

# Contents

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<b>Executive Summary</b>	<b>2</b>
<b>1. Introduction</b>	<b>13</b>
1.1 Background, terms of reference, and report structure	13
1.2 General and specific approval conditions	16
1.3 Review process	16
1.4 Consultation results	17
1.5 Conceptual framework: net public value	19
1.6 The BBC's digital TV strategy and its assumptions about audience behaviour	23
1.7 Television is a mass medium, not a niche medium	26
<b>2. Performance Against the Approval Conditions</b>	<b>35</b>
2.1 CBeebies	35
2.2 CBBC	37
2.3 BBC3	41
2.4 BBC4	47
2.5 Interactivity	50
2.6 Driving digital takeup	52
2.7 Value for money	54
2.8 Performance against conditions: summary and conclusions	58
<b>3. Market Impact</b>	<b>63</b>
3.1 Introduction	63
3.2 In what ways might the BBC's services impact the market?	65
3.3 Clarifying the "base case"	66
3.4 Direct impact on commercial channels' revenue	69
3.5 Impact on programme supply market	77
3.6 Impact on long-run competitiveness of the market	79
3.7 Market impact: summary and conclusions	80
<b>4. How Might the Services Develop in the Future?</b>	<b>82</b>
4.1 Summary of conclusions: performance and market impact	82
4.2 The evolving market context and the BBC-TV portfolio	87
4.3 Recommendations for future development	91
<b>Appendix: Ofcom Analysis of Genre Mix</b>	<b>98</b>
<b>Supplementary Reports*</b>	
Report on CBeebies and CBBC, by Máire Messenger Davies	
Report on BBC3 and BBC4, by Steve Hewlett	
Assessment of the Market Impact of the BBC's New Digital TV and Radio Services, by Ofcom	
<b>About the Author</b>	<b>100</b>

## Executive Summary

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This report reviews the BBC's digital television services CBeebies, CBBC, BBC3 and BBC4. Part 1 introduces the issues and framework and presents relevant evidence on viewing behaviour. Part 2 then discusses the four services' performance against their approval conditions. Part 3 gives my assessment of their market impact. Part 4 reviews the conclusions of Parts 2 and 3, describes the evolving market context and the BBC-TV channel portfolio, and gives my recommendations. This executive summary follows the same structure as the report.

### Part 1: Introduction

#### Background and Terms of Reference

In September 2001, Tessa Jowell, Secretary of State for Culture, Media and Sport, approved the BBC's proposals for the relaunch of their digital channels, BBC Choice and BBC Knowledge, as BBC4, CBeebies and CBBC. The BBC's proposal for BBC3 was rejected, and the Governors submitted a revised proposal in December 2001. The Secretary of State gave approval to BBC3 in September 2002. All the approvals were subject to a number of conditions, one of which was that the services would be subject to a review after two years.

On 30 April 2004, Tessa Jowell announced the terms of reference for the independent reviews and opened a public consultation process. I was appointed to lead the television review, alongside Tim Gardam's parallel review of the BBC's digital radio services. The Secretary of State had already written to the BBC Governors in October 2003 asking for their own reports on the performance of the digital television and radio services against the approvals and conditions. The BBC submitted its reports on 19 March 2004.

The BBC stated that the new services had been *“designed to help drive digital take-up, create public value and extend the reach of public service broadcasting”*. According to the Governors' foreword, *“In reaching out to audiences such as the young and ethnic minorities [the digital services] would help reconnect these key audience groups with public service broadcasting”*.

The terms of reference for this review required me to:

- Consider whether, in providing its digital television services BBC3, BBC4, CBeebies and CBBC, the BBC is acting in accordance with the facts and assurances on the basis of which approval to proceed with the services was given;
- Produce an assessment of the market impact of the digital services under review;
- Consider, in the context of the approaching review of the BBC's Charter, what the role of the digital services under review might be within the BBC's overall service;
- Have regard, in reaching these conclusions, to:
  - the BBC's own report on the performance of its digital services and to any subsequent evidence provided by the Corporation;
  - views submitted by other organisations and individuals in response to the BBC's report or in response to the invitation to comment issued by the reviewer; and
  - any additional evidence which the reviewer considers it appropriate to commission;

- Consider whether the reviewer has any views on how these services might develop in the future;
- Submit a report to the Secretary of State, in publishable form, setting out the conclusions of the review and, if appropriate, making any recommendations which the reviewer considers necessary to ensure that the digital services under review are operated in accordance with the terms of the original approval.

### **General and Specific Approval Conditions**

The Secretary of State placed a number of general conditions on the approvals of the television and radio services, as well as conditions specific to each service. They included requirements for the BBC to uphold high standards of content, quality and editorial integrity. The services were also to be promoted in order to encourage digital takeup, through a “vigorous and continuing campaign.” The Governors had to report on the performance of the channels each year in the annual report, and the services would be subject to periodic reviews by the Secretary of State, including an independent review after two years. Although BBC3 was approved a year later than BBC4, CBBC and CBeebies, the approval for it stated that an independent review would take place in conjunction with the reviews of the other services.

The specific conditions for each service, spelt out in Sections 2.1 to 2.4, relate to issues such as each channel's overall positioning and genre mix and the proportion of programming to be specially commissioned, produced within the EU/EEA, and so on.

### **Review Process**

In doing this review, I have received and commissioned a wide range of evidence. I received 65 responses to the public consultation. Of these, one-third came from organisations, including industry and campaigning groups, and two-thirds from individual licence fee payers. I also requested and received extensive further information from the BBC, the Satellite and Cable Broadcasters' Group, Nickelodeon UK, David Graham Associates (DGA) and Ofcom.

For specialist advice, I commissioned reports from Professor Máire Messenger Davies on the children's services and from Steve Hewlett on BBC3 and BBC4. Ofcom has conducted a major study of the market impact of the digital television and radio services (commissioned by DCMS). These reports are published in parallel to this report and are available on the DCMS website; [ww.culture.gov.uk](http://ww.culture.gov.uk). Ofcom also provided an assessment of the BBC's fulfilment of the genre commitments for each channel, the results of which are included in this report.

The Westminster Media Forum held a one-day conference on the radio and television services under review, at which BBC executives and representatives of other stakeholders discussed the evidence on the services' performance. I also held meetings with a large number of BBC staff, various experts on market impact, several commercial broadcasters, the DTI, and two television critics.

Finally, I have of course looked extensively at the services themselves, although I did not have time to conduct a systematic content analysis.

### **Consultation Results**

The consultation results are summarised in Section 1.4. The main pattern was a broad split between the responses from individuals, which were overwhelmingly positive about the new services, and those

from commercial broadcasters, which mainly emphasised the services' market impact. All the consultation responses, other than those which are commercially confidential, are available on the DCMS website ([www.culture.gov.uk](http://www.culture.gov.uk)).

### **Conceptual Framework: Net Public Value**

My overall criterion for judging the services is *net public value*, that is, public value after allowing for market impact. By public value, I mean the overall benefit of the services to the UK public. In practice, my judgements about public value are largely based on my view of the extent to which the services have met their remits combined with my analysis of their direct consumer benefits, especially value for money. The underlying criterion, however, is *net public value*, ie after allowing for any loss of public value resulting from the BBC potentially “crowding out” commercial players from the market. Market impact is an important issue but only part of a net public value evaluation.

### **The BBC's Digital TV Strategy and its Assumptions About Audience Behaviour**

The BBC's digital television strategy seems to be based on the idea that every channel, and even every programme, should have a clearly defined target audience. CBeebies, CBBC and BBC3 (accounting for over 80% of expenditure on the four services) all are explicitly labelled “audience-targeted services” by the BBC. The implicit assumption is that TV audience behaviour is sufficiently strongly segmented to justify the cost and inefficiency of targeting programmes at specific groups.

### **Television Is a Mass Medium, Not a Niche Medium**

Because the BBC strategy and execution put so much emphasis on audience segmentation and targeting, it is important to test its assumptions about audience behaviour against reality. The evidence is clearcut: the adult television audience is only weakly segmented, whether by programme-type preference, channel preference, or demographics. In contrast, children's viewing is strongly segmented by age.

Part 1 concludes with three questions:

1. Given the nature of the medium, is the BBC's strategy the most cost-effective way to “reconnect” with young adult viewers?
2. Given the high cost of BBC3, does it provide public value in terms of good value for money?
3. Given that an important aim of the new services is to help drive digital takeup, and that digital penetration is higher among younger viewers, does it make sense to allocate over 80% of the resources at services targeting younger viewers?

I return to these issues in Parts 2 and 4.

## **Part 2: Performance Against Approval Conditions**

Part 2 assesses the extent to which the commitments and conditions for the approval of the four services have been fulfilled. I have drawn on the reports by Máire Messenger Davies on the children's channels and Steve Hewlett on BBC3 and BBC4, as well as an analysis of the services' genre outputs kindly conducted by Ofcom.

## **CBeebies**

Máire Messenger Davies's assessment is that CBeebies has fulfilled all of its commitments and conditions of approval, except for the commitment to invest in animation co-production, which the BBC acknowledges. She concludes that CBeebies represents excellent value for money as the cheapest of the four services, which also attracts the largest audiences.

Taking also into account Ofcom's assessment of CBeebies' genre output, my own conclusion is that CBeebies is a triumph and an exemplary PSB service for preschool children. It has been extremely successful at reaching and engaging its audience. I also share Máire's view that it has not undermined preschool programming on BBC1 and BBC2.

## **CBBC**

Máire Messenger Davies's judgement is that CBBC is highly distinctive from the commercial children's channels in both content and quality. However she has concerns about the channel's tone and style, as well as some other potential areas for improvement. Another issue relates to the use of the BBC's extensive archive. Máire believes that there should be scope for CBBC to exploit the archive more fully.

I see CBBC as an overall success, but I agree with Máire's concerns about its tone and style. Given the BBC's long experience of successful children's programming on BBC1 and 2, I am confident that it can address these concerns.

I also support Máire's suggestion that the BBC should explore rebranding CBBC to distinguish it more clearly from the children's programmes on BBC1 and BBC2.

## **BBC3**

Steve Hewlett considers that BBC3 has achieved or exceeded virtually all of its many quantitative obligations on genre mix and original production, although he questions the usefulness of the BBC's very broad definition of "specially commissioned" programming. The BBC should be invited to propose a tighter definition, which is closer to the idea of "genuinely new to television". The quota for specially commissioned programming should be reduced to reflect this change.

In his assessment of the degree to which the service has succeeded in its primary purpose of reaching 25-34 year old viewers, Steve concludes that, so far, BBC3's success has been limited. Viewers in this age group have not "reconnected" with PSB television in the way envisaged by the BBC.

I support Steve's conclusions on BBC3, in particular questioning the desirability of aiming a channel at such a small segment of the audience. Despite its generous budget (£99 million), BBC3 has the most challenging remit of all the four services, in terms of its detailed obligations for genre output and original UK production. Its success is being held back by the obsession with targeting the 25-34 age group, which conflicts with the evidence that television is a mass medium, not a niche medium.

My main recommendation is therefore that BBC3's mission should be redefined somewhat, retaining the emphasis on innovation and entertainment but releasing it from the creative straitjacket of its target audience, which is defined too narrowly, and with more emphasis on overall audience share and reach.

## BBC4

Steve Hewlett concludes that BBC4 has met or exceeded most of its commitments, including its responsibility to be the most global and outward looking of the digital channels. However, as with BBC3, he feels that a number of programmes were included under the broad definition of “specially commissioned” which were not genuinely new to BBC4, or which would have been commissioned by BBC2 had BBC4 not existed.

While BBC4 has successfully established itself as “a place to think”, its viewing share and reach are still very low. Part of this stems from its low budget. It is hard to see how it could sustain a full schedule of the quality which viewers expect from the BBC with a budget of only £35 million. BBC4's budget and viewing share are interrelated with digital penetration. Since non-adopters of digital channels are on average older than those who have already adopted, increasing the budget and impact of this channel should take precedence over the other services, especially BBC3. BBC4 also needs to be pragmatic about which programmes work and which do not.

## Interactivity

The new DTV services are all committed to using new technologies to connect with the audience. There are numerous examples of success, perhaps especially on the children's channels but also on BBC3 and 4. This approval condition has certainly been met.

From a public value perspective, the immediate priority should be to improve the speed of the BBCi interactive TV services. It appears that both eTV and the text service 24/7 could be speeded up by 30% on Sky at a cost of £3 million per year. Assuming there are no technical constraints, I strongly recommend that the BBC do this, if necessary funding it by reducing the number of expensive eTV applications per year.

## Driving Digital Takeup

Although the BBC has made a huge contribution to digital takeup through the success of Freeview, the four services' contribution to this success has been small relative to their combined programme budget of £171 million in 2003. The role of the BBC digital services in the takeup of digital pay TV has been minimal. The BBC should allocate resources on free-to-air DTV programmes for all age groups, but, if anything, more for the over-35s than for the under-35s. The BBC has weighted its resource allocation precisely the other way.

## Value for Money

In light of the four services' modest contribution to driving digital takeup, I conclude that their value for money against this criterion is poor. Nor do I consider that the four services have significantly extended the reach of PSB television. Except for CBeebies and, to a lesser extent, CBBC, the new services have made limited impact to-date on their target audiences. Given their resources, the four services taken together represent poor value for money against this criterion.

The services have, however, delivered on their promised citizenship benefits by fulfilling the commitments and conditions of approval, and have operated within their projected budgets. They have therefore met the Governors' commitment to deliver value for money in citizenship terms.

In consumer terms, the services' value for money varies. CBeebies represents remarkable value for money, at around 2p programming cost per viewer hour. CBBC's programming cost per viewer hour has recently averaged under 10p, which also represents excellent value for money. In contrast BBC3 and BBC4, despite improvements over the last six months, have much higher costs per viewer hour, still about 25p.

Taking into account both citizenship and consumer aspects of value for money, CBeebies represents excellent value for money, CBBC very good value for money, and BBC3 and BBC4 fairly good value for money.

### **Performance Against Conditions: Summary and Conclusions**

Section 2.8 summarises the conclusions of Sections 2.1 to 2.7. The main issue is BBC3's and BBC4's relatively poor value for money due to their low viewing shares. These also reduce their ability to reach viewers and drive digital takeup.

## **Part 3: Market Impact**

### **Introduction**

The underlying question for each service in Part 2 was: "Would the public be better off without the service and with the licence fee reduced by an amount equivalent to its cost – assuming nothing else changed?". In each case, the conclusion was that the service's public value was higher than its cost and that the service has largely met its approval conditions. The main area of concern at this, still early, stage is that BBC3 and BBC4 are still delivering very small audiences and therefore represent relatively poor value for money.

The net public value framework, however, also seeks to take account of each service's impact on the market. The assumption in Part 2, that everything else (apart from the licence fee, at the margin) would be unchanged if the service did not exist, may be wrong. For instance, if a particular BBC service competed so successfully for viewers that a commercial service targeting the same viewers was forced to exit the market – even if the commercial service represented better value for money – this would represent a reduction in *net* public value. The same would be true if the BBC service prevented the launch of a new commercial service which would have created more public value.

In general, neither of these situations seems likely in practice. All four new services together currently account for only 2.8% of viewing in digital homes. This is not only significantly less than expected (at least in the case of BBC3) but also less than one-tenth of the BBC's 29% total viewing share in these homes. In a largely unsegmented medium, it is hard to see such small services having much impact on either the market as a whole or on specific competitors.

These arguments are reflected in what has been happening in the market. During the two years since the launch of CBeebies, CBBC and BBC4 (and the year since the launch of BBC3), 44 commercial digital TV channels launched and only 17 withdrew from the market, a net increase of 27 (excluding shopping channels). The idea that the four services, with a combined audience share of only 2.8%, have crowded commercial investment out of the market in general is implausible.

Nevertheless, there might be exceptions. In particular, children – especially young children – have quite different viewing preferences from adults. Although CBeebies and CBBC account for only 1.3% and 0.5%, respectively, of viewing in digital homes, their viewing shares within their target age groups are

much higher: CBeebies attracts 12% of viewing among 4- and 5 year-olds, CBBC 4% among 10-11 year-olds. Their impact on the market in general is likely to be small in absolute terms, but much of that impact is on commercial digital channels targeting the same age groups.

For this reason, Part 3 explores the services' market impact in some detail, drawing on work by Oliver & Ohlbaum (for the BBC) and Ofcom, as well as other experts.

Assessing market impact should be seen as work in progress. It involves conceptual issues as well as issues of technical estimation. Ofcom has proposed – and I agree – that the relevant experts should work together over the next few months to agree a conceptual framework and methodology for this analysis.

### **In What Ways Might the BBC's Services Impact the Market?**

There are four ways in which the BBC's services might impact the market: by encouraging digital takeup, by directly reducing the revenue of commercial channels, by influencing the market for programmes, and by affecting the long-term competitiveness of the market.

#### **Clarifying the "Base Case"**

In evaluating any project or activity (either before or after the event), one needs to consider the "base case" or "counterfactual", that is, what would happen – or would have happened – without the activity. In Section 3.3, I argue that the most valid and useful base case for evaluating the market impact of the four DTV services is one where the services do not exist but digital satellite, cable and Freeview penetration are unchanged. On this basis, my assessment excludes the services' indirect market impact via their (relatively small) contributions towards the growth of Freeview.

Section 3.3 also summarises Ofcom's approach in its study of market impact. Ofcom and I take somewhat complementary approaches but reach very similar conclusions.

#### **Direct Impact on Commercial Channels' Revenue**

I consider it unlikely that the channels have directly reduced commercial channels' advertising revenues except at the margin, since the BBC services have attracted such small audiences. Moreover, owing to advertising price elasticity, a small drop in audience would not lead to a proportionate fall in commercial revenue.

In my view, the direct impact of the new BBC services on channels' revenue from platform subscriptions is extremely small in the short term, and unlikely to change much in the long term.

I also consider it unlikely that the BBC digital services have significantly reduced the revenue of premium channels from consumer subscriptions. Even the premium arts and performance channel Artsworld has probably not lost many subscribers as a result of BBC4's existence, since its small number of subscribers probably watch both Artsworld and BBC4 for only a small proportion of their total viewing. Again, children's premium channels may be a partial exception.

#### **Impact on the Programme Supply Market**

I believe the impact of BBC3 and BBC4 on the programme supply market has been overstated. I do, however, accept ITV's argument that there may be circumstances where public value is reduced if the

BBC competes for high-priced acquired content against a universally available commercial channel, although I believe the argument applies equally to both players (ie the opportunity cost is the same to both players): I see no reason why it is fine for ITV to compete for content but not fine for the BBC to do so.

For CBeebies and CBBC, I am somewhat sceptical about their impact on the programme supply market, but because they are relatively big players in this market (in comparison with BBC3 and 4 in their market), I believe that there may be an issue which merits further work. I note that Ofcom takes a somewhat similar view.

### **Impact on the Long-run Competitiveness of the Market**

It would be hard to argue that the BBC has made the digital TV market less competitive. Freeview has added vigorous competition to Sky and digital cable after the collapse of ITV Digital, to the extent that Sky has now committed to an early launch of its free-to-air "Freesat" platform in what is widely seen as a defensive move.

At the channel level, the impact of the new services has been small but again, the effect has been to make the market more, not less, competitive. I agree with Ofcom's view that "It is unlikely that the BBC's new services have driven, or will drive, any established TV channels out of business".

The two areas where there may be concern about the impact on long-run competitiveness are first, the children's market and second, uncertainty about future BBC developments in digital TV.

As noted, the children's market represents a distinct segment within which CBeebies and CBBC are much bigger players than BBC3 and 4 within the wider market. There may therefore be a case for further work on the market impact of the BBC children's channels (and perhaps CBBC on BBC1 and 2), especially in terms of programme acquisitions and scheduling. My tentative judgement is that at its current scale the BBC is a vigorous competitor in this market rather than an anticompetitive player, but this is a market I know much less well than the main television market, so I am unable to be definitive.

Artsworld and others have argued that, whether or not the BBC's digital television services are having a significant negative market impact – the large number of commercial channel launches suggest that they are not – uncertainty about the BBC's future strategy and possible new services discourages commercial investment and innovation. Even though these concerns may be more about perception than reality, I agree that they should be addressed. I believe that, in practice, the BBC's priority should now be to consolidate rather than to launch new services, but if new services or large changes in programme budgets or strategy are planned, we need transparent mechanisms for such plans to be clearly signalled and discussed. The BBC's June 2004 document Building Public Value is partly designed to address this issue.

Overall I do not see the future development of these services posing a significant threat to competition in the broadcasting market.

### **Market impact: Summary and Conclusions**

This section summarises Sections 3.1 to 3.6.

## Part 4: How Might the Services Develop in the Future?

### Summary of Conclusions: Performance and Market Impact

This section summarises the conclusions I have drawn on performance and market impact in Parts 2 and 3.

#### The Evolving Market Context and the BBC-TV Portfolio

The main trend in television over the last 20 years has been the growth of multichannel TV, mainly funded by monthly subscriptions. In multichannel homes, viewing is spread over many more channels, most of which are single-genre thematic channels. However, the *fragmentation of viewing* has not led to a *segmentation of audiences*. As a result, television has lost some of its efficiency as a mass high-reach advertising medium. The growth of multichannels has also reduced the proportion of total revenue going into programming. More recently, the main trend has been the growth of digital television, although the impact on viewing behaviour has so far been limited.

Turning to the future, much is uncertain, but the following broad trends seem likely. There will be continuing digital penetration mainly driven by BSkyB (including “Freesat”) and Freeview. An evolving revenue mix will grow with the BBC's share of TV revenue continuing to decline. More new channels will be launched by both pure commercial operators and the advertising-funded PSBs (ITV, C4, and possibly five) and the BBC will face stronger competition.

Over the last seven years the BBC TV channel portfolio has grown from two to eight channels. Recent statements by the BBC suggest that it has no plans to expand this portfolio further. I agree with this policy: the evidence is that the BBC's resources are already stretched with eight channels. The priority should now be consolidation, with the aim of maximising the range, quality, and value for money of the existing services. This will also reduce uncertainty for commercial broadcasters. The BBC has also indicated a shift in the programming and scheduling of BBC1 and 2, with more emphasis on traditional public service content. This is an important part of the context for my recommendations on the digital services.

### Recommendations

I list my recommendations for the BBC under four headings, in order of priority. The fifth heading covers recommendations to Government.

#### 1. Increase the Impact of BBC3 and BBC4

The top priority is to increase the audience impact – and value for money – of BBC3 and BBC4 and the overall appeal of the four services, especially among those who have not yet adopted digital television.

- 1.1 The BBC's resources can, with careful stewardship, support four high-quality mixed-genre television channels but not more. Signal that no new services are planned.
- 1.2 Reclassify BBC3 and BBC4 as mainstream mixed-genre channels as opposed to BBC3 as “audience-targeted” (like CBeebies and CBBC) and BBC4 as “special-interest” (like News 24 and BBC Parliament).
- 1.3 Broaden the appeal of BBC3 by focusing less exclusively on stereotypical 25-34s in terms of topics and especially treatments.

- 1.4 Drop the BBC3 news at 7pm which currently means that the channel effectively does not come on air until 7:30. Start the evening with strong programming rather than trying to compete with C4 News and Five News.
- 1.5 Broaden the appeal of BBC4 by giving it more resources (see recommendation 2.2 below) and making it more like Radio 4 and less like Radio 3.
- 1.6 Explore ways of starting BBC3 and, if possible, BBC4 earlier in the evening.

## **2. Focus Resources to Drive Digital Takeup**

Increasing the impact of BBC3 and BBC4 will significantly help drive digital takeup, but it will also be important to focus resources more single-mindedly towards this objective.

- 2.1 Research the viewing preferences of the next 3-5 million homes, ie those who have not yet adopted digital television but whose attitudes suggest that they are the most likely to do so in the next three years.
- 2.2 Increase resources for BBC4, potentially the most important of the four services for driving digital takeup because its age profile matches that of the non-adopters much more closely than for CBeebies, CBBC, and BBC3.
- 2.3 Keep promoting digital television, focusing mainly on the extra TV (and radio) channel choice it provides rather than on the supposed joys of interactivity.

## **3. Incremental Improvements to CBBC**

- 3.1 Improve CBBC's tone of voice and presentation style.
- 3.2 Explore rebranding the CBBC channel to distinguish it from CBBC on BBC1 and 2.

Other issues related to CBBC are the question of whether the archive should be made available to commercial broadcasters (at a 'market price', if this can be determined) and the wider issue of market impact (see recommendation 5.4).

## **4. Other Detailed Recommendations for the BBC**

- 4.1 Speed up BBCi and improve its navigation, particularly 24/7.
- 4.2 Agree a standard definition of reach and use it for all channels.
- 4.3 Consider formally measuring diversity.

## **5. Recommendations for Government**

- 5.1 Ensure that policy uses evidence and analysis to maximise net public value.
- 5.2 Ensure that the BBC continues to drive digital takeup.
- 5.3 Ensure that the BBC has sufficient resources to maximise public value and drive digital takeup.
- 5.4 Ask Ofcom and the BBC to work towards an expert consensus on market impact. Two specific areas which in my view require further analysis are (a) the market impact of CBBC and (b) access to the BBC archive. My tentative view is that forcing the BBC to open its archive for sale would not increase public value, but this is a close call.

## Concluding Comment

To avoid misunderstanding, I stress that I see these recommendations as evolutionary not revolutionary. For instance, although I recommend releasing BBC3 from the perceived need to target 25-34s, I expect it to build on its early successes in edgy comedy and, more generally, innovative entertainment, in a way which will in practice tend to appeal more to younger viewers.

At the same time, increasing the share and reach of BBC3 and 4 in order to get them into more viewers' repertoires and drive digital takeup does not mean either making BBC-TV as a whole more populist or increasing its market impact. On the contrary, the mainstream portfolio as a whole – BBC1, 2,3, and 4 – would almost certainly be less populist than today (depending on the policies for BBC1 and 2), with a slightly lower combined viewing share and market impact. The recommendations for BBC3 and 4 should be seen in that context.

## Part 1: Introduction

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### 1.1 Background, Terms of Reference, and Report Structure

In 1996 the BBC published its plans for a number of new digital television services in *Extending Choice in the Digital Age*. The licence fee settlement of that year stated that the BBC “would now be able to pursue its plans for digital broadcasting.” In 1997, Chris Smith, Secretary of State for Culture, Media and Sport, gave approval “in principle” to specific plans for News 24 and ‘Programme Choice’, as set out in the BBC’s proposal of January 1997. The BBC launched its first digital channel, News 24, in November 1997. BBC Choice followed in 1998 and BBC Knowledge in 1999.

The licence fee settlement of 2000 further supported the development of the BBC’s digital portfolio by endorsing the BBC’s vision to refine and expand its existing channels. As a result, in January 2001 the BBC submitted proposals for replacing BBC Choice and BBC Knowledge with BBC3, BBC4, CBBC and CBeebies.

In September 2001, Tessa Jowell, the new Secretary of State, approved the BBC’s proposals for BBC4, CBeebies and CBBC. Five digital radio services were approved in parallel. The BBC’s proposal for BBC3 was rejected, and the Governors submitted a revised proposal in December 2001. The Secretary of State gave approval to BBC3 in September 2002. All the approvals were subject to a number of conditions, one of which was that the services would be subject to a review after two years.

In October 2003 the Secretary of State wrote to the BBC Governors asking for their own report on the performance of the digital television and radio services against the approvals and conditions, in preparation for an independent review. The BBC submitted its reports on 19 March 2004.

On 30 April 2004 Tessa Jowell announced the terms of reference for the independent reviews and opened a public consultation process, which was from 30 April to 11 June 2004. I was appointed to lead the television review, alongside Tim Gardam’s parallel review of the digital radio services (1Xtra, BBC6, BBC7, BBC Asian Network and Five Live Sports Extra).

Our reviews form part of a rolling programme of independent reviews of the BBC’s new services. The Lambert review of BBC News 24 was published in December 2002 and the Graf review of BBC Online in May 2004. The recommendations from all four reviews aim to contribute to the Secretary of State’s review of the BBC’s Royal Charter ahead of its expiry in 2006.

### Brief Chronology of the Four Services

1998	Launch of BBC Choice
1999	Launch of BBC Knowledge
February 2000	Chris Smith announces Licence Fee settlement, requiring the BBC to “drive the take-up of new digital and on-line services.”
November 2000	BBC consultation on new services closes
January 2001	BBC submits proposals to DCMS
January – February 2001	DCMS consultation on BBC proposals
June – July 2001	DCMS invites consultation on further information requested from the BBC
September 2001	DCMS approves CBBC, CBeebies, BBC FOUR and digital radio channels
December 2001	BBC submits revised proposal for BBC THREE to DCMS
February 2002	CBBC and CBeebies launch
March 2002	BBC FOUR launches
September 2002	DCMS approves BBC THREE
February 2003	BBC THREE launches

### The BBC's objectives in launching the new services

The Governors' foreword to the BBC's report on the four services states: *The BBC's digital services were designed to help drive digital take-up, create public value and extend the reach of public service broadcasting.*

The BBC argued that its research had suggested the need to “reconnect” some audience groups to public service broadcasting. It had especially concluded that young adults were “leaving” the BBC, and that this age group's consumption of all public service television, not just BBC channels, was significantly lower than in the past. BBC3 was specifically developed as a means of countering this trend. The digital radio services were also designed to cater for particular interests, particularly the Asian Network and BBC 1Xtra. According to the Governors' foreword, *“In reaching out to audiences such as the young and ethnic minorities [the digital services] would help reconnect these key audience groups with public service broadcasting”.*

### Terms of Reference

The terms of reference for this review, set out by Tessa Jowell on 30 April 2004, required me to:

- Consider whether, in providing its digital television services BBC3, BBC4, CBeebies and CBBC, the BBC is acting in accordance with the facts and assurances on the basis of which approval to proceed with the services was given;

- Produce an assessment of the market impact of the digital services under review;
- Consider, in the context of the approaching review of the BBC's Charter, what the role of the digital services under review might be within the BBC's overall service;
- Have regard, in reaching these conclusions, to:
  - the BBC's own report on the performance of its digital services and to any subsequent evidence provided by the Corporation;
  - views submitted by other organisations and individuals in response to the BBC's report or in response to the invitation to comment issued by the reviewer; and
  - any additional evidence which the reviewer considers it appropriate to commission;
- Consider whether the reviewer has any views on how these services might develop in the future;
- Submit a report to the Secretary of State, in publishable form, setting out the conclusions of the review and, if appropriate, making any recommendations which the reviewer considers necessary to ensure that the digital services under review are operated in accordance with the terms of the original approval.

## Report Structure

In the rest of Part 1, I first briefly review the new services' approval conditions, the review process, and the consultation results. I then spell out the conceptual framework I have used, based on *net public value*. Finally, I discuss the BBC's digital TV strategy, its assumptions about audience behaviour, and the evidence that television is a mass medium, not a niche medium, which leads me to question some of the BBC's strategic assumptions. In particular, I question the appropriateness of focusing BBC3 (with a £99 million annual programming budget) on such a narrow target market – young adults aged 25–34 years.

This introduction provides the foundation for the other three parts of the report, which correspond to the three main questions I have been asked about the new services.

Part 2 reviews the evidence on the services' *performance against their approval conditions*. Sections 2.1 to 2.4 focus mainly on content issues for each service in turn. These sections draw heavily on independent reports by Professor Máire Messenger Davies (on CBeebies and CBBC) and Steve Hewlett (on BBC3 and BBC4) as well as on a quantitative analysis of the four services' genre mix conducted at my request by Ofcom. Sections 2.5 to 2.7 assess the services' use of interactivity, their contribution towards driving digital takeup, and their value for money.

Part 3 addresses the complex and challenging issue of the services' *market impact*. It draws on recent work by a number of experts, especially the Oliver & Ohlbaum report commissioned by the BBC as part of its submission, a report conducted by Ofcom at the request of DCMS, and preliminary modelling by David Graham Associates (DGA), commissioned by Nickelodeon and the Satellite and Cable Broadcasters' Group. Part 3 covers some tricky conceptual issues and then assesses the services' impact on commercial channels' revenue, programme supply, and the long-run competitiveness of the market.

Finally, Part 4 summarises the conclusions of Parts 2 and 3 (performance and market impact), reviews the evolving market context and the BBC-TV channel portfolio, and gives my *recommendations* for the future development of the four services.

## 1.2 General and Specific Approval Conditions

The Secretary of State placed a number of general conditions on the approvals of the television and radio services, as well as conditions specific to each service. The general conditions were designed to ensure that the services maintain the BBC's overall public service remit and that the Governors would be accountable for them. They included requirements for the BBC to uphold high standards of content, quality and editorial integrity. The services were also to be promoted in order encourage digital takeup, through a "vigorous and continuing campaign." The Governors had to report on the performance of the channels each year in the annual report, and the services would be subject to periodic reviews by the Secretary of State, including an independent review after two years.

Although BBC3 was approved a year later than BBC4, CBBC and CBeebies, the approval for it stated that an independent review would take place in conjunction with the reviews of the other services.

For the television channels, targets for subtitling, audio description and signing were to be monitored by the Governors with a view to achieving the same targets as were being applied to existing BBC channels.

The specific conditions for each service, spelt out in Sections 2.1 to 2.4, related to issues such as each channel's overall positioning and genre mix and the proportion of programming to be specially commissioned, produced within the EU/EEA, and so on.

## 1.3 Review process

I received and commissioned a wide range of evidence. In addition to the 65 responses to the DCMS public consultation, I requested and received extensive further information from the BBC, the Satellite and Cable Broadcasters' Group, Nickelodeon UK, David Graham Associates (DGA) and Ofcom.

For specialist advice, I commissioned the reports from Professor Máire Messenger Davies on the children's services and from Steve Hewlett on BBC3 and BBC4. Both Máire and Steve have in turn requested and received further detailed information from the BBC. Ofcom has conducted a major study of the market impact of the digital television and radio services (commissioned by DCMS on behalf of Tim Gardam and myself). These three reports are published in parallel with this report on the DCMS website [www.culture.gov.uk](http://www.culture.gov.uk). Ofcom also provided an assessment of the BBC's fulfilment of the genre commitments for each channel, the results of which are included in this report.

On June 24, the Westminster Media Forum held a one-day conference on the radio and television services under review, at which BBC executives and representatives of other stakeholders discussed the evidence on the services' performance. Tim Gardam and I found the event constructive, thought provoking, and refreshingly free of well-rehearsed complaints.

I met with a large number of BBC staff, from governors to directors, controllers and channel teams for each of the services as well as other analysts and planners. Other broadcasters, including the terrestrial channels and Sky, were offered meetings but did not take up the offer, having already set out their views in their consultation responses. The Satellite and Cable Broadcasters' Group, whose members own thematic channels such as Nickelodeon and Artsworld, met me together with several representatives of commercial children's channels. I also had a helpful and wide-ranging meeting with representatives of the Department of Trade and Industry (DTI) and an informative and lively lunch with two television critics, Simon Horsford (Daily Telegraph) and Tara Conlan (Daily Mail).

I convened two meetings of experts to discuss the market impact of the services. I invited the BBC, Ofcom, the consultants Oliver & Ohlbaum (who prepared the BBC's report on market impact for this review), David Graham Associates (who had done some preliminary work for Nickelodeon on the impact of CBBC on commercial revenues) and a representative of Nickelodeon. Although we by no means resolved the issue of market impact, the meetings gave me a clearer understanding of the discrepancies between the BBC's and the commercial channels' views of this complex and sensitive area.

Finally, I have of course looked extensively at the services themselves, although I did not have time to conduct a systematic content analysis.

Throughout this review, I have been struck by the helpfulness and courtesy of all concerned. I would also like to thank those who have provided particular support: Karina Grazin (DCMS), Seetha Kumar and Jude de Souza (BBC), Guy Nesdale and Michael Johnson (Ofcom), and of course Máire Messenger Davies and Steve Hewlett.

## 1.4 Consultation Results

I received 65 responses to the public consultation (held in parallel to the radio services consultation). Of these, one-third came from organisations, including industry and campaigning groups, and two-thirds from individual licence fee payers.

The major broadcasters ITV, C4, and BSkyB all submitted responses, together with the Satellite and Cable Broadcasters' Group, PACT, the Arts Councils of both England and Wales, Voice of the Listener and Viewer, and a number of smaller digital channels.

There was a broad split between the responses from individuals, which were overwhelmingly positive about the new services, and those from commercial broadcasters, which mainly emphasised their negative market impact, particularly for BBC3 and CBBC. Only one broadcaster, Artsworld, felt that BBC4 had significantly affected its business.

### Commercial Submissions

Commercial organisations, including both terrestrial and satellite broadcasters, mainly argued that the services were creating a negative impact on the market, reducing competition (or increasing it unfairly), reducing their advertising revenues, and increasing the cost of acquired programming.

As part of its report on market impact<sup>1</sup>, Ofcom analysed those consultation responses which commented on the market impact of the digital services. Submissions from the TV industry made the following specific claims:

- The output of the BBC channels had diverged from their original remits. Some submissions highlighted evidence that there had been a general reduction in factual programming and UK originated content, especially at peak times (eg on CBBC).
- The output and target demographics of the BBC new services were causing significant overlap with the commercial networks' content and markets. This was claimed to have had serious financial effects on commercial enterprises. In addition, submissions referred to a perceived policy within the BBC of aggressive programme scheduling at peak viewing times and, in the case of CBBC, during holiday periods.

<sup>1</sup>Ofcom, *Assessment of the Market Impact of the BBC's New Digital Television and Radio Services, 2004*, available at [www.culture.gov.uk](http://www.culture.gov.uk)

- Concerns were also expressed about the BBC's competitive bidding for commercially attractive programmes, insisting on exclusivity clauses in contracts. Respondents claimed that this practice had inflated programmes prices. It was also argued that the BBC was keeping programmes in its archive for its own digital channels. There were concerns over whether budgets for the new BBC services were appropriate, the perception of some commercial competitors being that the BBC has limitless cash.
- The BBC's cross promotion of its new services was challenged on the grounds that Ofcom rules prevent some commercial networks from cross promoting in the same way.
- Some submissions doubted the BBC's claims regarding the extent to which the BBC's new channels had driven digital TV takeup.

### Individual Submissions

Among the individual submissions, particular praise was directed at CBeebies, including from a number of respondents who had bought Freeview specifically for this channel. CBeebies was considered to be a warm and caring channel which young children could be safely left to watch. In general parents and their children found CBBC fun, enjoyable and educational, although the level of repeats and the broadcasting of 'back to backs' were criticised. We also received a message from an 'anon' child (whose name was in his email address), threatening violent retribution to anyone who shut down CBBC! Máire Messenger Davies discusses the responses on the children's channels in more detail in her report on the performance of CBeebies and CBBC against their commitments.

Individual comments on BBC3 and BBC4 varied between those who considered the new channels a disappointment and those who considered BBC4 alone to be worth the licence fee. BBC4 was praised for its in-depth current affairs and world cinema, although its global news programme *The World* was criticised for poor production values and not achieving the scope or standard of World Service radio.

A recurring criticism was directed at BBC3 for broadcasting *Eastenders* repeats – although a number of responses welcomed this. However almost all those with positive views of BBC3 were enthusiastic about it providing a 'home for British comedy', in the words of one university student.

Many respondents commented on the value for money of the digital services. Although most have not watched or listened to all the new services, some people emphasised that the BBC provided a vast range of television, radio and online choices. In one respondent's view: "It is not an economic argument – the sheer quality for the fee is nothing short of miraculous." In contrast a number of responses lamented the high level of repeats, particularly on BBC3, and suggested that the channel should improve its value for money by broadcasting archive programmes instead, which are seen as different from repeats of new programmes.

Viewers applauded the absence of advertisements on the BBC channels although a few criticised the level of cross promotion or trailers on the BBC as a whole.

DCMS also received a significant number of responses from people who complained that, despite having paid for the digital services through the licence fee, they were unable to comment because they did not have digital television.

All the consultation responses, other than those which are commercially confidential, are available on the DCMS website ([www.culture.gov.uk](http://www.culture.gov.uk)).

## 1.5 Conceptual Framework: Net Public Value

In conducting this review, my overall criterion for judging the BBC's new digital TV services is *net public value*, that is, public value after allowing for both the cost of providing the services and the indirect effects of their market impact.

By public value, I mean the benefit of the services to the UK public. This includes both short- and long-term benefits, both direct and indirect benefits, and both consumer and citizenship benefits.

Assessing these benefits is inherently subjective. The direct consumer benefits (range, quality, value for money) can be partly assessed using objective measures such as ratings or shares, audience appreciation, the cost per viewer hour, and viewers' estimated or claimed willingness to pay. Indirect and/or citizenship benefits (eg from the BBC's investment in UK/regional production and training or in educational initiatives, or its social, cultural, or political contributions to the British quality of life) are generally even harder to evaluate. Ofcom's extensive research for its public service broadcasting review aims to develop practical metrics to help such evaluation without trying to quantify the unquantifiable.

For this review, judging the services' public value is considerably simplified by their rather detailed remits, which include a range of explicit criteria, and by the excellent Messenger Davies and Hewlett reports on their performance against these criteria. In practice, my judgements about public value are largely based on my view of the extent to which the services have met their remits (drawing heavily on the Messenger Davies and Hewlett reports) combined with my own analysis of their direct consumer benefits, especially value for money. I also give my assessment of the services' use of interactivity and their role in driving digital takeup. These assessments are covered in Part 2.

### Allowing for Market Impact

The underlying criterion, however, is *net public value*, ie after allowing for any loss of public value resulting from the BBC potentially "crowding out" commercial players from the market. An important part of this review is my attempt to assess the nature and scale of such market impact, drawing on work by O&O for the BBC, Ofcom, and other experts. This is a rather new and difficult topic which involves conceptual as well as technical estimation issues, as discussed in Part 3.

Market impact is an important issue but only part of a net public value assessment. This may sound obvious, but it appears to be far from obvious to everyone. To some people, public service broadcasting should exist only to compensate for so-called "market failure", that is, to provide programmes which the market will not. The – usually unstated and invariably untested – assumptions here are that:

- Programmes can be divided into clear categories of sheep (which the market will provide) and goats (which it will not), and
- The most cost-effective way of providing the sheep is for commercial broadcasters to have the market to themselves, with no competition from the BBC, and with only "light touch" regulation.

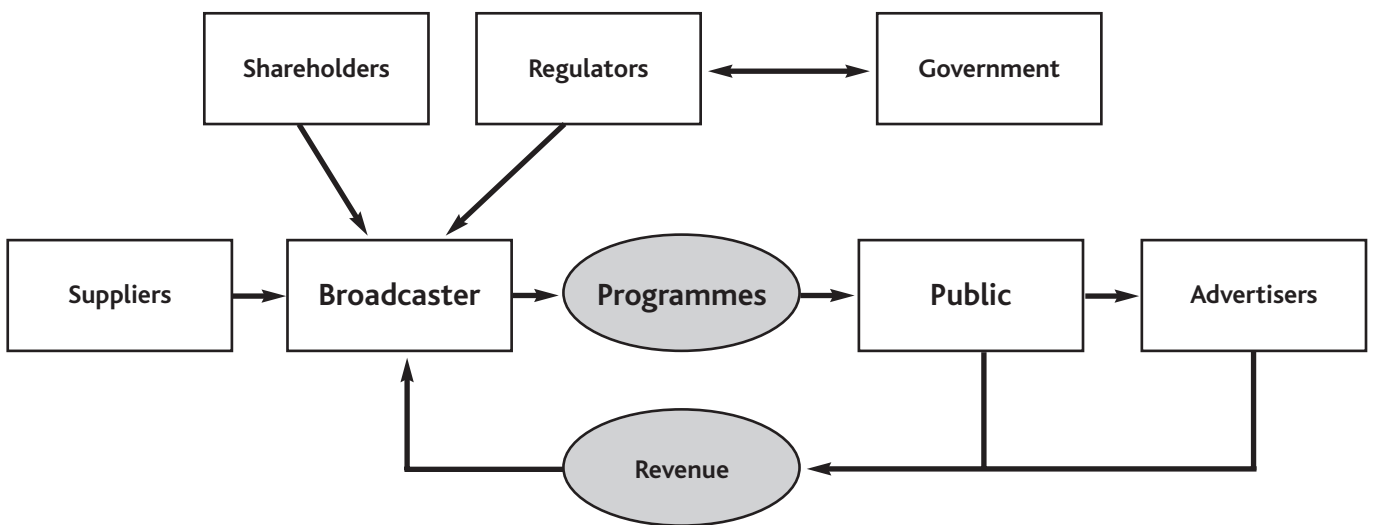
On this basis, commentators – from Financial Times editorials downwards – routinely argue for the scaling back or privatisation of the BBC without providing any evidence or even argument as to why this would benefit the public. The only reason given is that the BBC "distorts" the market. Obviously, this is true in the sense that the market is different from what it would be if the BBC – or any other major competitor – were not there. In fact the BBC "distorts" the digital TV market much less than the

terrestrial TV market, because it is a much smaller player in DTV. But that is not the issue, which is whether the negative effects of such “distortion” outweigh the BBC services’ positive public value, ie *does the BBC’s presence in the market on balance benefit the public?* That is the main question this review aims to address.

**Who Are the Stakeholders?**

Figure 1 is a simplified chart of the stakeholders in the broadcasting market and the main links between them.

**Figure 1: Stakeholders in Broadcasting**



The key item at the centre of the chart is *programmes*. Every programme – indeed, every new episode or edition – is a creative product. Programmes cannot be neatly divided into some types which the market will provide and other types which it will not, nor into programmes for consumers and programmes for citizens. Some genres tend to be more popular than others, some tend to be more challenging, some generally cost more to produce. But every programme (every episode, even) is unique, including in the extent to which it is innovative or derivative.

Similarly, it should be obvious that what viewers mostly want is *more good programmes* (range, perceived quality – in the sense of programmes which are “good of their kind”) and reasonable value for money. In fact, perceived quality matters more than cost to most viewers: watching – and discussing, and reading about – television takes up a far higher proportion of their time and interest than of their expenditure or disposable income. What they mainly want is more programmes which are “interesting and/or enjoyable”. They are less concerned about whether programmes are distinctive: the best (most interesting and/or enjoyable) programmes do tend to be distinctive, but distinctiveness is not an end in itself at either the programme or the channel level.

Nor are viewers very concerned about who makes the programmes they watch, or which channel they are on: with television (radio is somewhat different) people mainly watch programmes, not channels, although especially in multichannel homes, a programme is more likely to be watched if it is on a channel which forms part of the viewer’s regular ‘repertoire’ of, perhaps, eight or a dozen channels, and if they have heard about it in advance through promotion or word of mouth. All of this tends to reinforce the differences between different channels’ viewing shares.

Again, viewers are not interested in whether they form part of the programme's "target audience". As I discuss later (Section 1.7), television is a mass medium largely unsuited for targeting specific audience groups – unlike radio and, especially, print media.

The concept of *more good programmes* obviously raises issues, including that at the margin viewers as citizens believe that some public service programmes may have social value even if they themselves rarely or never watch them. Ofcom's Phase 1<sup>2</sup> review has explored this.

On the supply side, broadcasters are not just economic agents. Most broadcasters care passionately about television and want to make programmes which are both good (original, impactful, admired by other broadcasters) and popular. Their ability to do so depends on resource and other constraints (often, the pressure to minimise costs and maximise ratings), their own talent and skills, and the ethos of the institution(s) funding and producing the programmes.

Because broadcasting is a creative industry, market research has only a limited role in identifying unfilled audience needs, partly because these can evolve in response to the programmes on offer. The main management challenge is to attract talent (both internal and among external suppliers), provide conditions under which people can create a range of programmes they believe will be both good and popular, and then build on what works and drop or revamp what does not.

All of this may, again, sound obvious, but it appears not to be obvious to many advocates of the "market failure" view.

### **Commercial Players' Legitimate Vested Interests**

For this review, the key stakeholder is the public, as reflected in the net public value criterion. But there are other affected stakeholders: the broadcasters themselves, their shareholders (for those which are privately owned), their suppliers, advertisers, and government and the regulators.

The various commercial stakeholders all have a legitimate interest in influencing the scale and nature of the BBC. Quite properly, they represent this interest in their efforts to influence policy, including in their submissions to this review. Less obviously, some of them still seem to assume the equivalent of "what's good for General Motors is good for the United States", despite the new policy emphasis on net public value and on evidence and analysis.

In evaluating the submissions, I have tried to allow for the fact that the BBC has the most at stake and the most sophisticated resources for making its case; after that come the various commercial players (although they vary both in their degree of interest in this review and in their resources); finally, the public themselves, whose voice is limited but whose interests and preferences can – imperfectly – be deduced from viewing patterns, surveys, etc, as well as from individual submissions.

Among the commercial players, most broadcasters and advertisers have a vested interest in minimising the popularity of the BBC, thereby maximising commercial audiences and revenue and reducing competition for programme rights. They therefore typically lobby for BBC services to have tight, well-policed remits which focus on public service and minimise ratings. In the memorable words of Kelvin MacKenzie, head of the TalkSPORT radio station, "the BBC should stick to programmes about sparrows in Serbia" rather than making his life difficult by buying up sport rights using what many of the commercial players see as the BBC's unlimited coffers of cash.

<sup>2</sup>Ofcom, *Ofcom Review of Public Service Television Broadcasting: Phase 1 – Is television special?*, 2004, available at [www.ofcom.org.uk](http://www.ofcom.org.uk)

Each broadcaster's ownership and regulation also influence its view of the BBC. In the context of Figure 1, *public service broadcasting (PSB) is broadcasting regulated to maximise the net public value of the broadcasting system as a whole*. A distinction can be drawn, however, between:

- *Publicly owned PSBs* (BBC, C4), managed and regulated to maximise net public value, and
- *Privately owned PSBs* (ITV, five), managed to maximise shareholder value subject to regulation; and regulated to maximise net public value subject to the constraints of the capital market.

Publicly owned PSBs, including the BBC, are not immune to the “what's good for General Motors” syndrome but do not suffer from the inherent conflict of interest between shareholders and regulators (representing the public) suffered by privately-owned PSBs, as discussed in Ofcom's recent Phase 2 report on public service television<sup>3</sup>.

The success of ITV and five show that this conflict of interest can be manageable, provided there is enough advertising revenue to allow the regulator to impose some PSB obligations while still enabling the broadcasters to meet capital market requirements. The maturing of the TV advertising market (discussed further in Section 4.2) is starting to make this tradeoff more challenging.

For this and other reasons – including an institutional commitment to public service broadcasting – the commercially-funded PSBs are more ambivalent about the scale and scope of the BBC than their purely commercial competitors. For instance, BSkyB's confidential submission to this review consists of 24 closely spaced pages without saying a single positive thing about the BBC. (I should add that it makes a number of valid criticisms of BBC3 and of the O&O report on market impact, but it still gives no reasons why its recommendations would benefit the public). In contrast, ITV's submission supports the case for a strong BBC but criticises the impact of competitive acquisition and scheduling of imported animation on the public benefit of children's television, while C4 frames its criticisms of BBC3's budget and programme output in a value for money and public service context. Five did not submit any comments.

Finally, the suppliers have a simple vested interest in trying to maximise the volume and profitability of business they get from the BBC. The main organisation here is PACT, which represents independent producers. The PACT submission calls for an increased quota for independent productions, fairer terms of trade for producers, and more programmes commissioned from the nations and regions. It, too, fails to spell out the public value benefits of improving the opportunities and rewards available to independent producers. Nor does it address the concern that reduced in-house production and increased independent production might lead to a cutback in training and reinforce the casualisation of production in the UK.

These comments may sound unduly harsh. I am grateful to everyone who submitted their views to the consultation, especially knowing that there have been so many recent reports and consultations on broadcasting policy that a degree of fatigue has set in. But I was disappointed that many of the submissions were short on evidence and analysis and made little attempt to help me evaluate the issues from a net public value perspective.

<sup>3</sup>Ofcom, *Ofcom Review of Public Service Television Broadcasting: Phase 2 – Meeting the Digital Challenge*, 2004, available at [www.ofcom.org.uk](http://www.ofcom.org.uk)

## 1.6 The BBC's Digital TV Strategy and its Assumptions About Audience Behaviour

### Three Key Ideas Underlying the BBC's Mission and Strategy

Underlying the BBC's mission and strategy as an institution are three important ideas:

1. *It exists to serve the whole British public* (which implies, among other things, that as far as possible its services should be universally available and free at the point of use).
2. It has a number of *public service* roles, eg:
  - providing services which entertain, educate, inform and challenge the audience, rather than always seeking to maximise ratings.
  - investing in original UK (including independent and regional) production, in training, and in helping to set high standards for the industry (trust, quality, etc)
  - supporting social and public policy objectives such as digital takeup, e-learning, inclusiveness, and Britain's cultural life.
3. The end of spectrum scarcity, the emergence of new technologies, and the growth of multichannel commercial broadcasting should not reduce the BBC's *long-term public value as part of a mixed broadcasting ecology*, provided it is efficiently managed and continues to deliver on points (1) and (2).

I agree with all three points, although (2) and (3) raise a host of issues beyond the scope of this review. There is, however, an inherent tension between them. Reasonable people can disagree about the best balance between, say, achieving public service benefits (which almost invariably increase costs and reduce ratings – and the market impact on other broadcasters) and being sufficiently popular to achieve (1), partly as an end in itself, partly to ensure continuing public support for the licence fee. These tensions and tradeoffs have always existed and will always exist as long as we have a BBC in anything like its current form.

### The New Services' Strategic Objectives

The relevance of these issues to this review stems from the BBC's objectives in launching its new digital television (and radio) services, summarised in Section 1.1. The stated objectives were largely framed in terms of point (1), supported by research which claimed that young and multicultural audiences were “underserved” and that there was “significant public demand for greater coverage of the arts and cultural issues”. In my view, however, these claims have been greatly overstated.

The idea that young adults are an underserved audience is hard to support. Young adults (especially young, upscale men) tend to be light viewers of television and to choose entertainment programmes rather than, say, news and current affairs. But they are highly valued by advertisers – and therefore by advertising-funded channels (including C4, a major public service channel) – and also by pay-TV operators and channels. In fact, relative to their number and viewing levels, young adults are probably the most *overserved* age group in the population. (Arguably, advertisers overvalue them relative to their spending power and wealth, but that is another matter).

The BBC's claim that multicultural audiences were underserved was more supportable, while still suffering from the problem that if one asks any group within society “are you being underserved?” or “would you like us to provide more good programmes aimed at people like you?”, without also specifying a cost or opportunity cost, the answer is likely to be yes.

Finally, the claim that there was significant untapped demand for more coverage of the arts was, and remains, unconvincing. This does not mean that there was no case for increasing the BBC's arts coverage for public service reasons. It does, however, mean that one should not try to justify such coverage as a response to alleged large-scale consumer demand or as a way to improve value for money. Radio Three has long been the archetype here and raises the same issues and tradeoffs, except that the cost per hour is much lower on radio, enabling many more hours to be produced for a given budget, so the financial stakes tend to be lower.

### **The Real Issue: Young People in Multichannel Homes**

I believe that the BBC's dubious claim that young people were underserved (part of point (1) above) in reality reflected a different and more valid concern, that young people in multichannel homes were not only watching significantly less BBC television than older viewers, but also less than the same age-group in terrestrial-only homes and, crucially, less than previous cohorts at the same age. (For instance, someone born in 1980 on average watches less BBC-TV than someone born in 1970 did ten years ago, and to a greater extent than the equivalent comparison for older age groups). This concern mainly relates to point (3), the long-term relevance and future of the BBC.

The potential long-term decline in the BBC's share of viewing is a complex issue which requires further work. My personal belief is that the BBC is right to be concerned, but not as concerned as it seems to be, especially given the brilliant success of Freeview and the BBC's high viewing share in Freeview homes. Comparisons between cohorts (people born in different years) are complicated by the growth in the penetration of new platforms and channels, including commercial channels aimed at young adults, and the fact that multichannel penetration is higher in homes with younger viewers. If in 2024 the BBC still makes good programmes with broad appeal, today's 20-somethings will watch them, provided they are shown on channels with sufficient reach and familiarity.

Whether the aim is to serve allegedly underserved groups or to increase the BBC's viewing by young people in order to ensure its long-term role and relevance, the key issue is the BBC's strategy for addressing the problem. In the context of the digital TV services covered by this review, the strategy was to allocate the main resources (£95m in the original proposal) to a channel targeting young adults – BBC3 – with £41m for the two children's services (which became CBeebies and CBBC) and £31m for what became BBC4.

### **Market Segmentation, Targeting and Positioning**

This strategy is based on the classic textbook marketing concepts of market segmentation, targeting, and positioning<sup>4</sup>. But successful marketers are pragmatists. They use these concepts when and where the benefits (a better match between what they are selling and the needs and habits of target customers) exceed the costs (greater complexity and/or fewer customers).

Obviously, someone selling a specialist industrial product such as oil drilling equipment will target a specific sector and someone making dogfood will try to target dog owners. Ideally, a dogfood manufacturer would actually like to segment the market further, aiming its premium products (highest cost/gram) at the owners of the most pampered dogs – eg those that sleep in the owner's bedroom as opposed to the kitchen, garage, or (lowest cost/gram) a kennel in the yard.

<sup>4</sup>Philip Kotler, *Marketing Management*, 11th Edition, Prentice-Hall, 2003, Chapters 10 and 11.

In practice, however, marketing is the art of the possible. Dogfood manufacturers still advertise heavily on television despite knowing that most viewers of their commercials do not own dogs. It is possible that digital technology will eventually enable them to avoid this wastage, eg using store-card data and individual addressability to ensure that their advertisements go only to homes with dogs and even that those for premium products go only to homes which buy those products or might be persuaded to do so. But that is not the reality today or, in practice, any time soon.

A key distinction here is between traditional and direct (or “one-to-one”) individualised marketing. The most successful mass consumer marketer in Britain today is Tesco, which does both. Like the BBC, Tesco aims to be a trusted brand which serves the whole British public. In addition, through Clubcard, it has a direct relationship with 10 million individual consumers, allowing it to use micro-segmentation in its mailings and associated special offers. It is also the biggest online grocer in the world. BSkyB has just hired Dunn Humby, the specialist database analysis consultancy behind Clubcard, to improve its direct marketing. But in its product range and its stores, Tesco is still a mass marketer which does not target a single specific segment but aims to be simply better than its competitors at providing range, quality, service, convenience, a pleasant shopping experience, and value for money for the whole population under the slogan “every little helps”<sup>5</sup>.

### **The BBC's Continuing Obsession with Segmentation and Targeting**

The BBC is a relative newcomer to modern marketing but has become adept at branding (eg its channel identities), promotion (eg Freeview) and cross-promotion (eg it now prioritises its messages ruthlessly). It does however, appear unduly obsessed with segmentation, targeting and positioning. These are powerful concepts where they work, for instance with print media and, to a lesser extent, radio, and in most business-to-business markets. But television is not a strongly segmented medium. It is a mass medium, not a niche medium, and the evidence is that this will continue regardless of the number of channels. (This might change somewhat in a fully-digital world with individual addressability – equivalent to Tesco's Clubcard database – but this is unlikely to be a significant factor in the next 10 years).

The BBC is full of bright, enthusiastic people. Sometimes, it overcomplicates things. A few years ago, its planning and strategy group excelled itself with its notorious 250-page document, *100 Tribes*. This broke the UK population down into dozens of so-called “smart demographic” segments defined by age, life stage, gender, attitudes and interests<sup>6</sup>. In a market such as television, which is only weakly segmented, it is hard to see how *100 Tribes* could have encouraged clear and valid strategic thinking, intelligent resource allocation, or programme-making creativity (quite apart from the sloppy use of the term “tribe” which would, I suspect, horrify most anthropologists).

Although the BBC's digital television strategy is not (or is no longer) based on this kind of extreme segmentation, it still seems to be based on the idea that every channel, and even every programme, should have a clearly defined target audience. The implicit assumption continues to be that TV audience behaviour is sufficiently strongly segmented to justify the cost and inefficiency of targeting programmes at specific groups.

<sup>5</sup>Clive Humby and Terry Hunt, *Scoring Points: How Tesco Is Winning Customer Loyalty*, Kogan Page, 2003; Patrick Barwise and Seán Meehan, *Simply Better*, Harvard Business School Press, 2004, pp. 89-94.

<sup>6</sup>Georgina Born, *Uncertain Vision*, Secker & Warburg, 2004, pages 284-286.

The main segmentation variable in this strategy is age. The BBC proposed to allocate over 80% of the resources for the new services to channels targeting viewers under 35 (£136m for CBeebies, CBBC and BBC3 out of £167m total including BBC4). The fourth channel, BBC4, was to be targeted not at a specific age group but at viewers defined by their interest in more challenging programmes and topics: arts, sciences, history, current affairs, world cinema, etc. In practice, these viewers tend to be older, but not exclusively so.

## 1.7 Television Is a Mass Medium, Not a Niche Medium

Because the BBC strategy and execution put so much emphasis on audience segmentation and targeting, it is important to test its assumptions about audience behaviour against reality. The evidence is clearcut: the adult television audience is only weakly segmented, whether by programme-type preference, channel preference, or demographics.

### Only Weak Programme-Type Loyalty

Common sense suggests that someone who watches a programme of type X is much more likely to watch many other programmes of the same type. In this case, common sense is wrong. The near-absence of programme-type loyalty has been known for over 30 years and replicated many times<sup>7</sup>. For this review, I asked the BBC's extremely efficient audience research department to run some new analyses of viewing behaviour, specified by me. The results are in line with previous figures.

For example, in the last week of August 2003, the top-rating drama series was ITV's *Alibi*, watched by 9.5% of individuals aged 4+ in digital homes (average minute rating). One might suppose that those who watched *Alibi* were avid viewers of drama series in general, but they were not. If we look at their viewing the following week, we find that they watched a total of 28.7 hours of television, of which just 3.4 hours (about 12%) were of drama series<sup>8</sup>. For the top five drama series in the first week, this was typical: their viewers on average allocated about 12% of their following week's viewing to drama series – the exact figure is 12.1%.

This 12.1% was, as one would expect, higher than the proportion of viewing devoted to drama series that week by viewers of other programme types the previous week – but only just. For instance, viewers of the top five arts programmes in the first week (*Arena*, *South Bank Show*, *Newsnight Review*, *Talking Movies*, *The Story of Art Deco*) allocated 9.8% of their second week's television viewing to watching drama series.

Table 1 shows the equivalent calculation for all 16 of the BBC's standard programme genres. This shows that viewers of drama series were not a distinct segment. They were only about 20% more likely than the viewer of the average programme to watch a randomly-selected drama series the following week (12.1% vs 10.1%).

Much the same pattern applies to all programme types. Proportionately, the biggest exception was formal education programmes (four *Open University* programmes and one from the *BBC Learning Zone*). This genre accounted for just 0.4% of the viewing of the average programme audience from the previous week, against 1.9% of the viewing of the average education programme audience – a ratio of almost five to one. But that still meant that over 98% of the latter's viewing in the second week was of other genres. Even viewers of *Open University* programmes – an extreme case – devote almost all of their viewing to the same programmes as everyone else.

<sup>7</sup>GJ Goodhardt, ASC Ehrenberg and MA Collins, *The Television Audience: Patterns of Viewing*, Saxon House, 1975 and 1987; Patrick Barwise and Andrew Ehrenberg, *Television and its Audience*, Sage, 1988; Virginia Beal, Patrick Barwise and Martin Collins, 'TV Viewing Patterns: Are Viewers Loyal to Program Genres?', Research Report 18, The R&D Initiative, South Bank University and the Marketing Science Centre, University of South Australia, August 2004.

<sup>8</sup>Among all individuals in digital homes, the average viewing level the following week was 23 hours, typical for the time of year. The higher figure of 28.7 hours for viewers of *Alibi* reflects a well-established statistical selection effect: viewers of any specific programme tend to be heavier than average viewers of television in general (because heavier viewers are more likely than the average person to watch it).

**Table 1: % of Viewing Allocated to Drama Series in Week Ending 7 September 2003 Among Viewers of the Average Top-5 Programme of Each Programme Type in Week Ending 31 August 2003**

<b>Viewers of the Average Top 5 Programme w/e 31.8.03 (Individuals 4+)</b>	<b>% of Following Week's (w/e 7.9.03) Viewing Allocated to Drama Series</b>
<b>Drama series</b>	<b>12.1</b>
Hobbies/leisure	11.6
Drama: soaps	11.5
Religious programmes	11.2
Films: made for TV	11.0
Sport	10.3
Films: cinema	10.2
Entertainment	10.1
Music	10.1
News/weather	10.1
Documentaries	10.0
Arts	9.8
Children's programmes	9.5
Current affairs	9.4
Drama: single plays	8.5
Education (Open University/Learning Zone)	7.6
<b>Average (excl drama series)</b>	<b>10.1</b>

Source: BBC analysis of BARB

### **Channel Loyalty Is Also Weak**

Similarly, television channels do not have separate, loyal audiences. Table 2A shows how viewers of BBC3 during the week ending 31 August 2003 allocated their viewing across channels during BBC3's transmission hours (1900-2600) the following week. Even for these self-selected viewers, and limiting the analysis to the channel's transmission hours, BBC3 was ranked only seventh, with a 2.8% share.

This is not to say that there is no channel loyalty. Table 2B gives the equivalent analysis for viewers of BBC4. The rankings and shares are very similar to those in Table 2A for viewers of BBC3, but not identical. For instance, the rankings of C4/S4C and BBC2 are reversed in the two tables. BBC4 itself goes up from rank 27 (0.5% share) among those who watched BBC3 the previous week to rank 10 (1.4% share) among those who watched BBC4 itself the previous week. But a 1.4% share during its transmission hours still leaves BBC4 as a very small part of its own audience's viewing – half the size of Sky One, about one-fifth the size of BBC2, C4, and five, and well under one-tenth the size of ITV1 and BBC1.

**Table 2A: Channel Shares (1900-2600) During Week Ending 7 September 2003 Among Viewers of BBC3 During Week Ending 31 August 2003**

Rank	Channel	Share %
1	ITV1	21.5
2	BBC1	18.9
3	C4/S4C	7.0
4	BBC2	5.7
5	five	5.3
6	Sky One	3.2
<b>7</b>	<b>BBC3</b>	<b>2.8</b>
8	ITV2	2.7
.	.	.
27	BBC4	0.5
.	.	.
—	Others	32.4
—	<b>Total</b>	<b>100%</b>

Source: BBC analysis of BARB

**Table 2B: Channel Shares (1900-2600) During Week Ending 7 September 2003 Among Viewers of BBC4 During Week Ending 31 August 2003**

Rank	Channel	Share %
1	ITV1	19.0
2	BBC1	18.3
3	BBC2	8.0
4	C4/S4C	7.0
5	five	6.0
6	Sky One	2.8
7	ITV2	2.3
8	<b>BBC3</b>	<b>2.0</b>
.	.	.
<b>10</b>	<b>BBC4</b>	<b>1.4</b>
.	.	.
—	Others	33.2
—	<b>Total</b>	<b>100%</b>

Source: BBC analysis of BARB

## Children Are Different

The weak channel loyalty of BBC3 and BBC4 is not an aberration. It is normal for channels aimed at adult viewers. Children – especially small children – are different.

Table 3 shows the equivalent analyses to the last two tables but for viewers of CBeebies and CBBC, with the analysis limited to children in each channel's target age range (4-5 years for CBeebies, since children under 4 are not measured by BARB; 6-13 for CBBC) and to viewing during the channels' transmission hours of 0600-1900. In both cases – especially CBBC – viewing is spread over a larger number of channels than for adults (despite the analysis being restricted to daytime and early evening) so I have increased the number of channels listed to 10 and 12 respectively.

The key point is that, whereas viewers of BBC3 and BBC4 have strikingly similar channel preferences and show little loyalty to these channels (shares of only 2.8% for BBC3 in Table 2A and 1.4% for BBC4 in Table 2B), viewers of CBeebies and, to a lesser extent, CBBC show a quite different pattern. For viewers of CBeebies (aged 4-5), it was easily their most-watched channel the following week during its transmission hours, with a share of 24.2%. Their second favourite was Nick Jr (12.1%), while three other children's channels were in their top ten (Boomerang, Fox Kids, Cartoon Network). For these self-selected CBeebies viewers, the four BBC channels captured 37.4% of their daytime and early evening viewing the following week, mainly on CBeebies itself.

As one might expect, the pattern for CBBC viewers aged 6-13 fell in between those for viewers of CBeebies aged 4-5 and those for viewers of BBC3 and BBC4. The four BBC channels captured 36.4% of their daytime and early evening viewing.

Table 3 is based on small samples and the transmission hours restriction somewhat exaggerates the difference between children's and adults' viewing preferences, but the results are consistent with previous research: children, especially young children, have markedly different viewing preferences to those of adults. They represent the main exception to the general rule that television is a mass medium, with only weak segmentation, not a niche medium.

**Table 3 Channel Shares (0600-1900) During Week Ending 7 September 2003 Among Viewers of CBeebies (4.5 years) and CBBC (6.13 years) During Week Ending 31 August 2003**

Viewers of CBeebies (4-5)			Viewers of CBBC (6-13)		
Rank	Channel	Share %	Rank	Channel	Share %
1	<b>CBeebies</b>	<b>24.2</b>	1	BBC1	11.8
2	Nick Jr	12.1	<b>2</b>	<b>CBBC</b>	<b>10.9</b>
3	BBC1	5.5	3	ITV1	10.0
4	ITV1	5.5	4	BBC2	8.2
5	BBC2	4.4	<b>5</b>	<b>CBeebies</b>	<b>5.5</b>
6	Boomerang	4.4	6	Five	4.5
7	Fox Kids	4.4	7	C4/S4C	3.6
8	Five	3.3	8	Cartoon Network	3.6
9	Cartoon Network	3.3	9	Nickelodeon	3.6
<b>10</b>	<b>CBBC</b>	<b>3.3</b>	10	Sky One	2.7
–	Other	29.6	11	Boomerang	2.7
			12	ITV2	2.7
			–	Other	31.2
	<b>Total</b>	<b>100%</b>		<b>Total</b>	<b>100%</b>

Source: BBC analysis of BARB

## Channel Reach

Another way to look at channel loyalty is to break the viewing of each channel down into its reach – the percentage of people with access to the channel who watch it at all during a given time period – and its *average hours per viewer* over the same time period<sup>9</sup>. The usual time period for measuring reach is a week.

Weekly reach is a useful metric now employed widely within the BBC, reflecting the corporation's aim of serving the whole population. For instance, this aim is seen as one reason for most of the BBC's TV channels to be multigenre (the only exceptions being BBC News 24 and BBC Parliament): the argument is that a multigenre channel will provide something of interest to a wider range of viewers than a single-genre channel. As we have seen, programme-type loyalty is so weak that, in practice, a multigenre programming strategy is unlikely to make a huge difference, but for a given audience share it will increase channel reach at the margin.

Another benefit of reach is political. From time to time, opponents of the BBC suggest that, once its viewing share falls below some arbitrary level, say 25%, it will no longer be sustainable to fund it through a compulsory licence fee, since this is unfair on people who do not watch or listen to the BBC. In this context, the BBC rightly focuses on the reach of its services. In reality, the licence fee works much better in practice

<sup>9</sup>TP Barwise and ASC Ehrenberg, "The Reach of TV Channels", *International Journal of Research in Marketing*, 1, 1984, 37-49 and Patrick Barwise and Andrew Ehrenberg, *Television and its Audience*, Sage, 1988 pages 69-71. In order to count as having watched a channel, a viewer must have done more than look at it for a few moments while "surfing" for something to watch. The usual cutoff is 15 continuous minutes (ie to count as a viewer, someone must have watched the channel for at least 15 continuous minutes at some point during the analysis period). Unfortunately, as noted by Steve Hewlett, the BBC sometimes uses 3-minute reach, sometimes 15-minute reach, which makes comparisons difficult. One of my recommendations is to standardise on 15-minute weekly reach.

than in theory: only a tiny number of homes pay it but do not regularly watch or listen to the BBC, and taken as a whole, the cost per viewer-hour is significantly less than for pay TV, despite the BBC's public service obligations. This reflects the efficiency of the licence fee as a revenue source in a mixed broadcasting economy.

In talking to BBC executives, however, I received the impression that, at least for some of them, the focus on reach went so far that they assumed that it was not only much more important than share but also almost independent of it. It is a matter of opinion whether, or under which circumstances, share or reach is more important, but what is not a matter of opinion is that – with a few specific exceptions – the two are closely interrelated. In other words, even if the aim is to increase reach, the only way to do this significantly is to increase share. Similarly, it is share, not reach, which determines the cost per viewer-hour, the main measure of consumer value for money.

Table 4 shows the share, weekly reach, and average hours per week per viewer for the top 20 digital channels plus the smaller BBC digital channels (with CBBC and BBC4 highlighted) among all individuals in digital homes during the most recent calendar quarter, 2Q 2004. These figures were again kindly compiled for me by the BBC audience research department.

**Table 4: Share, Weekly Reach, and Average Hours/Viewer**

(Individuals aged 4+ in digital homes, 2Q 2004)

Channel	Share %	Weekly Reach %*	Ave Hours/Viewer
<b>BBC1</b>	<b>19.5</b>	<b>84</b>	<b>5.7</b>
ITV1	18.1	80	5.5
C4	7.7	66	2.8
<b>BBC2</b>	<b>6.2</b>	<b>63</b>	<b>2.4</b>
Five	5.0	51	2.4
Sky One	2.2	31	1.7
Sky Sports 1	1.7	17	2.5
ITV2	1.6	28	1.5
E4	1.5	19	1.9
<b>CBeebies</b>	<b>1.3</b>	<b>11</b>	<b>2.8</b>
UKTV Gold	1.3	20	1.6
Hallmark	1.0	8	3.1
Living	0.9	15	1.5
Sky Sports 2	0.7	10	1.8
Boomerang	0.7	9	2.1
Plus	0.7	9	2.0
<b>BBC3</b>	<b>0.7</b>	<b>21</b>	<b>0.8</b>
Sky News	0.7	11	1.4
Sky Sports News	0.7	15	1.1
UK TV Gold+1	0.6	14	1.1
–	–	–	–
BBC News 24	0.5	11	1.2
<b>CBBC</b>	<b>0.5</b>	<b>7</b>	<b>1.6</b>
<b>BBC4</b>	<b>0.3</b>	<b>8</b>	<b>0.8</b>
BBC Parliament	0.01	1	0.6

Source: BBC analysis of BARB

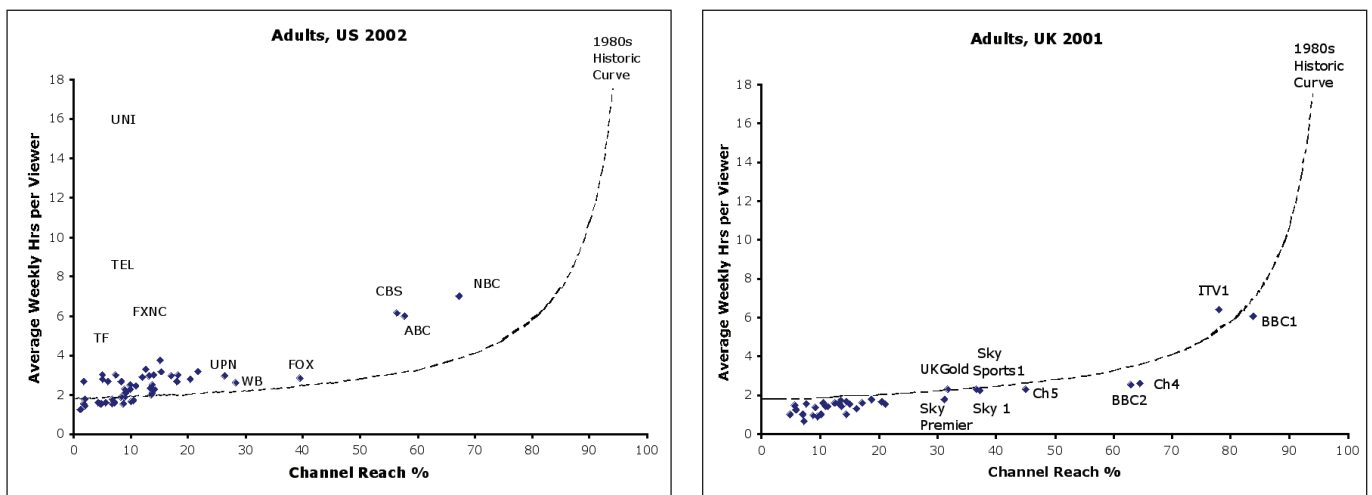
\*3+ continuous minutes

### The Main Pattern: Double Jeopardy

The main pattern is that the biggest channels, BBC1 and ITV1, have very high reach and also high hours per viewer, while small channels tend to suffer the so-called *double jeopardy* of lower reach and lower hours per viewer. There are no niche channels with very low reach but hours per viewer as high as or higher than BBC1 and ITV1.

The double jeopardy pattern for these channels is normal. Figure 2 shows results for adults in both the USA and UK, including the historic curve from the same analyses in the 1980s. Two major exceptions were observed in the earlier research in the USA: both Hispanic channels and religious channels had very low reach but some of them had average hours per viewer comparable to the main networks. (However, those who watched these minority channels – including the Hispanic ones – were also heavy viewers of network TV).

**Figure 2: Weekly Reach and Average Hours per Viewer: USA and UK<sup>10</sup>**  
(Adults in Multichannel Homes)



The US results in Figure 2 replicate both the main pattern and the exceptions, while tentatively finding that the main broadcast networks (NBC, CBS, and ABC) have somewhat lower reach and higher hours/viewer than predicted for their share. The same holds more dramatically for the Fox News Channel (FXNC in Figure 2), which in terms of reach and hours/viewer rather amusingly falls somewhere between a regular (eg news) channel and a religious channel. The UK results fit the historical pattern closely but with the channel loyalty (average hours per viewer) for small channels if anything even lower than in the 1980s – the very opposite of a “niche” pattern.

During discussions, one consultant referred to double jeopardy as a “theory”. This is wrong. Double jeopardy is not a theory, it is the label for an “empirical generalisation”, that is, a phenomenon which has been observed repeatedly over many years in a wide range of contexts such as the audience’s liking of radio announcers (where it was first observed in the US over 40 years ago) and the repeat-buying of consumer packaged goods. In television, it has been observed for both the repeat-viewing and the audience appreciation of regular series, as well as for channel reach and average hours per viewer<sup>11</sup>

<sup>10</sup>US data from Martin Collins, Virginia Beal and Patrick Barwise, “Channel Use Among Multi-Channel Viewers”, Research Report 15, The R&D Initiative, South Bank University and The Marketing Science Centre, University of South Australia, March 2003. UK data from BARB (w/b 1 September 2003).

<sup>11</sup>William N McPhee, *Formal Theories of Mass Behaviour*, Free Press, 1963, ASC Ehrenberg, GJ Goodhardt and TP Barwise, *Double Jeopardy Revisited*, *Journal of Marketing*, 54, 3 (July 1990), 1982-1991.

Double jeopardy and other “mass behaviour” patterns do not mean that viewers or consumers are all the same: “mass” does not mean monolithic. On the contrary, the patterns reflect the fact that every individual is different and that people cannot be fitted into neat clusters or segments. Double jeopardy stems from the way in which these individual differences are statistically distributed across the population (Ehrenberg et al 1990).

### Sub-Patterns and the New BBC Services

In the UK, no major exceptions have been reported to the double jeopardy pattern similar to the Hispanic and religious channels and the Fox News Channel in the USA (although we can conjecture that S4C and recently launched UK ethnic and religious channels may be similar). Closer inspection of Table 4 shows a number of subpatterns, however.

First, as one would expect, *children's channels* are different, with relatively low reach and high hours/viewer. CBeebies had a weekly reach of only 11% (mainly young children and their young adult parents) but its average hours/viewer, at 2.8, was higher than BBC2's 2.4 hours/viewer in digital homes.

Second, *pay TV channels*, such as Sky Sports 1, also tend to have somewhat low reach and high hours per viewer. The low reported reach is partly a measurement error: the base for the reported figures is all individuals aged 4+ in all digital homes. For strict comparability with the BBC and other free-to-air channels, one should compute reach only among individuals in homes able to receive the channel. I do not have data on Sky Sports 1's penetration, but suppose it were available in 40% of digital homes. In this case, its share and reach in these homes would increase to about 4.3% and 43%, respectively. Its 2.5 hours/week would still be slightly above trend, but this is to be expected: if someone is paying for a sports channel, one would expect them to watch it for several hours per week, otherwise they would have been unlikely to subscribe. The one anomaly is Hallmark, a free-to-air general entertainment channel showing US dramas and movies, which for some reason has lower reach and higher hours/viewer than normal for a channel with a 1% share. I believe that part of the explanation is that, although not a premium channel, it is not included in some of the popular channel packages.

Third, *BBC3 and BBC4* both had average hours/viewer of only 0.8 hours. That is, even among those who watched them at all in the average week (only 21% of people in digital homes for BBC3 and 8% for BBC4, even with only a 3-minute criterion), they were watched for an average of only about 50 minutes.

### Weak Demographic Segmentation

In line with the weak segmentation by programme type preference and channel preference, television audiences for both programmes and channels show only weak segmentation by demographics.

Table 5 illustrates this for the age profiles of the four services plus BBC1, 2, and News 24 for comparison. These figures are for the average minute on each channel.

**Table 5: BBC-TV Channels' Age Profiles (2Q 2004)**

Channel		4-15	16-24	25-34	35-54	55+	Total
BBC1	%	9	7	13	36	34	100%
BBC2	%	9	6	11	34	40	100%
BBC3	%	9	12	24	40	15	100%
BBC4	%	4	3	12	43	38	100%
News 24	%	4	3	10	34	49	100%
CBBC	%	72	6	6	14	2	100%
CBeebies	%	38	10	27	19	5	100%
Total TV	%	13	10	16	36	25	100%

Source: BBC analysis of BARB

Obviously, CBBC and CBeebies have quite different age profiles from the other channels, with a much higher proportion of their audiences being children (and, in the case of CBeebies, a substantial proportion being adults 25-34).

Among the five channels for adults, BBC3 stands out as having a younger age profile, in line with its intended strategy and positioning. Most strikingly, only 15% of the viewers of the average programme on BBC3 are aged 55+ versus 34-40% for BBC1, 2, and 4 and 49% for News 24.

24% of the viewing of BBC3 is by its core target audience aged 25-34, 36% is by all young adults (16-34), and as much as 45% is by all viewers aged less than 35. These figures are higher than the equivalent figures for BBC1 (13%, 20%, 29%) but not that dramatically, reflecting the general pattern of weak segmentation in television.

More importantly, BBC3's *viewing share* among 25-34s is only 1.0%. As we saw earlier, even among its own viewers the previous week, its viewing share during its broadcast hours was only 2.8% (Table 2A).

The problem is that, because television is a mass medium not a niche medium, BBC3's relatively young audience profile is mainly achieved by showing programmes which older viewers, especially those aged 55+, do not want to watch (rather than by showing programmes which all adults – especially younger ones – do want to watch). This raises three potential questions corresponding to the new services' three objectives.

1. Given the nature of the medium, is this the most cost-effective way to “reconnect” with young adult viewers?
1. Given the high cost of BBC3, does it provide good value for money?
2. Given that an important aim of the new services is to help drive digital takeup, and that digital penetration is higher among younger viewers, does it make sense to allocate over 80% of the resources at services targeting younger viewers?

I return to these issues in Parts 2 and 4.

## Part 2: Performance Against Approval Conditions

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As discussed in Section 1.2, the approvals for the new DTV services included a wide range of both general and specific conditions. These mainly focused on content issues do with the mix, quality and distinctiveness of programming, diversity, original/UK/regional/independent production, etc. In addition, there were four further conditions.

<i>interactivity:</i>	the BBC committed to use new technologies (the internet, interactive TV, mobile phones) to connect with the audience using multiple channels
<i>driving digital takeup:</i>	the BBC also committed to use the new services to help drive the takeup of digital TV.
<i>value for money:</i>	the BBC Board of Governors was required to ensure that the services represent value for money for licence payers.
<i>governance:</i>	the governors were also required to monitor the implementation of the new services and report on them each year in their annual report.

On the basis of the BBC's submission and my meetings with governors, I am satisfied that the last condition, governance, has been met. The role, structure, and composition of the BBC Governors are a wider issue outside the scope of this review.

In this section, I assess the extent to which the other conditions have been met. Sections 2.1 to 2.4 discuss this for each of the four services separately, focusing mainly on content issues and drawing heavily on the more detailed reports by Máire Messenger Davies (for CBeebies and CBBC) and Steve Hewlett (for BBC3 and BBC4)<sup>12</sup>. Sections 2.5 and 2.6 assess the evidence on interactivity and driving digital takeup, while Section 2.7 covers value for money. Section 2.8 gives a summary and conclusions.

### 2.1 CBeebies

The Secretary of State's approval of CBeebies confirmed the channel's role as a distinctive service providing education and entertainment for children under the age of six. The channel was approved subject to the general conditions (see Section 1.2) and a number of specific conditions about the content and origin of programming.

#### Máire Messenger Davies's Assessment of CBeebies

Máire Messenger Davies considers that CBeebies has fulfilled all of its commitments and conditions of approval, except for the commitment to invest in animation co-production, which the BBC acknowledges it has not fulfilled. Specifically:

*Together with all the new services, CBeebies was required to be a mixed genre channel, in this case covering music and movement, storytelling, make-and-do, simple science, natural history and puzzle programmes, and animation.*

MMD: This condition has been amply fulfilled. CBeebies' genre mix includes animation, live action, magazine formats, storytelling and information. Moreover, many programmes contain a variety of mini-genres, such as performance, stories or singing.

<sup>12</sup>Supplementary reports available electronically on the DCMS website ([www.culture.gov.uk](http://www.culture.gov.uk))

*Informal education (the channel's motto is 'learning through play') was to be at the heart of the service. One of the conditions of approval required the channel to broadcast educational programming throughout the day, including peak viewing hours, and required CBeebies to include a strong interactive strand: this included both interactive television and a website.*

MMD: CBeebies has successfully integrated education and incidental learning into programming throughout the day and supported it with interactivity through both interactive television (the “red button”) and BBC Online. CBeebies has a strong feeling of time and space, giving it a familiar ‘personality’, something which is more important to children than to adult viewers. She praises CBeebies’ success in “making it clear to the viewers where they are, because of the visual unity of the sets, the coherence of the schedule, the familiarity of many of the characters and [presenters], and the thematic way in which the programmes are linked”.

*Like all the digital services, CBeebies is under an obligation to ‘stimulate, support and reflect the diversity of cultural activity in the UK’.*

MMD: CBeebies has been notable for its success in this area. Presenters and characters on the channel are respectful, kind and represent a range of ethnic backgrounds and ability. She is critical, however, of the channel’s reinforcement of gender stereotypes, with authority figures tending to be male and carers female. She also feels that older people are underrepresented.

*Other conditions included a requirement that around 80% of output would be originally produced or commissioned programming.*

MMD was not able to verify this commitment independently. In general she accepts the governors’ assessment that CBeebies has fulfilled all of its commitments except the requirement to invest in UK animation.

*Around 90% of output was required to be made in the EU/EEA.*

MMD was not able to verify this commitment independently, but accepts the BBC’s assessment that over 90% of output was made in the EU/EEA.

*In addition, the approval for CBeebies stipulated that the channel must not undermine the programming zones on BBC1 and BBC2 for pre-school children.*

MMD: CBeebies has not undermined viewing shares for the CBeebies ‘zones’ on BBC1 and BBC2.

Overall, Máire Messenger Davies concludes that CBeebies represents excellent value for money as the cheapest of the four services which also attracts the largest audiences.

### **Ofcom’s Analysis of CBeebies’ Genre Output**

As the BBC’s report on the performance of CBeebies explains, there is currently no formal genre classification system for preschool output. For this reason, CBeebies was not committed to producing any specified percentage for genres such as drama or factual programming, and Ofcom has not analysed the output at that level of detail.

Máire Messenger Davies considers that CBeebies has amply fulfilled its commitment to deliver a mixed schedule, particularly in light of the mini-genres (for example, story-telling or arts and crafts) contained within many programmes on the channel. She also concludes that CBeebies is highly distinctive in comparison with commercial services, showing high-quality UK-made programmes without advertisements, most of which are both entertaining and educational (through “incidental

learning”), and some of which are highly innovative (eg *Balamory*, “the first preschool soap”, *The Blue Cow* and *Superbaby*, “some of the very best, most imaginative, creative, witty and stylish children’s programming I have seen”). She argues that it would be helpful to develop some more rigorous definitions of “educational”, but concludes that “however educational is defined, there is more of it on CBeebies” than on the commercial channels.

Table 6 shows that, using the BARB classification, Ofcom found that the proportion of “educational” programmes on CBeebies was even higher than claimed by the BBC (73.7% versus 61%). The Ofcom analysis of genres on all four services is described in the appendix.

**Table 6: CBeebies Genre Output (1.4.03 – 30.11.03)**

Genre	BBC		Ofcom/BARB	
	Hrs	%	Hrs	%
Educational/Schools	1702	61%	2056	73.7%
Children’s Ent and Info	1088	39%	733	26.3%
<b>Grand Total</b>	<b>2790</b>	<b>100%</b>	<b>2789</b>	<b>100%</b>

(Sources: BBC, Ofcom analysis of BARB)

Máire does make some detailed suggestions for the further development of both CBeebies and CBBC. I draw on these in Section 4.3, where I give my recommendations for all four services.

### My Assessment of CBeebies

CBeebies is a triumph, an exemplary PSB service for preschool children which lives up to its motto of ‘learning through play’. It continues a long tradition of such programming, meeting both the letter and the spirit of its remit. It has a feeling of integrity and public service but has also been extremely successful at reaching and engaging its audience as well as developing new techniques and formats and, as far as possible with this age group, exploiting interactivity. I accept Máire’s view that it has not undermined preschool programming on BBC1 and BBC2.

The BBC should be congratulated for its success with this service, which creates clear public value, as consistently reflected in audience research and in viewers’ submissions.

## 2.2 CBBC

The BBC’s proposal was for a mixed genre channel aimed at children aged 6 to 13 years, subject to the same general conditions as CBeebies (see Section 1.2) and a number of specific conditions relating to the content, scheduling, and origin of programming.

### Máire Messenger Davies’s Assessment of CBBC

Máire Messenger Davies’s overall judgement is that CBBC is highly distinctive from the commercial children’s channels in both content and quality as well as the absence of advertisements, with many successes but also some questions about tone and style and some other potential areas for improvement.

*The genre mix was to include live news, drama, comedy, entertainment, and factual programmes throughout the day, including peak viewing hours.*

MMD: As a mixed genre channel, CBBC succeeds in offering children a much wider variety of programmes than its commercial competitors. However, the after-school children's slot on BBC1 is more varied in terms of genre than the equivalent period on the CBBC channel, with more drama and more factual programming shown on the terrestrial channel. Given the wealth of the BBC children's archive, MMD wonders if there is a place in the digital future for a 'CBBC Gold' based on the BBC's back catalogue.

In each genre, the programming fulfils the BBC's commitments. For instance, Xchange, a factual programme broadcast before and after school, takes its audience seriously and engages them in a wide range of stimulating topics.

*The detailed conditions for the channel included a requirement to dedicate 75% of output and investment to programming made in the EU/EEA.*

MMD was not able to verify this commitment independently. In general she accepts the governors' assessment that CBBC has fulfilled all its commitments except the requirement to invest in UK animation.

*25% of the channel's output was to be original programming, which would constitute 75% of programming budget. The approval required the BBC not to increase the balance of acquired programming at the expense of originated programmes during peak viewing hours.*

MMD was not able to verify this commitment independently, but accepts the BBC's assessment that original programming constituted 51% of output and 90% of the budget for CBBC.

*In addition, the approval for CBBC stipulated that the channel must not undermine the programming zones on BBC1 and BBC2 for pre-school children.*

MMC: No firm conclusion. Overall, the BBC's share of children's viewing has decreased. The BBC attributes this to the rapid takeup of digital television by households with children. MMD saw no evidence that the range or quality of children's programming on BBC1 and 2 had declined.

*As with all the digital services, the Secretary of State required CBBC to 'stimulate, support and reflect the diversity of cultural activity in the UK'.*

MMD: Many ethnic and regional cultures are represented on CBBC (although she feels that Wales and Northern Ireland are underrepresented) but "there is one group of people almost totally unrepresented on the channel and that (with one or two exceptions) is people over the age of 21, or who look as if they're over 21. There are no elderly or middle-aged people except in buffoonish roles in the comedy dramas, and there are hardly any people who look like most children's parents or teachers. The CBBC channel is a less recognisable social world than CBeebies" (p 23).

MMD comments (p 14) that "Presenters on children's television are not only relentlessly young, they are even more relentlessly youthful – that is, bouncy, shiny, flirty, fashionably dressed and demotic in the way they speak, [although] CBeebies is much better than CBBC in having a wider range of different ages represented".

Again (p 23), "Looking at the scantily-dressed presenters, you have to ask: Who are these people and

where are they going? It's 4 o'clock in the afternoon and they look as if they're going to a nightclub. What kind of place is it, and is it the kind of place parents would want to leave their kids? Compared to the broadcast schedules on BBC1, which do have a solid sense of continuity and recognisable space, the answer would be, 'I'm not too sure'".

Related to this issue is the question of tone. "CBBC and CITV on broadcast terrestrial have a more confident and relaxed style with the audience [than the CBBC channel on digital TV], clearly from years of experience – but it seems to me from my brief sampling ... that this experience has yet to be transferred from CBBC on BBC1 and 2 to the channel" (MMD, p 22).

"There are many examples of tastelessness, eg vomiting on *Dick and Dom in da Bungalow* ... This show is funny and appealing, but it does seem to go a little too far sometimes in humiliating the children it features ... There is a lack of gentleness and courtesy – both qualities abounding on CBeebies" (MMD, p 22).

MMD also mentions the use of bad grammar, eg 'ain't' and 'you was', "something designed to send parents up the wall".

Similarly, "The frenetic, fun-filled tone of the channel also does not always recognise the element of seriousness in the child audience" (MMD, p 23). MMD refers to recent research on children and news in which children passionately objected to being, as they put it, 'patronised'. In this research, many children named the well-known, middle-aged Jon Snow (then presenting C4's news programme *First Edition*) as their favourite newscaster.

MMD acknowledges that "It is difficult to find a tone of voice that would reach the whole of [CBBC's target] age range ... But the BBC's long traditions of *Newsround*, *Blue Peter*, and even Saturday morning mayhem programmes have developed an expertise in talking to children intelligently, so it should not be impossible to get it right" (p 24), although also "It is worth asking who is watching CBBC in the daytime in term-time?" (MMD, p 26).

MMD singles out several CBBC programmes for praise. These include the comedy dramas *Tracy Beaker*, *The Queen's Nose*, and *Big Kids*, a serious and informative edition of *Xchange* featuring a 17-year-old jazz trumpeter, and the X-pert strand of *Xchange*, in which child critics review the latest books, TV programmes and films: "[The child critics] were confident, opinionated, probably quite unjust in some of their strictures, but it made for lively, intelligent, entertaining television" (MMD, p25).

Finally, MMD's qualitative research suggests that, unlike CBeebies, the CBBC channel has not yet achieved a separate identity distinct from that of CBBC programmes on BBC1 and 2. She raises the question of whether the CBBC channel should be given a new brand name to help communicate this distinction (p 35).

### Ofcom's Analysis of CBBC's Genre Output

The Secretary of State did not set any percentage requirements for CBBC's genre output. However, the channel was required to deliver a mixed schedule with at least 10% of output being schools programming, broadcast during school hours. Neither the BBC's nor BARB's classification system distinguishes between factual and schools programming, although the BBC's submission states that during school hours, 'Class TV' made up one third of the channel's output during the school day in term time. After adjusting for the slightly different genre definitions on BARB, Ofcom's analysis closely matched the breakdown in the BBC's submission. ('Revised BARB' column in Table 7).

**Table 7: CBBC's Genre Output (1.4.03 – 30.11.03)**

Genre	BBC		Ofcom/BARB		Revised BARB	
	Hrs	%	Hrs	%	Hrs	%
News	48	1.7%			47	1.7%
Factual and Schools	768	28.1%	832	30.4%	766	28.0%
Drama	643	23.5%	588	21.5%	632	23.1%
Films						
Entertainment	780	28.5%	706	25.8%	742	27.1%
Animation	497	18.2%	588	21.5%	544	19.9%
Other			22	0.8%	5	0.2%
<b>Grand Total</b>	<b>2736</b>	<b>100%</b>	<b>2736</b>	<b>100%</b>	<b>2736</b>	<b>100%</b>

Sources: BBC, Ofcom analysis of BARB

### My Assessment of CBBC

CBBC is a distinctive service with high-quality UK-produced content free from advertisements, covering a wide range of genres, and with a high proportion of original programming.

There is some evidence from a study by David Graham Associates (DGA) for Nickelodeon that the proportion of factual programming on CBBC has fallen<sup>13</sup>. The BBC's submission accepts this, while suggesting that there has been a corresponding increase in the proportion of original comedy and drama. Again, Nickelodeon has provided some evidence of aggressive scheduling by CBBC during school holidays, which (in Nickelodeon's view) goes against the spirit of the remit. I am not in a position to test these assertions in detail, but note that, once adjusted for the different genre definitions used by the BBC and BARB, Ofcom's analysis of CBBC's genre mix was virtually identical to the BBC's own figures, confirming the wide range of genres shown.

Although CBBC has largely met the formal conditions in its remit, and I believe it has created significant public value, I cannot give it as unequivocal a bill of health as I gave CBeebies.

I agree with Máire Messenger Davies's concerns about the tone and style of CBBC, the "relentlessly youthful" presenters, the virtual absence of anyone looking older than 21 (except as a target for jokes), and the sometimes nervous and potentially patronising approach to serious subjects.

I was appalled to find at first hand that *Dick and Dom's Golden Bogies* on the BBCi "red button" service for CBBC consisted of Dick and Dom first picking their noses on camera and then playing the Bogie Game – disturbing other readers in a public library by calling out "Bogies" in turn, increasingly loudly, until one of them was so helpless with laughter that he had to concede defeat. Despite Dick and Dom's popularity, this is not somewhere the BBC should be.

Given the BBC's long experience of successful children's programming on BBC1 and 2 – admittedly, in a less competitive market and perhaps a gentler culture for children, I am confident that it can address these concerns.

<sup>13</sup>David Graham Associates, Review of the BBC Digital Children's Channels, 2004, available at [www.culture.gov.uk](http://www.culture.gov.uk), thereafter referred to as 'DGA'.

Another issue relates to the use of the BBC's extensive archive. From a public value perspective, I agree with Máire's view that there should be scope for CBBC to exploit the archive more fully, although Nickelodeon will not thank me for saying so. It is hard to see how more public value could be created by making archive programmes available only to families who had paid for satellite or cable TV rather than to all families with digital TV (ie including Freeview) but this is a close call which may merit further analysis. If commercial broadcasters paid a high enough price for programmes from the BBC archive, the resulting revenue might be sufficient to enable the BBC to increase its budget for new programmes so much as to create even more public value than by itself broadcasting the archive programmes. A generic issue here is whether the commercial channel is also universally (or at least widely) available.

Finally, CBBC is operating in a more difficult market than CBeebies, because of the wide age range 6-13 (in practice, CBBC rightly focuses on the middle of this range and also appears to appeal somewhat more to girls than to boys), the greater intensity of competition, and the need for higher production budgets. Perhaps for these reasons, CBBC achieves less viewing with a bigger budget than CBeebies, and therefore represents less good value for money. It has also not yet created such a distinct brand identity. I support Máire's suggestion that the BBC should explore rebranding the CBBC channel to distinguish it more clearly from the children's programmes on BBC1 and BBC2.

## 2.3 BBC3

Of all the approvals for the new services, the Secretary of State's approval of BBC3 contained the most detailed set of conditions. These reflected the substantially more detailed second proposal submitted to her following her rejection of the BBC's original proposal for this service.

BBC3 was launched in February 2003, about a year after the other three services. At the time of writing, it has been on air for only 18 months so this review comes at a stage when BBC3 is still a very young channel.

BBC3 was to be a distinctive, mixed-genre channel aimed mainly at young adults, especially those aged 25-34. The approval, in response to the BBC's revised proposals, contained extensive conditions about content, innovation, new talent, and programme sourcing, the requirement that these commitments should not be met at the expense of programmes on BBC1 and 2 catering for the 25-34 age group, and the general conditions relating to standards, diversity, viewers with sensory impairments, interactivity, driving digital takeup, value for money, and governance.

In comparison with the other three services, BBC3 had an extremely challenging remit. This committed it to an expensive genre mix including drama and scripted comedy as well as a high proportion of original content (80%) "specially commissioned for BBC3 and genuinely new to television". To enable it to meet this tough brief, it has a generous programme budget (£95.7 million in 2003/4, 54.6% of the total budget for the four services).

### Steve Hewlett's Assessment of BBC3

Steve Hewlett has assessed BBC3 in two stages. First, he has evaluated the extent to which it has met the general and specific content and sourcing conditions in the remit. His views here are largely positive. He considers that BBC3 has achieved or exceeded virtually all of its many obligations on

programme mix and sourcing, although he questions some of the BBC's numbers and also the usefulness of its very broad definition of "specially commissioned" programming.

The second part of Steve's review of BBC3 focuses on "the degree to which [it] has succeeded in its primary underlying purpose in relation to 25-34 year-old viewers". He concludes that, so far, BBC3's success in reaching these viewers has been limited.

Turning first to his assessment of BBC3's performance against its general and specific commitments, as with CBeebies and CBBC, I list each commitment and then the assessor's conclusions.

*High general standards of content, quality and editorial integrity*

SH: From the available evidence, this condition has been met.

*The service shall stimulate, support and reflect the diversity of the UK*

SH: The evidence is that this condition has been met, but Steve recommends a formal scheme to monitor cultural diversity on and off screen.

*Promoting the understanding and enjoyment of the service by viewers with sensory impairments*

SH: The BBC's submission includes data showing that BBC3 has exceeded its targets for subtitling, audio description and signing. Steve has no reason to question these data.

*At least 25% of qualifying hours and budget to be commissioned from the independent sector*

SH: The BBC's submission claims that over 40% of qualifying hours and over 30% of budget have been commissioned from independent producers, and that there has been no reduction in such commissioning by the other BBC channels. Steve accepts these claims.

*90% of programme hours and expenditure to be for programmes made in the EU/EEA for first showing in the UK; from 2004-5, 33% of eligible budget to be spent on programming produced outside the M25.*

SH: Again the information supplied by the BBC shows that the EU/EEA commitments have been met and that BBC3 is well on its way to reaching its regional production target for 2004-5.

*The service must deliver a mixed schedule of programmes embracing drama, entertainment, news, current affairs, education, music, the arts, and science, including coverage of international issues.* In a subsequent letter to DCMS, the BBC made more specific commitments about news, current affairs, education, and music and arts programmes.

SH: The BBC's submission states that BBC3 has shown a wide range of genres and includes information to support the claim that it has met or exceeded all its specific genre commitments. He accepts most of these claims but his detailed enquiries reveal that, for some genres, the programmes included some which were hardly in the spirit of the approval. The only business programme was *Celebdaq*, in which viewers trade "stocks" in celebrities. The only science programme was *Leonardo's Amazing Machines*. The only programmes on religion/ethics were *Jerry Hall's Gurus* and 23 minutes of *Thought for Tomorrow*. In mitigation, some programmes categorised under education might have been put under these genres, eg the successful medical programme *Body Hits* under science or *New Tycoons* under business.

In conclusion, Steve accepts that BBC3 is a mixed-genre channel and that the specific genre commitments have been met in a 'box ticking' sense. He is, however, "Not convinced that the spirit of this condition has been fully met".

*The commitments must not be met at the expense of programmes on BBC1 and 2 catering for the 25-34 age group*

SH: This is impossible to evaluate fully without an extensive review. Further, the BBC's claim that BBC3 may have enabled the BBC to halt the observed decline in reach among 25-34s is complicated by the change in the BARB panel in January 2002. He accepts, however, that there has been no obvious decrease in programming for 25-34s on BBC1 and 2 and that these channels have benefited from co-commissions with BBC3 such as *Little Britain* (BBC2/3) and *Brief History of Rome* (BBC1/3). The BBC also reports broadcasting over 50 hours of BBC3's schedule in "zones" on BBC1. In conclusion, this commitment has been met.

*Programming must be of a consistently innovative and risk-taking character. 80% of programme hours must be specially commissioned for BBC3 and genuinely new to television. Both commissioned and acquired programmes will concentrate on developing new talent on and off screen*

SH: On new talent, "There is ample evidence that BBC3 has taken its obligations ... seriously".

On acquisitions, the picture is less clearcut. More than 80% of BBC3's acquisitions have been feature films (167 hours out of 206.4 hours). Much of the rest was the 24-hour thriller *24*, already acquired by the BBC. The main acquisition purely for BBC3 was *Platinum* (8 hours), a US show about a record label.

The commitment that 80% of programming be "specially commissioned" appears to have been met but this is not an especially helpful criterion, given that "specially commissioned" is defined to include origination and repeats of BBC3 programmes, origination and repeats of co-commissions with other BBC channels, spinoffs of existing BBC1 and 2 brands, and new commissions of BBC1 and 2 programmes which "otherwise would not have been commissioned". Steve recommends a tighter definition for "specially commissioned" with a correspondingly lower target.

As things stand, the definition includes 137 hours of *Fame Academy* spinoff content, episodes of *What Not to Wear*, 60 hours of *Johnny Vaughan* and 61 hours of football – including, but certainly not limited to – the *African Nations Cup*. The inclusion of these programmes masks BBC3's genuine achievements in innovation and developing new talent, especially in comedy, drama and animation.

### **BBC3's Impact on its Target Audience: Steve Hewlett's Assessment**

Turning to BBC3's underlying mission to "reconnect" young adults in digital homes to the BBC, and especially to its news and current affairs programmes, Steve is unconvinced.

His report includes a detailed discussion of the extent to which BBC3's PSB programmes are in fact watched by viewers aged 25-34, in particular news and current affairs, drama and comedy.

The analysis is hindered by the BBC's unfortunate tendency to use different definitions of audience reach in different contexts. Sometimes, the criterion is 3-minute reach (ie viewing the channel for at least three continuous minutes at some point within the analysis period), sometimes 15-minute reach – a significantly higher hurdle for a small channel. Sometimes the time period is a week, sometimes it is a month or even "ever".

For instance, the BBC claimed that cumulatively 40% of 25-34s in multichannel homes had seen at least 3 minutes of at least one news show on BBC3, ie 1.8 million people in this age group since launch. However, this includes viewing of *Liquid News*, a celebrity gossip show. If *Liquid News* is excluded, the cumulative 3-minute reach of news on BBC3 drops to just 16% of 25-34s in digital homes. Steve notes that, even within this audience – BBC3's prime target group – the viewing of BBC3 news is dwarfed by

these viewers' consumption of news on BBC1, C4, and other channels, as well as other news media (radio, newspapers, online, etc).

BBC3 has had one great success in this area, its excellent one-minute news summary *60 Seconds*, on the hour every hour. Clearly, this is limited to headlines only and does not necessarily constitute deliberate viewing, but it does ensure that the BBC3 audience is kept abreast of breaking news.

Steve also discusses current affairs, drama and comedy. He finds that BBC3's programmes in these genres have so far achieved very low viewing figures, rarely reaching 100,000 viewers per showing, the main exception being the repeats of *Eastenders*. More generally, he feels that BBC3's PSB programmes have so far failed to connect with its target audience to anything like the extent envisaged.

### Steve Hewlett's Overall Conclusions

Steve concludes that BBC3 has launched successfully as a mixed genre channel and has, for the most part, met its stringent approval conditions. However, he feels that BBC3 in general, and especially its PSB programmes such as news and current affairs, have so far failed to connect with the core audience of 25-34 year-olds in digital homes. He questions whether targeting a particular audience segment (as opposed to focusing on particular types or genres of programming) can be cost-effective. He also suggests that the definition of "specially commissioned" should be tightened, with a correspondingly lower quota.

### Ofcom's Analysis of BBC3's Genre Output

Of the four services, BBC3 was subject to the most detailed requirements for genre output. Table 8 shows Ofcom's analysis of its genre mix.

The revised BBC proposal for the channel committed it to broadcasting a 15-minute news programme in peak time on weekdays, together with hourly bulletins until midnight every day. The large discrepancy between the BBC's figure of 13% and the original BARB figure of 2.1% is mainly caused by *Liquid News*, categorised by the BBC as "news" and by BARB as "entertainment".

**Table 8: BBC3's Genre Output (1.4.03 – 30.11.03)**

Genre	BBC		Ofcom/BARB		Revised BARB	
	Hrs	%	Hrs	%	Hrs	%
News	272	13.0%	44	2.1%	271	12.9%
Current Affairs	75	3.6%	11	0.5%	77	3.7%
Arts & Music	130	6.2%	252	12.0%	130	6.2%
General Factual	475	22.6%	588	28.0%	486	23.2%
Education	81	3.9%			82	3.9%
Drama	167	8.0%	180	8.6%	169	8.1%
Films			109	5.2%		
Entertainment	750	35.7%	730	34.8%	730	34.8%
Other (religion, acquired, sport)	150	7.1%	184	8.8%	153	7.3%
<b>Grand Total</b>	<b>2100</b>	<b>100%</b>	<b>2098</b>	<b>100%</b>	<b>2098</b>	<b>100%</b>

In addition, the revised proposal stated that 15% of broadcast hours would be news, current affairs, education, music and the arts. The categorisation of *Liquid News* has a major impact on the performance of BBC3 against this requirement. The BBC's submission claims that 26% of programming has comprised news, current affairs, education, music and the arts, while according to the original BARB data the figure is 14.6%. If *Liquid News* is left out but other differences in categorisations resolved in the BBC's favour, the BARB figure increases to 16.6%, slightly above the BBC's commitment.

Within the 15% of output dedicated to news, current affairs, education, music and the arts, the BBC committed to: 15 new hours of current affairs programming per year, 30 new hours of education programming per year, and 50 new hours of music and arts programming per year. The BBC submission, although written before the service had run for a year, states that BBC3 had already met or exceeded the targets for current affairs, education and music and arts between February and November 2003.

The BBC also made a commitment to deliver a diverse mix of documentary programming across a range of subjects, above the targets for arts, current affairs and education, but did not set targets for hours.

### My Assessment of BBC3

BBC3 is by far the most important of the four services in terms of resources and the most problematic to assess. Its extremely detailed remit, its genre mix, the emphasis on original UK production, and especially the focus on a narrow, hard-to-reach target audience make its brief close to "mission impossible", even with such a high budget. Further, because of its later launch, I am reviewing it at an earlier stage of development than for the other three services.

I agree with Steve's view that, by and large, BBC3 is meeting its very tough remit in terms of genre mix, attempts to develop PSB programmes relevant to 25-34s, innovation, original UK/regional/independent production, content for viewers with sensory impairments, and general programme standards.

I am grateful to both Steve and Ofcom for digging into the way programmes have been categorised and showing that, in the case of some PSB categories, there is less in reality than the BBC's numbers suggest (eg *Liquid News* as a news programme, *Celebdaq* as a business programme).

I also agree with Steve's suggestion that the BBC be invited to propose a tighter definition of "specially commissioned" which is closer to the spirit of the Secretary of State's "genuinely new to television", with a correspondingly reduced quota. Alternatively, it may be better to have more than one quota, one broad, one narrower.

Despite these provisos, I accept Steve's overall conclusion that BBC3 has met its remit conditions on content and sourcing. The channel has had some flops, as is inevitable for a service dedicated to innovation and risk-taking, but it has also had some great successes such as the *60 Seconds* news, comedy shows such as *Little Britain* and the comedy animation *Monkey Dust*, the drama *Burn It*, the *Glastonbury* music festival and programmes such as *Little Angels* on parenting and *Body Hits* on health and medicine. If the only question were whether BBC3 has met its remit conditions, the answer would be a clear yes: with a few qualifications, BBC3 is a distinctive channel with many innovative UK-produced PSB programmes aimed at 25-34s.

However, I also agree with Steve's other conclusion, that BBC3 has so far failed to "reconnect" its target age group to the BBC.

Further, based on his analysis, it appears that BBC3's distinctive PSB programmes, notably news (excluding the headlines-only *60 Seconds*) and current affairs as well as most of the original drama, are attracting only tiny audiences. In other words, not only has BBC3 achieved limited impact within its target audience (as already discussed in Section 1.7), but most of that impact has come from mainstream content such as *Eastenders*, feature films, and BBC1/2 spinoffs such as *Fame Academy* and *What Not to Wear*.

The underlying reason, in my view, is the issue I discussed in Section 1.6, the BBC's continuing overemphasis of audience segmentation and targeting. The worst excesses (*100 Tribes*) are in the past, but even now the BBC's June 2004 *Building Public Value* report classifies BBC3 as an "audience-targeted service" alongside CBeebies, CBBC, Radio 1, 1Xtra, and the BBC Asian network (page 94).

CBeebies, CBBC, and many radio stations do indeed deliver strongly segmented audiences, but as shown in Section 1.7, with a few specific exceptions (children, foreign language channels, bible stations and, to a lesser extent, the Fox News Channel), television is a mass medium with only weak audience segmentation, not a highly targeted niche medium. It is time the BBC accepted the evidence on this.

The problem with trying to target 25-34s is that BBC3 tends to focus obsessively on topics, and to adopt a style, seen as relevant only to this age group. This creates two problems.

First, it means that the viewing of BBC3 among older adults is very low indeed, which reduces both the channel's ability to drive digital takeup (Section 2.6) and its value for money (Section 2.7).

Second, and less obviously, it probably reduces the appeal of the channel even among the 25-34 target age group. By reducing the channel's household and adult reach and share, it reduces 25-34s' exposure to it both onscreen and through talking to friends, family, and colleagues at work, reading newspaper reviews, and so on. Further, by focusing so narrowly on viewers in this age group, the temptation is to stereotype and patronise them, eg assuming that they are all celebrity-obsessed clubbers with the attention span of a gnat. 25-34s are as intelligent and – more to the point – as heterogeneous as any other ten-year age group. In years of formal education, they are on average more educated than any other such group. Like the rest of us, they like to relax but also like to be taken seriously.

Life stage is an important determinant of a person's interests and concerns, and BBC3 has done a good job of researching these. For instance, programmes such as *Body Hits* and *Little Angels* address issues of health and parenting of particular concern to this age group. But, as with CBBC, BBC3 has a slightly nervous feel about it, which CBeebies and BBC4 do not have. Targeting the 25-34s so obsessively seems to go beyond a helpful guideline and to have become a creative straitjacket.

My conclusion is that BBC3 should loosen up a little, worry less about what's different about the 25-34s, and concentrate on making good programmes with broad appeal, while still focusing on edgy comedy, new talent and innovation, which will tend to deliver a youngish audience as well as acting as an "entertainment laboratory" for BBC1 and 2. C4 is a PSB channel which has done this successfully (with a much bigger budget and somewhat different remit) and achieves high reach among all age groups – including 25-34s, who for instance see far more long-format news on C4 than on BBC3. (I recommend that BBC3 drop its 7 o'clock News and replace it with other factual programming: see Section 4.3).

My main recommendation is therefore that BBC3's mission should be redefined somewhat, retaining the emphasis on innovation and entertainment but releasing it from the straitjacket of its target

audience, which is defined too narrowly, and with more emphasis on overall audience share and reach. I return to this issue in Section 4.3, recommendations.

## 2.4 BBC4

According to its approval, BBC4 is “a distinctive, well-defined service intended to create a ‘forum for debate’ and aimed at ‘anyone interested in culture, arts and ideas’.” It “addresses the BBC’s public service remit to inform, educate and entertain, providing mixed genre programming in an area where most competitors are niche channels”. Specifically, these genres must include news (in particular, global news and current affairs), philosophy, science, history, art, performance, music and film.

Other specific conditions are that:

- Around 70% of airtime must be given to original programming (including repeats of that content); BBC4 is expected to emphasise content from the nations and regions
- Around 70% of output should be made in the EU/EEA
- BBC4 must not lead to a reduction in music and arts programmes on BBC1 and 2

As with the other services, BBC4 was expected to maintain high general standards, include various forms of interactivity, and help drive digital takeup, especially by appealing to older viewers who have been more resistant to adopting digital television. In line with this final objective, “It is important to maximise the public value of this service by attracting and engaging the widest possible audience”.

### Steve Hewlett’s Assessment of BBC4

Steve Hewlett’s general assessment of BBC4 is positive. He considers it to have largely met the conditions of its launch and to be good value for money, adding public value at moderate cost. He believes it has extended the range of content offered by the BBC and exploited well the opportunity to showcase new programming. He does, however, raise some issues related to BBC4’s wider underlying purposes. As with BBC3, he argues that multicultural programming is difficult to assess in the absence of a formal monitoring system. He also believes that, although the channel has been a good forum to debate matters of cultural interest, the new creative treatments promised by the BBC in its original submission are not yet in evidence.

*The channel was required to appeal to anyone interested in culture, arts and ideas. Like all the new services, BBC4 was to be a mixed genre channel, with an emphasis on global news and current affairs, philosophy, science, history, art, performance, music and film.*

SH: BBC4 has met or exceeded most of its commitments, including its responsibility to be the most global, outward looking service of the digital channels. He notes that BBC4 won an impressive 27 UK and international awards within its first two years.

*The detailed proposal for BBC4 committed the channel to performance from the Nations and Regions, including coverage of key festivals around the country, and to broadcasting classical and specialist music, including a world music agenda. Music performances, as well as documentaries, were required to run occasionally at a greater than usual length.*

SH: BBC4’s music and performance programming has extended the BBC’s overall coverage of major arts events, particularly *The Proms* and festivals such as the *Leeds International Jazz Festival* and *Celtic*

*Connections.* *The Proms* and individual performances such as *Sophie's Choice* have been broadcast for up to four hours. However Steve notes that both performance pieces and documentaries have sometimes in the past run on BBC2 for unconventional lengths, so it is difficult to judge the extent to which such programming has been enabled by the presence of BBC4.

*Detailed conditions included a requirement for 70% of air time to consist of originally produced or commissioned programming, including repeats of that content.*

SH: Although BBC4 has met its targets for originally produced or commissioned programmes, this category includes programmes co-commissioned with BBC1 or BBC2, spin-offs of existing brands, Open University funded programming, and new commissions of existing BBC brands (such as *Arena*). As with BBC3, Steve suggests that the definition of "specially commissioned" programming needs to be reassessed in order to highlight programmes which are genuinely new to television and unique to BBC4.

*BBC4 was required to broadcast a daily news programme appealing to multicultural groups, business people, and those interested in global news and current affairs.*

SH: Apart from noting that *The World* shows only five (not seven) nights a week, Steve is satisfied that BBC4's news programme fulfils its obligation to provide a broader perspective on world news and to offer more depth on international stories. However he notes that it is impossible to judge from BARB whether *The World* appeals to business people or multicultural groups. He adds that audiences for *The World* are very low, with average ratings (March-August 2004) of only 17 thousand viewers (a 0.14% share) and 3-minute weekly reach of only 0.4% of the available audience. [Given these tiny figures and the weakly segmented nature of television audiences, we can confidently conclude that *The World* does not appeal significantly to multicultural groups, business people, or anyone else: PB]

*A condition of the approval was that music and arts programmes on BBC1 and BBC2 should not be diminished as a result of investment in programming for BBC4.*

SH: This condition relates to the commitment to originally produced or commissioned programming. With such a wide definition, he considers it difficult to judge whether strands such as *Storyville* might have continued to be commissioned by BBC2 if BBC4 did not exist. Equally he doubts whether BBC4's most high-profile co-productions with BBC2 – the *Alan Clarke Diaries* and the *National Trust* – would not have been made by BBC2 in different circumstances. He notes that only 17 out of BBC4's top 70 programmes were unique to the channel.

*BBC4 was to provide a more secure home than other channels for world cinema, to offer more non-mainstream films on free-to-air television, and widen the choice of multicultural films in the UK.*

SH: This condition has been met. BBC4 shows two foreign films each week. It has also invested in distributing new world cinema and in the BBC4 World Cinema Award.

*70% of output on BBC4 was to be made in the EU/EEA.*

SH accepts the BBC's assessment that around 80% of BBC4's programming is produced in the EU/EEA. He also accepts the BBC's figures for the proportion of programming (both hours and money) commissioned from companies outside London, and its claim to have met its internal targets for subtitling, audio description and signing.

## Ofcom's Analysis of BBC4's Genre Output

Of the four services, the data for BBC4 produced the biggest differences between the BBC's and BARB's data. As the Ofcom report explains: "three areas of significant discrepancy remain: in current affairs, arts & performance, and general factual on BBC4. This was because in the time available the BBC was only able to provide examples of programmes "miscategorised" by BARB in these genres rather than a full list."

Despite these differences, Ofcom's revised figures are reasonably close to the BBC's (Table 9)

**Table 9: BBC4's Genre Output (1.4.03 – 30.11.03)**

Genre	BBC		BARB		Revised BARB	
	Hrs	%	Hrs	%	Hrs	%
News	78	4.2%	80	4.3%	80	4.3%
Current Affairs	152	8.1%	30	1.6%	130	6.9%
Arts & Performance	807	43.1%	567	30.2%	709	37.8%
General Factual	457	24.4%	740	39.4%	608	32.4%
Education						
Drama	74	4.0%	93	5.0%	80	4.3%
Films	179	9.6%	175	9.3%	175	9.3%
Entertainment	31	1.7%	17	0.9%	30	1.6%
Sport						
Other	94	75.0%	176	9.4%	66	3.5%
<b>Grand Total</b>	<b>1872</b>	<b>100%</b>	<b>1878</b>	<b>100%</b>	<b>1878</b>	<b>100%</b>

Sources: BBC, Ofcom analysis of BARB

## My Assessment of BBC4

BBC4 has successfully established itself as "a place to think". It exemplifies the BBC's traditional, self-confident public service values – meeting both the letter and the spirit of its remit – without undue stuffiness or paternalism. It is hard to assess whether it has been used as a "dumping ground" for arts and serious programming diverted from BBC1 and 2, but Steve Hewlett found no evidence that this had happened on a significant scale.

The negative aspect of BBC4's performance is that its viewing share and reach, while growing, are both very low. Part of this stems from its low budget, £35.2 million in 2003/4. This is still only 35% of BBC3's budget, 8.2% of BBC2's and 3.7% of BBC1's. Even allowing for the longer broadcast hours of BBC1 and 2 and their inclusion of programmes for the Nations and Regions, this is a massive imbalance. It is hard to see how BBC4 could sustain a full schedule of the quality viewers expect from the BBC with such a small budget.

BBC4's budget and viewing share are interrelated with digital penetration (Section 2.6). On the one hand, as digital penetration increases, the number of viewers able to receive BBC4 (and the other digital channels) will increase, justifying a somewhat higher budget. At the same time, future digital takeup

mainly depends on the appeal of the free-to-air digital channels to people who have not yet adopted. Since these non-adopters are on average older than those who have already adopted, and since BBC4 has the oldest age profile of the four services, increasing the budget and impact of this channel should take precedence over the others, especially BBC3, which already has a relatively big budget.

Increasing the impact of BBC4 is not only about resources, however, nor is it only about driving digital takeup. As with BBC3, although perhaps not to the same extent, BBC4 needs to be pragmatic about what works and what does not.

For instance, its weekday news programme *The World* (2000-2030) is in my view not working and should be either revamped or replaced by other factual programming.

Again, I would question the amount of time devoted to classical music concerts. These can work well, as with some of *The Proms* and the performances (and interactive content) linked to the drama documentary *The Genius of Mozart*, but in general, people do not want to sit in front of a television watching a concert.

The reason for these concerns is that, although BBC4 is already creating public value despite its tight budget, it is contributing little to the broader aims of driving digital takeup and connecting with audiences. Further, its viewing share is still so low that it currently represents rather poor value for money, as I discuss in Section 2.7.

## 2.5 Interactivity

Since the 1980s, the BBC has actively adopted and promoted digital technologies from home PCs to BBC Online, digital radio and television, and interactive applications of these technologies. These efforts are currently led by Ashley Highfield, controller of new media, an unabashed techno-enthusiast.

The new DTV services are all committed to using new technologies to connect with the audience. There are numerous examples of success, perhaps especially on the children's channels but also on BBC3 and 4. This approval condition has certainly been met.

The most important interactive medium for the BBC is the internet, via BBC Online (bbc.co.uk), which has just been subject to a major review by Philip Graf. In addition, the BBC is investing in interactive TV services linked to all its digital channels, including BBC1 and BBC2 for viewers with DTV. These fell outside the scope of the Graf review so I comment on them briefly here, although they are not limited to the four services covered by this review.

### Interactive TV Services (BBCi)

“Interactive TV services” (operating under the brand name BBCi) refers to all services which can be accessed by viewers in digital homes “pressing the red button” for extra content beyond the current broadcast stream (hence the alternative label, “red button services”).

Within the BBC, the distinction is made between “enhanced TV” (eTV) services and “24/7” services. eTV services are listed at the top of the BBCi menu which appears on-screen when the viewer presses the red button. eTV consists of a mixture of static text and pictures, video clips, and in some cases (eg Wimbledon and the Olympics) extra live channels for viewers who want to watch real-time programming – such as a different sport at the Olympics – which is not currently being shown on the

main channel. The material on eTV is generally linked closely to the content of the programme and is intended to enhance the viewing experience. In line with this strategy, since January 2004 eTV services have organisationally been part of BBC Broadcast, although working closely with BBC New Media.

“24/7” refers to the more generic teletext-like information accessed through the lower half of the BBCi menu. The main generic items – always listed – are news, sport and weather, with a full menu accessible with one more click. The label 24/7 refers to the fact that, like teletext, these services are available round the clock, with no connection to specific programmes. The information changes when there is breaking news, updated weather forecasts, etc. Organisationally, 24/7 is part of BBC New Media.

Overall, the BBCi services have been a success. They still consume relatively modest resources (£15.3 million in 2003/4, versus £66.7 million for BBC Online) and in some cases, such as Wimbledon, usage has been high (according to BBCi, four million viewers accessed the Wimbledon eTV service this year) and the service has helped to introduce viewers to this type of interactivity. For the DTV channels covered by this review, successful eTV applications include interactive discussions following some editions of *Newsround* on CBBC, BBC4's *The Genius of Mozart* season, which offered an innovative combination of on-screen scores and commentary text during performances, and *Richard II* live from The Globe with an optional on-screen commentary by a theatre critic.

I agree with Ashley's focus on using eTV to enhance the viewing experience rather than trying to offer standalone applications which interrupt or compete with viewing. This is in line with general experience with interactive digital television, in which the UK is the most advanced country in the world, thanks especially to BSkyB, but also the BBC and other broadcasters.

BSkyB has until recently taken the lead in driving digital takeup (over the last 18 months or so this has been driven by Freeview, as discussed shortly) as well as interactive programming (eg Sky Sports Active), interactive advertising, and other interactive services such as games, home shopping and banking, betting, and digital radio, all through the TV set.

In general, viewers find online PCs better than interactive DTV for complex “lean-forward” applications such as grocery shopping and banking. Most viewers with DTV have an online PC as well. They are also reluctant to interrupt their viewing of programmes in order to interact, although they are happy to do so during commercial breaks.

In general, interactive DTV works best as an entertainment medium (betting and some games) and especially as a way of enhancing the viewing experience, either through extra choice (mostly sport), extra information (sport, soap opera plots) or where interactivity is an inherent part of the programme concept (shows based on voting, quizzes and games). The cost of developing and distributing eTV content is usually high, however, so these applications need to be selective<sup>14</sup>.

The weakness of the BBCi services is that they can be a bit “techno-push”. There is a balance to be struck between encouraging consumers to use sophisticated new technology versus meeting their current needs as simply and efficiently as possible. The BBC tends to do the former. For instance, when interviewing Ashley, I had no difficulty persuading him to talk about examples where eTV had proved successful (eg Wimbledon) – but I failed to coax from him examples where it had failed to generate as

<sup>14</sup>P Mercier and P Barwise, *Digital Television in the UK: Consumer Responses to Interactivity*. Future Media Research Programme, London Business School, January 2004 ([www.idtvconsumers2.com](http://www.idtvconsumers2.com))

much audience response as hoped. The only exception was *The Murder Game* which he admitted was “too complicated – but very rewarding for those who made the effort”. Yet, as with any product or service, improvement comes as much from learning what does not work as from learning what does.

BBCi resources are being increasingly deployed towards eTV rather than 24/7, despite the fact that the latter accounts for significantly more usage (monthly reach of about 40% of people in Sky homes versus 10%-20% for eTV, rising to 30% during Wimbledon and 50% during the 2004 Olympics). The current budget for eTV shows a year-on-year increase of 67%, versus 18% for 24/7 (Table 10).

**Table 10: BBCi Expenditure Trends**  
(Production cost plus BBC Broadcast expenditure: £millions)

Service	2002/03 Actual	2003/04 Actual	2004/05 Budget
eTV	5.6	7.8 (+39%)	13.1 (+67%)
24/7	5.4	7.5 (+39%)	8.8 (+18%)
<b>Total</b>	<b>11.0</b>	<b>15.3</b>	<b>21.9</b>

These numbers involve some accounting assumptions and, as noted above, eTV applications are inherently expensive, but the overall pattern and trend are clear: the BBC seems to be increasingly prioritising eTV over 24/7 although viewers use the latter more. This shift may be driven by the technologists' greater interest in eTV than in the older and less sophisticated 24/7, or by the fact that eTV's budgets now come out of BBC Broadcast, which has more resources than BBC New Media. It is certainly not being driven by viewers or viewer preferences.

From a public value perspective, the immediate priority should be to improve the speed of BBCi, especially 24/7. The content of the 24/7 service is fine. The problem is that it is extremely slow, especially since the only way to navigate the menu is hierarchically, eg by scrolling down to “sport”, then “football”, then “scores” then “Premiership”. Traditional teletext – still used far more than 24/7 – is not only faster (or at least, feels faster) but also allows direct access to a page if one knows the page number, as with an EPG.

I have not explored the technical detail enough to know how difficult it would be to make the 24/7 service faster and more efficiently navigable. There may be technical constraints. But when I spoke to Ashley Highfield he did suggest that, at least for the Sky platform, both eTV and 24/7 could be speeded up by 30% by spending a relatively small amount (£3 million per year for an additional transponder). I strongly recommend that the BBC do this, if necessary funding it by reducing the number of expensive eTV applications per year. From a consumer perspective, this would be likely to increase the use of interactivity significantly, at a small cost relative to the total cost of BBCi (and even less compared with the cost of bbc.co.uk).

## 2.6 Driving Digital Takeup

The BBC submission (pages 26-27) argues that the new services have played a significant role in driving the dramatic growth of Freeview. According to the BBC:

- (i) BBC services represent a “significant proportion” of channels available on Freeview and consumer surveys suggest that they are a major influence on the decision to buy Freeview.
- (ii) The BBC has backed the services through on and off air marketing and cross-channel scheduling, eg showcasing the best BBC3/4 programmes on BBC1/2.
- (ii) Research shows that the new services have “particular and distinctive appeal[s] to particular audiences” and are therefore “instrumental in attracting new audiences to digital television”.

These claims, especially the third, are explored more fully in the O&O report (pages 48-61). According to O&O, the six BBC services – the four covered in this review plus BBC News 24 and BBC Parliament – make up “over one quarter of the extra channels on Freeview” (this is partly a matter of definition, but essentially valid) and are an important reason for its adoption. O&O gives viewing share figures to support this claim, which can be summarised as follows (Table 11):

**Table 11: Viewing Shares (%) to 2003 in Freeview Only and Pay-TV Homes**

	<b>Freeview Only Homes</b>	<b>Pay TV Homes</b>
BBC1, BBC2	41.6	23.2
ITV, C4, five	43.4	28.8
Total terrestrial/analogue	84.6*	52.1
<b>BBC3, BBC4, CBeebies, CBBC</b>	<b>4.9</b>	<b>2.0</b>
BBC News 24, BBC Parliament	0.8	0.5
All BBC digital	5.6	2.5
All other	9.6	45.4
<b>Total digital channels</b>	<b>15.4</b>	<b>47.9</b>

\*This is the figure in the O&O report; there may be a small error in one of the other figures which accounts for these figures not adding up

Source: BARB, O&O analysis; O&O Report p48

On this basis, the four services under review accounted for 4.9% out of the 15.4% share of viewing in Freeview homes captured by digital channels, ie about 32% of this digital viewing. This supports the idea that these four channels have been a significant (although not dominant) driver of Freeview takeup, especially given the heavy viewing of BBC1 and BBC2 – and therefore exposure to the BBC's cross-channel promotions – in these homes.

In contrast, in pay TV homes the four services accounted for only 2.0% out of the 47.9% share captured by digital channels, a proportion of only 4.2%. This suggests that (a) the four services have been only a minor driver in the growth of pay TV, but also that (b) only a small proportion of those buying Freeview would have bought pay TV if Freeview had not been available. Most of these would most likely have bought only a low-price package.

O&O provides some further evidence that Freeview growth has been largely additional to the demand for pay TV. For instance, “More than 8 of 10 Freeview households had not [previously] considered getting any other digital TV system” (O&O pages 49-50, source not given).

O&O gives an elaborate analysis of the distinctiveness of the BBC services in terms of demographic positioning, programme sourcing, genre mix and detailed topic and programme-type mix (pages 51-61). This was based on a programme classification and schedule analysis commissioned from DGA. According to O&O, this analysis again suggests that the services have driven digital takeup and not cannibalised from commercial services.

Ofcom, in its report on market impact, concludes that the BBC has lent credibility to Freeview and cross-promoted it successfully on BBC1 and BBC2, while noting that commercial channels such as ITV1 have also played a role cross-promoting Freeview (paragraph 5.14). Ofcom reports viewing figures for Q1 2004 in Freeview homes, showing that BBC3, BBC4, CBeebies and CBBC accounted for 30% of the viewing of digital channels in those homes (close to the 32% above, derived from O&O's analysis of viewing shares to 2003). Ofcom also notes that recent research shows that the one-off payment and lack of contract were “extremely important” to two-thirds of those who had bought Freeview, and that the prices of Freeview set-top boxes (STBs) had fallen rapidly since launch – a virtuous circle for digital uptake, the STB manufacturers, and consumers (paragraph 5.13).

### **My Assessment of the Services' Role in Driving Digital Takeup**

I agree with Ofcom's conclusions. The turnaround of the DTT platform has been driven by Freeview, a BBC-led project which has already created substantial public value and has been the main engine of digital takeup over the last two years. Freeview has also encouraged interplatform competition including the proposed launch of the BSkyB-led “Freesat”.

However, relative to their resource costs (combined programme budget of £171 million in 2003 – more than five's programme budget, Ofcom paragraph 2.10), the four services' contribution to this success has been modest, while their contribution to the takeup of digital pay TV has been minimal. The main reason why I see this contribution as only modest is that the services' combined viewing share is still low. If one assumes that the only reason for Freeview adoption is to access its free-to-air DTV services, the four services account for only about 30% of the viewing of these services in Freeview homes.

A second concern is that, as discussed in Section 1.6, the great majority of the new services' budget has been allocated to the channels targeting the under-35s. This is a clear mismatch with the age profile of those who have not yet adopted DTV. If the aim is to drive digital takeup, the priority should be to provide attractive free-to-air DTV programmes for all age groups, but, if anything, more for the over-35s than for the under-35s. The BBC has weighted its resource allocation precisely the other way. The implication is that, even for Freeview, the services' role in driving takeup has probably been less than equivalent to its 30% share of the viewing of extra channels in these homes.

## **2.7 Value for Money**

Value for money is a key criterion for evaluating all BBC services. The BBC's proposals for the new services included a value for money commitment which was an important part of the Secretary of State's approval decision: “The BBC Governors have confirmed their view that they would be able to

provide a quality service within the budgets set and that the services will represent value for money for licence fee payers"<sup>15</sup>.

Assessing value for money is not a simple numerical calculation. At the broadest level, it is about the relationship between the net benefits (or public value) of a service and the cost, or opportunity cost, of providing it. It therefore starts with an evaluation of the extent to which the service has achieved its objectives. As reported in Section 1.1, the Governors' foreword to the BBC's report stated that "*The BBC's digital services were designed to help drive digital takeup, create public value and extend the reach of public service broadcasting*".

### Driving Digital Takeup

In Section 2.6, I concluded that, although the BBC has greatly contributed to digital takeup through the success of the BBC-led Freeview, the four services' contribution to this success has been modest, while their contribution to the takeup of digital pay TV has been minimal. Given the services' £171 million combined programming budget, their value for money against this criterion is poor. As already noted, part of the reason is that the BBC's resource allocation, with over 80% of the budget going to services targeted at viewers under 35, is an extreme mismatch with the age profile of the "late majority" consumers who have not yet adopted digital TV but could be persuaded to do so if it gave them more relevant programmes. Among the four services, it is BBC4 – watched mainly by older viewers – which has the greatest potential for driving digital takeup. But to achieve this, BBC4 would need to be both better resourced and to broaden its appeal. I return to this in my recommendations (Section 4.3)

### Extending the Reach of Public Service Broadcasting

As stated in Section 1.6, I am sceptical about the extent to which younger viewers are or were as "underserved" as the BBC seems to have believed when developing its digital TV strategy, and more generally about the efficiency and cost effectiveness of using television to reach narrowly defined target groups such as BBC3's 25–34s. The main exception is children, especially young children, as reflected in the high viewing of CBeebies among preschoolers (and young parents).

Except for CBeebies and, to a lesser extent, CBBC, the new services have made limited impact to-date on their target audiences, both in terms of share and reach. I have not studied their *incremental* reach – ie how many people within their target audiences watch them in a week and watch no other BBC-TV. It is clearly minimal in both absolute and percentage terms. Further, from what we know about general patterns of viewing, even among these incremental viewers, the amount of time they spend watching these channels is likely to be very low.

Given their resources, the four services taken together currently represent poor value for money against this criterion.

### Creating Public Value

In Section 1.5, I defined public value as the overall benefit of the services to the UK public, including both short- and long-term benefits, both direct and indirect benefits, and both consumer and citizenship benefits.

With some provisos, consumer benefits can be judged in the same way as for any consumer product or service, via "revealed preference" (how many people buy or choose the service) and perhaps by measuring willingness to pay or other consumer attitudes. Because the BBC's DTV services are free at

<sup>15</sup>Conditions and Approvals, 2001.

the point of use, revealed preference – ie viewing share – is a good indicator of their consumer benefit. On this basis, again with some provisos, the best metric of consumer value for money is the *programming cost per viewer hour (programming CPVH)*, that is, the service's total programming cost over a given time period divided by the number of viewing hours over the same time period, where a viewing hour represents one individual watching the channel for one hour. I return to this shortly.

Citizenship benefits are captured in the various PSB commitments in each service's remit. As reported in Sections 2.1 to 2.4, Máire Messenger Davies (for CBeebies and CBBC), Steve Hewlett (for BBC3 and BBC4) and I (for all four services) conclude that the services have almost entirely delivered – and in some cases overdelivered – on these commitments.

Since the services have largely delivered on their promised citizenship benefits and have operated within their projected budgets, they have overall met the Governors' commitment to deliver value for money in citizenship terms, ie the citizenship part of public value.

To assess their consumer value for money, I now turn to the services' programming cost per viewer hour (programming CPVH).

### Programming Cost Per Viewer Hour (Programming CPVH)

There is no simple and valid comparison between the efficiency or value for money of a BBC service and a commercial service. In terms of total cost to the viewer (or advertiser), commercial services tend to be more expensive because they have higher non-programming costs than the BBC. But in terms of programming cost per viewer hour, BBC services can be expensive because their public service remits almost invariably increase their programming costs and reduce their viewing levels.

Within the BBC, however, the programming CPVH is a valid comparative measure of consumer (as opposed to citizen/PSB) value for money, provided that allowance is made for the differences in availability of analogue versus digital-only services.

Table 12 shows the programming CPVH for the four services plus BBC1, BBC2, and News 24 for the last six quarters. To make this a fair comparison, the figures for BBC1 and BBC2 show the total quarterly programming spend, divided by the number of viewing hours *in digital homes only*: in both cases, the programming CPVH among all homes is well under half the figure shown here.

**Table 12: Programming Cost per Viewer Hour (pence)**

Service	Q2 2003	Q3 2003	Q4 2003	Q1 2004	Q2 2004	Q3 2004 <sup>2</sup>	Average
BBC1 <sup>1</sup>	12	10	10	12	11	8	11
BBC2 <sup>1</sup>	16	15	12	13	13	14	14
BBC3	46	33	28	52	24	29	35
BBC4	38	44	32	43	23	27	35
CBeebies	2	2	2	2	1	3	2
CBBC	16	20	26	27	12	7	18
News 24	9	13	10	11	12	11	11

<sup>1</sup>Total programming cost ÷ viewer hours in digital homes

<sup>2</sup>1 July-7 September

Source: BBC

Naturally, the figures include accounting assumptions to do with the costing of co-commissions, repeats, etc. Nevertheless, the broad-brush conclusions are clear. By this criterion:

1. CBeebies represents remarkable value for money (programming CPVH of around 2p) even though this excludes viewing by children under 4 years, which is not measured by BARB.
2. BBC1 and BBC2, even in digital homes, as well as News 24, represent consistently good value for money, with programming CPVH averaging 11p for BBC1 and News 24 and 14p for BBC2.
3. The programming CPVH for CBBC fluctuates significantly, between a maximum of 27p in Q1 2004 to only 7p in Q3 2004 (1 July-7 September). Some of this variation reflects school holidays, but some may reflect more competitive programming and scheduling, as claimed by Nickelodeon, supported by a study they commissioned from David Graham Associates (DGA)<sup>16</sup>. Over the last two quarters, CBBC's programming cost per viewer hour has averaged under 10p, which represents excellent value for money.
4. BBC3 and BBC4 still have much higher programming costs per viewer hour although these have improved over the last six months. The figures for both channels are similar, since BBC3 has a programme budget about 2.7 times that of BBC4 but delivers about 2.7 times as many viewer hours. Specifically, the programming CPVH of both these channels has averaged about 25p over the last two quarters, down from about 40p over the previous four quarters.

It is a matter of opinion at what programming CPVH a channel represents good or bad value for money, and this judgement is likely to be influenced by the channel's remit, genre mix, etc. For instance, BBC2's 14p CPVH in digital homes does not necessarily represent poorer value for money than BBC1's equivalent figure of 10p because of the two channels' different remits and genre mixes. In fact, some critics of the BBC argue that both these channels have been too populist and should shift their programming and scheduling to emphasise public service values – distinctiveness, challenge, range, innovation. On average, such a shift would increase the CPVH but, according to these critics, improve the BBC's value for money: it depends on one's criteria.

My personal judgement is that, despite their recent improvement, at 25p, BBC3 and BBC4 still represent poor value for money in consumer terms. I note that in June 2002, the ITC agreed a 'bottom-up' model with the BBC which projected a viewing share for BBC3 of 2% after 2-3 years, or 3.1% if its public service commitments were less stringent. The ITC also made a broad-brush 'top-down' projection (based on other channels in the market) of 2%-4% viewing share within 2-3 years<sup>17</sup>. Given these projections – used to assess BBC3's potential market impact – the channel's actual share of only 0.7% by 2Q 2004 (15-17 months from launch) is disappointing, especially since most of this share was inherited from BBC Choice.

BBC3 has still been on air for a little over 18 months and BBC4 for only a year longer. These are young channels, still finding their feet. Moreover, BBC3 in particular has a remit to innovate. Innovation implies risk-taking, which means that there will be failures as well as successes. But both channels need to continue growing in order to bring their cost per viewer hour closer to those of the other BBC channels.

Continuing digital penetration will automatically improve the digital services' (and their free-to-air competitors') value for money. For the BBC, this is especially true for BBC4 and News 24, which have somewhat older audiences and therefore more to gain from increased digital penetration (since the later adopters will tend to be older than those who have already adopted). But in addition, BBC3 and BBC4

<sup>16</sup>op.cit., DGA.

<sup>17</sup>ITC, *The New BBC3 Proposal: A second assessment*, 2002, available at [www.ofcom.org.uk](http://www.ofcom.org.uk)

need to work hard to find programmes which are within their remit but which deliver bigger audiences than now. My recommendations in Section 4.3 include some suggestions.

Increasing the impact of BBC3 and, especially, BBC4 (with some increase in resources for BBC4) will also help the services drive digital takeup and increase the reach of public service broadcasting, the other two criteria against which the new channels, taken as a whole, have so far delivered poor value for money.

### **Do the Services Represent Good Value for Money?**

The services have all largely delivered their public service (citizenship) obligations within their agreements to launch. They have operated within the budgets proposed by the BBC. In consumer terms, CBBC represents good – and CBeebies outstanding – value for money. BBC3 and BBC4, however, are not yet delivering big enough audiences and the contributions of all four services towards driving digital takeup and increasing the reach of public service broadcasting have been modest to-date.

Taking both aspects into consideration – that is, citizenship (PSB obligations) and consumer (mainly CPVH) – I believe that CBeebies represents excellent value for money, CBBC very good value for money, and BBC3 and BBC4 fairly good value for money. Assuming that BBC3 and BBC4 successfully increase their viewing levels as suggested, their consumer value for money will improve proportionately.

In absolute terms, television consumes limited resources. Shared across the UK's 25 million or so television households (including those without digital TV), BBC3 costs each household 30p per month, BBC4 and CBBC each about 12p per month, and CBeebies 3p per month. If these services did not exist, the total saving per household would be only 57p per month off the licence fee. Until digital switchover, this represents a temporary subsidy from those without to those with digital TV, but the amount is small. For instance, the cost is just over 1% of the cost of higher and further education (about £50 per month for every household in the country).

## **2.8 Performance Against Conditions: Summary and Conclusions**

Sections 2.1 to 2.7 have assessed the extent to which the four services – CBeebies, CBBC, BBC3 and BBC4 – have met their approval conditions. Sections 2.1 to 2.4 focus on content and sourcing, drawing on the reports by Máire Messenger Davies (on CBeebies and CBBC) and Steve Hewlett (on BBC3 and 4) and on Ofcom's analysis of the four services' genre mix, using BARB's classification of programmes.

In addition to the content-related criteria assessed in Sections 2.1 to 2.4, the approvals specified four further criteria: interactivity, driving digital takeup, value for money, and governance. The first three of these are covered in Sections 2.5 to 2.7, respectively. The last condition – that the governors have monitored the implementation of the new services and reported on them each year in their annual report – has been met. (The wider issue of the role of the governors is outside the scope of this report).

### **CBeebies**

Máire Messenger Davies concludes that CBeebies is a high-quality, distinctive service which has fulfilled all its commitments and conditions of approval, except for the commitment to invest in animation co-production, which the BBC acknowledges it has not fulfilled. Ofcom's analysis confirms

that a high proportion of CBeebies' content can be categorised as "educational". Máire also concludes that CBeebies represents excellent value for money, as the cheapest of the four services which also attracts the largest audiences.

My assessment is that CBeebies is a triumph, an exemplary PSB service for preschool children which lives up to its motto of 'learning through play'. It continues a long tradition of such programming, meeting both the letter and the spirit of its remit. It has a feeling of integrity and public service but has also been extremely successful at reaching and engaging its audience as well as developing new techniques and formats and, as far as possible with this age group, exploiting interactivity. I also accept Máire's view that it has not undermined preschool programming on BBC1 and BBC2.

### **CBBC**

Máire Messenger Davies's judgement is that CBBC is highly distinctive from the commercial children's channels in both content and quality as well as the absence of advertisements, with many successes but also some questions about tone and style and some other potential areas for improvement. Her qualitative research suggested that, unlike CBeebies, the CBBC channel has not yet achieved a separate identity distinct from that of CBBC programmes on BBC1 and 2. She raises the question of whether the CBBC channel should be given a new brand name to help communicate this distinction.

Although CBBC has largely met the formal conditions in its remit, and I believe it has created significant public value, I cannot give it as unequivocal a bill of health as I gave CBeebies. I agree with Máire's concerns about its tone and style, the "relentlessly youthful" presenters, the virtual absence of anyone looking older than 21 (except as a target for jokes), and the sometimes nervous and potentially patronising approach to serious subjects. Given the BBC's long experience of successful children's programming on BBC1 and 2 – admittedly, in a less competitive market and perhaps a gentler culture for children – I am confident that it can address these concerns.

Another issue relates to the use of the BBC's extensive archive. From a public value perspective, there should be scope for CBBC to exploit the archive more fully.

CBBC is operating in a more difficult market than CBeebies because of the wide age range 6-13, the greater intensity of competition, and the need for higher production costs. Perhaps for these reasons, CBBC achieves less viewing with a bigger budget than CBeebies, and therefore represents less good value for money.

I support Máire's suggestion that the BBC should explore rebranding CBBC to distinguish it more clearly from the children's programmes on BBC1 and BBC2.

### **BBC3**

Steve Hewlett concludes that BBC3 has for the most part, met its stringent approval conditions. However, he feels that the channel in general, and especially its PSB programmes such as news and current affairs, have so far failed to connect with the core audience of 25-34 year-olds in digital homes. He also suggests that the definition of "specially commissioned" should be tightened, with a correspondingly lower quota.

BBC3 is the most important of the four services in terms of resources and the most problematic to assess. Its extremely detailed remit, its genre mix, the emphasis on original UK production, and

especially the focus on a narrow, hard-to-reach target audience make its brief close to “mission impossible”, even with such a high budget. Further, because of its later launch, I am reviewing it at an earlier stage of development than for the other three services.

I agree with Steve’s view that, by and large, BBC3 is meeting its extremely tough remit in terms of genre mix, attempts to develop PSB programmes relevant to 25-34s, innovation, original UK/regional/independent production, content for viewers with sensory impairments, and general programme standards. However, I also agree with his other conclusion, that BBC3 has so far failed to “reconnect” its target age group to the BBC.

Further, based on his analysis, it appears that BBC3’s distinctive PSB programmes, notably news (excluding the headlines-only *60 Seconds*) and current affairs as well as most of the original drama, are attracting only tiny audiences. Even with popular shows, BBC3 has so far achieved little impact among either 25-34s or digital viewers in general.

The underlying reason, in my view, is the issue I discussed in Section 1.6, the BBC’s continuing overemphasis of audience segmentation and targeting. With a few specific exceptions, television is a mass medium with only weak audience segmentation, not a highly targeted niche medium. It is time the BBC accepted the well established evidence on this.

My conclusion is that BBC3 should loosen up a little, worry less about what’s different about the 25-34s, and concentrate on making good programmes with broad appeal, while still focusing on comedy, new talent, innovation and so on, which will tend to deliver a youngish audience.

## **BBC4**

BBC4 has successfully established itself as “a place to think”. It exemplifies the BBC’s traditional, self-confident public service values – meeting both the letter and the spirit of its remit – without undue stuffiness or paternalism. It is hard to assess whether it has been used as a “dumping ground” for arts and serious programming diverted from BBC1 and 2, but Steve Hewlett found no evidence that this had happened on a significant scale.

The negative aspect of BBC4’s performance is that its viewing share and reach, while growing, are both very low. Part of this stems from its low budget, £35.2 million in 2003/4. This is still only 35% of BBC3’s budget, 8.2% of BBC2’s and 3.7% of BBC1’s. Even allowing for the longer broadcast hours of BBC1 and 2 and their inclusion of programmes for the Nations and Regions, this is a massive imbalance. It is hard to see how BBC4 could sustain a full schedule of the quality viewers expect from the BBC with such a small budget.

At the same time, future digital takeup mainly depends on the appeal of the free-to-air digital channels to people who have not yet adopted. Since these non-adopters are on average older than those who have already adopted, and since BBC4 has the oldest age profile of the four services, increasing the budget and impact of this channel should take precedence over the others, especially BBC3, which already has a relatively big budget.

Increasing the impact of BBC4 is not only about resources, however, nor is it only about driving digital takeup. As with BBC3, although perhaps not to the same extent, BBC4 needs to be pragmatic about what works and what does not.

The reason for these concerns is that, although BBC4 is already creating public value despite its tight budget, it is contributing little to the broader aims of driving digital takeup and connecting with audiences. Further, its viewing share is still so low that it currently represents rather poor value for money, as discussed in Section 2.7.

## Interactivity

The new DTV services are all committed to using new technologies to connect with the audience. There are numerous examples of success, perhaps especially on the children's channels but also on BBC3 and 4. This approval condition has certainly been met.

The most important interactive medium for the BBC is the internet, via BBC Online (bbc.co.uk), which has just been subject to a major review by Philip Graf. In addition, the BBC is investing in interactive TV services linked to all its digital channels, including BBC1 and BBC2 for viewers with DTV. These fell outside the scope of the Graf review so I comment on them briefly here, although they are not limited to the four services covered by this review.

"Interactive TV services" (operating under the brand name BBCi) refers to all services which can be accessed by viewers in digital homes "pressing the red button" for extra content beyond the current broadcast stream. Within the BBC, the distinction is made between "enhanced TV" (eTV) services and "24/7" services. eTV consists of a mixture of static text and pictures, video clips, and in some cases, extra live channels for viewers who want to watch real-time (usually sports) programming which is not currently being shown on the main channel. "24/7" refers to the more generic teletext-like information accessed through the lower half of the BBCi menu.

Overall, the BBCi services have been a success. They still consume relatively modest resources (£15.3 million in 2003/4, versus £66.7 million for BBC Online) and in some cases, such as Wimbledon, usage has been high and the service has helped to introduce viewers to this type of interactivity.

The weakness of the BBCi services is that they can be a bit "techno-push". There is a balance to be struck between encouraging consumers to use sophisticated new technology versus meeting their current needs as simply and efficiently as possible. The BBC tends to do the former. For instance, it seems to be increasingly prioritising eTV over 24/7 although viewers use the latter more. This shift may be driven by the technologists' greater interest in eTV than in the older and less sophisticated 24/7, or by the fact that eTV's budgets now come out of BBC Broadcast, which has more resources than BBC New Media. It is certainly not being driven by viewers or viewer preferences.

From a public value perspective, the immediate priority should be to improve the speed of BBCi, especially 24/7. It appears that both eTV and 24/7 could be speeded up by 30% on Sky at a cost of £3 million per year. I strongly recommend that the BBC do this, if necessary funding it by reducing the number of expensive eTV applications per year.

## Driving Digital Takeup

In Section 2.6, I conclude that, although the BBC has greatly contributed to digital takeup through the success of the BBC-led Freeview, the four services' contribution to this success has been modest, while their contribution to the takeup of digital pay TV has been minimal. Given the services' £171 million combined programming budget, their performance against this criterion is poor. Part of the reason is

that the BBC's resource allocation, with over 80% of the budget going to services targeted at viewers under 35, is an extreme mismatch with the age profile of the "late majority" consumers who have not yet adopted digital TV but could be persuaded to do so if it gave them more relevant programmes. Among the four services, it is BBC4 – watched mainly by older viewers – which has the greatest potential for driving digital takeup. But to achieve this, BBC4 would need to be better resourced and to broaden its appeal. I return to this in my recommendations (Section 4.3).

### **Programming Cost per Viewer Hour (CPVH)**

CBeebies represents remarkable value for money (programming cost per viewer hour of around 2p). The CPVH for CBBC has fluctuated significantly, between a maximum of 27p in Q1 2004 to only 7p in Q3 2004 (1 July – 7 September). Over the last two quarters, CBBC's cost per viewer hour has averaged under 10p, which represents excellent value for money.

BBC3 and BBC4 have much higher costs per viewer hour although these have improved over the last six months. The CPVH figures for both channels are similar, since BBC3 has a programme budget about 2.7 times that of BBC4 but delivers about 2.7 times as many viewing hours. Specifically, the CPVH of both these channels has averaged about 25p over the last two quarters, down from about 40p over the previous four quarters. Despite this recent improvement, BBC3 and 4 still represent poor value for money in terms of their programming cost per viewer hour.

### **Conclusion: The Main Issue Is BBC3's and BBC4's Poor Value for Money**

From a citizenship perspective, the services have all largely delivered their public service obligations within their agreements to launch. They have operated within the budgets proposed by the BBC. In consumer terms, CBBC represents good – and CBeebies outstanding – value for money. BBC3 and BBC4, however, are not yet delivering big enough audiences and the contributions of all four services towards driving digital takeup and increasing the reach of public service broadcasting have been modest to-date.

Taking both aspects into consideration – that is, citizenship (PSB obligations) and consumer (mainly CPVH) – I believe that CBeebies represents excellent value for money, CBBC very good value for money, and BBC3 and BBC4 fairly good value for money. Assuming that BBC3 and BBC4 successfully increase their viewing levels as suggested, their consumer value for money will improve proportionately. Before considering how the services might evolve in the future, however, I now turn to their market impact.

## Part 3: Market Impact

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### 3.1 Introduction

The starting-point for this review is to consider each service's performance in providing value to UK viewers, as both consumers and citizens, relative to its cost. I discussed this in Part 2, using input from Máire Messenger Davies, Steve Hewlett and Ofcom, and evaluating each service against its approval conditions.

The underlying question for each service in Part 2 was: "Would the public be better off without the service and with the licence fee reduced by an amount equivalent to its cost – assuming nothing else changed?". In each case, the conclusion was that the service's public value was higher than its cost and that the service has largely met its approval conditions. The main area of concern at this, still early, stage is that BBC3 and BBC4 are delivering very small audiences and therefore represent poor value for money compared with most other BBC services. Relatedly, the services have so far done little to increase the reach of public service broadcasting or to help drive digital takeup (although the BBC has certainly done so, through the success of Freeview).

The net public value framework, however, also seeks to take account of each service's impact on the market. The assumption in Part 2, that everything else (apart from the licence fee, at the margin) would be unchanged if the service did not exist, may be wrong. For instance, if a particular BBC service competed so successfully for viewers that a commercial service targeting the same viewers was forced to exit the market – even if the commercial service represented better value for money – this would represent a reduction in *net* public value. The same would be true if the BBC service prevented the launch of a new commercial service which would have created more public value.

#### **In General, the Services' Market Impact Seems Likely to be Small**

In general, neither of these situations seems likely in practice. As noted in Section 1.7, television is a weakly segmented medium. A service such as BBC3 may target viewers aged 25-34 but (a) most of its (and its competitors') viewing is by people outside this age group and (b) BBC3 accounts for only a tiny proportion of viewing by 25-34-year-olds, even in digital homes – 1.0% in the most recent quarter.

This 1.0% share is slightly higher than BBC3's 0.7% share among all viewers (aged 4+), but not much, because of the nature of television. It is hard to see how such a small viewing share could have a perceptible "crowding out" effect, especially since the commercial channels targeting much the same age group (E4, Sky1, ITV2) also have only weakly segmented audiences.

Importantly, in the case of BBC3, permission to launch was made after the ITC's June 2002 analysis of the channel's likely market impact. Recall that the ITC had projected a viewing share of 2-4% within 2-3 years of launch. BBC3's actual viewing share (0.7% in the most recent quarter) is much lower than this – especially bearing in mind that it already inherited most of this share from BBC Choice. At least for this channel, my starting assumption is that its market impact to-date has been minimal. That of BBC4, with a viewing share of only 0.3%, is likely to have been even less.

All four new services together currently account for only 2.8% of viewing in digital homes in the most recent quarter (Table 4). This is not only significantly less than expected (at least in the case of BBC3) but also less than one-tenth of the BBC's 29% total viewing share in these homes: BBC1 alone captures more than seven times as much viewing in digital homes as all four services combined. In a largely unsegmented medium, it is hard to see such small services having much impact on either the market as a whole or on specific competitors.

These arguments are reflected in what has been happening in the market. As the Oliver & Ohlbaum (O&O) report notes – and none of the commercial submissions has questioned – during the two years since the launch of CBeebies, CBBC and BBC4 (and the year since the launch of BBC3), 44 commercial digital TV channels launched and only 17 withdrew from the market, a net increase of 27 (excluding shopping channels). This was during an advertising recession and in a difficult climate for media – especially new media – investment after the collapse of the internet bubble in 2000 and ITV Digital in May 2002. True, digital penetration grew from 37% to 54% of homes, but much of this growth came from Freeview. Most of the new commercial channels were available only on digital satellite and/or cable, whose penetration increased only from 34% to 43% of homes during those two years.

The idea that the four services, with a combined audience share of only 2.8%, have crowded commercial investment out of the market in general is implausible.

### **But There Might Be Exceptions**

Nevertheless, there might be exceptions. In particular, as I noted in Section 1.7, children – especially young children – have quite different viewing preferences from adults. Although CBeebies and CBBC account for only 1.3% and 0.5%, respectively, of viewing in digital homes, their viewing shares within their target age groups are much higher: CBeebies attracts 12% of viewing among 4- and 5 year-olds, CBBC 4% among 10-11 year-olds. Their impact on the market in general is likely to be small in absolute terms, but much of that impact is on commercial digital channels targeting the same age groups, and on the advertising-funded terrestrial channels whose schedules include some programmes for children (ITV, five, GMTV).

Further, the net public value framework used in this review (and also being adopted by Ofcom and the BBC) explicitly requires us to consider each service's market impact. This is what I do in Part 3, which is inevitably rather complex and somewhat technical in places but includes no equations or other mathematics. Readers uninterested in the detail should fast-forward to Section 3.7 or Section 4.1.

### **Analysis of Market Impact is Work In Progress**

This analysis should be considered as work in progress. To my knowledge, in no other country has anyone attempted to estimate the market impact of a public service broadcaster. In the UK, the only previous attempts to do so were O&O's November 2001 report commissioned by the BBC as part of its revised BBC3 submission and the ITC's analysis of the same proposal in June 2002, developed with media analysts David Graham Associates (DGA) and in consultation with the BBC and O&O. For his independent review of BBC Online, Philip Graf commissioned Europe Economics to advise him on issues of market impact, and Tim Gardam's current review of the BBC's digital radio services also explores their market impact.

For this review, we have the new O&O report, which concludes that the services have had little market impact. We also have Ofcom's report which evaluates O&O report's findings on the revenue impacts of the new services, exploring the sensitivity of these findings to changes in the underlying assumptions. However, Ofcom also assesses the implications of these revenue impacts for consumers by looking at how the new BBC services are affecting competition and innovation. Ofcom's report was developed with the economic consultants Reckon LLP and media consultants Spectrum.

In addition, DGA, commissioned by Nickelodeon, proposed an econometric modelling method which would be more directly data-based and, in DGA's view, more valid and objective than previous approaches based on experts' subjective assumptions. DGA's<sup>18</sup> initial work to illustrate how its proposed method might be applied produced very high estimates of the impact of CBeebies and CBBC on the children's commercial channels' advertising revenue. More recent work has produced somewhat lower estimates of this impact. Reliable application of this approach, however, would involve a substantial development programme which tested a full range of explanatory variables.

"Who shall decide when doctors disagree?" During this review, I have convened two meetings bringing most of the relevant experts together to debate the issues. We have also exchanged views by email and telephone. Ofcom proposes to continue this process over the next few months, with the aim of agreeing a joint framework and method for assessing market impact. I strongly support this proposal.

Meanwhile, I give my personal assessment of the various market impacts, drawing on the work done to-date. I start with the deceptively simple qualitative question: in what ways might the BBC's services impact the market?

### 3.2 In What Ways Might the BBC's Services Impact the Market?

In principle, a BBC digital TV service such as BBC3 could impact the market in four ways.

First, by providing attractive programmes which are free-to-air but require digital reception, the service could encourage **digital takeup** as already discussed in Section 2.6. This aim was a significant part of the February 2000 licence fee settlement which provided the resources to launch the new services. Depending on the extent to which the resulting takeup affects the penetration of each platform (Sky, digital cable, and Freeview) it will increase – or in some cases possibly decrease – the subscription and advertising revenues of the various digital platforms and channels, and decrease the revenues of advertising-funded terrestrial channels (because their viewing levels tend to be lower in digital homes, with the exception of five in Freeview homes, reflecting its less-than-universal reception in analogue terrestrial homes).

Secondly, by competing for viewers within digital homes, the service might directly reduce commercial channels' **advertising and/or subscription revenue**. Non-terrestrial commercial channels derive their revenues from up to four sources: advertising and sponsorship; platform subscription fees (sometimes called "distribution revenue") paid by multichannel platforms such as BSkyB; individual consumer subscriptions (for premium channels, especially sport and movies); and other sources such as merchandise sales, programme sales, and premium-rate telephone charges. The last category ("other") is small and the impact of the BBC services on it is negligible.

It is important to follow through this assessment of the impact on revenue to ask what it means for viewers. O&O's approach involves directly analysing the impact of the BBC's new services on choice

<sup>18</sup>op.cit., DGA.

while Ofcom looks at the implications for competition. I have effectively adopted the Ofcom approach, asking whether the digital services' revenue impact might lead any commercial services to exit the market, thereby (potentially) reducing viewer choice.

Thirdly, the service's programming investment will impact the **programme supply market** in various ways, depending on the mixture of in-house commissions, independent commissions, acquisitions of existing programmes, and repeats. Linked to this issue is the BBC's investment in training, new talent, production methods, etc. In the BBC's view, these investments, in the long term, significantly benefit the whole industry.

Finally, depending on how the above three factors evolve, the service might impact the **long-run competitiveness** of the market. This is not really separate from the other factors, but brings them together and relates them to the possible future evolution of the BBC services and the market.

Before discussing the services' market impact in detail, however, I first need to clarify the "base case" against which I believe it should be evaluated.

### 3.3 Clarifying the "Base Case"

In evaluating any project or activity either before the event (eg an investment or policy proposal) or after the event (eg a post-audit or – as here – an impact study), one is comparing two scenarios, ie with versus without the project or activity. One needs to decide the exact scope of the activity being evaluated before one can judge the difference between the two scenarios. In particular, what is the "base case" or "counterfactual", that is, the state of the world without the activity? Defining the scope of the project or activity and evaluating the base case is often both difficult and important: judgements here can drastically affect the result<sup>19</sup>.

In the present case, the situation is complicated by two factors.

#### (1) Should the Base Case Include BBC Choice and BBC Knowledge?

The BBC services have evolved in two stages (see Section 1.1). The BBC launched BBC Choice in 1998 and BBC Knowledge in 1999. The approvals for CBeebies, CBBC, BBC3 and BBC4 were to replace BBC Choice and BBC Knowledge with the four new services, using the same physical distribution channels (with CBeebies and CBBC broadcast 0600-1900 and BBC3/4 1900-2600) but with combined programming budgets increased by a factor of 2.4, from £75m in 1999/2000 (Choice £54m, including children's programmes 0600-1800; Knowledge £21m) to £180.8m in 2003/2004 (BBC3 £99.4m, BBC4 £35.2m, CBeebies/CBBC £46.2m<sup>20</sup>).

Since the starting-point for this review is to evaluate the new services against the approval conditions, the BBC asked O&O to analyse their *incremental* market impact, ie comparing the market with the new services against what would have been the case if BBC Choice and BBC Knowledge had continued. This is compatible with the earlier O&O and ITC analyses of the projected market impact of the BBC's revised proposals for BBC3 in 2002.

From a policy perspective, however, it is more helpful to think of BBC Choice and BBC Knowledge as historical steps in the evolution of the BBC's digital TV offering and to consider each of the current services under review against a base case in which the service simply did not exist.

<sup>19</sup>Patrick Barwise, Paul Marsh and Robin Wensley, Must Finance and Strategy Clash?, *Harvard Business Review*, Sept-Oct 1989.

<sup>20</sup>BBC Annual Report and Accounts 1999/2000 and 2003/2004.

Like myself, Ofcom feels that “including BBC Choice and BBC Knowledge in the counterfactual understates the market impact of the new services. The actual impact is likely to be twice the effect calculated using the O&O/BBC approach” (paragraph 2.8).

## (2) Should the Impact Include Indirect Effects Via Freeview/Digital Takeup?

In theory, the base case for each service should be the complete state of the world if the service did not exist, including our beliefs about digital penetration and its composition (Sky/cable/Freeview) if the service did not exist.

In my view, however, we should exclude from our evaluation of market impact the indirect effects on commercial platforms' and channels' revenue of each service's contribution to digital takeup. The reasons are as follows:

1. We have no valid way of quantifying the incremental contribution of a single service such as BBC3 on digital takeup, partly because we cannot separate it from the simplicity and value for money of Freeview and the contribution of the BBC's trusted brand, its other digital channels, and its promotion of digital TV in general. As discussed in Section 2.6, the four services' contribution to digital takeup has in any case been modest relative to their resource levels.
2. If we consider the *combined* impact of the four services, we have the implausible base case where the BBC launches Freeview and vigorously promotes digital TV but itself has no digital channels apart from News 24 and BBC Parliament. This would be equivalent to turkeys not merely voting for Christmas but also energetically canvassing for it. It is not a realistic counterfactual. Alternatively, we have a base case with no Freeview and with digital penetration at about 40% and growing much more slowly, partly because the BBC's effort and resources would be focussed almost entirely on BBC1 and 2.
3. Even if we could validly quantify the contribution of each service, or of all four services together, to the success of Freeview, our understanding of Freeview's resulting impact on commercial channels' and platforms' revenues is limited. Nor do we know the BBC services' contribution to the takeup of digital satellite and cable, although the evidence is that it is small (see Section 2.6). Both the O&O and Ofcom reports explore this complex issue, but the results are highly speculative.
4. Above all, *the BBC was explicitly asked to drive digital takeup* and, especially through Freeview, has done so extremely successfully. It would be perverse if the success of Freeview led me to evaluate the four services less positively because, although Freeview has clearly driven digital takeup and created significant public value, it may have reduced the revenue of most (but not all) commercial channels and platforms. This review does not consider the public value of Freeview, so in my view it equally should not consider its resulting market impact or the four services' possible contribution to that market impact.

## Conclusion: the Most Valid and Useful Main Base Case

In conclusion, *the most valid and useful base case for evaluating the market impact of each service is one in which the service does not exist (and the licence fee is correspondingly slightly reduced) but digital satellite, cable, and Freeview penetration are unchanged.*

This conclusion is controversial. If, as Ofcom recommends (and I support), an effort is made over the next few months to agree a framework for assessing market impact, one of the tasks will be to agree the base case or “counterfactual”.

My approach to this issue is largely consistent with, but somewhat complementary to, Ofcom’s approach, which I now summarise.

### Ofcom’s Approach

Ofcom examined the impact of the BBC’s new services from two perspectives:

- an overview of the effect of the new services on the overall market – i.e. the impact on developments in market structure and competition. In particular, Ofcom looked at the impact of digital takeup on the effectiveness of competition in the broadcasting sector and the extent to which the BBC is contributing to these changes.
- a closer look at specific impacts where competition or innovation may be threatened by the presence of the BBC – ie the impact on the finances and business models of specific commercial operators and the implications of these effects for competition. The BBC’s own quantification of the monetary impact of BBC’s new services on their rivals provides an important input to this analysis.

Overall, Ofcom concludes that the growth of digital TV encourages competition and that the BBC’s new services have contributed to digital uptake, although the scale of contribution (which cannot be clearly separated or precisely quantified) may have been overstated in the analysis presented by the BBC (paragraphs 2.2, 2.12, 5.15, 7.2). Digital broadcasting helps the emergence of more effective competition in the broadcasting market which tends to deliver more benefits for both consumers and citizens.

However, Ofcom finds that there are potentially significant costs associated with the BBC’s activities. Ofcom finds that there is a real risk that the BBC’s involvement may make new market entry difficult in some areas or may discourage commercial operators’ experimentation with innovative new programming. Given the BBC’s large budgets this may, in time, diminish overall levels of commercial investment, competition and innovation.

Ofcom finds that it is difficult to quantify the precise impact of the BBC’s new services on the overall competitive environment or, indeed, to separate out the impact of the new services from that of the BBC’s overall support for digital TV and radio.

However, Ofcom’s view is that the O&O approach “is based on a number of assumptions that are frequently not verified (or verifiable) and that it tends to favour the BBC where there is any ambiguity.. However, O&O also make a number of good points and raise real issues” (paragraph 4.18). Ofcom considers the O&O analysis in detail in its report and an annex.

Ofcom looked in more detail at the competitive impact of the BBC’s new services. It found that the extent of this impact was related to the following factors:

- The size of the niche being targeted by the service and more importantly the diversity and robustness of demand in the niche.
- The scale of the BBC’s investment relative to the potential size and contestability of each particular niche.
- The risk that the BBC’s new services will grow their audience by pursuing more commercial audiences.

- The risk that the BBC's new services will drive up the programming costs for commercial rivals by bidding up the price of popular acquisitions.
- The risk that the BBC's new services might limit access to key rights in such a way that commercial rivals are put at a competitive disadvantage.

Ofcom considers that safeguards can and must be put in place to minimise these risks to competition. Perhaps, most importantly, measures should be considered to provide more certainty to commercial investors, about both the BBC's current service remits, and any future digital development plans.

Ofcom also suggests that there could be real benefits if Ofcom and the BBC Governors could agree a common approach for assessing the market impact of the BBC's new services in future. Each time a BBC service is proposed or reviewed, several different impact assessments are carried out. Frequently, this results in a duplication of effort and waste of resources that would be better focused on collecting evidence of the actual impact on the market's ability to deliver what consumers and citizens want.

Ofcom argues that this common assessment framework should be broader than just considering direct market impact – it should also look at whether the proposed service is the most efficient, best 'value for money' way of achieving what the service aims to achieve (ie taking into account the budget that has been allocated to it, the appropriateness of the service's objectives and the possibility that the markets might also partly or fully provide similar types of programming).

I now discuss the services' direct impact on commercial channels' revenue (Sections 3.4), their impact on the programme supply market (Section 3.5), and their impact on the long-run competitiveness of this market (Section 3.6).

### 3.4 Direct Impact on Commercial Channels' Revenue

In evaluating the BBC services' direct impact on commercial channels' revenue, I first discuss the impact on viewing and then relate this to the resulting impact on commercial channels' revenue from advertising and platform subscription fees. Finally, I discuss the potential impact on premium channels' revenue from individual consumer subscriptions.

#### Impact on Viewing: O&O

O&O assesses the direct revenue impact of each BBC service separately, focussing mainly on the impact on advertising revenue. Relative to its base case, which as just noted includes BBC Choice and BBC Knowledge, O&O estimates the following incremental share gains up to 4Q 2003:

#### Incremental Share Gains vs BBC Choice/Knowledge: 4Q 2003

(All-day viewing, all individuals aged 4+ in multichannel homes)

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<b>BBC3</b>	<b>+0.2%</b>
<b>BBC4</b>	<b>+0.15%</b>
<b>CBeebies</b>	<b>+0.2%</b>
<b>CBBC</b>	<b>+0.3%</b>
	<hr/>
	<b>+0.85</b>
	<hr/>

O&O then makes a series of assumptions about where each service has taken its share from – other BBC networks, “commercial networks” (ie the advertising-funded terrestrial networks ITV/C4/five), and “thematic channels” (ie commercial channels available only in multichannel homes, including multigenre entertainment channels such as Sky 1, ITV2, and E4). O&O’s assumptions about the sources of the BBC services’ share gains are subjective but based on a number of factors:

- which other channels have lost and gained share since the new BBC services were launched
- which channels are available in both pay-TV and Freeview homes (since the BBC’s digital TV share gains come mostly from Freeview homes) and which are available only in pay-TV homes
- each service’s positioning and demographic audience profile versus those of other channels.

On this basis, O&O estimates that the sources of the above share gains are as shown in Table 13.

**Table 13: Sources of Incremental Share Gains: O&O**

Service	Other BBC Channels	Commercial Networks	Thematic Channels	Total
<b>BBC3</b>	-0.05	-0.05	-0.10	-0.20
<b>BBC4</b>	-0.07	-0.06	-0.02	-0.15
<b>CBeebies</b>	-0.05	-0.05	-0.10	-0.20
<b>CBBC</b>	-0.10	-0.10	-0.10	-0.30
<b>Total</b>	<b>-0.27</b>	<b>-0.26</b>	<b>-0.32</b>	<b>-0.85</b>

Source: O&O pages 68, 71, 72 and 73

In fact, O&O is more specific than this, assuming that: (i) BBC3’s and BBC4’s share gains from other BBC channels came entirely from BBC2; (ii) BBC4’s share gain from commercial networks came entirely from C4; (iii) CBeebies’ share gain from thematic channels came entirely from *Nick Jr*, *Disney Playhouse and Boomerang*; and (iv) CBBC’s share gains from other BBC channels and commercial networks came entirely from BBC1 and ITV1.

These specific assumptions are, in my view, largely untestable and, at least for BBC3 and BBC4, implausible. However, the estimates of the services’ impact on commercial channels’ revenue are not very sensitive to these assumptions, mainly because their incremental viewing share (totalling only 0.85% in digital homes, according to O&O) is so tiny.

For future reference, I note that the BBC services attract so little viewing that I do not believe one can validly estimate the source of this viewing by looking at which other channels have lost and gained share since their launch (or, with a zero base case, since the earlier launch of BBC Choice and BBC Knowledge). Other factors have been far more important: changes in channel budgets, programming and scheduling strategies, platform penetration growth, and even the performance of individual major programmes (eg *Coronation Street* and *Emmerdale* account for almost 25% of ITV’s total commercial impacts and an even higher proportion of its advertising revenue, compared with which the effects of the BBC’s digital TV services are insignificant.

O&O’s subjective assumptions about the sources of the BBC services’ very small gains in viewing share could in principle be improved by analysing the viewing behaviour of individual BARB panel members

over time, but the effort required to do this would be unlikely to be justified by the reliability of the results or their importance in helping us evaluate the BBC services' market impact.

Given the largely unsegmented nature of TV viewing (see Section 1.7 above), the simplest base assumption, at least for BBC3 and BBC4, is that they have captured viewing from other channels in proportion to these other channels' viewing shares in digital homes. This assumption could be improved by using viewing shares (i) only for the times when the particular service is transmitted (pre/post 1900), (ii) by age-group, especially for CBeebies and CBBC, and (iii) separating Freeview homes from satellite/cable homes. This would not be a huge task and, in my view, the results would be more valid than a longitudinal analysis of individual BARB panellists, given the low viewing shares of BBC's DTV services and the large number of other reasons for commercial channels gaining and losing share.

Ofcom has not attempted to develop an independent estimate of which commercial channels, or types of channel, have lost audience share to the new BBC services, partly because Spectrum's analysis showed that the results are not especially sensitive to these assumptions.

Ofcom's view is that the O&O approach "is based on a number of assumptions that are frequently not verified (or verifiable) and that it tends to favour the BBC where there is any ambiguity... However, O&O also make a number of good points and raise real issues" (paragraph 4.18). Ofcom considers the O&O analysis in detail in its report and an annex.

### **David Graham Associates (DGA): "Commercial Impacts" on Commercial Children's Multichannels**

David Graham Associates (DGA), in its outline demonstration of its proposed econometric approach, estimated that the launch of CBeebies and CBBC had led to a large reduction in the growth rate of children's "commercial impacts", where a commercial impact is usually defined as one individual having an "opportunity to see" (OTS) one 30-second commercial, as measured by BARB<sup>21</sup>. It appears, however, that this outline analysis failed to allow for the January 2002 change in the BARB contractor which, at least initially, reduced children's measured ratings by about 15%, ie significantly more than the possible impact of CBeebies and CBBC. DGA's outline analysis also had other technical limitations.

In August 2004, DGA conducted a more detailed analysis on behalf of the Satellite and Cable Broadcasters' Group. This has not been published at the time of writing but has been made available to myself, Ofcom, and DCMS, with permission for me to quote the results in this report.

This second DGA analysis models the number of commercial impacts on children's digital channels as a function of children's viewing of these channels, the number of children in pay-TV homes, and a significant but unexplained time trend. The model finds a "structural break" in 2002 around the time at which CBeebies and CBBC are assumed to have started gaining audience share.

Simply stated, DGA shows that if its pre-CBeebies/CBBC model is extrapolated beyond these channels' launch date (February 2002), the predicted number of commercial impacts is substantially more than the actual number. DGA argues that the reason for this gap is the launch of CBeebies and CBBC. It believes that its method eliminates the only other two factors which might account for the gap; (i) the change in the BARB panel (January 2002; according to DGA, the underreporting on the new panel had been "rectified" by May 2002), and (ii) the collapse of ITV Digital (which ceased broadcasting at the

<sup>21</sup>op.cit., DGA.

end of April 2002). Presumably, the model assumes that the launch of Freeview (which carries no commercial children's multichannels) is captured via the number of children in pay-TV homes.

DGA's revised model is a great improvement on its initial work for Nickelodeon, but I remain to be convinced of its validity. Leaving aside more technical issues, the basic causal argument needs further development. Given that the assumption is, presumably, that the viewing of CBeebies/CBBC has reduced the viewing of children's commercial channels and therefore the number of commercial impacts on these channels, to test this model credibly one would need to include the viewing of CBeebies/CBBC as an explicit independent variable. Conversely, the inclusion of a significant unexplained time trend raises the question of why, before the launch of CBeebies and CBBC, the number of commercial impacts increased over time, over and above the effects of viewing levels and the number of children in pay-TV homes (the only independent variables in the model, apart from the unexplained time trend).

Trade sources have suggested to me that the children's multichannels may have juggled their commercial minutage over this time period, concentrating it into the peak hour 1600-1700 to maximise the number of commercial impacts. Once this process reached its natural limit (said to be 15 minutes of commercials per hour), the number of impacts was constrained by the channels' viewing levels. This or some other factor, rather than the launch of CBeebies/CBBC, may be why the number of commercial impacts on these channels has not kept growing as fast as before.

At this stage, I believe that DGA's proposed approach has potential merit but that even the revised model still greatly overstates the impact of CBeebies/CBBC on the number of commercial impacts on children's multichannels. To test the approach further, we would in my view need to bring in the viewing of CBeebies/CBBC as an explicit independent variable and also find satisfactory ways of eliminating the unexplained time trend in commercial impacts: if something grows over time, there is probably a reason.

Ideally, we would go further, eliminating commercial impacts and using advertising revenue itself as the dependent variable. However, this would depend on the availability of revenue data and on our ability to model time lags in the advertising market. We would also need to take account of other factors such as seasonality, the overall state of the advertising market, and the fact that some food and soft drinks advertisers have reduced their investment in advertising to children in response to concerns about obesity.

### **Direct Impact on Commercial Channels' Advertising Revenue**

If the viewing of advertising-funded channels is reduced, this in turn reduces the number of commercial impacts available to advertisers (although as just discussed, the relationship may be less straightforward than it appears). It does not follow, however, that advertising revenue will decrease proportionately with the decrease in the number of commercial impacts. In the very short term, budgets might already be committed and payment to channels already agreed, so in some circumstances there might be no immediate impact on revenue (depending on whether the channel had guaranteed to deliver a certain number of viewers, whether trading was at a fixed price per impact, etc).

For the purpose of this review, however, what matters is the medium- and long-term impact on advertising revenue resulting from reduced viewing of advertising-funded channels in digital homes caused by people watching the new BBC services.

The consensus among econometricians and other experts who have analysed the TV advertising market is that it operates largely as an auction in which changes in volume (commercial impacts) lead to partially compensating changes in price (the cost per thousand commercial impacts) so that net advertising revenue (volume times average price) changes proportionately less than the number of impacts. For instance, if the number of impacts decreased by 10%, we would expect net advertising revenue to decrease, but by less than 10%.

The ratio of small changes in volume to small changes in price is known as the “*price elasticity*”. For example, if the price elasticity is -2.0, a 2% decrease in volume would lead to a 1% *increase* in price. Revenue (volume time price) would then decrease by about 1%.

The long-term price elasticity of TV advertising cannot be observed directly but it can be roughly estimated from historical data using econometric models and the results checked against what we know about marketing expenditure trends and the way advertising budgets are set within companies. Ofcom is currently working in this area and plans to publish a report, including the results of an extensive modelling exercise by PriceWaterhouse Coopers, part of a long-term forecasting project on television advertising.

This is a somewhat technical area, so at this stage I simply reproduce from the Ofcom report O&O's estimates of the net direct impact on advertising revenue and the results of Spectrum's analysis for Ofcom.

**Table 14: Estimated Net Direct Impact on Advertising Revenue**

(£million/year)	O&O	Spectrum
<b>BBC3</b>	-1.2 to -4.0	-1.5
<b>BBC4</b>	-0.9 to -2.0	-1.1
<b>CBeebies</b>	-0.7 to -1.4	-0.8
<b>CBBC</b>	-1.0 to -2.0	-1.4
<b>Total</b>	<b>-3.8 to -9.4</b>	<b>-4.8</b>

Source: Ofcom paragraph A26, Exhibit 33

Both these analyses use O&O's base case, which includes BBC Choice and BBC Knowledge. O&O's estimates use O&O's subjective assumptions about price elasticity. Spectrum uses Ofcom's current estimates of price elasticity (-1.44 for terrestrial channels and -3.8 for multichannels). These elasticity estimates are for TV advertising in general; no one has published any separate estimates for children's TV advertising, but Spectrum assumes the same elasticities as for the main market. (I agree with this as a working assumption, although I believe the PwC/Ofcom assumption of an elasticity of -3.8 for multichannels may be a slight overestimate; reducing it to, say, -2.0 or -2.5 would marginally reduce the estimated impact on multichannels' advertising revenue).

As already discussed, DGA's revised model suggests that the launch of CBeebies and CBBC has substantially reduced the number of commercial impacts on advertising-funded children's multichannels. If the results of the model are combined with the monthly cost per thousand viewers (CPT) and a price elasticity of -3.0 is assumed, the implied revenue impact is £15 million per annum. Note that this is against a base case which included children's programming on BBC Choice. I believe it is a great overestimate and that Spectrum's estimate in Table 14 (£2.2million per annum, ie £0.8million for CBeebies and £1.4million for CBBC) is much closer to the mark.

In conclusion, I do not believe we can at this stage validly quantify the direct impact of the new services on commercial channels' advertising revenue. Spectrum estimates a total impact of £4.8million per annum for the four services combined, against a base case which includes BBC Choice and Knowledge. Ofcom estimates that the impact against a zero base case (which, like myself, it considers more valid and useful) would be roughly double this.

My personal view is that the impact is of the same order as Ofcom is suggesting, something like £10 million per annum against a zero base case.

Like Spectrum, I would attribute about 50%-60% of this to BBC3 and BBC4, because although they account for less viewing than CBeebies/CBBC (1.0% share versus 1.8%), they compete against channels aimed at adults, which generate significantly more revenue per impact than commercial children's channels.

This suggests an impact of order £5-6million per annum for these two channels, 70% (say £3.5-£4 million) of which is the impact of BBC3, in line with its higher viewing share than BBC4's (0.7% versus 0.3%).

On the same basis, the direct advertising impact of CBeebies and CBBC would be £4-5 million per annum, split roughly equally between the two, because CBeebies' higher viewing share (1.3% versus 0.5%) could be compensated by CBBC's competitors' higher revenue per unit of viewing.

All these numbers involve so many assumptions that they should be taken as no more than extremely rough estimates.

From a policy perspective, the direct advertising impact to-date of BBC3 and 4 is small both in absolute terms and (in the case of BBC3) relative to the ITC's projection in June 2002, on the basis of which the BBC was given approval to launch. Further, given the weakly segmented nature of adult television viewing, this impact is likely to be widely spread across all commercial channels, roughly in proportion to their adult viewing shares (apart from a second-order age effect).

In contrast, because children's viewing is much more strongly segmented, the direct advertising impact of CBeebies and CBBC, while somewhat smaller in absolute terms than the impact of BBC3 and 4, is more concentrated on a relatively small number of commercial children's channels.

### **Direct Impact on Commercial Channels' Platform Subscription Fees**

Platform subscription fees are negotiated separately with each platform. The platform pays the channel owner an agreed monthly fee for every home which buys a multichannel package that includes the channel. There is, to my knowledge, no direct performance-related element, ie once agreed, the fee per subscriber is fixed, regardless of how much subscribers view or enjoy the channel.

With some very minor exceptions, there are only four multichannel platforms: Freeview (digital terrestrial), BSkyB (digital satellite), and the two main cable companies, NTL and Telewest. Freeview is a special case. It has limited capacity and does not pay platform subscription fees. Therefore, for practical purposes the only sources of platform subscription fees are BSkyB, NTL and Telewest. These three companies, especially BSkyB, are in a strong and growing bargaining position when negotiating with channels.

Further, the dominant player, BSkyB, is itself also the leading owner of digital channels, further strengthening its bargaining power with other channel operators.

On the selling side, as the number of channels has increased and audiences have further fragmented, each channel's bargaining power has weakened. This weakened bargaining power has caused – and been partially mitigated by – consolidation of ownership.

The net effect of these shifts in market power has been that platform fees per subscriber have decreased steadily over the last few years as documented in Ofcom's report.

Because platform fees (unlike advertising revenue) are paid on a fixed per-subscriber basis, the only way that competition from the BBC could impact this revenue in the short term would be if some consumers decided either to trade down to a cheaper package which excluded some commercial free-to-air channels, or not to subscribe to pay TV at all (or to cancel an existing subscription) and instead to buy a Freeview box, thereby reducing the number of subscribers for which these commercial channels received platform fees. This would on almost any calculation represent a net increase in consumer welfare, but in any case relates to the general issue of whether this kind of indirect effect should be included in my assessment of the new BBC digital services. In my view it should not, as already discussed in Section 3.3.

In the short term, then, the BBC services have little or no direct impact on commercial channels' revenue from platform subscription fees. In the longer term, however, the fee per subscriber will be renegotiated. The situation is then more ambiguous.

On the one hand, competition from high-quality free-to-air BBC services might in principle put pressure on platform operators to invest more in content to persuade consumers to be willing to pay their monthly subscriptions. This would increase the bargaining power of the commercial channels, especially those commercial groups with strong channel portfolios. For instance, BSkyB's proposed "Freesat" service, a competitive response to Freeview, will not attract buyers without a compelling lineup of free-to-air channels not available on Freeview.

On the other hand, if a specific commercial channel lost a share of viewing proportionately more than other commercial channels competing for the same viewers, its bargaining position would be weakened during its next subscription fee negotiation and it would be likely to end up with a lower fee per subscriber.

Given the weakly segmented nature of television, the latter scenario seems to me unlikely, except perhaps in the children's market: it is possible that CBeebies/CBBC have captured more viewing from Nickelodeon (whose programming mix is different from the BBC's, but not as different as other commercial children's channels) than from, say, The Cartoon Network. However, this still leaves the former argument, that a platform operator seeking to persuade consumers to buy a digital satellite or cable package will want to include Nickelodeon, partly to compete with the quality of children's programming on Freeview, much of it provided by CBeebies/CBBC.

In conclusion, in the short term, the direct impact of the new BBC services on channels' revenue from platform subscriptions is virtually zero. In the longer term it is ambiguous. Given the arguments above, my tentative view is that the longer-term impact is neutral (especially given the channels' current low viewing levels) but this may merit further analysis in due course.

## Impact on Premium Channels' Revenue from Individual Consumer Subscriptions

For digital satellite and cable subscribers, the availability of high-quality free-to-air services from the BBC may reduce the incentive to pay extra for a premium package of channels or for individual premium services such as FilmFour or Artsworld. There are four reasons why this is not a major issue in general:

1. As already noted in Section 2.6, the new BBC services account for only about 2% of viewing in pay TV homes. The great majority of the other 98% is for viewing of other free-to-air services. For instance, BBC1 and 2 (with a 23% viewing share in these homes) account for more than 11 times as much viewing as the four new services combined.
2. Most of the revenue from individual consumer subscriptions to premium services is for sport and movie channels. Sport and movies account for only a small proportion of the new BBC services' programming and a small proportion of their 2% viewing share in pay TV homes.
3. The BBC services are all multigenre and, in any case, TV viewing is largely unsegmented. So, even allowing for some weak segmentation (eg BBC3's 0.7% viewing share among all adults 4+ in digital homes rises to 1.0% among those aged 25-34), no premium channel aimed at adult viewers is likely to have lost a significant number of subscriptions as a result of the new BBC services.
4. More fundamentally, from a net public value perspective, if consumers voluntarily decide not to buy a premium service because of the range and quality of free-to-air services, this corresponds to a net increase in public value even in pure consumer terms. If one also includes potential citizenship benefits (assuming the BBC services provide these more than the premium commercial service), the net gain increases. In general, the cost per viewer hour (from a consumer perspective, ie including non-programming costs) is much higher for premium channels than for the BBC. If some consumers voluntarily choose not to pay the premium, we should not criticise the BBC because of the resulting revenue loss to the channel owner: the channel owner's revenue loss is the consumer's gain in reduced expenditure.

On point (3), children are different. CBeebies and CBBC have a much higher combined viewing share among children aged 4-15 in pay TV homes than BBC3's and BBC4's combined share among adults 16+ in those homes. Disney, whose four premium children's channels (Disney, Disney+1, Toon Disney and Playhouse Disney) show a mixture of movies, cartoons, comedy, and pre-school content, mainly imported from the US, may have lost some subscriptions because of competition from CBeebies and CBBC. But even in this case, most of children's viewing in those homes is not of CBeebies or CBBC, so the impact is likely to have been small and still reflecting a net gain in public value – point (4) above.

### BBC4/Artsworld

In the case of Artsworld, the revenue impact of BBC4 is also likely to be small. We have seen in Section 1.7 that audience segmentation by demographics is weak and by genre preference even weaker, and that a small channel such as BBC4 fits the "double jeopardy" pattern of both low reach (weekly 3-minutes reach of only 8%) and low average hours per viewer (0.8 hours, Table 4). *Proportionately*, BBC4 doubtless competes against Artsworld for viewers (and therefore subscribers) more than most channels. But since BBC4's viewing share is only 0.3%, even if its share among actual or prospective Artsworld subscribers were five times as high as this – which is extremely unlikely – this would still amount to only 1.5% of their viewing.

BBC4 is a free-to-air multigenre service, not an arts channel, although it does show a high proportion of arts programmes. In contrast, Artsworld is a premium thematic arts channel. However, the well-established pattern of channel reach and average hours per viewer shows that premium and thematic channels also fall close to the “double jeopardy” curve (Section 1.7, Figure 2), that is, they do not have dedicated viewers who watch them a lot. The viewing of Artsworld is not reported by BARB, but if it were, we can say with some confidence that, like BBC4 (Table 2B), it would account for only a small proportion of its own subscribers' viewing. With a £6 monthly subscription fee and significant non-programme costs, Artsworld has an inherently challenging task attracting and retaining enough subscribers to generate sufficient revenue to fund its programming. Competition for viewers from BBC4 is a very minor factor in this.

Artsworld does, however, raise two other issues related to market impact: first, the impact of the new BBC services on the programme supply market (discussed below) and second, commercial operators' uncertainty about future BBC developments (discussed within Section 3.6).

### 3.5 Impact on the Programme Supply Market

In their market impact report for the BBC, Oliver and Ohlbaum (O&O) conclude that the BBC has overall had a positive impact on the programme supply market in the UK. They argue that the £150m spent by the four services “represents more than the entire annual spending of all non-news and shopping basic thematic channels in the UK” and that 33% of that programme spend is dedicated to independent production, compared to an average of 30% for all UK broadcasting.

O&O also believes that BBC3's use of established stars in new formats has not driven up the cost of talent, although it accepts that no evidence for this is available.

#### PACT's View

Both Ofcom and PACT dispute these findings, although for different reasons. PACT represents the UK independent production sector and is therefore preoccupied by improving the opportunities and benefits for independent producers. PACT highlights a number of areas in which the BBC's activities might have a negative impact on the programme supply market. However, new terms of trade to be introduced between the BBC and independent producers, should reduce some of these problems in the future.<sup>22</sup>

- Under the old terms of trade, the BBC take all or most of the intellectual property rights in perpetuity, and producers often receive no payment for repeats of independent commissions.
- Despite its success in achieving its 25% target for independent production, BBC3 pays lower prices than terrestrial channels for commissioned programmes. (From a consumer and value for money perspective, this is not a criticism).
- Although one third of independent companies are based in the nations and regions, only half of BBC3's stated expenditure in the regions (31% of programming spend) is fully produced outside London. PACT estimates that all pre and post production for about half the programming located in the regions is carried out in London.
- For interactive television, independent producers are more likely to be hired to deliver small, discrete projects, while the BBC retains more substantial BBCi projects in house.

<sup>22</sup>[http://www.bbc.co.uk/commissioning/structure/terms\\_trade.shtml](http://www.bbc.co.uk/commissioning/structure/terms_trade.shtml)

- The BBC's strategy of pre-buying and co-producing (rather than commissioning) new children's animation excludes animation producers from the new terms of trade. This is the only genre in which the BBC does not fully commission programmes.

### **Other Broadcasters' Views**

The major terrestrial broadcasters, as well as some of the digital channels, also discussed in their submissions the BBC's impact on the programme supply market.

Artsworld, whose views on BBC4 were noted in Section 1.4, argued that BBC4 has outbid it for programme acquisitions, as well as competitively scheduled and cross promoted its programmes against those of Artsworld. The channel claims that inflation in the programme supply market has forced it to reduce its budget for new commissions.

Channel 4's submission discusses the impact on the market for people rather than programmes. The channel criticises BBC3's approach of signing new performers and presenters for relatively high profile roles, such as leading a complete series (although it should be noted that encouraging fresh talent is a specific part of BBC3's remit). In Channel 4's view, this policy drives inflation in the talent market, despite the fact that BBC3 has a much smaller audience than terrestrial channels such as Channel 4.

For ITV, the impact on the cost of acquired programming is particularly acute for children's programmes. It argues that the BBC already engages in competitive bidding for American programmes in which commercial broadcasters have shown an interest, and claims that, as a result, the BBC has recently been paying above market prices. ITV considers such behaviour to be wasteful of licence fee funding, since the programmes would have been available to viewers if the BBC had not acquired them.

In the area of children's programming, ITV believes that CBBC should increase its investment in original UK animation. In ITV's view, the financial contribution made by CBBC for co-productions is at the same level as acquisition of a complete product. The BBC should therefore invest more in supporting UK animation, rather than using its resources to inflate prices for American programmes.

ITV further criticises BBC3 for pursuing US films and sports rights, which in its view are not part of the channel's remit, arguing that market prices have consequently been inflated.

### **Ofcom's view**

In Ofcom's view, the extent of the BBC's impact on programme supply is affected by a range of factors, including the risk of the digital services driving up prices for acquired programmes. Rather than making any specific judgments about whether the four services have resulted in higher programming costs for commercial competitors, Ofcom suggests that this is one of many factors with the potential to reduce competition and innovation in the multichannel market.

Like PACT, Ofcom accepts that BBC3's large programming budget makes it a likely candidate for driving up the cost of acquired programming. Nevertheless, BBC3's many quotas and restrictions have so far prevented it from competitively bidding for acquisitions on a large scale. If BBC3's remit remains distinctive, with continued emphasis on originated, EU/EEA programming, Ofcom believes that a serious threat to competition is unlikely to develop.

Ofcom considers that, in view of their less rigorous remits, CBBC or CBeebies might in the future drive up the costs of popular acquisitions, such as animation. Ofcom therefore argues that clearer, more distinctive remits for the children's channels would improve competition and innovation in the children's market, as well as prevent any escalation of prices for acquired programming.

Ofcom is less concerned about BBC4 having a negative impact on the programme supply market, especially since the financial difficulties of the commercial channel Artsworld can not be ascribed to any individual factor, such as BBC4 driving up the prices of arts and music programming. Ofcom concludes that although Artsworld may have exaggerated the specific impact of BBC4, a more clearly defined remit for BBC4 might limit any future price inflation of music and arts acquisitions.

### **My View**

Like Ofcom, I believe the impact of BBC3 and BBC4 on the programme supply market has been overstated. I do, however, accept ITV's argument that there may be circumstances where public value is reduced if the BBC competes for high-priced acquired content against a universally available commercial channel, although I believe the argument applies equally to both players (ie the opportunity cost is the same to both players).

For CBeebies and CBBC, I am also somewhat sceptical about their impact on the programme supply market, but because they are relatively big players in this market (in comparison with BBC3 and 4 in the wider market), I believe that there may be an issue which merits further work. I note that Ofcom takes a somewhat similar view.

## **3.6 Impact on the Long-Run Competitiveness of the Market**

As already discussed, the revenue impact of BBC3, with its audience share of less than 0.7% and only 1.0% even among its core target market of 25-34s, has been both small and widely distributed among commercial channels. The impact on programme supply, given BBC3's £99m budget, has been greater, but not in my view anticompetitive, especially since most of it has been spent on original UK production, in line with BBC3's remit.

BBC4, with an audience share of less than 0.3% and a programme budget of £35m, has had significantly less impact than BBC3 on both commercial revenues and programme supply. As discussed in Sections 3.4 and 3.5, BBC4 has had proportionately more impact on the subscription-based arts channel Artsworld but, like O&O and Ofcom, I do not think that, objectively, this has been a major contributor to Artsworld's financial difficulties. Subjectively, potential investors who mistakenly believe that Artsworld and BBC4 are niche channels competing for the same viewers may have been less willing to invest, but if this is so, the BBC should not be blamed for other people's misunderstanding.

The two areas where there may be concern about the impact on long-run competitiveness are first, the children's market and second, uncertainty about future BBC developments in digital TV.

### **Children's Market**

My tentative judgement is that at its current scale the BBC is a vigorous competitor in this market rather than an anticompetitive player, but this is a market I know much less well than the main television market, so I am unable to be definitive.

## Uncertainty About Future BBC Development

Artsworld and others have argued that, whether or not the BBC's digital television services are having a significant negative market impact – the analysis reviewed here and the large number of commercial channel launches suggest that they are not – uncertainty about the BBC's future strategy and possible new services discourages commercial investment and innovation. Even though these concerns may be more about perception than reality, I agree that they should be addressed. I believe that, in practice, the BBC's priority should now be to consolidate rather than launch new services, but if new services or large changes in programme budgets or strategy are planned, we need transparent mechanisms for such plans to be clearly signalled and discussed. The BBC's June 2004 document *Building Public Value* is partly designed to address this issue.

## 3.7 Market Impact: Summary and Conclusions

Overall, the impact on the market of the four services – BBC3, BBC4, CBBC and CBeebies, seems likely to be small. The large number of commercial channels entering the market and the small number exiting suggest that the BBC's services are neither forcing channels to close, nor preventing new channels from launching. The BBC's digital services accounted for only 2.8% of viewing in digital homes in the most recent quarter – significantly less than was expected before their launch, despite the growth of Freeview homes, where BBC channels are viewed more heavily than in digital satellite and cable homes.

However, there may be exceptions to the general view that the BBC services have had little impact on the market: The children's channels are much bigger players within their market than BBC3 and BBC4 within the wider market. Although their impact on the overall market is still likely to be small, most of this impact will be on the commercial children's channels.

In Part 3, I have examined three ways in which the BBC's services might create a significant market impact: by reducing commercial channels' advertising or subscription revenue, by influencing the programme supply market, and by affecting the long-term competitiveness of the market. (For reasons discussed in Section 3.3, I exclude the indirect effects of digital takeup, which fall outside the scope of this review).

I consider it unlikely that the channels have directly reduced the revenues of commercial channels through advertising except at the margin, since the BBC services have attracted such small audiences. Moreover, owing to advertising price elasticity, a small drop in audience would not lead to a proportionate fall in revenue to the commercial channels.

The direct impact of the new BBC services on channels' revenue from platform subscriptions is extremely small in the short term, and unlikely to change much in the long term. This is mainly because television is a weakly segmented medium, and audiences for the BBC's services are taken from other channels in proportion to the level of their audiences overall. However, since children's channels do attract a more discrete audience, a substantial loss of share might reduce the bargaining power of channels such as Nickelodeon with Sky or the cable companies.

I also consider it unlikely that the BBC digital services have significantly reduced the revenue of premium channels from consumer subscriptions. Even the premium arts and performance channel Artsworld has probably not lost many subscribers as a result of BBC4's existence, since its small

number of subscribers probably watch both Artsworld and BBC4 for only a small proportion of their total viewing. Again, children's premium channels may be a partial exception.

The third potential impact of the services is on the long-run competitiveness of the market. It would be hard to argue that the BBC has made the digital TV market less competitive. Freeview has added vigorous competition to Sky and digital cable after the collapse of ITV Digital, to the extent that Sky has now committed to an early launch of its free-to-air "Freesat" platform in what is widely seen as a defensive move.

At the channel level, the impact of the new services has been small but again, the effect has been to make the market more, not less, competitive. I agree with Ofcom's view that "It is unlikely that the BBC's new services have driven, or will drive, any established TV channels out of business" (Ofcom, paragraph 6.14).

The two areas where there may be concern about the impact on long-run competitiveness are first, the children's market and second, uncertainty about future BBC developments in digital TV.

As noted, the children's market represents a distinct segment within which CBeebies and CBBC are much bigger players than BBC3 and 4 within the wider market. There may therefore be a case for further work on the market impact of the BBC children's channels (and perhaps CBBC on BBC1 and 2), especially in terms of programme acquisitions and scheduling.

I agree with Artsworld and others who have argued that, even if the BBC's actual impact on the market may have been limited, uncertainty about which markets the BBC will enter has been an unhelpful deterrent to commercial investment and innovation. We need more predictability from the BBC. In practice, this should be less of a problem in future because the BBC is now in a consolidation phase (ie it is not about to launch any more television services) and because it is adopting an explicit and transparent public value framework when proposing and evaluating the evolution of its strategy.

Finally, I support Ofcom's proposal to work with the BBC Governors to agree a framework for assessing market impact. This will reduce duplicated effort and increase clarity.

## Part 4: How Might the Services Develop in the Future?

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### 4.1 Summary of Conclusions: Performance and Market Impact

#### CBeebies

CBeebies is a triumph, an exemplary PSB service for preschool children which lives up to its motto of 'learning through play'. It continues a long tradition of such programming, meeting both the letter and the spirit of its remit. It has a feeling of integrity and public service but has also been extremely successful at reaching and engaging its audience as well as developing new techniques and formats and, as far as possible with this age group, exploiting interactivity. I accept Máire Messenger Davies's view that it has not undermined preschool programming on BBC1 and BBC2.

The BBC should be congratulated for its success with this service, which creates clear public value, as consistently reflected in audience research and in viewers' submissions.

#### CBBC

CBBC is a distinctive service with high-quality UK-produced content free from advertisements, covering a wide range of genres, and with a high proportion of original programming.

Although CBBC has largely met the formal conditions in its remit, and I believe it has created significant public value, I cannot give it as unequivocal a bill of health as I gave CBeebies. I agree with Máire Messenger Davies's concerns about its tone and style, the "relentlessly youthful" presenters, the virtual absence of anyone looking older than 21 (except as a target for jokes), and the sometimes nervous and potentially patronising approach to serious subjects. Given the BBC's long experience of successful children's programming on BBC1 and 2 – admittedly, in a less competitive market and perhaps a gentler culture for children – I am confident that it can address these concerns.

Finally, I support Máire's suggestion that the BBC should explore rebranding the CBBC channel to distinguish it more clearly from the children's programmes on BBC1 and BBC2.

#### BBC3

BBC3 is by far the most important of the four services in terms of resources and the most problematic to assess. Its extremely detailed remit, its genre mix, the emphasis on original UK production, and especially the focus on a narrow, hard-to-reach target audience make its brief close to "mission impossible", even with such a high budget. Further, because of its later launch, I am reviewing it at an earlier stage of development than for the other three services.

I agree with Steve Hewlett that, by and large, BBC3 is meeting its very tough remit in terms of genre mix, attempts to develop PSB programmes relevant to 25-34s, innovation, original UK/regional/independent production, content for viewers with sensory impairments, and general programme standards. (However, I also agree with Steve's suggestion that the BBC be invited to propose a tighter definition of "specially commissioned" which is closer to the spirit of the Secretary of State's "genuinely new to television", with a correspondingly reduced quota).

The channel has had some flops, as is inevitable for a service dedicated to innovation and risk-taking, but it has also had some great successes, especially in comedy. If the only question were whether BBC3 has met its remit conditions, the answer would be a clear yes: with a few qualifications, BBC3 is a distinctive channel with many innovative UK-produced PSB programmes aimed at 25-34s.

However, I also agree with Steve's other conclusion, that BBC3 has so far failed to "reconnect" its target age group to the BBC.

Further, based on his analysis, it appears that BBC3's distinctive PSB programmes, notably news (excluding the headlines-only *60 Seconds*) and current affairs as well as most of the original drama, are attracting only tiny audiences. In other words, not only has BBC3 achieved limited impact within its target audience, but most of that impact has come from mainstream content such as *Eastenders* and feature films.

The underlying reason, in my view, is the issue I discussed in Section 1.6, the BBC's continuing overemphasis of audience segmentation and targeting.

My conclusion is that BBC3 should loosen up a little, worry less about what's different about the 25-34s, and concentrate on making good programmes with broad appeal, while still focusing on edgy comedy, new talent and innovation, which will tend to deliver a youngish audience as well as acting as an "entertainment laboratory" for BBC1 and 2.

## **BBC4**

BBC4 has successfully established itself as "a place to think". It exemplifies the BBC's traditional, self-confident public service values – meeting both the letter and the spirit of its remit – without undue stuffiness or paternalism. It is hard to assess whether it has been used as a "dumping ground" for arts and serious programming diverted from BBC1 and 2, but Steve Hewlett found no evidence that this had happened on a significant scale.

The negative aspect of BBC4's performance is that its viewing share and reach, while growing, are both very low. Part of this stems from its low budget, £35.2 million in 2003/4. Increasing the impact of BBC4 is not only about resources, however. As with BBC3, although perhaps not to the same extent, BBC4 needs to be pragmatic about what works and what does not.

For instance, its weekday news programme *The World* (2000-2030) is in my view not working and should be either revamped or replaced by other factual programming.

Again, I would question the amount of time devoted to classical music concerts. In general, people do not want to sit in front of a television watching a concert.

The reason for these concerns is that, although BBC4 is already creating public value despite its tight budget, it is contributing little to the broader aims of driving digital takeup and connecting with audiences. Further, its viewing share is still so low that it currently represents rather poor value for money (see Section 2.7).

## **Interactivity**

Overall, the BBCi services have been a success. They consume relatively modest resources (£15.3 million in 2003/4, versus £66.7 million for BBC Online) and in some cases, such as Wimbledon, usage has been high and the service has helped to introduce viewers to this type of interactivity.

From a public value perspective, the immediate priority should be to improve the speed of BBCi, especially 24/7. The content of the service is fine. The problem is that it is extremely slow, especially since the only way to navigate the menu is hierarchically, eg by scrolling down to “sport”, then “football”, then “scores” then “Premiership”.

I have not explored the technical detail enough to know how difficult it would be to make the 24/7 service more efficiently navigable. But when I spoke to Ashley Highfield, the BBC's head of new media, he did suggest that, at least for the Sky platform, both eTV and 24/7 could be speeded up by 30% by spending a relatively small amount (£3 million per year) on an extra transponder. I strongly recommend that the BBC do this, if necessary funding it by reducing the number of expensive eTV applications per year. From a consumer perspective, this would be likely to increase the use of interactivity significantly, at a small cost relative to the total cost of BBCi (and even less compared with the cost of [bbc.co.uk](http://bbc.co.uk)).

### **Driving Digital Takeup**

The turnround of the DTT platform has been driven by Freeview, a BBC-led project which has already created substantial public value and has been the main engine of digital takeup over the last two years. Freeview has also encouraged interplatform competition including the proposed launch of the BSkyB-led “Freesat”.

However, relative to their resource costs (combined programme budget of £171 million in 2003 – more than five's programme budget, Ofcom paragraph 2.10), the four services' contribution to this success has been modest, while their contribution to the takeup of digital pay TV has been minimal. The main reason why I see this contribution as only modest is that the services' combined viewing share is still low.

A second concern is that, as discussed in Section 1.6, the great majority of the new services' budget has been allocated to the channels targeting the under-35s. This is a clear mismatch with the age profile of those who have not yet adopted DTV.

### **Value for Money**

The services have all largely delivered their public service (citizenship) obligations within their agreements to launch. They have operated within the budgets proposed by the BBC. In consumer terms, CBBC represents good – and CBeebies outstanding – value for money. BBC3 and BBC4, however, are not yet delivering big enough audiences and the contributions of all four services towards driving digital takeup and increasing the reach of public service broadcasting have been modest to-date.

### **Market Impact**

The underlying question for each service in Part 2 was: “Would the public be better off without the service and with the licence fee reduced by an amount equivalent to its cost – assuming nothing else changed?”. In each case, the conclusion was that the service's public value was higher than its cost and that the service has largely met its approval conditions. The main area of concern at this, still early, stage is that BBC3 and BBC4 are still delivering very small audiences and therefore represent poor value for money compared with most other BBC services. Relatedly, the services have so far done little to increase the reach of public service broadcasting or to help drive digital takeup (although the BBC has certainly done so, through the success of Freeview).

The net public value framework, however, also seeks to take account of each service's impact on the market. The assumption in Part 2, that everything else (apart from the licence fee, at the margin) would be unchanged if the service did not exist, may be wrong. For instance, if a particular BBC service competed so successfully for viewers that a commercial service targeting the same viewers was forced to exit the market – even if the commercial service represented better value for money – this would represent a reduction in *net* public value. The same would be true if the BBC service prevented the launch of a new commercial service which would have created more public value.

In general, neither of these situations seems likely in practice. As noted in Section 1.7, television is a weakly segmented medium. A service such as BBC3 may target viewers aged 25-34 but (a) most of its (and its competitors') viewing is by people outside this age group and (b) BBC3 accounts for only a tiny proportion of viewing by 25-34-year-olds, even in digital homes – 1.0% in the most recent quarter.

All four new services together currently account for only 2.8% of viewing in digital homes in the most recent quarter (Table 4). This is not only significantly less than expected (at least in the case of BBC3) but also less than one-tenth of the BBC's 29% total viewing share in these homes. BBC1 alone captures more than seven times as much viewing in digital homes as all four services combined. In a largely unsegmented medium, it is hard to see such small services having much impact on either the market as a whole or on specific competitors. Further, in the case of BBC3, the approval was given on the assumption that the channel's viewing share – and therefore, market impact – would be much higher than has actually happened to-date.

These arguments are reflected in what has been happening in the market. As the Oliver & Ohlbaum (O&O) report notes – and none of the commercial submissions has questioned – during the two years since the launch of CBeebies, CBBC and BBC4 (and the year since the launch of BBC3), 44 commercial digital TV channels launched and only 17 withdrew from the market, a net increase of 27 (excluding shopping channels). This was during an advertising recession and in a difficult climate for media – especially new media – investment after the collapse of the internet bubble in 2000 and ITV Digital in May 2002.

The idea that the four services, with a combined audience share of only 2.8%, have crowded commercial investment out of the market in general is implausible.

Nevertheless, there might be exceptions. In particular, children – especially young children – have quite different viewing preferences from adults. Although CBeebies and CBBC account for only 1.3% and 0.5%, respectively, of viewing in digital homes, their viewing shares within their target age groups are much higher: CBeebies attracts 12% of viewing among 4- and 5 year-olds, CBBC 4% among 10-11 year-olds. Their impact on the market in general is likely to be small in absolute terms, but much of that impact is on commercial digital channels targeting the same age groups, and on the advertising-funded terrestrial channels whose schedules include some programmes for children (ITV, five, GMTV).

For this reason, Part 3 explores the services' market impact in some detail, drawing on work by Oliver & Ohlbaum (for the BBC) and Ofcom, as well as other experts.

Assessing market impact should be seen as work in progress. It involves conceptual issues as well as issues of technical estimation. Ofcom has proposed – and I agree – that the relevant experts should work together over the next few months to agree a conceptual framework and methodology for this analysis.

Meanwhile, my analysis covers three aspects of market impact: the services' direct impact on commercial channels' revenue, their impact on the programme supply market, and their impact on the long-run competitiveness of the market.

### **Direct Impact on Commercial Channels' Revenue**

I consider it unlikely that the channels have directly reduced commercial channels' advertising revenues except at the margin, since the BBC services have attracted such small audiences. Moreover, owing to advertising price elasticity, a small drop in audience would not lead to a proportionate fall in commercial revenue.

The direct impact of the new BBC services on channels' revenue from platform subscriptions is extremely small in the short term, and unlikely to change much in the long term.

I also consider it unlikely that the BBC digital services have significantly reduced the revenue of premium channels from consumer subscriptions. Even the premium arts and performance channel Artsworld has probably not lost many subscribers as a result of BBC4's existence, since its small number of subscribers probably watch both Artsworld and BBC4 for only a small proportion of their total viewing. Again, children's premium channels may be a partial exception.

### **Impact on the Programme Supply Market**

I believe the impact of BBC3 and BBC4 on the programme supply market has been overstated. I do, however, accept ITV's argument that there may be circumstances where public value is reduced if the BBC competes for high-priced acquired content against a universally available commercial channel, although I believe the argument applies equally to both players (ie the opportunity cost is the same to both players).

For CBeebies and CBBC, I am also somewhat sceptical about their impact on the programme supply market, but because they are relatively big players in this market (in comparison with BBC3 and 4 in their market), I believe that there may be an issue which merits further work. I note that Ofcom takes a somewhat similar view.

### **Impact on the Long-run Competitiveness of the Market**

It would be hard to argue that the BBC has made the digital TV market less competitive. Freeview has added vigorous competition to Sky and digital cable after the collapse of ITV Digital, to the extent that Sky has now committed to an early launch of its free-to-air "Freesat" platform in what is widely seen as a defensive move.

At the channel level, the impact of the new services has been small but again, the effect has been to make the market more, not less, competitive. I agree with Ofcom's view that "It is unlikely that the BBC's new services have driven, or will drive, any established TV channels out of business" (Ofcom, paragraph 6.14).

The two areas where there may be concern about the impact on long-run competitiveness are first, the children's market and second, uncertainty about future BBC developments in digital TV.

As noted, the children's market represents a distinct segment within which CBeebies and CBBC are much bigger players than BBC3 and 4 within the wider market. There may therefore be a case for

further work on the market impact of the BBC children's channels (and perhaps CBBC on BBC1 and 2), especially in terms of programme acquisitions and scheduling. My tentative judgement is that at its current scale the BBC is a vigorous competitor in this market rather than an anticompetitive player, but this is a market I know much less well than the main television market, so I am unable to be definitive.

Artsworld and others have argued that, whether or not the BBC's digital television services are having a significant negative market impact – the large number of commercial channel launches suggest that they are not – uncertainty about the BBC's future strategy and possible new services discourages commercial investment and innovation. Even though these concerns may be more about perception than reality, I agree that they should be addressed. I believe that, in practice, the BBC's priority should now be to consolidate rather than to launch new services, but if new services or large changes in programme budgets or strategy are planned, we need transparent mechanisms for such plans to be clearly signalled and discussed. The BBC's June 2004 document *Building Public Value* is partly designed to address this issue.

## 4.2 The Evolving Market Context and the BBC-TV Portfolio

Before developing recommendations about how the four services might develop in the future, we need to consider both their own performance and market impact to-date (summarised in Section 4.1 above) and the evolving context within which they will be operating. In this section, we discuss this context under two headings: the wider market and the BBC's portfolio of television services.

### Evolving Market Context

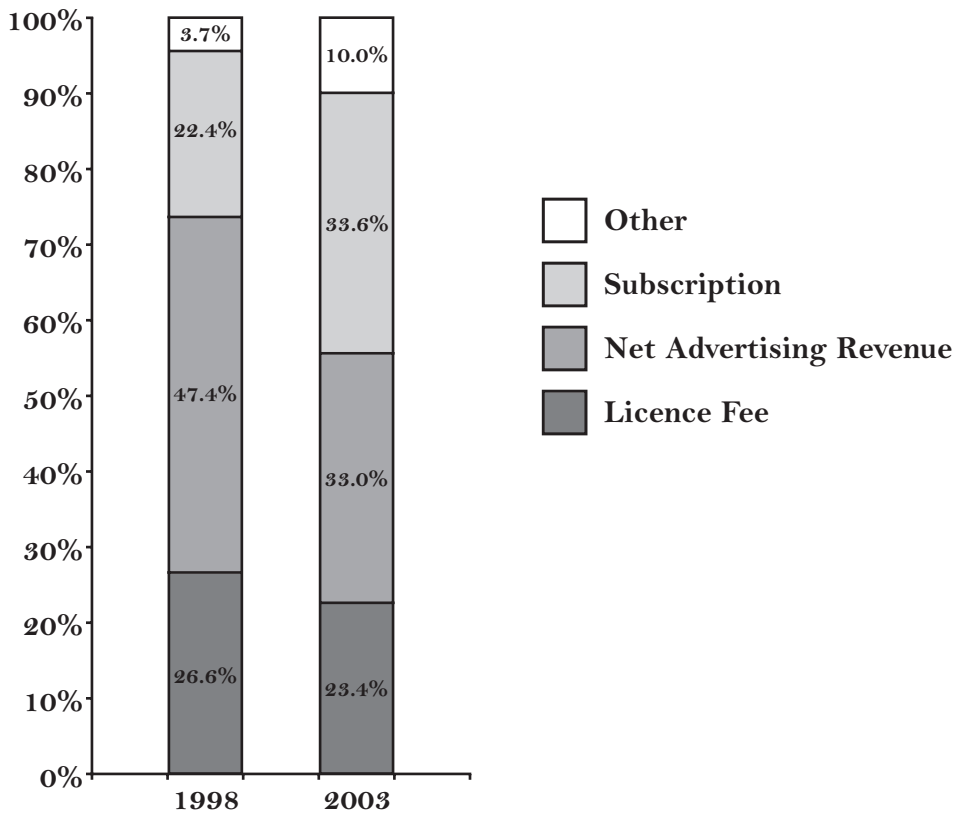
The main trend in television over the last 20 years has been the growth of **multichannel TV**, mainly funded by monthly subscriptions. This has had several effects:

- The shift from a simple market with a few universally-available channels to a *complex, multi-tier* market comprising over 40% of homes still with only four or five channels and the rest varying from Freeview homes with 30 free-to-air channels, through homes paying different levels of monthly subscription, up to about 400,000 homes (1.6%) with multichannel pay-TV and Sky+ personal video recorders (PVRs).
- In multichannel homes, *viewing is spread over many more channels*, although the five terrestrial channels still attract almost 60% of viewing in multichannel homes (85% in Freeview homes, 52% in digital satellite/cable homes) about 75% of viewing in all homes, and 80% of peak-time viewing in all homes. Channel shares among the multichannels are also extremely skewed. Even in homes with 200 channels, the average person watches only about 10–12 in any week, dominated by terrestrial channels and the top multichannels.
- Although most of the multichannels are single-genre thematic channels, *the fragmentation of viewing has not led to a segmentation of audiences*. As discussed in Section 1.7, television is a mass medium, not a niche medium. In fact, audience fragmentation has led to even lower channel and programme loyalty than in the 1980s, roughly in line with the double jeopardy pattern mentioned in Section 1.7.
- Because multichannel growth has fragmented the audience without segmenting it, *television has lost some of its efficiency as a mass high-reach advertising medium* without becoming a highly targeted medium. Overall revenue from TV advertising and sponsorship has grown somewhat faster than GDP but the consensus is that the market is now mature, partly because of a long-term shift of marketing expenditure from traditional media advertising to direct, and now interactive, marketing<sup>23</sup>.

<sup>23</sup>P Barwise and A Styler, *The MET Report 2003: Marketing Expenditure Trends 2001-04*, London Business School, 2003, ([www.london.edu/marketing/met](http://www.london.edu/marketing/met)).

- Because most of the multichannels also sell advertising, *the combined share of advertising impacts of the advertising-funded PSBs (ITV, C4, five) has declined.* Therefore, their combined share of advertising revenue has also declined, although less than proportionately to the decrease in their share of commercial impacts because the multichannels (and five) still generate less revenue per commercial impact than ITV and C4, for the reasons discussed in Section 1.7.<sup>24</sup>
- *Most of the growth in total revenue has come from pay-TV,* almost entirely monthly subscriptions (as opposed to video-on-demand or pay-per-view live events) and dominated by BSkyB, with annual revenue of £3.2 billion in 2002/03 of which 80% was subscriptions, 9% was advertising and sponsorship, and the remaining 11% was from other revenue sources such as interactive betting and the sales of extra set-top boxes.
- Despite the generous 1996 and 2000 licence settlements, *the licence fee's share of total revenue has continued to decline,* from 26.6% in 1998 to 23.4% in 2003 – despite the even steeper advertising decline (as a % of revenue) over the same period (Figure 3).

**Figure 3: Total TV Industry Revenues, by source**



Source: Ofcom

<sup>24</sup>Multichannels currently generate, on average, at least 25% less advertising revenue per commercial impact than ITV/C4. In contrast, the Financial Times generates at least 400% more ad revenue per reader column centimetre than a mass market newspaper. This reflects the difference between TV, a weakly segmented medium, and print, a strongly segmented medium. Radio is in between.

- Because commercial operators have higher non-programming costs than the BBC, with commercially funded PSBs in between, *the growth of multichannels has reduced the proportion of total revenue going into programming*. This is despite the proportion of BBC revenue going into programmes having increased from 76% in 1999/2000 to 88% in 2003/2004.
- Because lightly regulated commercial channels spend most of their programme budget on imported (mainly US) programmes, *the growth of multichannels has reduced investment in UK programming* as a proportion of both total programme expenditure and total revenue. As a result, the UK's balance of payments in TV programming has changed from a small surplus to a large deficit.
- The growth of BSkyB, combined with the collapse of ITV Digital and the historical fragmentation and unprofitability of UK cable, has led to *pay-TV being dominated by a single player* which operates as both the dominant platform and the top multichannel operator.

The recent dramatic growth of **digital TV** has reinforced these trends, mainly by increasing the number of channels which can be distributed within a given amount of physical capacity (whether by satellite, cable or terrestrial signal). The switch to digital has not yet significantly changed viewing behaviour: the overwhelming reason why people buy digital TV is to get more and/or better television, not because of DTV's new interactive capabilities.

Turning to the future, much is uncertain, but the following broad trends (and their implications for the BBC) seem likely:

1. **Continuing digital penetration** driven by BSkyB (including "Freesat") and Freeview, potentially supported by some growth in cable penetration, conversion of the remaining 800,000 analogue cable homes to digital, and some homes (eg in apartment blocks) using ordinary telephone lines converted to broadband or wideband. The Government's target for 100% digital conversion (and analogue switch-off) is 2012, just eight years away. *At this stage, all the BBC's channels will be universally available.*
2. **An evolving revenue mix**, with *the BBC's share of TV revenue continuing to decline*. Pay-TV revenue is expected to continue growing but at a decreasing rate as the market matures: BSkyB (and cable) should be able to generate more revenue per home from existing subscribers but their new customers will on average provide significantly less TV revenue per home. Revenue from advertising and sponsorship is likely to be relatively flat and may even decline if personal video recorders (PVRs) and other new technologies lead to a significant increase in viewers skipping or avoiding advertisements. (I expect PVR penetration to grow fast but recent evidence suggests that they may have less impact on advertising revenue than appeared likely a few years ago. More and better research is needed). Non-broadcast revenues from betting, games, voting etc will continue to grow from a low base, although their net profit contribution (after allowing for their incremental costs) will still be small.
3. **More new channels** will be launched by both pure commercial operators and the advertising-funded PSBs (ITV, C4, and possibly five). Currently announced plans include ITV3 and C4's More4, both aimed at 35-54s, the relaunch of AtTheRaces, and several dozen others. These channels will be funded by a combination of advertising, platform subscriptions (distribution revenue) and individual subscriptions, plus some supplementary revenue. At the same time, some further consolidation of multichannel ownership seems likely, while any decline in the advertising-funded PSBs' revenue is likely to be compensated through reduced licence payments

and perhaps weaker PSB commitments and/or some loosening of the regulation of TV advertising and sponsorship. Although some of the weaker channels will disappear, the net effect is that *the BBC will face stronger competition*, especially in satellite and cable homes.

4. **Reduced investment in UK programming** as a proportion of revenue and, perhaps, in absolute terms, continuing the trend over the last 20 years. The balance of trade on TV content may deteriorate further as lightly regulated multichannels mainly broadcasting US programmes continue to grow and/or if ITV or five is controlled by a US company. *This will reduce commercial competitors' programming costs but potentially reinforces the case for a strong BBC* (and other PSBs with commitments to invest in UK/EU/EEA content).
5. **Aggressive anti-BBC lobbying** mainly, but not exclusively, by organisations with a commercial vested interest. *The BBC will need credible, evidence-based analysis of net public value to counter these assaults.*
6. **New technologies.** Some commentators expect the growth of new interactive technologies to change dramatically what and how people watch over the next ten years. In particular, many expect a significant shift towards an "on-demand" model whereby (a) viewers pay for most of what they watch, when they watch it and (b) most viewing is time-shifted, eg off a PVR or equivalent. Some commentators also expect a new golden age of TV advertising using a range of interactive techniques and technologies, perhaps even with individual addressability. I am sceptical about the scale and speed of these trends, apart from the likely takeup of PVRs, but no-one knows how much and how fast these new technologies will impact the television market. *As now, the BBC will need to monitor these developments and adapt accordingly.*

## The BBC-TV Portfolio

Over the last seven years the BBC-TV channel portfolio has grown from two to eight channels (including BBC Parliament). Recent statements by the BBC suggest that it has no plans to expand this portfolio further. I agree with this policy: the evidence is that the BBC's resources are already stretched with eight channels. The priority should now be consolidation, with the aim of maximising the range, quality, and value for money of the existing services. This will also reduce commercial players' uncertainty about the BBC's future market impact.

News 24 was reviewed by Richard Lambert in 2002. In response to the Lambert review, the BBC acknowledges that there is scope for improvement. News 24 has made a commitment to 'a more analytical and international news agenda, with state-of-the-art interactive services' (summary of BBC's policy for News 24, p 83). BBC Parliament is a special case, with limited resources, very low viewing, and minimal impact on other channels.

BBC1 and BBC2 are the dominant channels in the BBC-TV portfolio, accounting for 87% of expenditure, 89% of BBC viewing in digital homes, and 95% of BBC viewing in all homes. The BBC's plans for these channels are spelt out in *Building Public Value* and the BBC's response to Charter Review, but it is already clear that these channels will be re-emphasising public service programming.

This is the context within which I develop my recommendations for the future development of CBeebies, CBBC, BBC4, and BBC3.

### 4.3 Recommendations for Future Development

In this review, I have concluded that CBeebies, CBBC, BBC3 and BBC4 are all creating net public value, that is, they have all largely met their remits and their market impact is limited relative to their public value, although somewhat more for CBeebies and CBBC than for BBC3 and 4, because they are bigger players within the children's market than BBC3 and 4 are within the general market.

At this stage, the main issue is that BBC3 and BBC4 have so far achieved very low viewing levels and are therefore providing relatively poor value for money as well as doing little to connect (or reconnect) the BBC with viewers. A related consequence is that, when BBC3 invests in high-cost original drama, say, little public value is created because the audience is so small compared to the number who would have seen the programme if it had been shown on BBC1 or 2. (This is partly alleviated by sharing content, but that in turn raises the question of how much of this programming would have been made anyway).

At the same time, the four services' contribution towards driving digital takeup has been modest, for three reasons:

- their low viewing levels
- over 80% of the resources are allocated towards BBC3, CBBC and CBeebies – all aimed at viewers under 35 years – although future digital takeup depends largely on older viewers, especially those aged 55+
- BBC3's excessively narrow targeting of stereotypical 25-34s, which tends to alienate older viewers and perhaps even some 25-34s themselves.

Moving forward, the priority is to increase the audience impact – and value for money – of BBC3 and BBC4 and the overall appeal of the four services, especially among those who have not yet adopted digital television but will do so if and when they believe it offers them significant relevant extra choice.

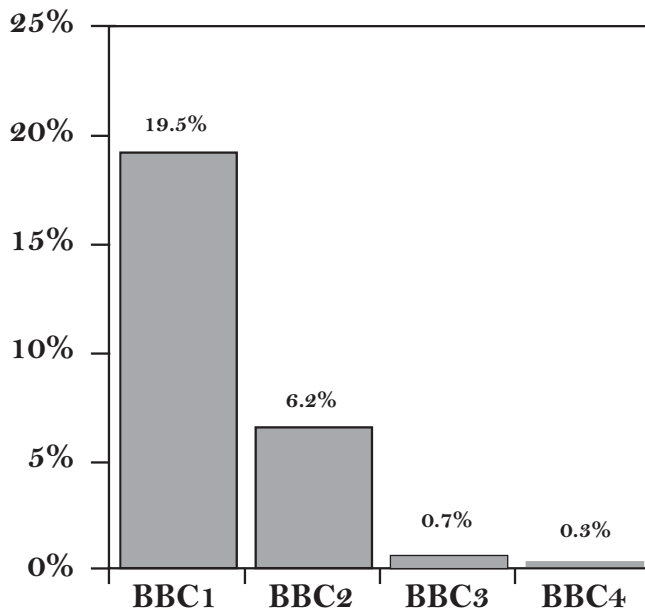
The context is an increasingly competitive and fragmented market, tight resources for the BBC, programming costs rising faster than inflation (especially for acquired programmes), and uncertain and continuously shifting competition, technology, and regulation. At the same time, the indications from the BBC are that BBC1 and BBC2 are likely to become somewhat less populist, showing more traditionally public service type programmes, potentially reducing the need for BBC3 and BBC4 to carry so much of the public service load, although reasonable people will disagree about the right balance. The net effect is that the four channels' combined viewing share (and market impact) will be lower than today, but distributed less unequally.

CBeebies and CBBC are working well, although I have some recommendations for their development, discussed later. News 24 is developing in line with the recommendations of the Lambert report. BBC Parliament, cash-strapped and constrained by broadcasting restrictions, is a separate issue. The question is how to develop BBC3 and BBC4 within the portfolio of the BBC's four mixed-genre channels for adults.

At present, the imbalance in viewing levels is extreme (Figure 4):

### Figure 4: Viewing Shares in Digital Homes

(All individuals 4+, 2Q 2004)



Source: BBC analysis of BARB

What this means is that both BBC3 and BBC4 lack salience in viewers' minds. They barely appear on the mental radar screen. As we saw in Section 1.7, even using the low cutoff of three continuous minutes, their weekly reach among all individuals in digital homes is only 21% for BBC3 and 8% for BBC4 (Table 4). In other words, they are not part of most viewers' regular channel repertoire.

We also saw that, even among those who do watch them in a week, they do so for only 0.8 hours on average – a tiny proportion of these viewers' total television viewing. Similarly, we saw that, among those who watched BBC3 in a given week, only 2.8% of their viewing the following week was of that channel (Table 2A). The equivalent figure for BBC4 was only 1.4% (Table 2B). That is, even among their own viewers, they represent a tiny proportion of viewing hours, despite apparently being seen by the BBC as niche channels.

Finally, the viewing of BBC3 is much lower than the 2%-4% projected by the ITC in 2002 when evaluating its likely market impact<sup>24</sup>.

Against this background, I list my recommendations for the BBC under four headings, in order of priority:

- Increase the impact of BBC3 and BBC4
- Focus resources to drive digital takeup
- Incremental improvements to CBBC
- Other detailed recommendations

Finally, I also list some recommendations for Government.

<sup>24</sup>ITC, *The New BBC3 Proposal: A second assessment*, 2002, available at [www.ofcom.org.uk](http://www.ofcom.org.uk)

## 1. Increase the Impact of BBC3 and BBC4

This is my most important recommendation. I am a researcher and analyst, not a broadcaster, so these suggestions about how to increase these channels' impact are tentative. The creative challenge will be to increase the channels' impact and value for money while retaining their essential public service ethos.

- 1.1 The BBC's resources can, with careful stewardship, support four high-quality mixed-genre television channels but not more. The aim should be to consolidate and rebalance this portfolio, so that within, say, 3-5 years, all four are part of most viewers' regular – or at least occasional – channel portfolios. This implies a clear strategy of *no further channel launches or major repositionings*, which will also remove a perceived source of uncertainty for commercial broadcasters.
- 1.2 *Reclassify BBC3 and BBC4 as mainstream mixed-genre channels* like BBC1 and 2, as opposed to BBC3 as “audience targeted” (like CBeebies and CBBC) and BBC4 as “special-interest” (like News 24 and BBC Parliament)<sup>25</sup>.
- 1.3 *Broaden the appeal of BBC3 by focusing less exclusively on stereotypical 25-34s* in terms of topics and especially treatments. The obsession with 25-34s is a creative straitjacket from which BBC3 should be released. Continue the process, already started by BBC3 controller Stuart Murphy, of dropping shows which did not build an audience within the first season or two and recommissioning and further developing those which did.
- 1.4 *Drop the BBC3 news at 7pm* which achieves nothing, attracts tiny audiences and means that the channel effectively does not come on air until 7:30. Redeploy the resources towards other factual programmes such as current affairs, science, and business. Start the evening with strong programming rather than trying to compete head to head with *C4 News* and *Five News*.
- 1.5 *Broaden the appeal of BBC4 by giving it more resources* (see recommendation 2.2 below) and *making it more like Radio 4 and less like Radio 3*. For instance, BBC4 should be more selective about showing arts and other programmes which virtually no-one watches. Its 8pm 30-minute news programme, *The World*, like BBC3's *7 o'Clock News*, attracts minimal audiences and should be substantially revamped or replaced with other factual programming.
- 1.6 *Explore ways of starting BBC3 and, if possible, BBC4 earlier in the evening*. This involves technical as well as financial issues which I was unable to address within this review.

How far and fast the audience of BBC3 and BBC4 should be grown depends on the BBC's overall resources as well as on the evolution of BBC1 and BBC2. A reasonable aim for BBC3 would be a viewing share of 2%-2.5% and a 15-minute weekly reach of 35%-40% (adults in digital homes) within three years. This is roughly three times the current level of viewing but still towards the bottom end of the 2002 ITC projection of a 2%-4% viewing share within 2-3 years of launch.

For BBC4, I would suggest a target of a 1.5%-2% viewing share and 25%-30% weekly reach within three years. To achieve this target, BBC4 will need significantly more resources (recommendation 2.2) as well as broader appeal (recommendation 1.5).

<sup>25</sup>BBC, *Building Public Value*, 2004, page 94

## 2. Focus Resources to Drive Digital Takeup

Increasing the impact of BBC3 and BBC4 will significantly help drive digital takeup, but it will also be important to focus resources more single-mindedly towards this objective.

- 2.1 *Research the viewing preferences of the next 3-5 million homes*, ie those who have not yet adopted digital television but whose attitudes suggest that they are the most likely to do so in the next three years. Recruiting this group is crucial for maintaining momentum towards analogue switch-off in 2012. The research should focus on what these viewers are currently watching, ideally using hard (metered) data, rather than asking them what they want, which tends to produce biased, socially acceptable responses. Programming and marketing resources can then be allocated to encourage takeup among these viewers and to maintain BBC3's/BBC4's viewing shares in those homes when they adopt.
- 2.2 *Increase resources for BBC4*, potentially the most important of the four services for driving digital takeup because its age profile matches that of the non-adopters much more closely than for CBeebies, CBBC, and BBC3. How quickly BBC4 should be built up depends on the results of the research in 2.1 as well as the wider portfolio strategy, but I recommend a significantly faster buildup than seems to be currently planned, eg doubling the budget to £70million within 2-3 years, if necessary switching some resource from BBC3.
- 2.3 *Keep promoting digital television*, as now, focusing mainly on the extra choice it provides (including digital radio) rather than on the supposed joys of interactivity. Again, the marketing strategy should be based on the results of recommendation 2.1 and other consumer research about the next 3-5 million adopters.

## 3. Incremental Improvements to CBBC

- 3.1 *Improve CBBC's tone of voice and presentation style*. The CBBC channel appears to lack the self-confidence both of CBeebies and of many children's programmes on BBC1 and 2. I recommend Dorothy Prior (controller of CBBC) and her team to read Máire Messenger Davies's report carefully and address the issues she raises: the virtual absence of anyone looking older than 21, the crassness of some of the presentation, the tastelessness and occasional cruelty of some of the programmes, the challenge of dealing with serious news topics, the unreality of the world represented on the channel. These are executional details, not fundamental issues – CBBC is performing well overall, but unlike CBeebies, it has significant scope for further improvement. Other executional recommendations by Máire include the encouragement of traditional interactivity (singing along, showing letters and drawings sent in by viewers, direct conversation with questions to camera), more European co-operation, and more use of the BBC's archive – but see (5.4b) below on the last point.
- 3.2 *Explore rebranding the CBBC channel* to distinguish it from CBBC on BBC1 and 2. The CBBC channel has not yet established itself in the minds of its target audience as a separate channel. This may be partly because the same branding is also used – and more familiar to most viewers – on BBC1 and 2. Rebranding the channel would not be costless but might be justified. I agree with Máire's suggestion that this should be explored.

In terms of resource allocation and audience impact, I see no need for significant change. CBeebies is doing a terrific job with its existing resources. CBBC needs to maintain, or

marginally grow, its share of viewing to ensure that it provides good value for money and may merit rebranding, but does not in my view need a large increase in resources to become a significant channel among its target age group.

CBBC's (and CBeebies') value for money will improve gradually as more homes adopt digital television, but less than for the other digital channels (eg BBC4 and especially News 24) because most children are already in homes with DTV.

#### 4. Other Detailed Recommendations for the BBC

- 4.1 *Speed up BBCi and improve its navigation.* The main problem with BBCi (interactive television, also referred to as the “red button services”) is its slowness. This seems to be especially an issue for the teletext-like “24/7” service, which is used more than the enhanced television (eTV) services – the other part of BBCi – but less than traditional broadcast teletext (eg Ceefax), partly because of unfamiliarity but also because of perceived slowness. Likely actions include the addition of page numbers and/or other navigation aids and the purchase of extra bandwidth, at least for the Sky platform. More generally, BBCi needs to build on its initial successes through continuing experimentation, but with more emphasis on speed, simplicity, and real consumer needs and with more explicit learning from what does not work as well as from what does.
- 4.2 *Agree a standard definition of reach and use it for all channels.* I suggest 15-minute weekly reach among all individuals in homes able to receive the channel. Other standard metrics are viewing share (at least as important as reach in most contexts) and programming cost per viewer hour.
- 4.3 *Consider formally measuring diversity on and off-screen.* This is one of Steve Hewlett's recommendations, which I support, but the BBC should investigate its practicality and whether it creates more problems than it solves. In line with the evidence that television is a mass medium not a niche medium, diversity on screen should be mainly addressed via mainstream programmes, not via separate programmes for minorities. (Radio is somewhat different).

#### 5. Recommendations for Government

- 5.1 *Ensure that policy uses evidence and analysis to maximise net public value.* Policy can never be a purely analytical exercise because it always involves both value judgements and uncertainties about the likely consequences of alternative actions. But it can and should be conducted within an explicit conceptual framework (as I have tried to do in this review – see Section 1.5) and with a clear focus on net public value. Both the BBC and Ofcom are seeking to do this, using analysis and evidence to support their proposals, but many of those seeking to influence policy do not (I single out Financial Times editorials on broadcasting policy, because the quality of analysis in the FT is usually so good). There is a need to “raise the bar” so that proposals based only on slogans, metaphors, adjectives and dogma are discounted. In the current debate, most such proposals come from people seeking to weaken or marginalise the BBC, while providing no argument or evidence as to why the public would benefit, but the same criteria should be applied to the BBC's supporters too.
- 5.2 *Ensure that the BBC continues to drive digital take-up.* The Government is aiming for analogue switch-off during the next BBC charter period, probably in 2012. Pay-TV is a maturing market, so most of the homes which have not yet gone digital will have to be either forced to do so, “bribed” through subsidy, or persuaded to switch voluntarily in order to get free-to-air digital TV

(and radio) channels. Some of them may then upgrade to a (probably low-tier) pay package and some will use the interactive features. Over time, DTV may also develop a clear advantage in sound and picture quality. But the evidence is that the main drivers will be the perceived quality of the extra free-to-air channels, the simplicity of buying and using DTV, and the fact that adoption involves a one-off payment and no monthly fees. These have been behind the success of Freeview and will also drive "Freesat". They apply equally to the replacement or conversion of analogue sets in homes which already have a digital TV. The BBC is only one of the suppliers of free-to-air digital channels, but it is an extremely important one, and could be more so if it follows the recommendations listed above, especially those listed under (1) and (2) relating to BBC3 and 4. The Government should seek to ensure that this happens.

- 5.3 *Ensure that the BBC has sufficient resources* to maximise public value and drive digital take-up. This is controversial, but in my view, recommendations 5.1 and 5.2 imply the need for a strong, well-funded BBC, which means either continuing to increase the licence fee faster than inflation (but more slowly than both GDP and commercial TV revenue) or finding other ways to ensure sufficient resources. It also implies a gradual increase in the proportion of BBC revenue going into digital broadcasting, although this is a matter for the management and governors. The need for the BBC to help drive digital take-up (and encourage BSkyB to invest in a strong free-to-air package to drive "Freesat") is only one consideration. Others include the need to continue investing in PSB content, UK and regional production, training, etc. The BBC is not the only public service broadcaster, but it is obviously a key part of the broadcasting ecology.
- 5.4 *Ask Ofcom to work towards an expert consensus on market impact.* As discussed in Part 3, market impact is a complex and still controversial topic. Ofcom has proposed that, over the next few months, there should be an attempt to agree a consensus about it especially between Ofcom itself and the BBC governors. This would need to cover the issues of definition and scope (see Sections 3.1 to 3.3) and methods for estimating the scale of market impact (see Sections 3.4 to 3.6). I agree. Two specific areas which in my view require further analysis are (a) the market impact of CBBC and advertising and (b) access to the BBC archive:
- (a) The market impact of CBBC. My judgement is that CBeebies produces huge net public benefit but CBBC is a more marginal case, because children's viewing is significantly segmented and the BBC is overall a big player in this market (with a 37.5% share on weekend breakfast-times mornings, according to an analysis sent to me by GMTV). The public value of CBBC is still substantially more than its market impact but the issue may merit further work looking at the market impact of children's BBC as a whole.
  - (b) Access to the archive. My judgement is that forcing the BBC to provide access to its archive to commercial broadcasters paying "market prices" (however determined) would not increase net public value, but this is a fairly close call and also merits further work.

## Concluding Comment

To avoid misunderstanding, I stress that I see these recommendations as evolutionary not revolutionary. For instance, although I recommend releasing BBC3 from the perceived need to target 25-34s, I expect it to build on its early successes in edgy comedy and, more generally, innovative entertainment, in a way which will in practice tend to appeal more to younger viewers. I also expect it to continue with factual programmes on topics especially relevant to these viewers, although with less of a "yoof" look and feel.

At the same time, increasing the share and reach of BBC3 and 4 in order to get them into more viewers' repertoires, and to drive digital takeup, does not mean either making BBC-TV as a whole more populist or increasing its market impact. On the contrary, the portfolio as a whole – BBC1, 2,3, and 4 – would almost certainly be less populist than today (depending on the policies for BBC1 and 2), with a slightly lower combined viewing share and market impact. The recommendations for BBC3 and 4 should be seen in that context.

## Appendix: Ofcom Analysis of Genre Mix

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### Programme Data

Ofcom was asked by DCMS in July 2004 to check the programme data provided by the BBC in its reviews of BBC3, BBC4, CBBC and CBeebies, and to compare this with other data sources.

The BBC has separately provided Ofcom with programme data about its digital channels for the purposes of the PSB Review and for measuring performance against the independent productions quota. From these two sources it is possible to derive figures for the amounts of time allocated to different genres. However, neither produced results which matched exactly the figures in the BBC Reviews. This is not in itself significant since the periods covered differ. The BBC Reviews contain data for 1 April – 30 November 2003 and other periods depending on when the channel in question started broadcasting while PSB Review data is for the calendar year 2003 and the independent productions data covers the period July 2003 – March 2004. However, the extent of the differences suggested that a further check should be made if possible.

The only independent source of data (i.e. not provided by the BBC) to which Ofcom has access is that provided by BARB. Programmes are categorised by BARB in order to measure and compare performance in audience terms of different types of programmes on different channels. However, the BARB list of programme categories is different from the BBC's. This can be overcome to some extent by combining BARB categories. More serious is the fact BARB and the BBC disagree over which categories some programmes belong to.

Not surprisingly, therefore, the first attempt to check figures in the BBC Reviews against BARB produced major discrepancies. This was despite the period covered being the same (1 April – 30 November 2003). After discussion with the BBC it was possible to resolve most of these discrepancies which were due to differences in programme categorisations, as indicated above. A number of errors were also found in the BBC's own figures and correcting these helped to reconcile the results.

The attached table compares the revised BBC figures with the original BARB figures and the revised BARB figures (i.e. amended to take account of BBC categorisations). As will be seen, the revised BBC figures and revised BARB figures are a reasonably close match. Only three areas of significant discrepancy remain: in current affairs, arts & performance and general factual on BBC4. This was because in the time available the BBC was only able to provide examples of programmes "miscategorised" by BARB in these genres rather than a full list.

It will be obvious from the above that decisions about the categorisation of programmes are key. Where differences exist it is not possible to say that the BBC is right and BARB wrong or vice versa. Programme categorisation is a highly subjective process and some programmes can legitimately fall into more than one category. To take one example, *Liquid News* on BBC3 is categorised by the BBC as "news" and by BARB as "entertainment". This accounts for most of the discrepancy between the reported figures for news (BBC 13% compared with BARB 2.1%). It also has a major impact on the reported performance of BBC3 against the requirement that at least 15% of broadcast hours must consist of news, current affairs, education, music and arts. The BBC Review reports a figure of 26%

while according to the original BARB data it is 14.6%. If *Liquid News* is left out but other differences in categorisations resolved in the BBC's favour the BARB figure increases to 16.6%.

At the end of the day a judgement has to be made based on the content of the programmes in question. Ofcom has adopted the programme classification system previously used by the ITC and expects broadcasters to use this. Until Ofcom came into existence the BBC had its own classification system but this has now been aligned with the Ofcom system. This revised BBC system was used to classify programmes on BBC digital channels for the purposes of the Reviews.

Ofcom carried out a further analysis of BARB data for the period 1 January – 30 June 2004. Some significant changes compared with the earlier BARB figures emerged such as an apparent fall in the amount of time allocated to arts & performance on BBC4 from 30.2% to 17.8% but as before, this may be due to differences in categorisations. Overall the two sets of BARB figures appear consistent.

### Comparison between BBC and BARB figures

BBC 3	1 April 2003 to 30 November 2003					
	BBC		BARB		Revised BARB	
News	272	13.0%	44	2.1%	271	12.9%
Current Affairs	75	3.6%	11	0.5%	77	3.7%
Arts & Music	130	6.2%	252	12.0%	130	6.2%
General Factual	475	22.6%	588	28.0%	486	23.2%
Education	81	3.9%			82	3.9%
Drama	167	8.0%	180	8.6%	169	8.1%
Films			109	5.2%		
Entertainment	750	35.7%	730	34.8%	730	34.8%
Other (religion, acquired, sport)	150	7.1%	184	8.8%	153	7.3%
<b>Grand Total</b>	<b>2100</b>	<b>100.0%</b>	<b>2098</b>	<b>100.0%</b>	<b>2098</b>	<b>100.0%</b>

BBC 4	1 April 2003 to 30 November 2003					
	BBC		BARB		Revised BARB	
News	78	4.2%	80	4.3%	80	4.3%
Current Affairs	152	8.1%	30	1.6%	130	6.9%
Arts & Performance	807	43.1%	567	30.2%	709	37.8%
General Factual	457	24.4%	740	39.4%	608	32.4%
Education						
Drama	74	4.0%	93	5.0%	80	4.3%
Films	179	9.6%	175	9.3%	175	9.3%
Entertainment	31	1.7%	17	0.9%	30	1.6%
Sport						
Other	<b>94</b>	<b>5.0%</b>	<b>176</b>	<b>9.4%</b>	<b>66</b>	<b>3.5%</b>
<b>Grand Total</b>	<b>1872</b>	<b>100.0%</b>	<b>1878</b>	<b>100.0%</b>	<b>1878</b>	<b>100.0%</b>

CBBC	1 April 2003 to 30 November 2003					
	BBC		BARB		Revised BARB	
News	48	1.7%			47	1.7%
Factual and Schools	768	28.1%	832	30.4%	766	28.0%
Drama	643	23.5%	588	21.5%	632	23.1%
Films						
Entertainment	780	28.5%	706	25.8%	742	27.1%
Animation	497	18.2%	588	21.5%	544	19.9%
Other			22	0.8%	5	0.2%
<b>Grand Total</b>	<b>2736</b>	<b>100.0%</b>	<b>2736</b>	<b>100.0%</b>	<b>2736</b>	<b>100.0%</b>

Cbeebies	1 April 2003 to 30 November 2003			
	BBC		BARB	
Educational/Schools	1702	61%	2056	73.7%
Children's Ent and Info	1088	39%	733	26.3%
<b>Grand Total</b>	<b>2790</b>	<b>100.00%</b>	<b>2789</b>	<b>100.0%</b>

Source: BBC/BARB/Ofcom 4.8.04

## About the Author

Patrick Barwise is Professor of Management and Marketing at London Business School. He joined LBS in 1976, having spent his early career with IBM, and has held numerous management and governance roles during his 28 years at the School.

His previous publications include the books *Television and its Audience*, *Accounting for Brands*, *Strategic Decisions*, *Predictions: Media and Advertising in a Recession*, as well as academic and practitioner papers and reports on brands, consumer and audience behaviour, strategic investment decisions, marketing expenditure trends, and new media.

His latest book *Simply Better: Winning and Keeping Customers by Delivering What Matters Most* ([www.simply-better.biz](http://www.simply-better.biz)) was described by the Financial Times as "a book about marketing for people who have read too many books about marketing". Published by Harvard Business School Press in August 2004, *Simply Better* has already sold out its initial print run of 6000.

Professor Barwise's outside activities comprise consulting, expert testimony, and pro bono work, including three years as Deputy Chairman of Consumers' Association. He is also an advisor to Ofcom, mainly on audience research.