBC is itself subject to. It is not clear to us that existing (or new) PSB providers would elect to seek funding from the licence fee.
- 5.64 The major downside of a top-slicing model is that it does not lead to incremental investment in the system, as existing licence fee funds would be shared among other players. The result would be a smaller BBC and a potential fragmentation of impact among other players. Policy makers would need to consider whether a smaller but sustainable PSB system (funded entirely or in the most part by the licence fee) was acceptable. The only way to ensure an *increase* in PSB investment would be to increase the licence fee (on the understanding that this larger licence fee would no longer just finance the BBC) and share the additional proceeds accordingly; such a move would face significant political barriers. This system would also require a degree of administrative oversight to maintain a system of funding allocation and delivery of obligations.

*Alternative BBC funding models*

- 5.65 A more radical change to the BBC’s funding model could see the licence fee abolished and replaced by a commercial model. Such wholesale change would have implications for the scope, scale and nature of the BBC and involve practical execution issues.
- 5.66 At the outset, it is almost certain that a commercial BBC would cease to operate the breadth and depth of services that it currently does. While a commercial BBC would likely continue to make content in some PSB genres (including news, drama, comedy, current affairs, children’s), there would be no guarantees as to the scale of investment or output over time; even if the BBC retained PSB status under a commercial model, policy makers would have a significantly reduced ability to compel the production of content in PSB genres. There would be no commercial imperative to operate as many services in the nations and regions and funding for marginal genres (e.g., religion, specialist factual, speech radio) and non-English language services would be reduced or removed. A commercial BBC would also no longer justify the funding of S4C, local TV or other external obligations.
- 5.67 The BBC already operates commercial activities that give the BBC access to additional income. The scope and scale of these activities are closely monitored to ensure that any market impacts are justifiable in light of its position as a publicly funded PSB. There may be scope for the BBC to maintain its public funding for a much-reduced number of services and compete commercially in other segments. The impact of a commercial BBC able to rely on core (if much reduced) public funding would however generate considerable opposition, as has been seen in markets where public money and commercial funding are co-mingled.<sup>108</sup>
- 5.68 We have looked at three specific models as follows:
- **Advertising** – the licence fee is abolished, and the BBC seeks advertising income from its TV, radio and online properties via the sale of commercial inventory;

<sup>108</sup> Ireland and Canada are prime examples.

- **Subscription** – the licence fee is abolished, and the BBC seeks subscription income from the sale of monthly subscriptions from those willing to pay for continued access to the BBC; and
- **Hybrid** – the BBC replaces the licence fee with a mixed proposition, offering some services for free (funded by a reduced licence fee or advertising) and upselling access to additional content and services through consumer payment.<sup>109</sup>

### *An advertising-funded BBC*

- 5.69 An ad-funded model would place the BBC on a commercial footing while retaining free-to-air universal distribution. The BBC's inventory, including the delivery of mass-market audiences, would also be highly attractive to advertisers.
- 5.70 Placing advertising on the BBC's services would create a material increase in the supply of commercial impacts in the UK market, with potentially significant impacts on the price of commercial inventory. Multiple studies have found that increasing advertising inventory can lead to a fall in the revenues of other players as the BBC potentially steals revenue from competitors, rather than increases overall commitments to TV advertising.<sup>110</sup> In practice, the market outcome of a newly ad-funded BBC is likely to see a combination of some overall market growth (as advertisers seek access to the BBC's audiences) and some material substitution effects (as increases in marketing spend face budgetary constraints).
- 5.71 We have used the US market as a read-across to estimate what an advertising market without a licence fee intervention might look like. Assuming that the UK markets in TV and radio expand to reach the same equivalent size as the US, and that the BBC could secure a share of these larger advertising markets in line with its respective share of consumption (32% in video and 49% in audio), the BBC could secure up to £2bn in TV advertising<sup>111</sup> and £0.5bn in radio advertising.
- 5.72 The BBC would also be able to monetise its online properties – notably BBC News and BBC Sport – by including commercial inventory alongside stories and content. The BBC's online sites have a similar number of monthly visitors as Reach and DMGT, which generate £107m and £76m in online advertising revenues respectively. Using these figures as benchmarks, we might expect the BBC to generate up to £100m of annual revenue from its online properties.
- 5.73 In overall terms therefore, an ad-funded BBC could potentially secure up to £2.7bn of revenues, informed by a read-across from international markets and benchmarking against similar publishers. An advertising model would thus see the BBC lose up to £1.1bn in revenue compared to the current licence fee model; this is equivalent to the entire content budget of BBC One, or double the BBC's total expenditure on radio. Such an outcome would necessarily lead to reductions in content output and services at the BBC and have material implications for the delivery of PSB objectives. Of course, some people would welcome a smaller more focussed BBC, although the BBC would be less recognisable and influential internationally and also play a reduced role as a quality threshold for other PSBs and broadcasters.
- 5.74 It is not clear-cut whether a commercial BBC would place the BBC's funding on a more sustainable basis, although it would certainly remove its funding from political influence and negotiation. An ad-funded BBC would also pose key consumer and execution issues for the BBC and policy makers.

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<sup>109</sup> By definition, there are many options in and around these categories. For example, as we mentioned above, a hybrid model might marry a licence-fee funded core BBC (at a lower quantum), with additional services available on a paid-for or ad-funded basis. This might, for example, support the concept of a single BBC TV channel, focussed on 'market failure' genres, including news, current affairs, education, kids, possibly alongside a public service radio station (e.g., Radio 4).

<sup>110</sup> [Ofcom's own work remains the primary evidence base for changes in advertising minutage](#), although published work has not specifically tested the impact of placing advertising on the BBC's services.

<sup>111</sup> This would include a combination of spot advertising and broadcast video-on-demand (BVOD) revenues where the main competitors to a commercial BBC would be ITV Sales, Channel 4 Sales and Sky Media.

- As we suggest above, placing advertising on the BBC's services may potentially have significant substitution effects on the existing commercial PSBs' inventory, as well as other commercial broadcasters in TV and radio. The resulting reduction in their commercial income would compound pressures on the funding on PSB content further, given the likelihood of increased pressures on the commercial PSBs.
- An ad-funded BBC would risk making virtually all PSB provision reliant on the advertising markets. Spot advertising, particularly on TV, is increasingly challenged in the face of audience transition away from linear consumption. These structural challenges would thus affect all PSB providers and any subsequent impact on content funding would be magnified. It would also make the entire PSB system exposed to concurrent cyclical shocks.
- Advertising creates a direct link between viewing/listening, the delivery of commercial impacts and thus financial returns; this is different from a licence fee (or even subscription) model where value is derived holistically across the full portfolio of content and services. This may force the BBC to cut back on challenging and innovative programming, particularly in peak.
- The introduction of advertising on the BBC's services would create a significant intrusion within and alongside programmes and shift the UK broadcast landscape towards one that is more heavily influenced by commercial messaging. Audiences may ultimately regret the loss of a clutter-free, non-commercial free-to-air environment across TV, radio and online.

#### *A subscription-funded BBC*

- 5.75 A subscription BBC model might replicate that of Netflix and other global SVOD players – placing all the BBC's services behind a pay wall via an online portal; the service could also be made available on connected devices including TVs, mobile phones and tablets and conceivably reach agreements to be bundled within pay TV propositions such as Sky and Virgin.
- 5.76 A voluntary subscription model would by definition limit access to the BBC's services to those with an internet connection and those willing and able to pay and would cease to offer universal access which has historically been the cornerstone of the PSB system.
- Consumer willingness to pay for discrete subscription services continues to grow significantly, driven largely by services from global players. Ofcom<sup>112</sup> reports that 47% of UK households paid for at least one SVOD service in 2019 and evidence confirms that an increasing proportion of homes are taking more than one SVOD service: 18% of households subscribed to at least two of Netflix, Amazon Prime Video or Now TV, and 14% use all three services.
  - The UK's compulsory licence fee is arguably a brake on the take-up of commercial SVOD as it is a *de facto* subscription payment itself. Without the licence fee, it is reasonable to assume that a proportion of existing payers would use any licence fee savings to put toward an SVOD or other service. The BBC has a significant advantage in seeking subscriber growth in its home market, by virtue of an existing powerful corporate brand, strong programme brands and access to talent. Nevertheless, converting all 26m existing licence fee payers to a commercial subscription service would be highly challenging.
  - Some existing licence fee payers claim that they would be willing to pay more than they currently do to access the BBC's services, and the BBC would be able to offer a wide mix of audio and TV services,

<sup>112</sup> See [Ofcom Media Nations: UK 2019](#).

However, in practice, the BBC would need to face commercial reality and price its SVOD service competitively within an increasingly crowded landscape.<sup>113</sup>

5.77 We have suggested a range of outcomes below, based on various subscriber and price levels.

- These outcomes present a significant range of revenues accruing to the BBC; by definition, unless the BBC can charge significantly more than the current licence fee, anything less than 100% take-up would reduce the amount of income that the BBC would secure compared to the current model.
- Some combinations of higher price points and high subscriber rates are not credible but are included for comparative purposes. For example, we think it unlikely that the BBC could persuade a majority of UK homes to pay more than the current licence fee for access to an SVOD service, particularly if the overall outcome resulted in a smaller BBC with less content and less variety.
- We have shaded the most credible options in grey, to illustrate the most likely range of outcomes for a BBC subscription service.

Figure 36: BBC subscription revenues, under different take-up and price points, annual £m (Mediatique)

Relevant benchmark from the US market	Household penetration	Number of BBC subscribers	Revenues, at different monthly price points <sup>114</sup>			
			£7.99	£10.00	£12.88	£15.00
US SVOD penetration <sup>115</sup>	75%	20.7	£1,654m	£2,070m	£2,665m	£3,105m
US homes taking >2 SVOD services	50%	13.8	£1,103m	£1,380m	£1,777m	£2,370m
US Hulu penetration	30%	8.3	£663m	£828m	£1,066m	£1,242m

5.78 Our working assumption is that a BBC subscription service would also give subscribers access to audio services, including BBC radio. The end of free BBC radio would almost certainly stoke demand for subscription audio and the BBC might be able to forge a hybrid service offering radio and audio-on-demand. There is no precedent for subscription radio services outside the US. We have assumed that the BBC might be able to generate up to £240m a year for its audio services, based on a read-across from SiriusXM in the US and Spotify. In practice, the BBC might offer a blended price for access to TV and audio services, but the BBC will be able to drive incremental value from subscribers to audio services however they choose to subscribe.

5.79 A combination of video and audio subscriptions could yield a wide range of financial outcomes for the BBC. However, even in the most optimistic of credible cases, the financial outcome would represent a material reduction in the BBC’s scale compared to its existing £3.8bn of licence fee income; this would also have significant implications for the BBC’s outcome, in terms of scale, breadth and depth. There would also be significant start-up costs for the BBC to create and launch a subscription service, including securing commercial resources, billing technology and marketing expertise.

5.80 A subscription BBC model may have potential effects on market structure and dynamics.

- A subscription model would necessarily limit access to only those households that had paid a subscription. While there are technical solutions to incorporate encryption on all TV platforms, the BBC

<sup>113</sup> A standard Netflix subscription in the UK currently costs £8.99 a month, Amazon Prime Video costs £7.99 per month and Now TV (Entertainment Pass) costs £7.99 a month; the current licence fee costs £12.88 a month, covering all BBC services. More expensive services are available in other territories, largely for significant premium content – for example, HBO Max costs \$14.99 a month in the US.

<sup>114</sup> Price points include VAT ; total revenue calculations exclude VAT.

<sup>115</sup> Broadband TV News, [“Research: 74% of US households have an SVOD service”](#) (2019).

would necessarily stop being a universal service and many households would cease to be able to access the BBC's services.

- One of the main policy advantages of the current licence fee model is that it allows the BBC to invest in a varied mix of content and grants it the ability to appeal to all audiences. By contrast, a subscription operator would rationally focus on producing content that appeals to those with the highest willingness to pay and that is likely to optimise customer retention. This outcome will necessarily prioritise certain audiences over others, leaving some audiences over-served and some ignored. Indeed, the 2015 Select Committee report on funding models for the BBC found that “broadcasting funded through subscription on the whole only caters to pre-existing tastes and encourages people to pay only for things they like”.<sup>116</sup>

We would therefore expect a subscription BBC to focus its investments on drama, comedy, factual and perhaps sport – in line with the output of players such as Netflix or Sky – and necessarily reduce its commitments to other genres. Such a service would also likely target connected households, younger audiences and those in higher socio-economic groups (ABC1).<sup>117</sup>

- The BBC's previous analysis of subscription funding as part of its last Charter renewal found that a subscription model “would harm UK content investment and quality, restrict access for audiences, particularly the poorest, and increase the cost they pay—ultimately damaging the UK's media ecology which is based on competition for quality but not funding”.<sup>118</sup> Indeed, a fully commercial BBC would likely re-assess engagements in PSB ventures or industry bodies (e.g., BritBox, Freeview, YouView) and its overall willingness to cooperate with other PSBs.

5.81 There is a broader existential point here – if a fundamental principle of PSB is that content is made freely and universally available, then a subscription BBC would fall outside this definition of PSB, even if it continued to make content that has PSB attributes or in PSB genres.

#### *A hybrid BBC model*

5.82 A future BBC might follow a hybrid approach, combining multiple funding models – this might include some public funding via a reduced licence fee alongside commercial elements.

5.83 Many media propositions are based on hybrid models that offer customers different options for engagement; this includes ‘freemium’ models that offer a basic level of functionality or choice at a free (ad-funded) price point and access to additional services or functionality for an additional fee (e.g., Hulu, Spotify, ITV Hub+, All4+). One benefit of such a model is that it allows a more effective segmentation of customer demand, enabling operators to match differences in users’ willingness to pay with a specific content offer. This potentially mitigates some of the downsides of a ‘one size fits all’ solution that may leave some audiences under-served.

5.84 These models provide a potential option for the BBC, whereby it could seek to maximise its customer base in an environment where it no longer has guaranteed universality. The BBC might offer an initial freely available layer of content (funded by a smaller licence fee or by advertising) and inviting those with a higher willingness to pay to access additional services for an additional fee.

<sup>116</sup> See [Future of the BBC](#), Culture, Media and Sport Committee (2015).

<sup>117</sup> See [ONS – Internet Users, UK](#): “Virtually all adults aged 16 to 44 years in the UK were recent internet users (99%) in 2019, compared with 47% of adults aged 75 years and over. 7.5% of adults had never used the internet in 2019”. [Ipsos MORI reports](#) that internet penetration among AB males was 97% in Q1 2019; the equivalent figure for DE females was 76%; among DE females aged 65+, the figure was 46%.

<sup>118</sup> See [British, Bold, Creative: The BBC's submission to the Department for Culture, Media and Sport's Charter Review public consultation](#), BBC (2015).

- The BBC might decide to offer its flagship TV channels and radio stations, and on-demand access to content on these services (via iPlayer) as part of the basic offer; any additional services and content would require on-going monthly payments.
- However, every BBC user will have a different concept of what constitutes a ‘core’ service. In practice, there might be a high willingness to pay for these flagship services and an optimal commercial approach might actually place them behind the pay wall.

5.85 We do not believe that any combination of commercial models would lead to an outcome where income would be higher than the current licence fee. Policy makers would therefore need to consider the implications of having a smaller BBC – balancing the potential benefits of a more focussed commercial operation against the downside of a less influential organisation nationally and globally. Many of the issues that face a fully ad-funded or subscription model would still obtain under a hybrid model, including the implications on universality and exposure to cyclical shocks. A hybrid model would also pose specific additional challenges including the costs of running two business models concurrently. The BBC would face costs of securing new relevant skill sets (the BBC has strong production talents and some sales expertise in BBC Studios but has no track record in direct-to-consumer skills and technologies or airtime sales). There is also a question as to whether the BBC would or even should be allowed to take its legacy brand, archive and other assets with it, or might have to compensate the public purse so to do.

#### *Direct funding, including contestable funding*

5.86 A system of direct funding could see policy makers allocate public money directly to PSB institutions or to fund PSB content. The source of this funding could be two-fold:

- General taxation – where PSB content is defined more rigidly as a public service and deserving of direct funding via DCMS; and
- Hypothecated levies – where PSB content is funded by a levy on specific activities, most likely in the form of a digital services tax on online players (including Google, Amazon, Netflix, Facebook, Apple). This option is generally supported by those who feel that domestic broadcasters need to be compensated for the leeching of value towards global players in online markets.

5.87 A digital services tax has already been introduced in the UK from 1 April 2020 with a 2% tax on the revenues of search engines, social media services and online marketplaces which derive value from UK users.<sup>119</sup> There is no suggestion that the proceeds be hypothecated, however.

5.88 An interventionist direct funding model would likely only be possible if recipients committed to the delivery of content that met very tightly defined PSB characteristics or within specified genres – for example, news, current affairs, children’s or arts. Funding could also be made available across the entire audio-visual sectors, including to commercial radio and online providers. A relevant arbiter – DCMS, Ofcom, a new body – would need to determine what share of any overall funding could be allocated to each PSB institution and on what basis; they would also need to prescribe and monitor the delivery of additional obligations in return for such funding. We found no consensus among our interviewees concerning the merits or demerits of direct funding – some broadcasters welcomed the idea of a direct funding source and others resisted the consequences of greater accountability or oversight.

5.89 A less institutionalised model might see funding allocated on a contestable basis – this would allow a range of providers (including existing PSB institutions) to apply or bid for funding to deliver specific content

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<sup>119</sup> As of June 2020, Austria, France, Hungary, Italy, Poland, Turkey, and the United Kingdom have all implemented a digital services tax. Among implemented taxes, the scope and rate vary significantly – some apply only to online advertising, others to any organisation associated with data provision or a digital interface; tax rates vary from 2% (UK) to 7.5% (Hungary and Turkey).

obligations, specific programmes or services. Again, a relevant arbiter would need to administer and monitor the allocation of funding and the delivery of PSB outcomes.

- Such a contestable model could create new suppliers of PSB content and secure additional plurality in the PSB system – with new voices, greater innovation, competition for quality, and the ability to reach new audiences. This model has been considered before: Ofcom decided not to proceed with a Public Service Publisher in 2008 in light of the challenges that such a model poses.
- A fully contestable model risks spreading PSB funding too thinly; it also risks funding content that is unable to secure impact if it is not associated with an established brand that audiences know and use. Policy makers would need to impose rules on what would constitute PSB – this is likely to include an obligation that the content is freely-available without subscription.
- Our interviews confirmed some of the benefits of an institutional PSB structure including the ability of institutions to withstand cyclical shocks and to minimise risks.

5.90 DCMS already operates a Contestable Fund of £60m – the majority of which is used for the Young Adults Content Fund, managed by the BFI and designed to fund up to 50% of production costs for content targeted at under 18s for broadcast on free-to-access platforms; a residual amount is used for the Audio Content Fund to support public service content on radio.<sup>120</sup> The funds come from unallocated underspend from the Broadband Hep Scheme originally funded by the licence fee. This fund is a 3-year pilot scheme<sup>121</sup> but could provide a blueprint for greater targeting funding of PSB content. Some stakeholders raised concerns that this and other schemes may distort incentives and fund content that would have been made anyway.

5.91 Securing direct funding will always face significant political hurdles. Recent licence fee settlements illustrate the desire of governments to reduce direct spending on PSB and PSB-like content including reducing funding for the World Service, BBC Monitoring, S4C and over-75s licence fees. Given the restrictions imposed as a result of Covid-19 on many providers in the creative industries – including theatres, concerts, galleries and festivals – PSB is likely to be far down the list in terms of prioritised assistance at present.

#### *Indirect funding – tax relief*

5.92 Creative industry tax reliefs are currently claimable by those involved in the production and development of the following:

- Films;
- High-end television;
- Children’s television and animation television;
- Video games;
- Theatrical productions and orchestral concerts; and
- Museum or gallery exhibitions.

5.93 Existing PSBs already take advantage of some of the activities on this list to fund their PSB output in drama, high-end natural history and children’s. These tax reliefs are typically subject to minimum spending requirements which preclude the majority of PSB output. For example, tax reliefs for high-end television are only applicable to output in drama, comedy or documentary where the average hourly expenditure is at least £1m.

5.94 There is evidence that these reliefs are highly effective and enable content to be made that would otherwise not be funded. A 2018 report funded by the BFI, Pact and others found that an estimated £632 million in tax

<sup>120</sup> See [Contestable Fund Pilot: Supporting Young Audiences and Audio Content](#), DCMS (2018).

<sup>121</sup> The final year’s funding is subject to review this year.

relief seeded £3.16 billion in direct production spend in 2016.<sup>122</sup> The report also identified significant associated benefits from employment, inward investment, exports and infrastructure.

- 5.95 Our primary research confirmed widespread support among existing institutions to reduce the high-end TV spending thresholds to less than £1m to allow more content to be valid for relief<sup>123</sup> and to widen tax reliefs to other genres (including news, current affairs, arts and religion) or to include radio/audio production. There is also a case to extend tax reliefs to specific content characteristics that remain important to PSB delivery including content made in the nations and regions. Such moves would certainly cement incentives to create PSB content particularly in marginalised genres or locations or those that face funding challenges in the commissioning process. Such an approach would extend the benefits of tax relief through the UK production sector beyond those large producers capable of making high-end drama commissions.
- 5.96 It may even be possible to give PSB institutions special status in the tax system (particularly after the UK exits the European Union) which would have tangible benefits on their ability to fund content; however, this would likely face significant opposition from non-PSB media organisations and limited political support. There is also a risk that new extended tax reliefs are defined too broadly and the scope of this support would need to be reconciled to specific PSB characteristics or else risk supporting output that would fall outside public policy objectives
- 5.97 At present, these reliefs are typically claimed by production companies and incorporated into the budgets of commissioned content – this can of course include the commercial production activities of the BBC and ITV.<sup>124</sup> As such, these reliefs are not focussed on the PSB institutional structure itself, and there are risks of conflicting incentives or outcomes that do not mitigate the pressures on PSB provision specifically. However, it is certainly the case that there are wider economic benefits from these reliefs to the extent that they support the UK’s production sector and enable the creation of valuable exportable rights and formats.
- 5.98 As with all funding models requiring fiscal support from government, additional tax relief will face significant policy barriers in the current political climate. Following the impact of Covid-19 restrictions, there are likely to be pleas for tax relief from various industries (notably leisure and tourism) and there will be limits to the extent to which PSB will be able to secure sufficient traction in the short to medium term.

*Summary of options – changes to public funding models*

5.99 We set out below a summary of our evaluation of options in this category.

Option	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution
<b>Reform of licence fee</b>	Changes to <i>mechanism</i> of licence fee collection unlikely to affect overall scale of BBC funding, but may place BBC funding on a more secure basis (e.g., less scope for evasion)	All decisions on public funding are potentially contentious. A change to the current system inevitably carries that risk that the BBC’s overall funding will be cut or limited

<sup>122</sup> See the [report](#) here, showing UK tax reliefs help fuel boom in the screen sector.

<sup>123</sup> The House of Lords Select Committee on Communications and Digital recently suggested that the £1m threshold incentivised producers to increase budgets unnecessarily in order to be eligible for tax relief; this, they argue “makes it less attractive to produce mid-budget drama, which is crucial to the development of skills in the production sector. High-end TV Tax Relief should be tapered in from £800,000 to remove the incentive to spend more to reach a cost of £1m per hour”. See *Public Service Broadcasting: as vital as ever*, 2019.

<sup>124</sup> By definition, these reliefs can only be claimed by organisations that pay corporation tax which thus precludes the BBC and Channel 4’s public service activities. Channel 4 does not produce content itself; neither does Channel 5, except very limited in-house production in children’s – less than 1% of its total output.

Option	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution
<b>Top slicing of licence fee</b> (e.g., permitting further use of licence fee proceeds by entities other than the BBC)	Recipients of licence fee funding would be protected from cyclical/structural pressures. But overall scale of PSB funding would not be augmented unless the licence fee is increased	Policy makers would need to consider whether a smaller but sustainable PSB system (funded entirely or in the most part by the licence fee) was acceptable
<b>Abolition of licence fee – and transition to a commercial BBC</b> (e.g., subscription, advertising or hybrid models)	Political element of BBC funding would be removed, and the BBC may become more focussed  But scale of output and BBC’s ability to fund current PSB obligations would be significantly curtailed	BBC would require significant upfront investment in commercial expertise  Niche audiences and nations/regions content would be at risk. Future of S4C, World Service, Monitoring, orchestras in doubt
<b>Direct funding of PSB</b> (e.g., hypothecated tax for the BBC, for ‘all’ applicants, and/or new content levies)	Cash funding to the PSBs (or via a contestable fund for new PSB providers) would mitigate pressures on existing funding models	Government support will be required – but creative industries will face significant competition for funding from other industries in the current climate
<b>Indirect funding of PSB</b> (e.g., extending current credit relief to other genres, services)	Tax reliefs are a proven way of targeting investment – and could be directed at specific genres, locations, provider or content categories	Government support will be required – but creative industries will face significant competition for funding from other industries in the current climate

Overall findings

5.100 Our analysis has identified several options to recalibrate the delivery of PSB in light of changing market dynamics. These options vary in terms of impact and are not without practical challenges. As we mentioned at the outset, many of these options are not mutually exclusive and a combination of approaches could be considered to secure the most sustainable outcome for future PSB provision. We have set out in the remainder of this section a summary of our evaluation of these options.

5.101 The reforms under consideration are all aimed at addressing the challenges that we identified in sections 3 and 4 of our report, namely: declining linear audiences; reduced ‘traditional’ TV revenues; intensifying pressures on the licence fee and the concomitant impact on levels of UK content expenditure.

5.102 The specific issues identified, which any reform would seek to address, include:

- 1: The lack of affordable access/prominence in online/digital for PSB providers – particularly to ensure engagement with younger audiences, thus leading to limited (and worsening) bargaining power in relation to distributors (and lack of a level playing field between broadcasters and digital natives)
2. Reduction in PSB output owing to revenue challenges
3. Significant content inflation in key genres and across distribution (upstream/downstream); and
4. A constrained regulatory environment for linear advertising (reducing advertising income).

5.103 It is not within the scope of our work to recommend actions for Ofcom, but we have scored each option on a relative scale based on their impact and their practicability. Our assessment confirms that most viable options for sustaining PSB outcomes are those that extend elements of the existing PSB compact across the PSBs’ full services and augment their bargaining power – this includes updating the regime for prominence and access, and allowing the PSBs to secure attribution and compensation.

5.104 Other options that appear both feasible and that address the issues around sustainability raised in our analysis include extending the current use of tax credits (linked to specific PSB outcomes on content genre,

for example) and creating new content levies, conceivably funded by digital entrants (online video platforms, social media providers) and ‘traditional’ pay TV operators.

5.105 Options that include wholesale reform of the licence fee appear to us to be less practical and effective if the aim is to ensure the sustainability of the PSB compact. Alternatives are likely to raise less money (subscription, advertising) or lead to a two-tier system that erodes universality as a key principle. These drawbacks are not necessarily relevant if the view is taken that the objectives of PSB are no longer to be protected. Direct funding appears more problematic on our assessment, owing to issues around governance and accountability, as well as the likelihood of competing claims on the public purse in a post-Covid-19 period.

5.106 Finally, we underline here that options under review elicit various levels of support from the stakeholder interviews for this report. While there is a broad consensus on the need to protect PSB, and general support for at least some public funding to ensure content outcomes, significant divergences of opinion have emerged. These are summarised in the table following this section (with further details contained in the Annex to this report), and are presented in headline form here:

5.107 Considering our three categories of reform, stakeholder views can be summarised as follows:

- Multi-channel groups, pay TV operators and digital natives oppose the extension of prominence to non-linear content and any suggestion of a regulatory backstop to govern carriage discussions, while all PSBs in favour of such protections; some broadcasters argue in favour of CRR reform (but not outright abolition) but views are mixed among commercial PSBs; there is a similar range of opinion on minutage; understandably, there is strong support for Terms of Trade reform from broadcasters, but this is opposed by external suppliers.
- On funding, extension of the tax credit approach is widely supported by all stakeholders; little appetite for an abolition of the licence fee (and strong views against a subscription-funded BBC from digital natives, multi-channel operators and pay TV platforms; stronger support from non-PSBs for a contestable licence fee but staunch opposition from most (although not all) PSBs; and significant support (except among digital natives) for a new levy applied to, *inter alia*, digital natives.

Impact and effect of funding options – summary table

5.108 Overleaf is a summary table that reviews all of the options evaluated in the module above; it refers to each option’s impact, and whether its introduction would sufficiently address the issues and objectives affecting PSBs and whether there are any ‘trade-offs’ or risks. It also alludes to the level of stakeholder support for each option, and how viable each would be.

5.109 Below we include a key for the four key challenges facing PSBs as surfaced in our analysis; a ‘✓’ or ‘✗’ in the table overleaf is indicative of the option’s ability or otherwise to enable the relevant challenge to be met.

1)	Lack of affordable access/prominence in digital for PSBs – particularly to ensure engagement with younger audiences – and limited, worsening bargaining power in relation to platforms
2)	Reduction in PSB content output owing to revenue challenges
3)	Significant content inflation in key genres and across distribution (upstream); and
4)	A constrained regulatory environment for linear advertising (reducing advertising income)

Figure 37: Summary of PSB options – impact, risks, stakeholder support and viability

Options	Example / details	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution	Stakeholder support	Viability
<b>Category: 1 (Strategy)</b>					
<b>Changes to strategy</b>	e.g., aggressive expansion in SVOD, exclusive arrangements with distributors, closure of channels/services	Self-help options can place the PSBs on more sustainable financial footing – although by themselves do not improve incentives to invest specifically in PSB content	The most valuable approaches here are likely to see greater experimentation with pay/SVOD models, or exclusive arrangements which are not in tune with PSB objectives; closure of services risks reducing reach, viewing/usage and undercutting PSB outcomes	Tacit agreement of all stakeholders PSB players concerned that self-help is not an adequate replacement for regulatory relief	●
		1. ✓ 2. ✓ 3. ✗ 4. ✗			
<b>Cooperation and collaboration</b>	e.g., jointly launching a PSB Player, creating a joint digital sales house, co-operating on virtual CDNs	Working together can improve the PSBs' collective bargaining position, reduce costs and secure synergies	Implications for plurality and diversity if PSBs cooperate too closely. Competition issues may prevent close cooperation particularly upstream (sourcing of content) and downstream (advertising sales, customer acquisition). Divergent incentives may also prevent workable collaboration	Tacit agreement of all stakeholders Some concern expressed by non-PSBs if co-operation is too close on, e.g., airtime trading	●●
		1. ✓ 2. ✓ 3. ✓ 4. ✗			
<b>Consolidation and rationalisation</b>	e.g., ITV-STV merger; BBCS-C4 combination	Formalised tie-ups would protect smaller PSBs, and give greater scale to the PSB players (depending on nature of consolidation)	Implications for plurality if number of PSB institutions is reduced. Potential risk to nations/regions if smaller PSBs lose influence (e.g., S4C, STV)	Tacit agreement of all stakeholders	●
		1. ✗ 2. ✓ 3. ✓ 4. ✗			
<b>Category: 2 (Compact)</b>					
<b>Liberalisation of PSB advertising restrictions</b>	e.g., abolition/reform of minutage limits or CRR system	Uncertainty as to market outcomes if PSB restrictions are equalised (or ad restrictions removed entirely) Some scope for incremental investment from liberalised sponsorship regime or potential for greater PSB ad sales cooperation	An improved financial position for the commercial PSBs is likely to be at the expense of other commercial broadcasters. Appetite for short-term disruption from an ad sales review is limited among stakeholders	PSBs have mixed views on CRR reforms; M/C players broadly supportive of reform but not abolition Changes to minutage elicit wide variety of views	●
		1. ✗ 2. ✗ 3. ✓ 4. ✓			
<b>Changes to Terms of Trade</b>	e.g., remove requirement to share rights with suppliers	A less restrictive rights position for the PSBs would level the playing field when competing with global players or non-PSBs – with potential for incremental value retention in secondary windows	Improving the PSBs' rights position may directly leech value from the UK production sector Too prescriptive an approach (e.g., company size criteria) may distort incentives for the production sector	PSBs argue in favour; suppliers (understandably) are against	●
		1. ✗ 2. ✗ 3. ✓ 4. ✗			

Options	Example / details	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution	Stakeholder support	Viability
<b>Extension of PSB prominence to non-linear</b>	e.g., requiring smart devices to carry PSB players prominently on platform/device home pages	Enables easier discovery of PSB content, and updates the PSB compact in line with market developments	Platforms will argue that imposed prominence stifles innovation and imposes opportunity costs by disfavouring their own services or those of other commercial players. Affording prominence to all content on PSB's non-linear content may promote content that is not necessarily PSB	All PSBs are in favour; M/C and digital natives (including those with operating systems) are against	●●●
		1. ✓ 2. ✓ 3. ✓ 4. ✗			
<b>Right of access for PSB non-linear services</b>	e.g., create a 'must carry' obligation on all platforms	Secures reach for PSB services, and protects smaller PSBs from being ignored or facing significant imbalance in negotiations	Platforms may incur additional costs if forced to carry all PSB services/content	Strong divergence: PSBs in favour, all other players against	●●●
		1. ✓ 2. ✓ 3. ✓ 4. ✗			
<b>Protection of attribution for PSB services</b>	e.g., ensure content from PSBs cannot be 'unbundled' by platforms/operators	Maintains link between PSB brands and underlying content. Also mitigates threat of misattribution and promotes long-term value of PSB brands	Intervention may stifle consumer benefits from highly-functional search/navigation	Strong divergence: PSBs in favour, all other players against	●●●
		1. ✗ 2. ✓ 3. ✗ 4. ✗			
<b>Right to compensation for commercial PSB services</b>	e.g., 'backstop' a requirement for platforms/operators to compensate if terms cannot be commercially agreed	Allows the PSBs the freedom to seek compensation for the carriage of their services – and provide additional funding	Without prescription, there may be no guarantees that any additional value secured by the PSBs in invested in PSB content	Strong divergence: PSBs in favour, all other players against	●●●
		1. ✓ 2. ✓ 3. ✓ 4. ✗			
<b>Category: 3 (Public funding)</b>					
<b>Reform of licence fee</b>	e.g., change to collection mechanisms or status of licence fee	Changes to <i>mechanism</i> of licence fee collection unlikely to affect overall scale of BBC funding, but may place BBC funding on a more secure basis (e.g., less scope for evasion)	All decisions on public funding are potentially contentious. A change to the current system inevitably carries the risk that the BBC's overall funding will be cut or limited	Licence fee is broadly supported, but not necessarily quantum or precise collection mode	●
		1. ✗ 2. ✗ 3. ✗ 4. ✗			
<b>Top slicing of licence fee</b>	e.g., permitting further use of licence fee proceeds by entities other than the BBC	Recipients of licence fee funding would be protected from cyclical/structural pressures. But overall scale of PSB funding would not be augmented unless the licence fee is increased	Policy makers would need to consider whether a smaller but sustainable PSB system (funded entirely or in the most part by the licence fee) was acceptable	Mixed views, even among PSBs; non-PSBs broadly in favour	●
		1. ✗ 2. ✗ 3. ✗ 4. ✗			

Options	Example / details	Impact and contribution to PSB objectives	Trade-offs, risks and ease of execution	Stakeholder support	Viability
<b>Abolition of licence fee – and transition to a commercial BBC</b>	e.g., subscription, advertising or hybrid models	Political element of BBC funding would be removed, and the BBC may become more focussed. But scale of output and BBC's ability to fund current PSB obligations would be significantly curtailed	BBC would require significant upfront investment in commercial expertise Niche audiences and nations/regions content would be at risk. Future of S4C, World Service, Monitoring, orchestras in doubt	Broadly viewed as undesirable among all categories of stakeholder	●
		1. ✗    2. ✗    3. ✗    4. ✗			
<b>Direct funding of PSB</b>	e.g., hypothecated tax for the BBC, for 'all' applicants, and/or new content levies	Cash funding to the PSBs (or via a contestable fund for new PSB providers) would mitigate pressures on existing funding models	Government support will be required – but creative industries will face significant competition for funding from other industries in the current climate	General taxation option seen as problematic; new content levy supported by PSBs, some broadcasters, but not digital natives or pay TV platforms	●●
		1. ✗    2. ✓    3. ✗    4. ✗			
<b>Indirect funding of PSB</b>	e.g., extending current credit relief to other genres, services	Tax reliefs are a proven way of targeting investment – and could be directed at specific genres, locations, provider or content categories	Government support will be required – but creative industries will face significant competition for funding from other industries in the current climate	Tacit agreement of all stakeholders, assuming credit relief available to all	●●●
		1. ✗    2. ✓    3. ✗    4. ✗			

## Appendix: Background information on PSB regulation and the role of Ofcom<sup>125</sup>

### The status of the PSB system and institutions

- The current system is based on a balance between the rights and obligations accruing to these key institutions and is aimed at ensuring that “UK audiences can enjoy a wide range of high-quality programmes that meets people’s needs as citizens and their interests as individuals” as specified in the Act.
- The Act also defines the ‘purposes’ of PSB as the provision of: “programmes that deal with a wide range of subject matter; television services that meet the needs and satisfy the interests of as many different audiences as practicable; television services which are properly balanced, so far as their nature and subject matter are concerned, for meeting the needs and interests of audiences; and programmes which maintain high general standards (including in terms of content, quality of programme making and editorial integrity).”<sup>126</sup>
- Other core documents informing the PSB compact include the Operating Framework and Operating Licence of the BBC, as agreed with Ofcom, and Channel 4’s annual statement of Media Policy. Channel 3 and Channel 5 licensees, along with Channel 4, are issued licences by Ofcom in which various undertakings are specified. These include various remit considerations, such as regional output (specifically news and current affairs), original content undertakings, quotas on commissions from independents and ‘out-of-London’ commitments, as well as ‘must-offer’ obligations (under which PSB channels must be made available, subject to the need to agree terms, to TV platforms).
- The BBC is primarily funded by the licence fee, payable by all households to watch broadcast TV or use iPlayer; the BBC also secures commercial income from a number of permitted commercial activities in the UK and internationally. ITV, Channel 4 and Channel 5 all operate commercial business models. ITV is a listed corporation and Channel 5 is owned by Viacom-CBS; uniquely, Channel 4 is owned by the Government and does not return a profit to shareholders.
- The PSBs are subject to Ofcom’s Broadcasting Code (as are all broadcasters licensed by Ofcom), which includes offence, impartiality and the protection of children; they are also required to fulfil specific quotas relating to programming obligations including output (hours) of news, current affairs and original content; and the commercial PSBs are required to fulfil their specific statutory remits (set out in the Communications Act) and to contribute to the fulfilment of the PSB purposes (s264 Communications Act).
- All PSBs are required to commission at least 25% of their original (qualifying<sup>127</sup>) content hours from independent producers (which must be ‘independent’ of a UK broadcaster).<sup>128</sup>
- In light of its unique funding model, the BBC operates under a far more detailed and quantitative regime, compared to commercial PSBs, as set out in the Operating Framework and the Operating Licence. While the BBC maintains the responsibility for setting strategy, taking creative decisions and allocating resources, Ofcom oversees the BBC in three critical areas – Standards (including complaint resolution); delivery of its mission and public purposes and Competition (ensuring that the BBC operates fairly and transparently).
- While not technically PSB, the contribution of BBC radio (and other audio services from the public service broadcaster) and elements of the content provided by the commercial and community sectors (including news

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<sup>125</sup> The information in this appendix is provided for background only, and is not an exhaustive, definitive treatment of PSB and Ofcom’s role.

<sup>126</sup> Section 264(4), the [Communications Act](#) (2003).

<sup>127</sup> Hours of first-run original content, excluding news.

<sup>128</sup> Defined in [this Glossary](#) by Ofcom.

and current affairs, particularly at local/regional level) contribute to the plurality and diversity of available UK audio content. As Ofcom writes: “The current PSB system is based on television services, but radio and audio also help to ‘inform, educate and entertain’[...] A range of national, local and community radio services continue to contribute to the delivery of the PSB objectives, by producing news, current affairs and programmes that appeal to different communities across the UK.”<sup>129</sup> The BBC radio services are funded by the licence fee and subject to licence terms agreed between Ofcom and the BBC.

### Ofcom’s role in the PSB system

- Ofcom formally reviews the BBC’s delivery every year, and is able to review specific areas of performance on an ad hoc basis.<sup>130</sup> The current operating licence was issued in 2017, and the latest performance review was published in late 2019.<sup>131</sup> Channel 3 and Channel 5 licensees are reviewed for compliance annually, as is Channel 4 (through a review of its annual Statement of Media Content Policy). The current operating licences for Channel 4 and ITV (and STV) run to 2024, although the multiplex licences through which Channel 4 and ITV have digital terrestrial television capacity expire in 2022, as does the licence for the commercial multiplex known as SDN, now owned by ITV plc.<sup>132</sup>
- Ofcom also reviews the PSB system in its entirety every five years. During the last full review, published in 2015, Ofcom summarised the obligations for PSB delivery as follows:
 

*“[PSB is] ...legislated for by Parliament, which requires high-quality content, made for as wide a range of audiences as possible, and for public benefit rather than purely commercial ends. PSB’s mission is essentially the same as Lord Reith’s original BBC dictum ‘to inform, educate and entertain’. Crucially, it should be available to all.”*

*“PSB brings significant benefits to us all. It ensures diversity in the media, plurality in news and it drives programming that reflects and examines society as a whole. Economically, it supports the wider creative industries, and in particular the independent production sector. Non-PSB commercial broadcasters are also providing more content that meets many of the PSB objectives, creating greater choice for audiences. However, their scale of investment remains modest when compared to the PSBs.”<sup>133</sup>*
- At the time of the 2015 review, Ofcom had already pointed to looming pressures on the PSB system, including the growing difficulty of reaching younger audiences. Since then, the challenges have intensified, as measured, for instance, by further declines in PSB reach and viewing, downward pressures on revenues (licence fee and advertising) and significantly greater competition from online video (especially YouTube among younger viewers) and on-demand platforms such as Netflix and Amazon.
- Five years on, as Ofcom writes in its introduction to *Small Screen, Big Debate* (2020): “There have been significant changes in the way in which people watch television. Live broadcast viewing has declined, as

<sup>129</sup> See Ofcom’s [Small Screen: Big Debate](#) (2019).

<sup>130</sup> Ofcom points to a number of regulatory tools to hold the BBC to account in its [Annual Report](#) on the broadcaster: “setting enforceable regulatory on the BBC’s UK public services through the BBC’s operating licence”; “a performance measurement framework to assess compliance with regulatory conditions and examine the BBC’s wider performance”; “an annual report on performance measures and the BBC’s compliance with regulatory conditions”, and “at least two in-depth reviews of the BBC’s performance during the Charter period.” Ofcom can also conduct ad hoc reviews, where [it] feel[s] appropriate.”

<sup>131</sup> See [Ofcom’s Annual Report on the BBC](#).

<sup>132</sup> As described in [a speech made by Nicky Morgan](#), DCMS will consult on the terms of any renewal of the Mux licences: for example, harmonising these with the operating licences to 2024, extending them to 2026 to be in line with commercial multiplex licences held by Arqiva, or even to 2027, when the BBC’s current operating and multiplex licences both expire. Other options might emerge, depending on government policy on PSB and spectrum. For example, the ITV and Channel 4 mux licence might be harmonised or rolled over while the commercial multiplex owned by ITV (SDN) might even be re-advertised and awarded to another bidder.

<sup>133</sup> See [Ofcom’s last full review](#), published in 2015.

audiences increasingly choose to view content at a time that suits them on global online and on-demand content services [...] The broadcasters responsible for the PSB channels are responding to these changes, innovating and offering online and on-demand services to try and meet audience expectation. But these new services have not yet fully made up for the loss of live broadcast viewers, particularly amongst younger people, who increasingly prefer global streaming services, like Netflix and YouTube.”<sup>134</sup>

- As in 2015, Ofcom recognises in its 2020 review the contribution made to the original content market in the UK by non-PSBs: “We recognise the large volume and wide range of content that other television, audio and online services have provided for audiences during our review period. Multichannel commercial broadcasters (Sky especially) and some SVOD services have increased their investment in original UK content although this is typically focused in a comparatively narrow range of genres. YouTube and other online sources provide an enormous volume of content including a long tail of niche interests, but of varying quality and trustworthiness.”<sup>135</sup>

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<sup>134</sup> Ofcom, [Small Screen: Big Debate](#) (2019).

<sup>135</sup> Ofcom, [Small Screen: Big Debate](#) (2019).

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