



Proposed changes to BBC
Three, BBC iPlayer, BBC One and
CBBC
Market Impact Assessment

NON-CONFIDENTIAL VERSION –
REDACTIONS ARE INDICATED
BY A [X]

Statement

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Section 1

Executive summary

- 1.1 The BBC's Royal Charter and Agreement requires the BBC Trust (the Trust) to undertake a Public Value Test (PVT) before a decision is taken to make a significant change to the BBC's UK Public Services.
- 1.2 In January 2015 the Trust launched a PVT in response to the BBC Executive's application to proceed with the following proposed changes:
 - the closure of BBC Three as a broadcast channel;
 - the reinvention of BBC Three as an online only service;
 - the launch of a BBC One+1 channel;
 - the extension of CBBC by two further hours to broadcast from 7am until 9pm;
 - the development of BBC iPlayer beyond existing catch-up services to include an increased number of premieres and selected content commissioned by third party partners; and
 - increased investment in first run drama for BBC One (though in isolation this does not require formal approval).
- 1.3 In preparing a PVT, the Trust takes account of two separate reviews:
 - a Public Value Assessment (PVA), carried out by the Trust, which assesses the likely value of any proposed changes to the licence fee payer, particularly in terms of its contribution to the BBC's public purposes; and
 - a Market Impact Assessment (MIA), carried out by Ofcom, which assesses the effect of the proposed service changes on other services in the market. It considers both the direct impact on consumers and producers of other services, for example in terms of price and choice, and the likely impact on competition and market development, which will affect consumer and citizen interests in the longer term.
- 1.4 We have identified the following product and service providers as being most relevant to this MIA: commercial broadcasting channels; video on demand (VOD) providers and subscription VOD providers; pay TV retailers and independent production companies.
- 1.5 In assessing the potential impacts of the BBC's service proposals we have considered:
 - The static impacts in relation to affected products and services – these are the direct effects of the BBC's service proposals on affected services without taking account of how other service providers might respond. Where possible, we have sought to quantify these impacts in this MIA over the period 2015 to 2018.
 - The dynamic impacts in relation to affected products and services – these are the effects that result from changes in competitor behaviour as a result of the BBC's

service proposals and potentially broader market trends. We have not quantified these effects, which are inherently more uncertain.

- 1.6 In developing our findings we have received written responses from 13 stakeholders, commissioned our own qualitative consumer market research and sought additional data from various media tracking agencies including BARB and 3 Reasons.
- 1.7 Our assessment is based on the proposed set of changes set out in the Trust's service description for this PVT. We understand that the BBC has continued to develop its proposals beyond the service description, which may merit further assessment before being taken forward.

Context

- 1.8 The BBC's proposals state that it has to adapt to two aspects of change in the TV landscape: an increasingly complex value chain for distribution; and increasing competition from global players. In addition the BBC observes that there has been a structural shift in media consumption habits that is contributing to lower reach for BBC linear broadcast services, particularly with 16-24 year olds.
- 1.9 The BBC has noted that current proposals, to reinvent BBC Three as an online channel and extend BBC iPlayer, are part of a series of responses to these changes that focus on creating and adding more content and ensuring wider availability, with a greater emphasis on online distribution. In its role as the cornerstone of public service broadcasting (PSB), there are clearly public benefits to be gained from the BBC using new technology and new media to enhance and extend existing services, delivering benefits to consumers in the form of new and improved services.
- 1.10 In addition, we note that the BBC has the potential to act as a catalyst for market development. For example, BBC iPlayer has helped build consumer interest and take-up of on-demand services, providing opportunities for other providers to deliver new, innovative services beyond traditional TV. However, there is a balance to be struck. The BBC's involvement in new services should contribute positively to the market outcomes as a whole, rather than act to restrict competition, innovation or choice.
- 1.11 Recognising the importance of the changing TV landscape, and the fact that the BBC's proposals are part of an ongoing response, many stakeholders' comments have gone beyond considering the direct static and dynamic effects of these proposals to discuss broader issues.

Key findings from our MIA

BBC One+1 and BBC One Drama

- 1.12 The introduction of a BBC One+1 channel, combined with increased investment in BBC One drama, is likely to lead to an increase in BBC audience share. Of the proposed changes, the launch of a BBC One+1 channel will create the greatest adverse market impact on commercial channels, likely resulting in reduced profitability.¹ This is due to either a fall in commercial channel audiences leading to

¹ We estimate that the impact of launching BBC One+1 could equate to about 0.3% to 0.6% of net advertising revenue.

an expected fall in advertising revenues or, more dynamically, an increase in costs as a result of investment in content designed to recapture lost audiences.

- 1.13 In addition, the impact is unlikely to be spread evenly over different channels. ITV, for example, is likely to be more affected because of the greater direct competition between its main channel and BBC One.
- 1.14 The proposed increased investment in BBC One drama may lead to a complex mix of effects. Our analysis shows that it will heighten the impact of the proposed introduction of BBC One+1. We also note that historical data indicates that overall BBC One spend and ITV spend tend to track each other and an uplift in total BBC One spend on first run programmes may cause ITV to follow in order to maintain its advertising revenue, but not necessarily by increasing spend on drama.

The reinvention of BBC Three and BBC iPlayer enhancements

- 1.15 The proposed changes to BBC Three (i.e. closure of the broadcast channel and its reinvention online) are likely to have a positive market impact for rival TV channels. Our analysis of the changes to BBC iPlayer, as proposed, suggests that these are too limited in scale to have a notable market impact. This reflects the limited scope of the changes that are being proposed to BBC iPlayer.
- 1.16 Our consumer research commissioned in January 2015 suggests that although BBC iPlayer is increasingly being used to browse for content, typically consumers still see BBC iPlayer primarily as a place to seek specific content, rather than as a place to browse (in contrast to SVOD services such as Netflix). This limits the impact of the BBC's proposals relating to BBC iPlayer. However, should the shift in consumer behaviour towards browsing accelerate, potentially partly due to the reinvention of BBC Three online changing the perception of BBC iPlayer, then there could be a greater impact on commercial channels and on-demand providers.
- 1.17 In addition, the market research indicated that the existing BBC Three broadcast channel is perceived as primarily a "flicking channel" where viewers stumble across content. Given the BBC's plans to transfer some BBC Three programmes to other BBC broadcast channels, the recently announced loss of BBC Three's most popular content (*Family Guy* and *American Dad*), and the availability of alternative "flicking channels" (such as E4 or Dave), existing BBC Three audiences may be less likely to follow BBC Three content online (or to BBC iPlayer).
- 1.18 The BBC is proposing to include selected third-party commissioned content on BBC iPlayer. However, the criteria proposed by the BBC for selecting third-party partners is imprecise and subject to interpretation.² Without a clearer proposal (and more precision around the criteria for selecting third-party partners) there is a risk of discrimination which could result in some third-party partners being unfairly excluded from including their content on BBC iPlayer.

CBBC extension

- 1.19 We consider that the impact of the BBC's proposal to extend CBBC broadcast hours is likely to be very small.

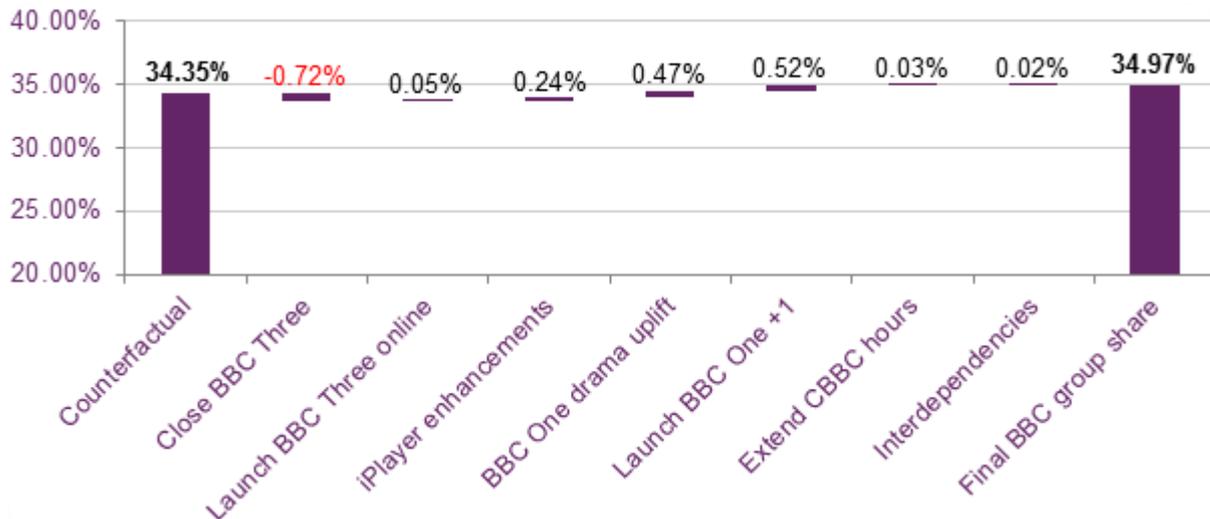
² The BBC proposes that partnerships would be limited to not-for-profit cultural and arts organisations, such as the Arts Council, who help to support the BBC's public purposes and strategic objectives.

Summary

1.20 Our modelling indicates that the aggregate financial impact of the BBC’s service proposals on commercial broadcasters’ advertising revenues (absent a dynamic response) is likely to be negative. For example, for ITV (excluding ITV Studios) we estimate the impact represents about 0.4% to 0.8% of its advertising revenues and would reduce its 2013 profit after tax by the order of 1.5% to 3.0%.

1.21 Since Channel 4 is a not-for-profit PSB it is more difficult to consider the impact of these changes on its profitability. However the impact of these proposals would directly feed through to Channel 4’s programming budget, and therefore its ability to deliver its public remit. We estimate the impact would equate to about 0.2% to 0.5% of its advertising revenues, slightly less than the impact for ITV and Channel 5. This corresponds to around 0.5% to 1.0% of Channel 4’s first run, UK originated programme budget.³ While these proposals are unlikely to call into question the sustainability of Channel 4 Corporation in and of themselves, they will add to the already challenging environment in which it is operating.

Figure 1.1: BBC viewing share changes from each proposal, 2018 modelled share^{4 5}



Source: Ofcom calculations based on adaptation of the Communications Chambers’ model using BARB data. Individuals 4+.

Note: change from each proposal as though applied on a standalone basis. “Final BBC group share” is the BBC’s estimated share of all viewing (live linear, PVR and catch-up) if all proposals were adopted in the base case.

1.22 Figure 1.1 above provides our forecast of the change in the BBC’s viewing share as a result of each of the BBC’s service proposals, in our base-case scenario. It shows that overall these proposals will lead to the BBC gaining share of total viewing, largely due to the BBC capturing more viewers as a result of launching BBC One+1 which is not completely offset by the closure of BBC Three.

³ Source: Based on 2013 data. PSB Consultation

<http://stakeholders.ofcom.org.uk/binaries/consultations/psb-review-3/summary/PSBR-3.pdf>

⁴ This is the BBC group share of total viewing. Total viewing is defined as: total live linear viewing hours + total PVR viewing hours + total catch-up viewing hours.

⁵ Counterfactual represents the expected viewing share of the BBC without the proposed service changes and with no change in total viewing hours or in viewing options provided by commercial broadcasters.

Our recommendations

- 1.23 The BBC's service proposals, notably BBC One+1, will result in a net negative impact on commercial broadcasters, particularly commercial PSBs. This may have implications for investment in content. The Trust will need to take account of these effects, alongside the outcomes of its own PVA, in forming its overall PVT decision.
- 1.24 Our recommendations focus on the following areas:
- commissioning of on-demand content production;
 - syndication of BBC on-demand content;
 - inclusion of third party content on BBC iPlayer; and
 - cross-promotion between BBC broadcast channels and on-demand content.
- 1.25 **On-demand content production.** The existing framework for BBC commissioning of content from independent production companies excludes the commissioning of on-demand only content. The shift of commissioning budgets from broadcast to on-demand could therefore lead to the loss of regulatory protection for independent production companies. This could result in less content being commissioned from the independent production sector and/or less favourable terms for independent production companies.
- 1.26 In addition, the BBC's current proposals for online commissioning are outside the existing commercial arrangements for repeat showings. The proposals to reinvent BBC Three online could result in content receiving increased online exposure due to the number of 30 day periods it will be made available online, effectively increasing the number of repeat showings relative to broadcast, with a corresponding reduction in the value of secondary content rights.
- 1.27 The Terms of Trade between the BBC and independent production companies that govern these issues have been established through commercial negotiation. The new arrangements that would be required by the service proposals are currently under negotiation. These are important commercial negotiations which may address the issues identified. We recommend that the Trust monitors progress carefully before considering whether any further action is necessary.⁶
- 1.28 **BBC on-demand content syndication.** The BBC's on-demand content syndication policy advocates standard syndication products. In practice this has generally meant standard BBC iPlayer "over the top" (OTT) applications, serving as a gateway to BBC content, rather than bespoke solutions integrated to each platform. While this is beneficial to the BBC in managing its costs, in some cases this could mean that BBC content is not as fully integrated into these platforms, making it more difficult for some users to discover BBC content and navigate between BBC and other content.
- 1.29 In the context of the scope of the changes to BBC iPlayer being considered by this MIA, the risks identified are likely to be relatively limited. However, acknowledging the BBC's long-term strategy, the terms on which platforms can access and integrate BBC on-demand content is likely to grow in importance. The Trust has recently

⁶ Ofcom has powers to provide guidance and dispute resolution to ensure 'appropriate' Terms of Trade are established.

opened a consultation on the distribution framework for BBC services and content.⁷ We believe this review is important in ensuring that commercial platforms are not unfairly disadvantaged by the way in which the BBC makes its content available.

- 1.30 **Third party content on BBC iPlayer.** We consider that the proposals for third party content on BBC iPlayer need to be developed further, particularly around the criteria for selecting third-party partners, to ensure that these are clear, objective and do not result in prospective partners being unfairly excluded.
- 1.31 **Cross-promotion of BBC services.** Our assessment of market impacts assumes that cross-promotion between BBC broadcast and BBC iPlayer services fulfils a similar role as at present. However, the Trust should note that extensive cross-promotion by the BBC may increase these impacts. We encourage the Trust to consider the role of cross-promotion as part of its assessment.
- 1.32 In conclusion, we believe the above recommendations will help the Trust to secure a balance between enabling the BBC to bring enhanced and new services to the benefit of licence fee payers while reducing the risk of adverse consequences for the development of commercial services.
- 1.33 We do not recommend specific modifications to the proposals beyond the BBC clarifying its specific proposals for third party content on BBC iPlayer. However given the BBC's long-term strategy, if the BBC wishes to extend the scope of the BBC iPlayer proposals materially, we recommend that the Trust should consider the need to conduct a further PVT.

⁷ http://www.bbc.co.uk/bbctrust/have_your_say/distribution_framework

Section 2

Introduction

The role of the MIA in the PVT process

- 2.1 Under the BBC Royal Charter and Agreement, which came into effect on 1 January 2007, a Public Value Test (PVT) must be applied before a decision can be taken to make any significant change to the BBC's public services.
- 2.2 The decision on whether to authorise a proposed change will be made by the BBC Trust (the Trust), following the application of a PVT. In reaching a decision on a PVT, the Trust must take into account the findings of two separate assessments:
- a Public Value Assessment (PVA), carried out by the Trust, which assesses the likely value of the service to licence fee payers, particularly in terms of its contribution to the BBC's public purposes; and
 - a Market Impact Assessment (MIA), carried out by Ofcom, which assesses the effect of the proposed service change on other services in the market. It considers both the direct impact on consumers and producers of other services, for example in terms of price and choice, and the likely impact on competition and market development, which will affect consumer and citizen interests in the longer term.
- 2.3 For more detail on the methodology adopted for our MIAs, please refer to the methodology document published in May 2007.⁸

The BBC's service proposals

- 2.4 In December 2014, the BBC Executive (the BBC) submitted a PVT application⁹ seeking permission to make a set of changes to the BBC's UK public services. We refer to the set of changes proposed as the service proposals.¹⁰
- 2.5 The BBC proposed to make the following changes to its UK public services:
- the closure of BBC Three as a broadcast channel in the autumn of 2015;
 - the reinvention of BBC Three as an online only service;¹¹

⁸ <http://stakeholders.ofcom.org.uk/market-data-research/other/tv-research/bbc-mias/statement/>

⁹ Public Value Assessment of the re-invention of BBC Three online and related proposals, Submission to the BBC Trust, BBC Executive, January 2015

http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/bbc_three_application.pdf. We refer to this document as the 'BBC Service Proposals document' in our Statement.

¹⁰ All documents provided by the BBC to the Trust in support of its PVT application can be found on the Trust's website http://www.bbc.co.uk/bbctrust/news/press_releases/2015/bbc_three_proposals

¹¹ We note that in April 2015, the BBC announced that the closure of BBC Three as a broadcast channel and its reinvention as an online only offering would be delayed until 2016 pending the outcome of the Trust's PVT decision. In our MIA statement we have assessed the impact of all service proposals assuming they are introduced in autumn 2015 (as described in the Trust's Service

- the development of BBC iPlayer beyond existing catch-up services to include an increased number of premieres and selected content commissioned by third party partners;
- the launch of a BBC One+1 channel (in standard definition);
- the extension of CBBC by two further hours to broadcast from 7am until 9pm; and
- increase the investment in first run drama for BBC One (though in isolation this does not require formal approval).¹²

Further details relating to each proposal is provided in the relevant sections of this document.

2.6 A full service description was produced by the Trust¹³ at the outset of the PVT process, drawing on the BBC's PVT application to the Trust.

Strategic context for BBC's service proposals

2.7 The BBC explained in its Service Proposals document that its proposals are designed to respond to a set of strategic challenges. In particular, it has indicated:¹⁴

- the competitive landscape has changed, with the emergence of global media brands offering new services and investing in global genres, such as drama and entertainment;
- the amount of funding available for the BBC to spend on its UK public services will be 25% less in real terms than it would have been by 2016/17, as a result of the licence fee freeze and new obligations placed on the BBC by government. Given these financial constraints, it is not possible to maintain the quality of the main television services through marginal cuts to existing programme budgets. It is argued that sufficient savings within the portfolio of services provided by the BBC can only be found by closing a television service, alongside continued efficiency savings; and
- a gradual transition to on-demand and a structural shift in media consumption has significantly affected the ability of the BBC to reach younger audiences: 16-24 year olds watch 14% less television than four years ago. Non-linear television viewing is growing: it accounts for 28% of average daily viewing for 16-24 year olds, but is expected to reach 40% by 2020.

2.8 The BBC has also spoken publicly about its vision of 'The BBC in the internet era', both in Tony Hall's recent speech¹⁵ and in its response to our PSB Review

Description). We consider that the announced delay by the BBC has a limited effect on our findings and conclusions.

¹² Although changes in investment are made at the discretion of the BBC, subject to oversight by the Trust, there is a dependency between the increase in drama investment on BBC One and the closure of BBC Three as a broadcast channel. Therefore, in agreement with the Trust and the Joint Steering Group, this is being considered as part of the PVT and hence the MIA.

¹³ Public value test service description of proposed changes to BBC Three, BBC iPlayer, BBC One and CBBC, BBC Trust, 20 January 2015.

http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/service_description.pdf

¹⁴ BBC Service Proposals document, pages 1-2.

consultation.¹⁶ In these the BBC recognises the continuing value of broadcast channels but sees the internet as a complement to that, with BBC iPlayer seen as a key tool in delivering its vision.

- 2.9 Our role in fulfilling the Terms of Reference is specific to considering the impact of the BBC's service proposals only (as opposed to considering potential implications of its long-term strategy).
- 2.10 However, in responding to this MIA many stakeholders' comments have gone beyond considering the direct static and dynamic effects of these proposals to discuss broader issues.
- 2.11 While the scope of our MIA is focussed on assessing the market impact of what might be considered relatively modest changes to the BBC's services, we recognise that the proposals fit within a broader long-term strategy by the BBC (that fall outside the scope of the MIA). This longer-term strategy is likely to have a significant bearing on the development of the market, competition and consumers in the future.

MIA Terms of Reference

- 2.12 For the purposes of conducting the MIA, Ofcom and the Trust established a Joint Steering Group. The Joint Steering Group set the Terms of Reference for this MIA, which were published on 20 January 2015.¹⁷ The substantive findings of the MIA, however, remain a matter of judgement for Ofcom rather than the Joint Steering Group.
- 2.13 The purpose of the MIA is to identify the products and services affected by the BBC's service proposals and to assess the impact of those proposals on these products and services.
- 2.14 In these Terms of Reference, Ofcom is charged with assessing the potential impact of the BBC's service proposals on products and services, including:¹⁸
- broadcast television services on various delivery platforms, including related advertising services;
 - on-demand services, including those offered on various platforms;
 - TV platform services; and
 - independent production, including online content providers.

¹⁵ 'The BBC in the internet era' – Tony Hall, March 2015.

<http://www.bbc.co.uk/mediacentre/speeches/2015/tony-hall-bbc-internet-era>

¹⁶ Public Sector Content in a Connected Society, Submission to Ofcom's third review of Public Service Broadcasting, February 2015, BBC

<http://stakeholders.ofcom.org.uk/binaries/consultations/psb-review-3/responses/BBC.pdf>

¹⁷ Proposed changes to BBC Three, BBC iPlayer, BBC One and CBBC, MIA Terms of Reference, Ofcom 20 January 2015. http://stakeholders.ofcom.org.uk/binaries/research/tv-research/bbc-mias/MIA_BBC_terms_of_reference_document.pdf

¹⁸ The list is not exhaustive.

Structure of this document

2.15 The remainder of this document is structured as follows:

- Section 3 discusses our approach and methodology to the MIA
- Section 4 discusses the counterfactual case used in our MIA
- Sections 5 to 10 provide our analysis of the impact of each individual proposal. The sections are structured as follows:
 - Summary of proposal;
 - Stakeholder responses;
 - Identification of affected services;
 - Assessment of impacts; and
 - Recommendations.
- Section 11 provides our assessment of the aggregate impact of the BBC's proposals
- Annex 1 is a glossary

Section 3

Approach and methodology for our MIA

- 3.1 Following Ofcom's standard approach to MIAs, our assessment involved three stages:
- first, we identified the set of products and services likely to be affected by the BBC's service proposals;
 - second, we assessed the impact of the BBC's service proposals on those products and services; and
 - third, where impacts are identified, we have considered whether the BBC's service proposals might be modified to reduce or remove the impacts identified.
- 3.2 Below we expand on our approach to the first two stages described above. We consider how the service proposals might be modified at the end of each of sections 5 to 10.
- 3.3 At the end of this section, we describe the sources of evidence we have drawn on for this MIA.

Identification of affected services

- 3.4 Our analysis to identify affected services is not a competition law market definition exercise. Instead, we have taken a broader approach, and have aimed to identify the range of related products and services that could be affected by the BBC's service proposals including affected services at different parts of the value chain.
- 3.5 We took the following steps to identify the relevant affected services:
- we examined the main features of the BBC service relevant to each service proposal (e.g. platform, content and functionality);
 - we then assessed the candidate services for which the BBC service might be a substitute. Candidate services were considered in relation to service characteristics (e.g. platform, content and functionality);
 - if there was sufficient evidence to conclude that a candidate service would be affected we then moved to the next candidate service. In each case, we drew on a mix of evidence including stakeholder responses, secondary data on substitution, market research and an assessment of service characteristics; and
 - we then considered the potential implications in other parts of the value chain relative to the candidate services identified.
- 3.6 Having gone through this process, we consider that the affected products and services are broadly the same as the preliminary view in the Terms of Reference. However, we have refined our categorisation and now consider the affected products and services as follows:

- commercial broadcasters' (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
- other Video on Demand (VOD) providers including Subscription Video on Demand (SVOD) and pay TV retailers as a result of changes in audience volumes;
- independent production companies; and
- video sharing and social media platforms e.g. YouTube, Facebook, Twitter.

Assessment of impacts

3.7 Following the identification of the affected services, we assess the impact of the BBC's service proposals in three steps:

- we assess the current and future prospects of the affected products and services in the absence of the BBC's service proposals (the counterfactual);
- we consider the likely changes in demand for the BBC's services as a result of the service proposals; and
- we assess the impact of this on the demand for affected products and services (so assessing where the change in demand for BBC services is likely to come from or flow to). Where appropriate, we assess the financial implications of the change in demand on the affected products and services.

3.8 Drawing these together allows us to reach overall conclusions on the market impact of the BBC's service proposals.

3.9 In assessing the market impacts, we have considered:

- **Static impacts** – the first-order effects of the BBC's service proposals on directly affected products and services, without taking account of how other service providers might respond, for example by altering their pricing policies or investment plans. Where possible, we have sought to quantify the static impacts over the period 2015 to 2018.
- **Dynamic impacts** – the effects of the BBC's service proposals on directly affected products and services that result from changes in competitor behaviour as a result of the BBC's service proposals and potentially broader market trends. We have not quantified these effects, which are inherently more uncertain (and potentially span a longer period in the future than the static impacts), but describe the possible nature of these impacts.
- **Wider impacts** – the effects of the BBC's service proposals for other products and services that are not directly affected. For example, this could include the impact for services that are further up the value chain such as for content rights holders (i.e. rights holders selling content rights to content service providers).

3.10 We note that in April 2015, the BBC announced that the closure of BBC Three as a broadcast channel and its reinvention as an online only offering would be delayed until 2016 pending the outcome of the Trust's PVT decision. In our MIA statement we have assessed the impact of all service proposals assuming they are introduced in

autumn 2015 (as described in the Trust’s Service Description). We consider that the announced delay by the BBC has a limited effect on our findings and conclusions.

Static impacts

3.11 This part of our analysis focuses on the likely changes in take-up and usage as a result of the BBC’s service proposals and considers how much substitution there is likely to be away from, or to commercial services. We have considered the period to 2018 (at which point we have assumed that the effects of the BBC’s service proposals will have reached a steady state).

We have not estimated the changes to consumer surplus

3.12 In principle the total static impact of the BBC’s service proposals will comprise of both:

- the change in consumer surplus – which measures the difference between the total amount that consumers are willing to pay for a good or service and the total amount that they actually pay; and
- the change in producer surplus – which measures the difference between the price at which producers are willing to supply a good or service and the price they actually receive (i.e. economic profit).

3.13 When consumers switch from consuming commercial services to consuming BBC services, there is a reduction in consumer surplus from commercial services and an increase in consumer surplus from BBC services. In some previous MIAs, we have calculated the change in consumer surplus from the change in demand for commercial services.¹⁹ We did not calculate the change in consumer surplus related to the change in demand for BBC services, as we considered that a matter for the Trust rather than Ofcom.

3.14 In relation to this MIA, the Trust has informed us that it will not be calculating the part of the change in consumer surplus related to the change in demand for BBC services. This is consistent with the approach the Trust has taken in previous MIAs. The Trust will therefore not calculate the net change in consumer surplus. Because of this, in our static analysis, we have decided not to calculate the change in consumer surplus resulting from changes in the viewing of commercial services.

3.15 We note that when consumers switch their viewing, for example, from watching commercial services to watching the BBC, then provided the service consumers switch from is still available (which is what we assume in the static analysis), viewers will only switch if they derive greater benefits (i.e. consumer surplus) compared to what they switch from. In this case, there can only be a net consumer surplus gain (at least in the short term).²⁰

¹⁹ For example, we did this in the 2006 BBC new on-demand proposals MIA, <http://stakeholders.ofcom.org.uk/binaries/research/tv-research/bbc-mias/bbc-new-ondemand.pdf>

²⁰ Consumer surplus could nevertheless reduce in the longer term if the commercial services ceased to be available or the quality reduced, and consumers then no longer had the option of moving back to using commercial services. We consider this in our assessment of dynamic impacts.

Estimating the changes to producer surplus

Overall approach to modelling changes in producer surplus

- 3.16 We have quantified the static impact of the BBC's service proposals on commercial broadcasters by estimating the change in producer surplus. We do this by estimating the impact on commercial providers' advertising revenues, which we consider a good proxy for the change in producer surplus.²¹ In this static analysis, we assume that the commercial broadcasters do not change their investment in production as a result of the BBC's service proposals.
- 3.17 To estimate the change in advertising revenue, we have adapted a version of a model produced for the BBC by Communications Chambers (CC), which the BBC provided to us. CC used this model as part of its work for the BBC to assess the impact of its service proposals on commercial services. CC's assessment (the CC report) was provided to the Trust as part of the BBC's PVT application.²²
- 3.18 We consider that this model provides a reasonable starting point for our own analysis of the static impacts of the BBC's service proposals. Using an adapted version of this model, we assess the static effects by:
- Estimating the take-up and usage of BBC and commercial services (to 2018) before the introduction of the BBC's service proposals (i.e. a counterfactual case). To forecast the counterfactual, we project total viewing hours across linear broadcasting, personal video recorder (PVR) viewing and on-demand²³ viewing.
 - Estimating the changes in viewing hours and viewing share for different channel families for each of the following, with each one considered relative to the counterfactual:
 - closing BBC Three as a broadcast channel;
 - closing BBC Three as a broadcast channel and reinventing it as an online only channel;
 - changes to BBC iPlayer;
 - increased investment in BBC One drama;
 - the launch of BBC One+1 channel; and
 - changes to the CBBC channel.

²¹ In terms of the change to producer surplus, we have assumed that the commercial providers' marginal costs are zero over the relevant change in take-up and usage. The costs of producing and distributing content is likely to be relatively invariant to small changes in viewing volumes and therefore the change in revenues will be equivalent to the change in producer surplus over the relevant change in viewing.

²² Forecast consumption and preliminary market impact assessment of revised BBC services, Communications Chambers, January 2015
http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/market_impact_assessment.pdf

²³ The model includes free-to-view long form on-demand content but excludes subscription VOD.

- For each of the service proposals above, we estimate the static change in producer surplus by estimating the impact on commercial providers' advertising revenues as a result of the change in viewing hours, as described in more detail below.
- Estimating the change in viewing hours, viewing share and advertising revenues of all the service proposals together, including any interactions between them.

3.19 In contrast to CC's approach, we initially considered the impact of each of the service proposals in isolation rather than sequentially. The exception to this is for the launch of the BBC Three Online service, where we only considered this in the context of closing BBC Three as a broadcast channel. The difference between considering the impacts of the service proposals in isolation and considering them sequentially is generally small, because many of the service proposals are independent of one another. The largest interaction is between the increased investment in BBC One drama and the launch of a BBC One+1 channel. We consider this and other interactions, in our overall financial assessment in Section 11.

3.20 We made a number of other changes to CC's modelling. These are discussed in more detail throughout this document and include the following:

- CC considered the proposed increase in BBC One Drama spend to be part of the counterfactual (i.e. what would happen without the Service Proposals). We have included this change in the MIA and have therefore excluded it from the counterfactual, for the reasons set out in paragraph 4.4 below.
- We have updated a number of input assumptions to account for more recent data; and
- We changed the approach and assumptions related to how the impact on advertising revenue is calculated, which we explain in detail below.

Estimating the change to advertising revenues

3.21 TV is a mass market advertising medium in that it allows advertisers to reach large numbers of potential consumers at the same time. In very general terms, channels which have the larger audiences are more attractive to advertisers. In practice, commercial broadcasters and advertisers actually trade in terms of "commercial impacts" (or, on an annual basis, a channel's share of commercial impacts) rather than the absolute size of audience. One commercial impact is one viewer watching one advert so changes which affect the size of audiences for different channels will affect the volume of commercial impacts that broadcasters can deliver (all other things being equal) and there would be expected to be a knock-on effect on advertising revenues.

3.22 In its analysis, CC calculated the change in advertising revenues for commercial broadcasters as a result of the BBC's service proposals by combining the changes in the shares of viewing that it had modelled with estimates of changes in the price of TV advertising. This was on the basis that changes in the share of viewing can be used as a proxy for the change in the volume of advertising. On the pricing side, CC derived estimates of the change in the price of TV advertising from assumptions it

made about the elasticity of demand for TV advertising.²⁴ With estimates of changes in both price and volume, this enabled CC to derive an estimate of the change in advertising revenue.

- 3.23 In its modelling CC assumed a uniform price elasticity for all commercial broadcasters but offers three different scenarios in terms of the elasticity of demand. That is, whether the demand for TV advertising: is inelastic; has unitary elasticity; or is elastic.²⁵
- 3.24 As a result the CC approach means that the change in TV advertising revenues (as a proxy for the change in producer surplus) for a commercial broadcaster as a result of the BBC's service proposals will be determined by:
- the assumption about the price elasticity of demand for TV advertising on different channels or with different broadcasters; and
 - the broadcaster's change in share of viewing hours.
- 3.25 We consider that the CC analysis represents a reasonable starting point for estimating the change in advertising revenues. However, we have also looked to extend and refine the analysis in a number of ways.
- 3.26 In principle, a decline in commercial impacts may lead to a rise in the price of advertising on that channel. This is because in the short term (which in this case would be less than one year) advertisers' budgets for TV advertising would typically be relatively inflexible. As the number of commercial impacts delivered falls, the price of TV advertising measured in terms of the 'cost per thousand impacts' (a standard industry metric) will increase. However, our focus is on the longer-term impact on broadcasters' revenues and whether price increases can be sustained.
- 3.27 In the longer-term the interaction between changes in the volume of commercial impacts and changes in prices at both the firm level and the market level is likely to be complex and involve a number of different interactions. The trading mechanism for TV advertising tends to emphasise how a channel performs relative to other commercial channels (known as a channel's share of commercial impacts (SOCI)). If a channel increases its audience relative to other channels it could become more attractive to advertisers. In addition, if a reduction in overall audiences reduced the overall supply of commercial impacts, then the "scarcity" value of TV advertising might increase. At the same time, advertisers could anticipate the changes in audiences of commercial broadcasters as a result of the BBC's service proposals and factor this into their annual negotiations with those broadcasters. Furthermore, if audiences for commercial TV channels fall overall then the effectiveness of TV

²⁴ In general terms, the own price elasticity of demand for a product is a measure of the responsiveness of demand for that good to changes in the price of that good. Own price elasticity is typically expressed as the absolute value of the percentage change in the quantity demanded of a good as a result of a percentage change in price of that good.

²⁵ In this case, if demand for TV advertising is "inelastic" (or less than 1 in absolute terms), demand is not that responsive to changes in price. In this case, a small change in volume has a large offsetting price change. If demand is "elastic" (greater than 1 in absolute terms), then demand responds more than proportionately to a change in price. In this case, the price change as a result of a volume change will be relatively modest. If there is unitary elasticity (i.e. the elasticity of demand is equal to 1), then demand responds in proportion to the change in price. With unitary elasticity, the price change will fully offset the volume change (for sufficiently small changes in volumes).

advertising may be perceived to lessen. This could in turn reduce the overall amount advertisers are prepared to pay to reach a given volume of commercial impacts.

- 3.28 Because of the above complexities, we have not sought to rely on explicit elasticity assumptions in quite the same way as the CC approach. Instead, we have considered the maximum revenue impact if revenues changed in direct proportion to the change in commercial impacts and then considered the extent to which these could be offset by a price change.²⁶ If there were no change in price, then for a given percentage reduction in commercial impacts, there would be a similar percentage reduction in advertising revenue. Equally, if prices rose by the same percentage as the volume of commercial impacts had fallen, then there would be no change in revenue. Neither of these scenarios – either prices being completely inflexible or varying in direct proportion to the change in commercial impacts – are viewed as particularly realistic. In our analysis, we have considered scenarios where prices change to offset (respectively) a third, a half and two-thirds of the potential change in revenue.²⁷
- 3.29 Moreover, the impact on the audiences of different broadcasters is likely to vary across the different proposals (depending on how close a substitute they are to the BBC's services in question). Therefore, we have presented our estimates of the impact on commercial broadcasters' revenues in terms of a range, according to the extent to which price changes may (differentially) offset any change in commercial impacts. The smaller the loss of audiences, the smaller the loss of advertising revenue is likely to be. If the impact on a broadcaster is expected to increase its share of viewing, then we anticipate that there will be an increase in advertising revenue.
- 3.30 For each of the BBC's service proposals, we have estimated the percentage change in total viewing hours for each of the main commercial providers, and the implications for advertising revenue (as a proxy for producer surplus). As a modelling simplification we have assumed that the advertising revenue earned from an hour of linear viewing, on-demand viewing and PVR viewing is the same. Our estimate of the effect due to each service proposal is presented in the section analysing that service proposal.
- 3.31 In addition, we provide a cumulative view, as a result of implementing all of the BBC's service proposals, on the change to producer surplus in Section 11.

²⁶ We recognise that our approach could be taken to imply a particular view of demand elasticity values, however, for this to be true it would be necessary for the demand curve to be otherwise unchanged (i.e. for TV advertising as a whole). Moreover, since transactions in the TV-advertising market are based on shares of advertising budgets (essentially aggregate expenditure), the pricing is very non-linear, whereas the simple theory of demand elasticity assumes uniform (i.e. linear) pricing of every unit (in this case commercial impacts). The number of econometric studies of the price elasticity of demand ("PED") for TV advertising in the UK is limited e.g. Hendry (1992), PwC (2004) and Analysys Mason, Brandscience and Crawford (2010) - the latter two both for Ofcom. Furthermore, the results of these studies are not entirely consistent. As a result, we have used them to inform our thinking in this area rather than relying on them, as we explain below.

²⁷ The range of price offset we have considered does encompass the range of estimates of the price elasticity of demand from the previously noted econometric studies, but as noted in the preceding footnote, caution is required in interpreting the results in this way. For example, if the price increased to offset 50% of the reduction in the volume of commercial impacts (the mid-point of the range of price offset considered) this would be equivalent to a price elasticity of demand of approximately (-)2. Although, this is somewhat higher (in magnitude) than most elasticity estimates for PSBs, it would still be within what is quite a broad range.

Impact on subscription services

- 3.32 In addition to the impact on advertising revenues for commercial broadcasters, we have also considered the potential impact on subscription revenues for platforms such as Sky or Virgin Media, and subscriptions for VOD services such as Netflix.
- 3.33 However, for the reasons set out in Sections 5 – 10, we do not consider that the BBC's service proposals are likely to result in a meaningful number of households altering their subscription purchasing decisions. Therefore, we consider that the impact on subscription revenues and the consequent change to producer surplus as a result of the BBC's service proposals will be minimal and we have not attempted to quantify it.

Dynamic impacts

- 3.34 The assessment of dynamic impacts builds on the analysis of static impacts but also requires a view of the longer term development of the sector and the potential for companies to respond to the BBC's service proposals. For example, a change that leads to viewing shifting from commercial services to the BBC may lead to higher or lower investment by commercial providers. They may raise investment if they try to win back viewers by increasing the attractiveness of their channels (which could result in a benefit to consumers). On the other hand, they may reduce their investment because the BBC's investment makes it more costly for them to compete (which could have a detrimental impact for consumers).
- 3.35 We do not try to quantify the dynamic impacts resulting from changes in behaviour by the commercial channels, as we consider there to be too much uncertainty to have sufficient confidence in any quantitative estimates. However, we identify the potential dynamic effects, and where possible give our view on their likelihood and scale.

Wider impacts

- 3.36 In addition to their direct effect on the markets in which they are provided, the BBC's service proposals could also have an impact on related markets, either further up the value chain, or for complementary services.
- 3.37 One specific area where there are likely to be wider impacts is in the content rights market and the market for the production of content as a result of the BBC's proposal to establish BBC Three as an online service.
- 3.38 Our analysis of the wider impacts is subject to uncertainty. For example, in relation to the BBC's proposals to establish BBC Three as an online service, the BBC has yet to finalise the terms and conditions with content rights holders. The outcome of these negotiations between the BBC and rights holders is likely to have a significant bearing on this particular market impact. Due to the uncertainty involved, we have again focussed on considering the qualitative impacts, rather than attempt an explicit quantitative analysis.

Evidence used in our MIA

- 3.39 In conducting this MIA we have relied on evidence from the following sources:
- 3.40 **BBC:** The BBC provided us with information about its proposals and its assessment of what the impact of these could be on other affected products and services. The

BBC's PVT application was particularly useful in this regard as was the model and analysis provided by CC on behalf of the BBC, which estimated the impact of the BBC's service proposals. Our own quantitative assessment of the market impact of the BBC's proposals was based in part by assessing the CC analysis and model.

- 3.41 Where necessary, we also requested information from the BBC regarding their proposals; their analysis of the impacts; and underlying data that assisted us in undertaking our own analysis.
- 3.42 **Market research:** In July 2014, the BBC commissioned PAPA to conduct audience research on the appeal of its proposals.²⁸ In October 2014, CC published the findings of market research (CC market research report) conducted on its behalf by GfK aimed at assessing an audience's response to the BBC's service proposals.²⁹ Where relevant, we used the output from this research to help inform the possible impacts of each proposal.
- 3.43 In January 2015, Ofcom commissioned Kantar Media (Kantar) to undertake additional qualitative market research to explore motivations for watching broadcast television, catch-up television and video on demand; and to explore how audience behaviour might change in response to the BBC's service proposals relating to BBC Three Online and BBC iPlayer. Kantar's findings (the Kantar report) are published alongside our document.³⁰
- 3.44 We also had access to the findings from previous market research carried out by Ofcom. Of particular note, was the market research and market data that was used to inform Ofcom's Communications Market Report published in August 2014 (2014 CMR).³¹
- 3.45 **Stakeholder interviews:** We held five separate stakeholder meetings during February and March 2015.³²
- 3.46 **Stakeholders' written submissions:** Stakeholders submitted written evidence in response to a stakeholder questionnaire published on 20 January 2015. The questionnaire focussed on the way the BBC's service proposals might affect the products and services provided by other stakeholders (both immediately and in relation to future plans). We asked stakeholders to provide evidence and analysis to support their views. We received contributions from 14 stakeholders. We discuss these responses in Sections 5 – 10.

²⁸ Deliberative audience research into the proposed changes to BBC Three, BBC iPlayer, CBBC and BBC One+1, A research report from PAPA, September 2014
http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/audience_research.pdf

²⁹ BBC Three PVT, Summary of results from the quantitative research regarding proposed service changes, Communications Chambers, October 2014,
http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/quantitative_research.pdf

³⁰ BBC Market Impact Assessment, Proposed changes to BBC iPlayer and BBC Three, Qualitative research report, Kantar Media <http://stakeholders.ofcom.org.uk/binaries/research/tv-research/bbc-mias/mia-jun-15-kantar-report.pdf>

³¹ The Communications Market Report, Ofcom, 7 August 2014
http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr14/2014_UK_CMR.pdf

³² We held separate meetings with BT, ITV, PACT, Viacom and Virgin Media.

- 3.47 **Desk research:** Desk research was used to inform our analysis. We have drawn on secondary data and analysis from various sources including broker reports, consultants and market researchers. References to relevant research sources are included throughout this document.
- 3.48 **TV viewing data:** We used TV viewing data supplied by the Broadcasters' Audience Research Board (BARB) to conduct elements of our analysis. BARB data covers metrics including audience viewing time, audience size and the share of the total TV audience watching a certain programme or channel. The data and our subsequent analysis has been used to verify CC's work and as an input to our model, including 2014 data.

Section 4

Counterfactual for our MIA

- 4.1 The counterfactual represents our view of the situation were the BBC's service proposals not to happen. This is an important baseline for our MIA and is the situation against which each of the BBC's service proposals is assessed.
- 4.2 To construct the counterfactual for this analysis we have forecast:
 - 4.2.1 Total viewing hours by type (i.e. live linear, PVR and catch-up);³³
 - 4.2.2 The live linear/PVR viewing share for channel families (i.e. BBC family, ITV family³⁴, Channel 4 family, Channel 5 family, and other channels); and
 - 4.2.3 The catch-up viewing share for the channel families.
- 4.3 In developing our counterfactual, we have used the CC model as the starting point and we discuss below where we have made amendments to this model.
- 4.4 One important change we made to CC's counterfactual relates to the additional investment in BBC One drama. CC included this additional investment in its counterfactual case. Although changes in investment are made at the discretion of the BBC, subject to oversight by the Trust, there is a dependency between the increase in drama investment on BBC One and the closure of BBC Three as a broadcast channel. Therefore, in agreement with the Trust and the Joint Steering Group, this is being considered as part of the PVT and hence the MIA. Therefore, our counterfactual does not reflect the impact of the additional BBC One drama investment – instead, this is modelled as one of the proposals and is discussed in Section 8.

Viewing hours by type

- 4.5 CC derived its counterfactual case for viewing hours using forecasts developed by Mediatique. The Mediatique forecasts were published in October 2013 as part of its report on the implications of changing the BBC iPlayer catch-up period from 7 to 30 days (the Mediatique report).³⁵ The latest full year of actual information available to Mediatique to make its projections was 2012.
- 4.6 Mediatique estimated total industry viewing hours for each of live linear, PVR and catch-up³⁶ over the period 2013 to 2018.³⁷ Mediatique predicted that total viewing per

³³ This includes catch-up on all devices e.g. smart TV, laptop, tablet.

³⁴ We use the term ITV family to include STV and UTV. See the glossary at the end of this document for more detail on these terms.

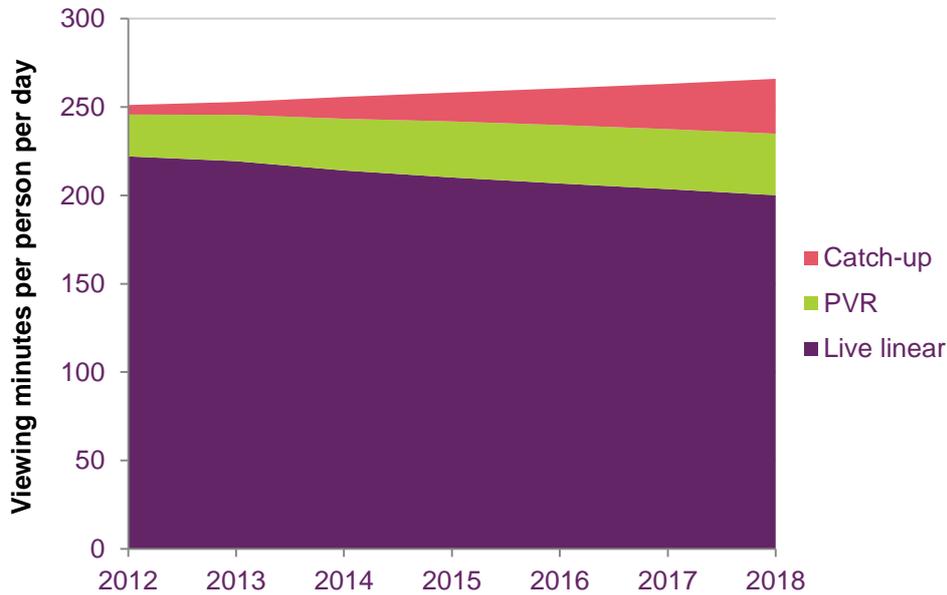
³⁵ Implications of a change in the BBC's TV on-demand permissions, Mediatique, October 2013 http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/on_demand/2014/mediatique_on_demand.pdf

³⁶ Mediatique separately forecast the following on-demand categories; catch-up (up to 30 days after linear broadcast), archive VOD (more than 30 days after broadcast) and Pay-VOD viewing. The CC model uses the catch-up category only. We consider that this is appropriate. The reasons we consider Pay-VOD unlikely to be significantly affected by the proposals are discussed in sections 5-10.

³⁷ Mediatique used a figure for UK individuals aged four plus of 51.9m in 2012, rising to 52.9m in 2018. The Office of National Statistics projects the population of individuals aged four plus of 60.5m in

person would slowly increase over time, with a decline in live linear viewing more than offset up by increases in PVR and catch-up viewing. The Mediatique forecast is shown in Figure 4.1.

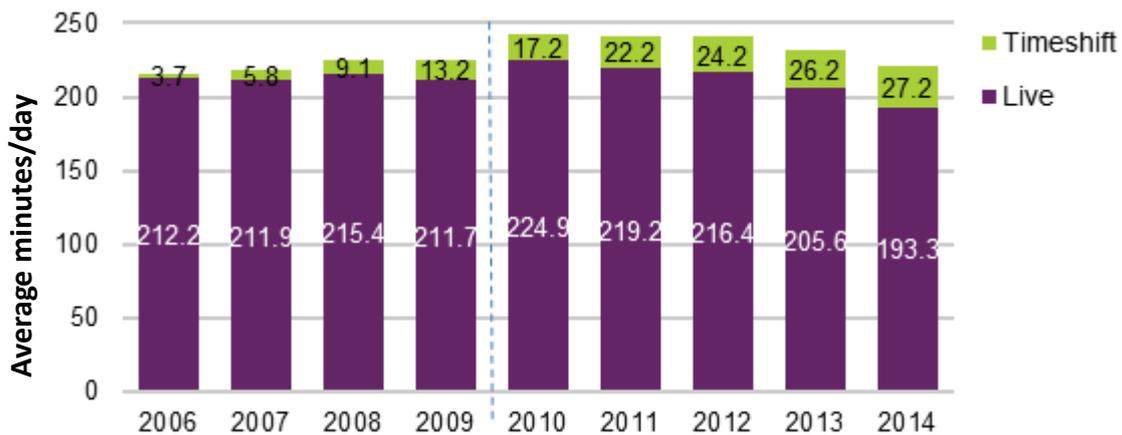
Figure 4.1: Mediatique forecast of viewing by type



Source: Mediatique (2013)

4.7 Since the Mediatique report was published in 2013, we have observed a decline in the amount of TV viewing, as illustrated in Figure 4.2. Using BARB data, we find that between 2012 and 2014 TV viewing for all individuals (over four years old) declined by 8.4%. Within total TV viewing we can see that time-shifted viewing (PVR and catch-up) has increased (by 12.4% since 2012) while live linear viewing has fallen (by 10.7% since 2012).

Figure 4.2: Average minutes of viewing per day: Total TV, Individuals aged 4+

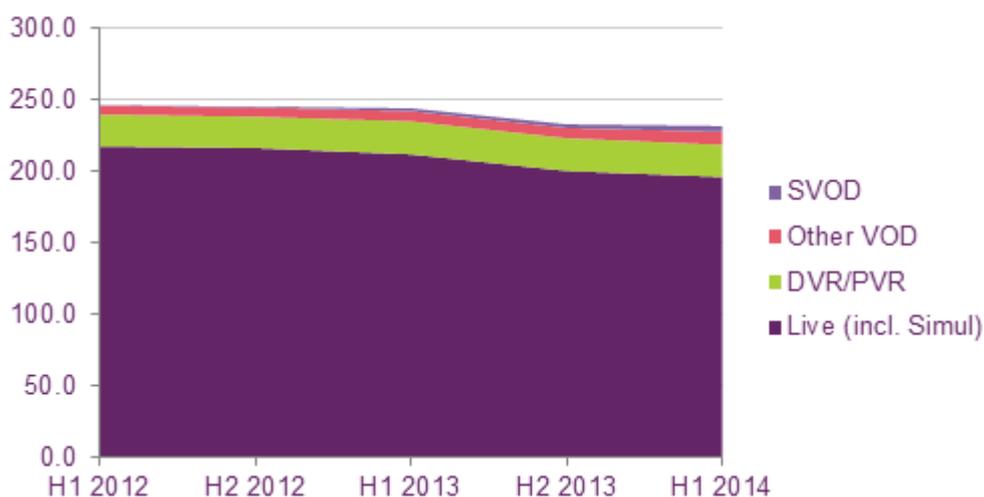


Source: BARB Note: New BARB panel introduced on 1 January 2010. As a result comparison between pre and post panel change data must be treated with caution (see dotted line)

2012, rising to 63.0m in 2018. Applying this amendment does not affect the distribution of hours between the viewing types or the viewing hours per person, however, it does mean that the aggregate level of viewing (across the population) is higher.

- 4.8 Figure 4.2 only includes time-shifted viewing that occurs through the TV set because the available BARB data does not capture viewing away from the TV (unlike the Mediatique forecasts that predict time-shifted viewing across all devices e.g. including laptops and tablets). We recognise that in relation to total time-shifted viewing, a significant proportion of catch-up viewing could be on laptops, computers or tablets (which the BARB information does not capture) – therefore Figure 4.2 is likely to understate total-time shifted viewing.³⁸
- 4.9 However, using information which aims to capture total long form viewing from all devices we still find that total viewing has declined – driven by a decline in live linear viewing which is not fully offset by increases in PVR and catch-up viewing. This is illustrated in Figure 4.3 below which shows 3 Reasons estimates for total long form AV viewing by type from all devices (including laptops etc.) from 2012 to H1 2014.

Figure 4.3: Viewing minutes per person per day, 3 Reasons estimates: Individuals aged 4+



Source: 3 Reasons/Ofcom/BARB

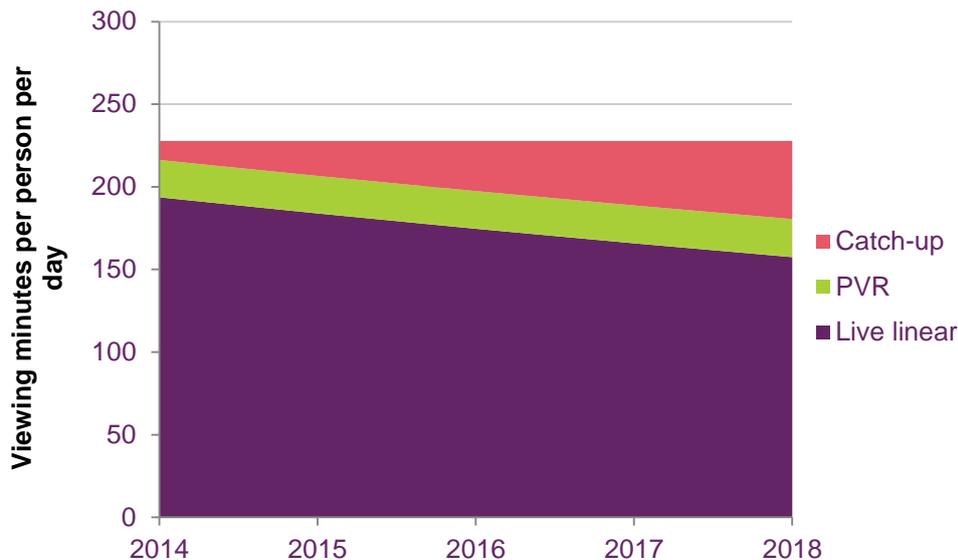
- 4.10 In light of the recent trend, which differs from the increase in viewing in Mediatique's earlier predictions, we have changed the forecast of total viewing hours in the model for the period up to 2018. We have used the 3 Reasons data in developing our forecast. For the purposes of this MIA, we have assumed:
- Total live linear, PVR and catch-up viewing combined remain constant at the H1 2014 level. We recognise there could be a number of plausible alternative views of total viewing over the period to 2018. In particular, total viewing may continue to decline as it has in recent years. For the purposes of this MIA, we consider that assuming constant total viewing over the forecast period is a reasonable assumption. This is because our assessment of the impact of the service proposals is driven by variations in viewing compared to this counterfactual, rather than being driven directly by the absolute level of viewing. Therefore, it would likely make little difference to our results if we assumed that the recent small decline in overall viewing continued in the counterfactual case;

³⁸ For example, in February 2014 76% of requests for TV programmes from BBC iPlayer were from mobile devices, tablets and computers combined. Source: 2014 CMR, figure 2.85.

- Live linear viewing continues to decrease at the H1 2012 to H1 2014 rate (i.e. 5.0% per year);
- PVR viewing remains almost flat, increasing at the H1 2012 to H1 2014 rate of 0.5% per year; and
- Catch-up viewing makes up the difference.

4.11 The resulting forecast is as follows:

Figure 4.4: Ofcom forecast of viewing minutes per person per day: Individuals aged 4+ (for the purposes of this MIA)



Source: Ofcom

4.12 The most significant difference relative to the Mediatique forecast is that we predict a lower level of live linear viewing and greater catch-up viewing.

Live linear/PVR viewing share

4.13 The CC model forecasts the viewing share for:

- 4.13.1 each of the main BBC channels (BBC One, BBC Two, BBC Three, BBC Four, CBBC and CBeebies);
- 4.13.2 each PSB's family of channels in aggregate, including non PSB channels that each PSB provides (i.e. BBC family, ITV family, Channel 4 family and Channel 5 family); and
- 4.13.3 other channels (in aggregate).

Base year data

- 4.14 CC used 2013 BARB data as the base data for its viewing share forecasts. We now have information available for viewing shares for 2014 and have therefore updated the model to reflect actual 2014 BARB viewing data.³⁹
- 4.15 The channel shares for 2014 do not differ significantly relative to those for 2013. The largest changes are that the BBC One viewing share has increased from 21.0% to 21.7% and the Channel 3⁴⁰ services viewing share has fallen from 15.3% to 14.7%.⁴¹

CBBC viewing share

- 4.16 CC assumed that the viewing share for CBBC drops from 0.6% in 2013 to 0.4% in 2014 and then remains constant at that level to 2018. In making this assumption CC noted that:

“CBBC has seen significant share contraction, dropping from around 0.8% at the start of the decade to 0.5-0.6% currently. The Disney Channel has had a similar contraction. Cartoon Network, Nickelodeon and Pop have been more steady, albeit from a lower base. However, since the beginning of the decade these channels have in aggregate lost approximately 15% of their viewing share.

In part this is due to a decline in children’s total viewing, which fell 11% between 2010 and 2013, compared to a 3% fall for adults.

In our counterfactual, we have assumed that CBBC’s share falls to 0.4% and then stabilises at this level. For the purposes of assessing market impact, this is a conservative assumption relative to assuming continuing declines, since it increases the incremental consumption resulting from the proposed service change.”

- 4.17 In constructing its forecast CC redistributes the reduction in CBBC’s share to the other channels in proportion to their 2013 viewing share.
- 4.18 CC’s prediction that CBBC’s viewing share would decline has been corroborated by actual BARB data for 2014 which shows that CBBC’s viewing share has fallen from 0.6% in 2013 to 0.5% in 2014. In light of this evidence, we consider that CC’s forecasts for the viewing share of CBBC are reasonable. Therefore, in our counterfactual case, we assume that CBBC’s viewing share will decline to 0.4% in 2015 and then remain constant after this point. Viewers released from the reduction in CBBC’s viewing share are reallocated among all other channels/channel families according to their proportion of viewing share in 2014.

BBC Three viewing share

- 4.19 CC noted that BBC Three’s viewing share has been approximately flat this decade and forecast that its share would continue at the current level to 2018.

³⁹ The BARB data is based on all viewing through the TV set (live, PVR and catch-up) and is unable to differentiate between catch-up versus PVR time shifted viewing. Given that catch-up viewing is currently only a small part of total viewing (we estimate around 5% in 2014) we consider that the BARB data provides a reasonable proxy for live linear and PVR viewing shares.

⁴⁰ This comprises the viewing shares of the main ITV channel (previously ITV1), UTV and STV.

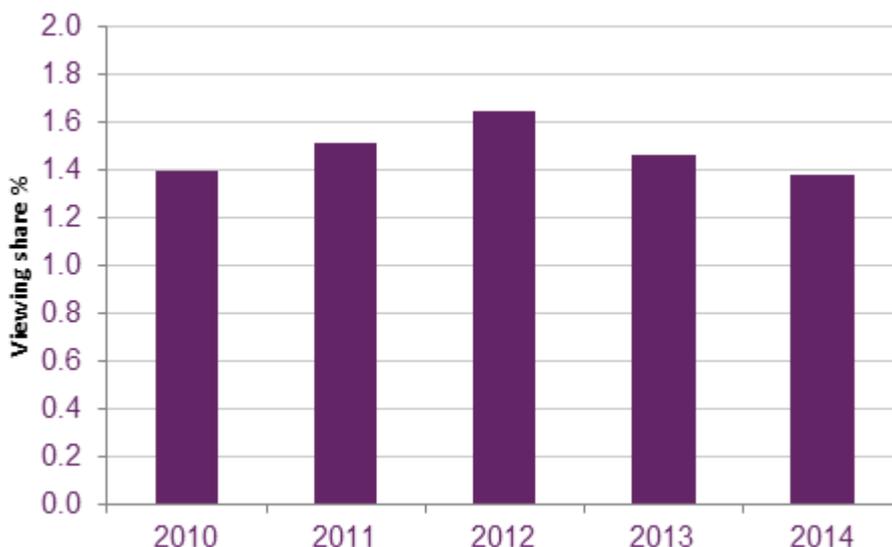
⁴¹ Viewing shares over time are shown in Figure 4.6 below.

4.20 We have assessed CC’s assumption with particular reference to the impact of changes to BBC Three’s budget and possible changes in content.

Impact of changes to budget

4.21 We note that BBC Three’s viewing share has declined slightly over recent years (see Figure 4.5).

Figure 4.5: BBC Three viewing share between 2010 and 2014



Source: BARB. Individuals 4+

4.22 The BBC service proposal said that BBC Three’s total content budget has fallen over the past two years and as a result there has been a decline in the hours of originations shown on the channel.⁴² The BBC notes it is difficult to identify whether reductions in BBC Three’s content budget have had an impact on BBC Three’s performance or whether this is due to changing consumption habits amongst younger audiences. We recognise that one of the determinants of viewing hours for a channel is likely to be the size of the content budget for that channel. That is, we would expect that as a channel’s content budget increases it is able to improve the quality/quantity of its programming and attract more viewers.

4.23 A key aspect of the BBC’s service proposals is the reduction in BBC Three’s budget – realised by closing BBC Three as a broadcast channel and reinventing it online. For the purposes of deriving our counterfactual, we needed to make an assumption about BBC Three’s budget in the event that it continued as a broadcast channel and was not reinvented online. This is relevant to our analysis since if BBC Three as a broadcast channel did not close but operated on a reduced budget, this may impact on the quality or quantity of content which could have a knock-on impact on BBC Three’s viewing share.

4.24 We have requested information about the budget for BBC Three in the event that it continued as a broadcast channel. The BBC has indicated that it would likely review its budget plans for BBC Three as a broadcast channel if its proposals relating to BBC Three are not approved by the Trust. However, it does not have an agreed estimate of what the budget would be in the event that its proposals do not get

⁴² BBC service proposals document, page 21.

approval from the Trust.⁴³ The BBC budget presented to the Trust in March 2014 indicated that the budget for BBC Three would be broadly stable in nominal terms (based on the BBC Three broadcast channel continuing to operate).

4.25 Although we recognise that there is uncertainty over setting the correct level of the BBC Three budget for the counterfactual, for the purposes of our MIA we have assumed that the budget remains constant in nominal terms for the period to 2018. In making this assumption we note:

- This corresponds to the budget forecast presented to the Trust in March 2014 (based on BBC Three continuing to operate as a broadcast channel only);⁴⁴ and
- In the event that the BBC's proposals relating to BBC Three are not implemented, it is not clear why the BBC Three budget would necessarily need to decline significantly (given it is not clear that the increased investment in BBC One drama would go ahead).

Changes in BBC Three content

4.26 The most popular BBC Three programmes are *Family Guy* and *American Dad*, which according to BARB data accounted for a combined 27.3% of BBC Three viewing hours in 2014. Subsequent to the BBC submitting its Service Proposal, it was announced that the future rights to these programmes will move to ITV2 and that the new series of *Family Guy* due in Autumn 2015 will air exclusively on ITV2.⁴⁵

4.27 In light of this future change, we have considered whether an adjustment is needed in our counterfactual, since if viewers were to follow these programmes to ITV2, then it is possible that the viewing share of BBC Three could decline. However, adjusting the counterfactual for such a change would require us to make a number of assumptions regarding how and whether viewers switch between channels, which are complex and subject to uncertainty. For example, in determining the switching behaviour of viewers from BBC Three because of *Family Guy* and *American Dad* moving to ITV2 we would also need to consider the effect of BBC Three replacing these programmes in its schedule with alternatives (possibly other acquisitions). The ultimate impact on BBC Three's viewing share would depend on how many viewers follow the programmes to ITV2 and how the replacement BBC Three programmes perform – factors which are difficult to predict.

4.28 Therefore, we have decided not to amend BBC Three's viewing share in the counterfactual to reflect the loss of *Family Guy* and *American Dad*.

4.29 In light of the considerations above, in the counterfactual we have assumed that the BBC Three viewing share would remain broadly stable at the 2014 level.⁴⁶ This means the BBC Three share of viewing is assumed to be 1.38% in the counterfactual (whereas the CC model used a figure of 1.48%).

⁴³ Correspondence between Ofcom and BBC, February 2015.

⁴⁴ We note that the BBC Three budget presented to the Trust in March 2015 reported a significant reduction for 2015/16 onwards. However, we do not think this is the correct counterfactual because it is premised on BBC Three broadcast being closed.

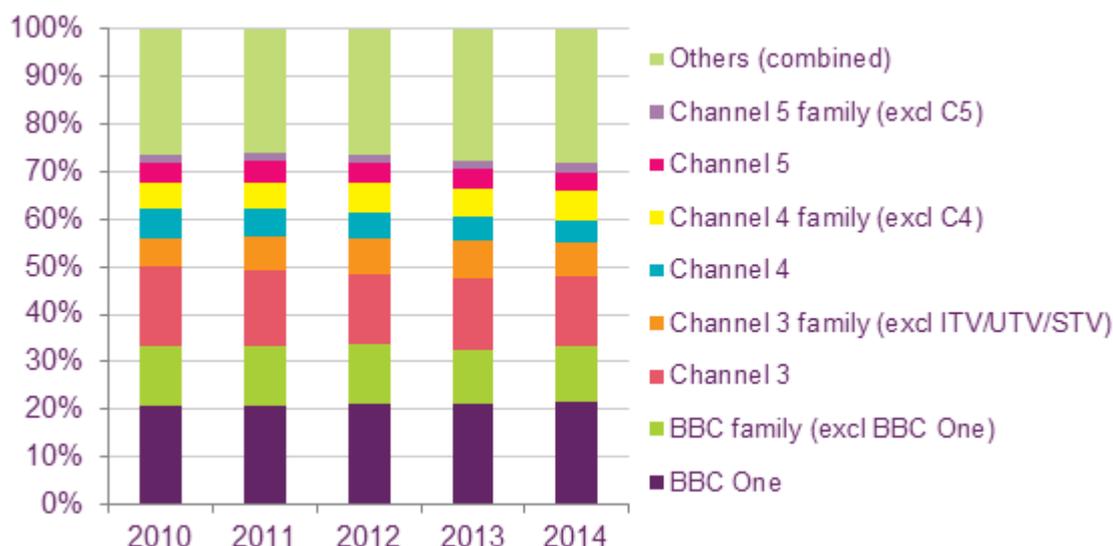
⁴⁵ <http://www.theguardian.com/media/2015/mar/23/family-guy-leaves-bbc3-for-itv>

⁴⁶ Subject to the minimal adjustments in relation to reallocating the reduction in CBBC's viewing share across all other channels discussed above.

Forecast viewing shares for other channels

- 4.30 CC assumed that the viewing share for other channels/channel portfolios remains constant over the period 2013-2018, with the exception of CBBC (see discussion above).⁴⁷
- 4.31 We have considered the viewing shares for the main channels/channel portfolios over recent years (see Figure 4.6).

Figure 4.6: Viewing shares for main channels/channel portfolios



Source: BARB. Individuals 4+

- 4.32 There is some variation in the viewing share of the main channels/channel portfolios year by year. However, overall the shares are reasonably stable. Therefore, we consider it reasonable to assume that the channel viewing shares remain broadly constant in the counterfactual over the modelling period. However, as noted above we have updated the base year to 2014 and therefore have assumed that viewing shares remain broadly constant at the 2014 level.⁴⁸

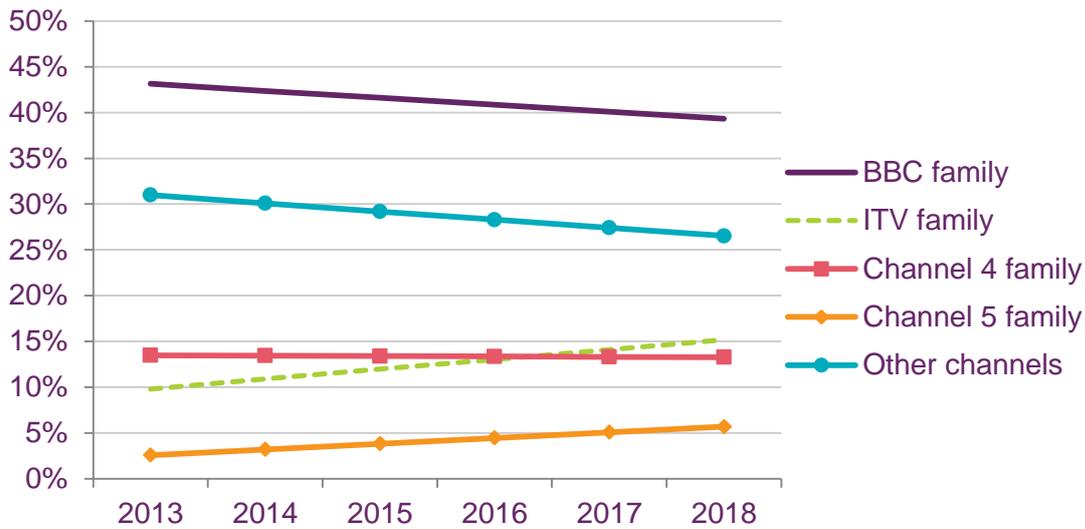
Catch-up viewing share

- 4.33 The Mediatique report forecasted total catch-up hours in each year to 2018 which it split between the BBC and others combined.
- 4.34 Mediatique also estimated the share of catch-up hours for each of the PSBs' on-demand services and 'others' in 2012 and 2018 only (assuming that the BBC iPlayer catch-up window was at seven days only after broadcast). CC use this information (adjusted to reflect the revised BBC viewing share post the BBC iPlayer catch-up extension to 30 days after broadcast) to forecast catch-up hours for each PSB over the period 2015 to 2018. The resulting catch-up viewing share of each broadcaster is shown in Figure 4.7.

⁴⁷ CC adjusted BBC One's viewing share in its counterfactual to reflect increased drama investment. We have modelled the increased drama investment as part of the proposals rather than the counterfactual, as discussed in Section 8.

⁴⁸ Subject to minimal adjustments in relation to reallocating the reduction in CBBC's viewing share across all other channels discussed above.

Figure 4.7: Share of catch-up viewing



Source: Mediatique

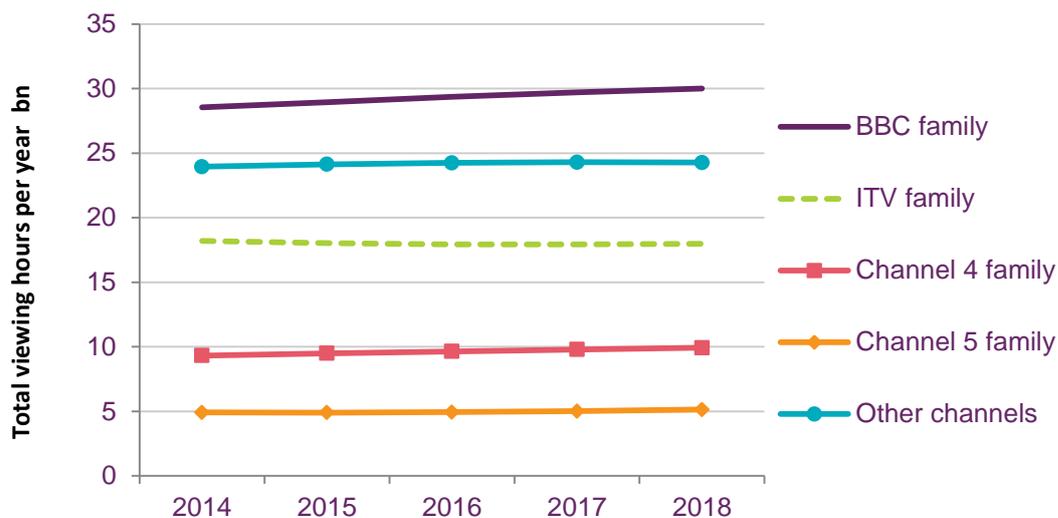
- 4.35 There is a small decline in the viewing share for BBC iPlayer (from 43% in 2013 to 39% in 2018) and an increase in the viewing shares for the ITV Player (from 10% to 15%) and Demand 5 (from 3% to 6%). The 4 on Demand (4oD) share remains constant. Mediatique explained that the BBC’s current share of consumption reflects, in part, the strength of BBC iPlayer brand and that ITV’s more modest market share reflected a bias because of ITV’s focus on live/event programming. Over time Mediatique expected that market shares would converge closer to the live linear shares.⁴⁹
- 4.36 It is particularly difficult to predict catch-up viewing shares given that this is currently an area of market growth and may not reach a ‘steady-state’ for some time. Overall, we consider that the CC forecast is reasonable. In particular, we recognise that the BBC has been, and is likely to remain, the market leader in catch-up viewing over the forecast period. However, as use of on-demand becomes more widespread and other market players develop/promote their catch-up services it is plausible that catch-up viewing shares will move closer to live linear viewing shares.

Summary of viewing hours in the counterfactual

- 4.37 Taking all these assumptions together, we forecast viewing hours for each PSB channel family in the counterfactual. This is shown in Figure 4.8.

⁴⁹ Mediatique report, page 12.

Figure 4.8: Total viewing hours (live linear, PVR and catch-up combined) by channel family in the counterfactual



Source: Ofcom

- 4.38 All channel families benefit from slight upward growth in population over the period, which when combined with our assumption of constant viewing per person results in growth in total viewing hours. Another factor which affects individual channel families differently is the shift from live linear/PVR viewing to catch-up viewing. This tends to increase the BBC family share because it has a higher share of catch-up viewing than live linear/PVR viewing.
- 4.39 The short term impact of each proposal discussed in Sections 5 to 10 is presented in terms of the change in aggregate viewing hours (live linear, PVR and catch-up combined) for each PSB relative to this counterfactual.

Financial position of commercial broadcasters in the counterfactual

- 4.40 For each of the service proposals, we consider the financial impact in 2018 on the commercial broadcasters relative to the counterfactual. We do this by considering the impact of the service proposals on the net advertising revenue (NAR) of the commercial broadcasters.
- 4.41 We assume in the counterfactual that NAR in 2018 would remain at the same level as it was in 2013 in real terms. While we recognise that in reality NAR may vary year to year in real terms⁵⁰, we consider this a reasonable and neutral assumption.
- 4.42 CC used annual reports and Ofcom's Communications Market Report 2014 to estimate current net advertising revenues of each of the commercial broadcasters. Their approach omitted some revenues which relate to viewing included in the BARB data used to estimate the impact on each channel group.⁵¹ In our estimation of current revenues we have attempted to account for these revenues in order to make the revenue base consistent with the viewing data used in the modelling.

⁵⁰ For example, NAR is affected by the economic cycle and fell in real terms between 2008 and 2013. See paragraph 3.9 of our December 2014 PSB Review Consultation,

<http://stakeholders.ofcom.org.uk/binaries/consultations/psb-review-3/summary/PSBR-3.pdf>

⁵¹ For example, CC did not include online net advertising revenues or revenues from STV/UTV viewing.

Section 5

Closing BBC Three as a broadcast channel

- 5.1 The BBC is proposing to close BBC Three as a broadcast channel by the autumn of 2015 and reinvent it as an online only service.
- 5.2 Although the proposals to close BBC Three as a broadcast channel and reinvent it online are linked (i.e. the proposal to reinvent BBC Three online is dependent on the Trust giving approval to close the BBC Three broadcast channel) for ease of analysis and presentation we have separated the proposals into two steps. The first step in this section is an assessment of the potential effects from closing BBC Three as a broadcast channel only. The second step, covered in the next section, is an assessment of the potential effects from reinventing BBC Three online.

Summary of proposal

- 5.3 Launched in 2003, BBC Three broadcasts every day from 7pm to 4am and is available on digital cable, terrestrial, IPTV and satellite platforms (from Virgin Media, Freeview, YouView, Sky and FreeSat). The channel, which is aimed at the 16-34 year old audience, provides a mixed schedule encompassing hourly news bulletins, current affairs, drama, entertainment, music, arts, animation and factual programming.
- 5.4 The BBC has explained that, in common with other BBC TV services, BBC Three's content budget has been falling over the last two years and as a result there has been a decline in the hours of origination shown on the channel. In light of potential further cuts to the channel's budget and shifts in the viewing behaviour of young people (which represent BBC Three's target audience) the BBC is seeking permission to close BBC Three as a broadcast channel by autumn 2015.
- 5.5 As part of its proposals for BBC Three, the BBC is also seeking permission to reinvent BBC Three as an online service. This is discussed in more detail in Section 6.

Stakeholder responses

- 5.6 Channel 4 and ITV specifically noted the static impacts of closing BBC Three as a broadcast channel.
- 5.7 In its response, Channel 4 understood the BBC's decision to close BBC Three broadcast in the context of financial constraints and given the changing media consumption habits of young people.
- 5.8 Channel 4 undertook its own analysis of the likely (static) market impact that resulted in the BBC's proposals to close BBC Three as a broadcast channel. Although noting that its analysis was dependent on a number of variables it estimated that the BBC's proposals could have a small but positive impact (around 0.2 percentage points) on Channel 4's portfolio share of the audience and thereby advertising revenues. It noted that this increase in revenues would potentially enable it to increase

investment in content and provide a distinctive public service offering to young audiences.⁵²

- 5.9 ITV recognised that there would be some positive effect from the closure of BBC Three on ITV2 and ITVBe, but noted that there were many channels competing for the 16-34 audience demographic. It has modelled the impact of closing BBC Three broadcast to be in the range of [X]. Its analysis takes BBC Three's current viewing share (1.38%) as its starting point. It then assumes that following the closure of BBC Three a proportion of BBC Three's viewing share will switch to ITV2/ITVBe viewing (and none will switch to other ITV channels). To maintain consistency with its approach to other modelled impacts (explained in later sections), [X].

Identification of affected services

- 5.10 We have identified the following services that could potentially be affected as a result of closing BBC Three as a broadcast channel:
- commercial broadcasters' (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
 - other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes; and
 - independent production companies as result of the loss of production hours specific to BBC Three's profile of programming.

Assessment of impacts

Static impacts

- 5.11 In this sub-section we assess the static impact on viewing hours and revenues for commercial broadcasters/providers.
- 5.12 We note that closing BBC Three will 'release' viewing hours which could increase the viewing of subscription services e.g. subscriptions to pay TV (such as Sky) or SVOD (such as Netflix). For example, in our Kantar qualitative research participants mentioned Fox and Comedy Central as pay channels that meet similar needs to BBC Three. It was also noted that services like Netflix could benefit where viewers are already engaged in watching a series.⁵³
- 5.13 However, it was noted that where viewing shifts are envisaged these were most likely to be marginal rather than major changes.⁵⁴ We consider it unlikely that the closure of BBC Three alone will significantly affect the take-up of subscription services and hence subscription revenues. 16-24s (the heaviest viewers of BBC Three) watched BBC Three for 5.7 minutes per day on average in 2014.⁵⁵ This compares to average total TV viewing for 16-24's in 2014 of 138.5 minutes per day.⁵⁶ It is unlikely that releasing this relatively small amount of minutes would tip a significant amount of

⁵² Channel 4 response to MIA stakeholder questionnaire, page 2.

⁵³ Kantar report, page 67-68.

⁵⁴ ibid

⁵⁵ Source: BARB.

⁵⁶ Source: BARB.

people towards purchasing subscription services. Furthermore, evidence indicates that 16-24 year olds are typically not responsible for making the decision in a household on whether to subscribe to additional TV channels.⁵⁷

- 5.14 In addition, no stakeholders indicated that pay TV or SVOD would be impacted by the closure of BBC Three.
- 5.15 In the rest of this sub-section we therefore focus on the impact on commercial free-to-air broadcasters.

CC model – Overview

- 5.16 CC estimated the change in the viewing hours and viewing share for the BBC and commercial broadcasters as a result of closing the BBC Three broadcast channel. In doing so CC made a number of assumptions:
- 5.16.1 Were the broadcast channel not to close, BBC Three’s viewing share would remain constant at 1.5% (at least to 2018).
- 5.16.2 Overall TV viewing (live linear plus catch-up) is fixed i.e. any viewing lost to BBC Three as a result of the closure of the broadcast channel is transferred to other channels.
- 5.16.3 The transferred hours are distributed across other channels according to the viewing of “heavy” BBC Three viewers.⁵⁸
- 5.16.4 The transferred hours are distributed between live linear/PVR and catch-up viewing in proportion to the forecast share of each within overall viewing.
- 5.16.5 Showing ongoing BBC Three programmes on other BBC channels does not result in any recovered viewing to the BBC.

Our assessment of the CC model

- 5.17 We consider that CC’s overall approach to modelling the impact of closing BBC Three broadcast is broadly reasonable. In this sub-section we discuss the main assumptions in more detail and outline the adjustments we have made.

Viewing share

- 5.18 We discuss BBC Three’s viewing share in the event that the broadcast channel is not closed in the counterfactual section; see paragraphs 4.19 to 4.29. For the reasons set out there, we consider it reasonable to assume BBC Three’s viewing share remains constant at 1.4% (the actual viewing share in 2014) in the event the broadcast channel is not closed. This is slightly lower than the viewing share assumption used by CC which was based on the actual viewing share in 2013 (1.5%).

⁵⁷ Table 137, Ofcom regions and nations tracker, Main set Quarter 1 2015, Ofcom http://stakeholders.ofcom.org.uk/binaries/research/statistics/2015April/Ofcom_Technology_Tracker_Wave_1_2015_Data_Tables.pdf. In this research, only 24% of 16-24 year old were responsible (or jointly responsible) for deciding on whether to purchase additional TV channels.

⁵⁸ Heavy BBC Three are those who, in aggregate, represent around 90% of viewing hours of the channel.

Total TV viewing fixed

- 5.19 It is possible that some people who would otherwise watch BBC Three broadcast will choose to do activities other than watching TV (e.g. other leisure activities) as a result of its closure. However, we consider the most likely substitute for BBC Three broadcast viewing is other TV viewing. We consider the assumption that there is no incremental increase/decrease in total viewing is reasonable.

Distribution of hours to other channels

- 5.20 CC assumed that the viewing hours released from the closure of BBC Three are distributed across other broadcast channels according to the viewing patterns of the heaviest BBC Three viewers. We note that the viewing habits of BBC Three viewers are likely to differ from the population at large and we consider that the CC assumption is reasonable. We also note:
- 5.20.1 BBC Three is aimed at young adults – in 2014 42.4% of BBC Three viewers were aged 16 to 34⁵⁹ – and this demographic is likely to have particular viewing characteristics/preferences.
- 5.20.2 The Kantar qualitative research indicated that the BBC Three broadcast channel meets a particular need for viewers (described as effortless and easy viewing) and is perceived as primarily a “flicking channel” where one stumbles across content. The availability of alternative “flicking channels” like E4 or Dave could suggest that the audience is more likely to switch to other broadcast channels and less likely to switch to viewing online such as to VOD due to the perceived “effort” of accessing and selecting online only content.⁶⁰
- 5.21 As a general approach to modelling, different stakeholders have argued that different measures of “heaviness” should be used to generate the viewing shares by which viewing is redistributed. We have not taken CC’s approach to measuring heavy viewers as we believe it is likely not to capture the skew of viewing on the channel well enough, resulting in viewing shares closer to the national average than we would expect. Rather, we have taken the viewing habits of those viewers which account for the top third of viewing hours to BBC Three in 2014. Due to the way these metrics are calculated⁶¹, there is no single correct measure to estimate where viewing is likely to come from or go to when channel shares change. We believe that using the top third of viewing strikes a reasonable balance between capturing the skew in viewing habits of BBC Three viewers without overstating it. This changes our results minimally compared to CC’s original assumption, affecting channels’ viewing shares by hundredths of a percentage point each.

Split of viewing between live linear/PVR and catch-up

- 5.22 CC assumed that the viewing hours released from the closure of BBC Three are distributed between live linear/PVR and catch-up services in proportion to the forecast share of each within overall viewing. We note that evidence from the 2014

⁵⁹ Source: BARB.

⁶⁰ Kantar report, page 68.

⁶¹ The viewing of “heavy” viewers of BBC Three is estimated by first constructing an audience based on a threshold of viewing “heaviness” and then then measuring the viewing habits of that heavy audience to other channels. Depending on the audience and “heaviness” applied, a different measure of the skew of viewing from BBC Three viewers will be captured.

CMR indicates that time-shifted viewing is more prevalent in younger than older adults.⁶²

- 5.23 In light of this evidence, we might expect that a greater proportion of viewing is transferred to PVR and catch-up services as a result of the closure of BBC Three as a broadcast channel. However, we have not attempted to model this explicitly, but given that the effects on commercial broadcasters are calculated by reference to total viewing hours (which aggregates live linear, PVR and catch-up viewing), the distribution of PVR and catch-up viewing within the total share of viewing for a commercial broadcaster does not have a material impact on the overall results.

Showing ongoing BBC Three programmes on other channels

- 5.24 The BBC has indicated that it intends to broadcast ongoing BBC Three programmes on BBC One, BBC Two and the 'Red Button'.⁶³
- 5.25 CC has not included any 'recovered' viewing due to the broadcast of BBC Three content on other BBC channels, citing two reasons:⁶⁴
- 5.25.1 The BBC's Service Proposal indicates that this would likely be a transitional arrangement; and
- 5.25.2 Any BBC Three programme on another BBC channel would displace another programme for that channel (presumably one selected to be optimal for that channel's existing audience).
- 5.26 In light of this, CC considered the net impact on the BBC's viewing share due to this recovered viewing was likely to be minimal.⁶⁵
- 5.27 We have considered whether an adjustment should be made to the CC assumption regarding showing BBC Three programmes on other BBC channels.
- 5.28 We would expect that the BBC would have a motivation to displace programmes on other channels with better performing BBC Three content. Therefore, directionally, the BBC's viewing share is likely to increase. However, quantifying this effect is subject to high level of uncertainty since it will depend on a number of factors including the popularity of the BBC Three programme, degree of promotion, timeslot and the popularity of the displaced programme(s).
- 5.29 CC explains that one reason that it has not chosen to model the effect of recovered viewing is because the BBC's service proposals indicate that this is likely to be a transitional arrangement only. We have estimated the static effects of the BBC's proposals in relation to 2018. Although the BBC has not provided detail regarding the length of the 'transitional arrangement', there is a prospect that the transitional arrangements could have run their course by 2018. In light of this, and the uncertainty around quantifying the effect of recovered viewing, we consider that CC's approach represents a reasonable modelling simplification and we have not adjusted this assumption.

⁶² 2014 CMR, figure 2.79.

⁶³ BBC Service Proposals document, page 23 and page 31.

⁶⁴ CC report, page 24.

⁶⁵ CC does not explicitly discuss the possibility of viewing BBC Three content on the 'Red Button' which enables viewing of BBC Three content on the TV.

Impact on viewing hours and viewing share

5.30 Figure 5.1 below shows the impact of closing BBC Three broadcast on the viewing hours and viewing share for the BBC family of channels and the main commercial providers' channel families in 2018.⁶⁶ The results are shown on the basis that only the BBC Three closure changes are implemented (i.e. absent all other changes described in the service proposal).

Figure 5.1: Estimated impact on viewing from closure of BBC Three broadcast in 2018

Channel family	Share of total viewing counterfactual	Change in viewing as a result of closing BBC Three broadcast (hours bn)	Change in viewing share (percentage points)	Share of total viewing post closure of BBC Three broadcast	Percentage change in viewing share
BBC	34.4%	-0.6	-0.7 p.p.	33.6%*	-2.1%
ITV	20.6%	+0.2	+0.2 p.p.	20.8%	+1.1%
Channel 4	11.4%	+0.1	+0.2 p.p.	11.5%	+1.4%
Channel 5	5.9%	+0.1	+0.1 p.p.	6.0%	+1.2%
Other channels	27.8%	+0.2	+0.3 p.p.	28.1%	+1.0%
Total	100.0%	0.0	0.0 p.p.	100.0%	-

*Note: The difference between outputs and the sum of counterfactual viewing share and change in viewing share values is due to rounding.

- 5.31 In our base case scenario the BBC's viewing share falls by 0.7 percentage points, with small gains for each of the commercial providers.
- 5.32 In response to the MIA stakeholder questionnaire Channel 4 estimated the impact of the closure of BBC Three on its portfolio viewing share – its estimate of a 0.2 percentage point increase corresponds to ours.⁶⁷
- 5.33 While we have only modelled the effect on channel families, we recognise that within the channel families some channels are likely to gain to a greater extent than others. For example, 16-34s tend to watch Channel 4, E4 and ITV2 to a greater extent than the population at large.⁶⁸ In our qualitative research participants mentioned Dave, Channel 4, Fox and Comedy Central as channels that meet similar needs to BBC Three.⁶⁹ Given that these channels provide content that is likely to be a closer substitute for BBC Three content, we would expect these channels to gain to a greater extent if BBC Three broadcast is closed.
- 5.34 This is consistent with Channel 4's own analysis. In its response to the consultation Channel 4 noted that, "...Channel 4 has a particularly strong relationship with young people:

⁶⁶ The channels included in each channel family are defined in the Glossary.

⁶⁷ Channel 4 response to MIA stakeholder questionnaire, page 2.

⁶⁸ In 2014 Channel 4 (including Channel 4+1), E4 (including E4+1) and ITV2 (including ITV2+1) had channel shares of 7.6%, 5.5% and 4.0% respectively for adults 16-34. For all individuals the equivalent shares were 5.5%, 2.0% and 2.4%. Source: BARB.

⁶⁹ Kantar report, page 67.

- Channel 4 is the only public service broadcaster in the world that attracts a larger share of viewing among hard-to-reach 16-34s than the general population.
- Channel 4 has grown its portfolio share of 16-34s over the last five years.
- In 2014 viewing amongst 16-34s to both Channel 4 and E4 increased year-on-year.
- Over 50% of all individuals in this group in the UK have registered to Channel 4's database of viewers.
- A survey commissioned by Channel 4 in 2014 showed that E4 is the favourite channel of 17% of all 16-34s, a higher proportion than chose any other channel.
- Channel 4's channels were selected by 29% of all 16-34s as being their favourite channels, more than chose the channels of any other broadcaster.⁷⁰

5.35 ITV considered that the closure of BBC Three could have a positive impact on ITV2 and ITVBe.⁷¹

Impact on producer surplus

5.36 We have estimated the financial impact on the main commercial broadcasters in the base case by estimating the change in producer surplus (we describe our methodology in Section 3). The results are shown on the basis that only the BBC Three closure changes are implemented (see Section 11 for the change to producer surplus from the cumulative impact of all the proposals).

Figure 5.2: Estimated impact on producer surplus from closing BBC Three broadcast in 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV ⁷²	+1.1%	1,710	+6.0	+9.1	+12.1
Channel 4	+1.4%	813	+3.7	+5.5	+7.3
Channel 5	+1.2%	358	+1.5	+2.2	+2.9
Other channels	+1.0%	999	+3.3	+4.9	+6.5
Total	+1.1%	3,881	+14.4	+21.7	+28.9

5.37 The closure of BBC Three as a broadcast channel has a positive effect on the advertising revenues for the other channel families. The Channel 4 and Channel 5 families show the largest percentage increases in viewing (1.4% and 1.2% respectively) and hence the largest relative increases in advertising revenues. This reflects the viewing profile of the heaviest BBC Three viewers which, as discussed earlier, is used to allocate the released BBC Three viewing hours to channel families.

5.38 In absolute terms, the ITV portfolio benefits the most with a gain in revenues of between £6.0m and £12.1m. In response to the MIA stakeholder questionnaire, ITV

⁷⁰ Channel 4 response to MIA stakeholder questionnaire, page 2.

⁷¹ ITV response to MIA stakeholder questionnaire, page 2.

⁷² The changes in viewing for the ITV family includes STV and UTV. We therefore include proxies for the advertising revenues of STU and UTV in the net advertising revenue figure for the ITV family. For STV we include its consumer revenues and for UTV we include its sales to third parties relating to television.

estimated a smaller positive impact from the closure of BBC Three of [3] ⁷³ We consider that ITV's estimate is likely to understate the benefit of the closure of BBC Three because it has only estimated the gain as a result of ITV2 and ITVBe increasing viewing share. While we recognise that ITV2 and ITVBe target a similar audience to BBC Three, we consider it unreasonable to assume that the other ITV channels (in particular the main ITV channel) gain no viewing hours as a result of the closure of BBC Three. The main ITV channel is the second-most viewed channel among "heavy" BBC Three viewers. ^{74 75} For comparison, ITV2 is the sixth-most viewed channel (excluding BBC Three) among this audience. We therefore believe that ITV's analysis is likely to significantly underestimate the gain to the ITV portfolio as a result of the closure of the BBC Three broadcast channel.

- 5.39 Television viewing has fallen for all individuals over time, ⁷⁶ however, the fall in viewing among adults has been particularly marked for adults aged 16-24. ⁷⁷ Because young adults are watching less television, television advertisers are likely to find this age group relatively difficult to reach and thus they are more valuable. As BBC Three is aimed at young adults (21.4% of viewers were aged 16-24 in 2014) ⁷⁸ the diversion of BBC Three viewers to commercial channels could be a particular financial benefit because it releases a relatively scarce and valuable viewer cohort.

Sensitivity analysis

- 5.40 Given the degree of uncertainty in the modelling assumptions we have tested how sensitive the viewing shares are to different scenarios.
- 5.41 As part of this exercise, we estimated that total BBC Three viewing hours in the counterfactual represented 1.4% of live linear viewing in 2018. In the event that all BBC Three viewing switched to commercial channels (i.e. no hours switched to other BBC channels) this would represent an upper limit to the number of hours that commercial broadcasters could gain by 2018 as a result of the closure of BBC Three as broadcast channel. In this scenario the BBC portfolio's share of total viewing (including live linear and catch-up) would fall from 34.4% to 33.2%. This would result in commercial broadcasters' advertising revenue rising by around £21.7 to £33.0m, compared to the counterfactual (assuming a 50% price offset effect).
- 5.42 At the other extreme, if the BBC lost zero hours following the closure of BBC Three as a broadcast channel (because all BBC Three broadcast viewing switched to other BBC channels), then commercial channels share of viewing and advertising revenues would remain unaltered from the counterfactual.

Dynamic impacts

- 5.43 As discussed earlier, BBC Three is aimed at 16-34 year olds and closing BBC Three as a broadcast channel will release viewing hours for this age group. It is possible this will create a 'gap' in the market in relation to the target audience and commercial

⁷³ ITV response to MIA stakeholder questionnaire, page 13.

⁷⁴ Based on analysis of 2014 BARB data

⁷⁵ Heavy viewers = individuals (aged 4+) who watched between 66-100% of total programming hours to BBC Three in 2014 (for at least 15 minutes consecutively).

⁷⁶ Average minutes of television viewing for all individuals per day fell by 9.0% between 2010 and 2014, source: BARB.

⁷⁷ Average minutes of television viewing for 16-24's fell by 17.9% between 2010 and 2014, source BARB.

⁷⁸ Source: BARB.

providers could seek to exploit this opportunity by investing in content for this target audience. Any such increased investment would be good for consumers. However, any provider considering such a strategy would also have to weigh up the fact that young adults are generally watching less broadcast TV, which makes the age group valuable to advertisers but also more difficult for broadcasters to reach.

- 5.44 It is also possible that with the closure of BBC Three as a broadcast channel, commercial providers will find it easier to attract the target audience and may find it profitable to invest less in content. This would tend to increase profits for commercial broadcasters, but reduce consumer surplus.
- 5.45 Given the trend (particularly in younger cohorts) towards on-demand viewing it is possible that commercial providers (similarly to the BBC) will focus on capturing this audience through their on-demand content rather than via broadcast content. We discuss the potential dynamic impact in the context of the BBC launching BBC Three as an online only service in Section 6.

Wider impacts

Commercial broadcasters – EPG slot

- 5.46 The closure of BBC Three as a broadcast channel will vacate an EPG slot (i.e. a position on the electronic programme guide) on the Freeview, YouView, Freesat, Sky and Virgin Media TV platforms.
- 5.47 Ofcom is not in a position to comment on the likelihood of any particular outcome with respect to how the EPG positions will be allocated in the event that BBC Three closes as a broadcast channel. This is decided by the relevant platform provider subject to the EPG code of practice. However, in the event that the slot is allocated to a commercial broadcaster and recognising the prominence of BBC Three's existing EPG slot, this could be of benefit to a commercial broadcaster.

Independent production companies

- 5.48 We recognise there could be an impact on independent production companies as a result of the closure of the BBC Three broadcast channel and its reinvention online. We discuss this in Section 6.

Recommendations

- 5.49 Other than the potential impacts on independent production companies that we discuss in Section 6, we have not identified any negative market impacts from the proposal to close BBC Three as a broadcast channel.

Section 6

BBC Three Online

Summary of proposal

- 6.1 At the same time as the proposed closure of BBC Three as a broadcast channel in autumn 2015, the BBC is seeking permission to create an online only BBC Three service.⁷⁹
- 6.2 The key features of the proposed BBC Three Online service are as follows:
- It will target 16-34 year olds (i.e. the same as the existing BBC Three broadcast channel).
 - The content budget for the service will be around £30m in 2016/17. This compares with a c£60m content budget to run the BBC Three broadcast service in 2013/14.⁸⁰ These budget figures all exclude news, sport and other related costs.⁸¹
 - The content offered will include scripted comedy, entertainment, drama, current affairs, factual, documentaries and news. Both long form content and short form (and new form) content⁸² will be provided.
 - Long form programmes would be available on-demand (over a five-year period) up to 24 times with each time comprising a 30 day availability window.⁸³ Long form programmes would be shown online and also air on BBC One and BBC Two on an interim basis.
 - Short form content and new form content would remain available online for a longer period than long form content.
 - BBC Three content would be available via a range of BBC services – on a dedicated website, on programme pages on BBC Online, on BBC iPlayer and potentially on Connected Red Button.⁸⁴ The dedicated BBC Three website would provide:
 - the latest releases of long form programmes available in BBC iPlayer
 - a curated stream of BBC Three content on a continuous loop

⁷⁹ The BBC has since announced that the closure of BBC Three as a broadcast channel and its reinvention as an online only offering would be delayed until 2016. See paragraph 3.10.

⁸⁰ BBC Service Proposals document, page 24.

⁸¹ 'Other related costs' include allocation of central managed production costs, presentation costs, commissioning and scheduling costs and copyright allocation costs.

⁸² Short form content is described as short audio visual programmes. New form content is described as including, but not limited to, text-based content such as blogs and articles.

⁸³ BBC Three programmes are currently available for 30 days online after every transmission (first run and repeats) on the linear channel.

⁸⁴ Connected Red Button provides access to additional information and content via internet connected TVs.

- shareable short and new form content
- BBC Three content will also be promoted and made available on video-sharing and social media platforms such as YouTube, Facebook and Twitter. The Service Proposal indicates that some content may be unique to an individual platform. However, any differences in availability will be on the basis of clear objective criteria reflecting factors such as the functionality of individual platforms and user demographics/expectations.⁸⁵

Stakeholder responses

Impact on commercial channels

- 6.3 Viacom estimated that the impact of closing BBC Three as a broadcast channel and reinventing it online would result in the Channel 5 family share of viewing (for all individuals) increasing by 1.3% or 0.11 percentage points and its share of commercial impacts (for all individuals) declining by 0.3%.⁸⁶ It modelled the impact of closing BBC Three as a broadcast channel by assuming that BBC Three viewing would switch to other channels according to the viewing profile of “heavy” BBC Three viewers.⁸⁷ It assumed that BBC Three Online would gain audience from linear channels only. It uses a BBC Report estimate that 6% of BBC Three’s current audience is via online viewing, and assumes that BBC Three’s online viewing will double following the closure of BBC Three as a broadcast channel and its reinvention online. Viewers were assumed to switch from linear channels to BBC Three Online according to the viewing profile of “heavy” BBC Three viewers.

Impact on independent production companies

- 6.4 PACT was concerned that the BBC should not be able to use BBC Three Online commissions as a means of commissioning content which is primarily aimed at audiences on BBC One and BBC Two (given that the BBC initially plans to show BBC Three Online long form content on BBC One or BBC Two as well, following its online premiere). It considered that this might be used to stretch budgets and cut costs, but would not best serve the interests of viewers, nor of the BBC’s suppliers. It thought that if the BBC wants to transmit content originally commissioned for BBC Three on BBC One or BBC Two, then it must negotiate additional rights packages with producers.⁸⁸
- 6.5 PACT was concerned about the lower budget for BBC Three commissioning as a result of closing BBC Three as a broadcast channel and re-inventing it as an online only service. It considered the BBC Three budget for independent producers is likely to decline more significantly than that for the BBC’s in-house productions. This is in part because of the type of content which is currently commissioned on BBC Three.
- 6.6 PACT explained that under the proposals the BBC budget for scripted comedy on BBC Three would decline to a quarter of its current level. However, under the Window of Creative Competition (WoCC), in 2013/14 independent producers won

⁸⁵ BBC Service Proposals document, page 31.

⁸⁶ Viacom response to MIA stakeholder questionnaire, page 4.

⁸⁷ Viacom defines “heavy” BBC Three viewers as the top 25% of viewers by average time spent viewing the channel and the frequency of tuning in. It says that the audience defined by this measure accounts for 53% of BBC Three’s total viewing.

⁸⁸ PACT response to MIA stakeholder questionnaire, page 4.

79% of all contestable hours in comedy (compared to 21% commissioned from the BBC in-house). It argued that given this balance towards independent producers a reduction in BBC's commissioning budget would disproportionately impact the revenues of independent producers in this genre.⁸⁹

- 6.7 PACT noted that under the current Terms of Trade arrangements between the BBC and independent producers, the BBC is able to transmit content nine times on BBC Three with a narrative repeat within seven days of the original transmission. If the BBC wishes to show the programme more than this it can purchase another package of rights at 2% of the primary rights licence fee.
- 6.8 PACT noted that the proposals would mean that the BBC has the rights to show content 24 times and that it would retain the rights to show the content for a period of five years. It was concerned that this would create an unacceptable loss of income for independent producers commissioning content for BBC Three at a time when commissioning budgets are under significant pressure.⁹⁰
- 6.9 PACT considered that segregating suppliers into long form and short form risked devaluing the BBC Three Online service to suppliers, with the term 'short form' used as shorthand for reducing budgets. Therefore, it considered that all content commissioned on BBC Three Online should be subject to the Terms of Trade, as per Section 285 of the 2003 Communications Act (even though the content was not distributed via traditional linear broadcasting) and there should not be any distinction between long form and short form content terms. This would ensure that content producers have the ability to exploit the rights to their content in secondary markets and enable them to build businesses and invest funds into developing additional content and services.⁹¹
- 6.10 PACT was concerned about the proposal to promote BBC Three Online content on video sharing and social network platforms. It highlighted that in its PVT application the BBC does not reference the need to agree commercial terms with producers who own content rights as part of any arrangements to promote content on video sharing platforms (such as YouTube). PACT explained that under current arrangements, complementary promotion online of programmes made by independent producers for the BBC is an independent producer's right.
- 6.11 PACT considered that the BBC's entry into this market would have a considerable impact on the ability of producers to build innovative content which offers opportunities to monetise their intellectual property rights.⁹² PACT considered it important that independent producers who make content for the BBC are afforded equal opportunities in order to build their businesses and promote their brands. It would therefore seek amendments to the BBC Fair Trading Guidelines so as to put the external production sector on an equal playing field with the BBC.⁹³
- 6.12 In addition, PACT was concerned that given the BBC's strong, globally recognised position in the market, its entry onto YouTube in order to source new talent could

⁸⁹ PACT response to MIA stakeholder questionnaire, page 11.

⁹⁰ PACT response to MIA stakeholder questionnaire, page 9.

⁹¹ PACT response to MIA stakeholder questionnaire, page 12.

⁹² PACT response to MIA stakeholder questionnaire, page 13.

⁹³ PACT response to MIA stakeholder questionnaire, page 17.

severely diminish opportunities for talent that wish to get recognised by publishing their own material.⁹⁴

- 6.13 Entertainment One noted that the closure of BBC Three and its re-invention online would have limited immediate impact on it given the amount of product that it normally licensed to BBC Three.
- 6.14 However, it did have concerns if the proposals are extended, relating to the amount of time that a licensed product remains on an online service and the value ascribed for such rights. It explained that under the BBC Three Online proposals content could be online for up to 24 x 30 days and that this was effectively Free VOD, which has a negative impact on all other revenues, especially SVOD, transactional VOD (TVOD), electronic sell through and DVD sales, since a consumer need not buy or rent content if it is freely available for an extended period of time. Furthermore, even after it is no longer freely available, the consumer will be less likely to want to purchase it since they are more likely to have ‘had their fill’ during the free window. It indicated that availability of content on a Free VOD basis for a few weeks would have a small impact. However, it considered that two years of free availability would have a potentially huge impact on the revenues expected to be received for other rights (e.g. SVOD, TVOD, electronic sell through and DVD sales).⁹⁵

Impact on pay TV platforms

- 6.15 Virgin Media considered that if the Trust approves the proposals it would set a precedent which would ‘smooth the pathway’ to allow the BBC to place all BBC services online via only BBC iPlayer.⁹⁶
- 6.16 Virgin Media raised concerns about how the proposals relating to reinventing BBC Three Online would be syndicated across different TV platforms. It considered that BBC iPlayer content should be ‘must offer’.⁹⁷ It was concerned that the BBC’s proposals included the possibility of individual syndication arrangements with third parties. It argued that whilst the BBC can choose how to promote its services on third party services, such as YouTube, if it is producing new content (such as short form comedy programming) it should be syndicating this content on a fair, reasonable and non-discriminatory basis to all platforms. In this regard, Virgin Media explained that it would like the opportunity to deliver BBC short form content via its TV platform.⁹⁸
- 6.17 Virgin Media expressed concerns that the BBC’s proposals were unspecific about how it will utilise third-party platforms. In particular Virgin Media was unclear whether the entire catalogue of BBC Three content would be available and how consumers would be able to search for that within the EPG; and whether BBC Three content would be available to watch on the move via portable devices.⁹⁹
- 6.18 [§<]¹⁰⁰
- 6.19 Virgin Media stated that “*distributing a linear channel via IP multicast is far more expensive than via linear broadcast*”. It was concerned that IP delivery would become

⁹⁴ PACT response to MIA stakeholder questionnaire, page 13.

⁹⁵ Entertainment One response to MIA stakeholder questionnaire, page 3.

⁹⁶ Virgin Media response to MIA stakeholder questionnaire, page 3.

⁹⁷ Virgin Media response to MIA stakeholder questionnaire, page 9.

⁹⁸ Virgin Media response to MIA stakeholder questionnaire, page 3.

⁹⁹ Virgin Media response to MIA stakeholder questionnaire, page 7-8.

¹⁰⁰ Virgin Media response to MIA stakeholder questionnaire, page 8.

‘the norm’ for channel distribution. It noted that the BBC has not provided any analysis of the efficiency of broadcasting channels via IP – i.e. “multicast” (where the content is streamed once to an exchange or cabinet and from there it is provided to multiple consumers) compared to the more efficient traditional “broadcast” linear delivery technology.¹⁰¹

6.20 Overall, Virgin Media was not in favour of the proposals. However, in the event that they are approved it thought that the Trust must also consider how the BBC will work with third party platforms including Virgin Media to ensure that:

- i) BBC content is distributed in a platform neutral manner without favouring any particular platform or distribution technology;
- ii) BBC iPlayer content (including BBC Three) is fully distributed including within Virgin Media’s TV Anywhere service; and
- iii) The BBC makes full use of Virgin Media’s future features which are in development and designed to make TV content easily accessible to viewers outside of existing linear technologies. Such functionality will ensure the widest available access to public service content and in innovative ways.¹⁰² Virgin Media considered that to date the BBC had been reluctant to use the enhanced functionality.

Identification of affected services

6.21 We have identified the following services that could potentially be affected as a result of re-inventing BBC Three as an online only service:

- commercial broadcasters’ (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
- other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes;
- independent production companies as a result of how the BBC might commission the production of content for the BBC Three Online service; and
- video sharing and social media platforms e.g. YouTube, Facebook, Twitter.

Assessment of impacts

Static impacts

6.22 We have considered whether reinventing BBC Three online will have an impact on subscription services (e.g. subscriptions to pay TV (such as Sky) or SVOD (such as Netflix)). We note that Entertainment One thought that the availability of BBC Three programmes online for up to 24 x 30 days over five years could have a negative impact on other revenues, especially SVOD, TVOD, electronic sell through and DVD sales. Entertainment One thought that even after content is no longer freely

¹⁰¹ Virgin Media response to MIA stakeholder questionnaire, page 8.

¹⁰² Virgin Media response to MIA stakeholder questionnaire, page 6.

available, the consumer will be less likely to want to purchase it since they are more likely to have ‘had their fill’ during the free window.¹⁰³

- 6.23 We recognise that the availability of BBC Three Online content could result in reduced viewing of subscription services. However, we consider that the amount of additional content available¹⁰⁴ is unlikely to result in households altering their subscription (or DVD) purchasing decisions. We note that requests for TV programmes from BBC iPlayer have increased over time – from 1.77 billion requests in 2012 to 2.22 billion requests in 2013.¹⁰⁵ Yet at the same time subscription revenues (for pay TV services) have grown – from £5.5 billion in 2012 to £5.9 billion in 2013.¹⁰⁶ This suggests that increased viewing of BBC online content has not resulted in a significant substitution away from subscription services.
- 6.24 In our 2013 pay TV research when asked, “What were the reasons your household got a TV service that you pay for on your main set rather than having free TV channels only” – 54% of adults spontaneously cited to get more channels in general, 12% to get more channels of a specific type and 11% to get specific sports channels.¹⁰⁷ This suggests that access to a variety of channels is a significant motivator behind the purchase of pay TV. The reinvention of BBC Three online is unlikely to reduce the appetite for consumption of a variety of pay TV channels.
- 6.25 Nevertheless, we recognise that the impact could be more significant if, in the future, the BBC makes a substantially larger amount of material available on an online only basis and the availability remains 24 x 30 days over a period of five years. As noted in paragraphs 6.97 to 6.99 below, were the BBC to propose changes along these lines it may be appropriate for the Trust to consider conducting a further PVT.
- 6.26 In the rest of this sub-section we therefore focus on the impact on commercial free-to-air broadcasters.

CC model – Overview

- 6.27 CC estimated the impact on broadcasters’ advertising revenues as a result of reinventing BBC Three online in a number of stages.
- 6.28 First, for the purposes of establishing the counterfactual case, CC forecast BBC Three viewing on BBC iPlayer in the absence of closing the BBC Three broadcast channel and launching it online. In the counterfactual case, CC assumed that BBC Three viewing on BBC iPlayer will grow in line with BBC iPlayer’s overall growth.
- 6.29 Second, for the purposes of modelling the impact of the proposals, CC made various adjustments to its estimate of BBC Three iPlayer viewing in the counterfactual to reflect the closure of the BBC Three broadcast channel and its online reinvention.

¹⁰³ Entertainment One response to MIA stakeholder questionnaire, page 3.

¹⁰⁴ The BBC Service Proposals document (pages 81-82) provided an indicative BBC Three monthly schedule which indicated that originated long form content would be around 5 hours per month, catch-up and archive content would be 30 hours per month and acquired content would be 3 hours per month. Therefore total new BBC Three Online content would be around 8 hours per month.

¹⁰⁵ Source: BBC iStats. Excludes clips and off schedule.

¹⁰⁶ 2014 CMR, figure 2.35.

¹⁰⁷ See <http://stakeholders.ofcom.org.uk/binaries/research/tv-research/tv-data/pay-tv-research/Pay-TV-omnibus-2013-data-tables.pdf>, page 538.

More specifically, CC made the following adjustments to its estimates of BBC Three iPlayer viewing:^{108,109}

- i) CC applied an 'online only' uplift of 153% to its estimate of BBC Three viewing on BBC iPlayer to reflect the transfer of some live linear viewing to BBC Three Online.
- ii) the loss of linear promotion (e.g. because individuals will no longer be able to discover BBC Three content on TV) was assumed to result in a reduction of viewing on BBC Three Online of 50% initially, falling to 25% by 2018.
- iii) CC assumed that the optimisation of BBC Three content for online viewing will increase consumption by 25% (this includes the impact of greater integration with social media).
- iv) CC assumed that the reduction in the BBC Three budget will reduce consumption in proportion to the reduction in budget, implying a 44% reduction in consumption.¹¹⁰

6.30 CC assumed that the increase in BBC Three Online viewing (relative to BBC Three iPlayer viewing in the counterfactual) would reduce catch-up viewing of other channels in proportion to their share of on-demand viewing. CC assumed there was some intra BBC substitution i.e. increased viewing of BBC Three Online reduced some other BBC iPlayer viewing.

Our assessment of the CC model

6.31 In this sub-section we discuss the CC assumptions and any adjustments that we have made to these in our modelling.

Viewing of BBC Three on BBC iPlayer in the counterfactual

6.32 CC used an estimate of BBC Three viewing on BBC iPlayer in its counterfactual as a starting point for forecasting the take-up of the reinvented BBC Three Online. In the counterfactual, CC assumed that viewing of BBC Three on BBC iPlayer will grow in line with total forecast BBC iPlayer growth. To inform our view of the CC assumption, we have examined whether the number of BBC Three iPlayer requests has historically grown in line with total BBC iPlayer requests. The growth in requests over 2012 to 2014 is shown in Figure 6.1 below.

¹⁰⁸ We note that some BBC Three content will be available from online sources other than BBC iPlayer e.g. the BBC Three website and YouTube will provide short form content. At least initially all long form content will play out from BBC iPlayer. We have confirmed with the BBC that viewing of BBC Three content away from BBC iPlayer is currently small, and is anticipated to remain small over the modelling period (to 2018).

¹⁰⁹ These adjustments are multiplicative, so that the BBC Three BBC iPlayer viewing figures for 2018 are calculated to be $(1+153\%) \times (1-25\%) \times (1+25\%) \times (1-44\%) \times$ BBC iPlayer viewing in 2018 in the counterfactual.

¹¹⁰ CC took the BBC Three budget for originations and repeats of ~£54m in 2013/14 and compared it to the forecast budget of ~£30m in 2016/17 for BBC Three Online. The 44% reduction in consumption is derived as the £24m reduction in spend divided by original £54m budget.

Figure 6.1: Growth in BBC iPlayer requests and requests of BBC Three content on BBC iPlayer

	2012	2013	2014
Growth in total BBC iPlayer requests	20%	26%	14%
Growth in BBC Three (on BBC iPlayer) requests	20%	29%	8%

Source: BBC (2015)

- 6.33 While there is some difference in the growth rate historically, we note that the geometric mean growth rates are broadly comparable over the 3-year period. Therefore, we consider that the CC assumption is broadly reasonable to forecast the growth of BBC Three iPlayer viewing in the counterfactual.

Transfer to online viewing

- 6.34 CC applied an 'online only' uplift of 153% (to its estimate of BBC Three viewing on BBC iPlayer in the counterfactual) to reflect the transfer of some live linear viewing to BBC Three Online.
- 6.35 CC's assumption regarding the amount of viewing transferred online is informed by the experience of four titles that have premiered online. CC considered that this information provides a reasonable proxy for the situation when the programmes will be available online only since it provides evidence of viewer behaviour before a programme is broadcast on a linear channel when a viewer is obliged to seek out the programme online.
- 6.36 CC recognised that using online premiering as a proxy for online only availability could lead to an underestimate of usage in relation to estimating BBC Three Online viewers, since some potential users of BBC iPlayer in the premiering scenario, might have simply decided to wait for the linear broadcast – an option they would not have in the online only scenario. However, it also noted that for the two BBC Three programmes in the premiering sample it used, viewing via BBC iPlayer (with premiering) represented around 43% of the total viewing of each programme and therefore, based on that data, the remaining 57% of viewing was the maximum increment available (and therefore the maximum threshold for an underestimate in viewers). It considered that the 'waiters for linear' will form only part of this viewing – it would likely include both viewers who simply stumbled across the programme in the EPG and those who are not BBC iPlayer users. In addition, it considered that even for 'the waiters for linear', there was no guarantee that the disappearance of linear broadcast would cause a transfer to viewing to online since their willingness to delay consumption despite the programme already being available suggested that their relationship with the programme may not be that strong.¹¹¹
- 6.37 We consider that premiering is an imperfect proxy for the situation when content is available on BBC Three Online only. As CC noted, this could lead to an underestimation of online viewing because where programmes are premiered viewers have the option of viewing linearly, whereas in an online only situation viewers are forced to seek a programme online. At the same time we recognise that the BBC has not, to date, moved programmes from linear broadcast to online only

¹¹¹ CC report, page 27.

therefore it is difficult to construct a ‘natural experiment’ to inform the impact of going ‘online only’.¹¹²

- 6.38 In the absence of better information, we have retained CC’s online only uplift assumption, though to account for the degree of uncertainty we have rounded it to 150%. In our sensitivity analysis below we have considered a higher online only uplift factor of 300% (double our base case assumption).

Loss of linear promotion

- 6.39 CC considered that while BBC Three has a linear broadcast channel the viewing of BBC Three on BBC iPlayer benefits from a promotion effect resulting from heightened awareness of BBC Three content because it is being broadcast.¹¹³ Specifically CC referred to the cross-promotional benefits resulting from:
- 6.39.1 discovering a programme on TV but deciding to view it online at a later date;
 - 6.39.2 viewers receiving recommendations from those who have seen the broadcast programme which prompts them to seek the programme on BBC iPlayer; and
 - 6.39.3 media outlets reviewing a broadcast programme which builds awareness.
- 6.40 CC considered that the relevance of these factors was confirmed by the results of the market research it commissioned for the BBC. The research indicated that only 25% of users of online TV had used the service to discover a new programme in the last month, while 73% mainly or only used online services for seeking out specific content.¹¹⁴ In addition, when viewers were asked how they found out about programmes they sought out online, 57% of respondents mentioned the TV channel; 22% said word of mouth; 16% mentioned a website; and 15% a publication.¹¹⁵
- 6.41 Therefore, CC considered that the reinvented BBC Three Online would lose the benefit of linear promotion which would thereby dampen online consumption.
- 6.42 However, CC considered that determining the impact of the loss of linear promotion was challenging. It assumed that the loss of linear promotion leads to a 50% reduction in BBC Three online consumption in 2014.¹¹⁶ It also assumed that over time as viewers become more sophisticated and diverse in their use of online services (such as BBC iPlayer) they may be more likely to use online services as a destination to discover new content (rather than as a place to seek specific content). As such, the dampening effect resulting from the loss of linear promotion was

¹¹² We have a number of comments on the sample used to derive the premiering uplift – we discuss these in Section 7.

¹¹³ This is separate to any benefits that might derive from TV trailers (which could continue on other channels even if BBC Three closed as a linear channel).

¹¹⁴ CC market research report, page 7.

¹¹⁵ Ibid.

¹¹⁶ CC estimated the impact of the loss in linear promotion at the time the model was developed in 2014. However, the impact is not felt in their modelling until the proposed launch of BBC Three Online in 2015.

assumed by CC to become less critical over time and by 2018 results in a loss in online consumption of 25%.¹¹⁷

- 6.43 We agree that showing programmes on a broadcast channel could generate online viewing, and that the importance of this effect could reduce over time in the event that the BBC's online services are increasingly seen as a place to discover content.
- 6.44 However, it is very difficult to predict how much the loss of a broadcast channel will affect viewing online and how this will change over time. We found that varying CC's assumption made relatively little difference to the results, and hence, in the absence of any better information, we have not revised it.

Optimising content for online viewing

- 6.45 CC noted that BBC Three content is currently commissioned primarily with traditional TV consumption in mind and that as BBC Three is reinvented as an online only proposition its content will be optimised for online viewing e.g. by offering more short form content and also by exploiting integration with social media (such as Twitter, Facebook). To reflect the optimisation of content for BBC Three Online, CC included an online optimisation uplift factor of 25% in determining its estimate of BBC Three Online viewing.
- 6.46 We agree that optimising BBC Three content for online consumption could have an impact on viewing, though the strength of this impact is uncertain and difficult to quantify. However, making significant changes to this uplift assumption has very little impact on the BBC's viewing share. For example, quadrupling the uplift to 100% increases the BBC's viewing share by 0.1 percentage points in 2018 (to 33.8%) compared to the case when a 25% uplift factor is used.
- 6.47 Given the marginal impact of this assumption in the model we have not revised the CC assumption in our base case and assume a 25% uplift factor to account for the optimisation of content on BBC Three Online.

Reduction in BBC Three budget

- 6.48 BBC Three Online is proposed to have a significantly lower content budget compared to the current BBC Three broadcast channel. CC compared the BBC Three 2013/14 content budget of £54m (for originations and repeats but excluding acquisitions¹¹⁸) to the forecast budget for the online service in 2016/17 of c£30m. CC assumed viewing of BBC Three Online would reduce in line with the reduction in its budget thereby implying a 44% reduction to BBC Three Online viewing.¹¹⁹
- 6.49 We agree that the amount of budget is likely to influence the quality and/or quantity of content and therefore viewing. While it is not necessarily the case that a change in the budget would cause the same proportional change in viewing, we consider this a reasonable modelling assumption.

¹¹⁷ Between 2014 and 2018 the loss of linear promotion trends linearly.

¹¹⁸ CC used a budget figure which excluded acquisitions because the vast majority of these (e.g. *Family Guy*) are not currently available on BBC iPlayer for content rights reasons. It thus considered the loss of this portion of spend will have a minimal impact on BBC iPlayer consumption. It noted this may be somewhat conservative as an ambition for the proposals is to improve quality which may mitigate the audience loss.

¹¹⁹ $(£54m - £30m) / £54m = 44\%$

- 6.50 As part of our discussions with the BBC we have received revised BBC Three budget information. We have used this to update the budget reduction figure so that it changes from the 44% in CC's model to 47%.

Impact on other channels

- 6.51 CC assumed that increased viewing of BBC Three Online (relative to BBC Three viewing on BBC iPlayer in the counterfactual) results in a reduction in viewing for other catch-up channels (including other BBC channels on BBC iPlayer), with live linear/PVR viewing unaffected.
- 6.52 We consider that the changes in viewing may be more complex as people may watch BBC Three Online in place of live linear viewing.
- 6.53 However, given that the overall impact on commercial operators is calculated by reference to total viewing hours (which aggregates live linear and catch-up viewing), we consider that revising the model to account for the effect of people watching BBC Three Online in place of live linear viewing would not have a material impact on the overall results. Therefore, we consider that CC's approach represents a reasonable modelling simplification which we have not changed.

Impact on viewing hours and viewing share

- 6.54 In Figure 6.2 below we show the cumulative impact of closing BBC Three as a linear channel and reinventing it online, in terms of viewing hours and viewing share for the BBC and the main commercial providers in 2018.

Figure 6.2: Net impact on viewing from closing BBC Three broadcast and reinventing BBC Three online in 2018

Channel family	Share of total viewing counterfactual	Change in viewing hours due to closure of BBC Three broadcast in hours bn (percentage points in parenthesis)	Change in viewing hours due to reinvention of BBC Three online in hours bn (percentage points in parenthesis) ¹²⁰	Share of total viewing after closing BBC Three broadcast and launch of BBC Three Online	Percentage change in viewing share relative to counterfactual
BBC	34.4%	-0.6 (-0.7pp)	+0.04 (+0.05pp)	33.7%*	-2.0%
ITV	20.6%	+0.2 (+0.2pp)	-0.01 (-0.01pp)	20.8%	+1.0%
Channel 4	11.4%	+0.1 (+0.2pp)	-0.01 (-0.01pp)	11.5%*	+1.3%
Channel 5	5.9%	+0.1 (+0.1pp)	-0.00 (-0.00pp)	5.9%*	+1.2%
Other	27.8%	+0.2 (+0.3pp)	-0.02 (-0.02pp)	28.1%	+0.9%
Total	100.0%	0.0 (0.0pp)	0.00 (0.00pp)	100.0%	-

*Note: The difference between share of total viewing after BBC Three changes and the sum of counterfactual viewing share and change in viewing share values is due to rounding. The change in viewing is reported here to 2 decimal places (rather than to 1 decimal place) to show that the effects of the proposal on viewing are not precisely zero – since they would round to zero if reported to 1

¹²⁰ Compared to the situation when BBC Three broadcast is closed.

decimal place. This also applies to all figures elsewhere in this document that present changes in viewing to 2 decimal places.

- 6.55 The net impact on viewing hours and viewing shares from closing BBC Three as a broadcast channel and reinventing it online is positive for commercial broadcasters. The results are similar to those presented for the closure of BBC Three as a broadcast channel because this is the dominant effect; the online relaunch has a relatively small mitigating impact. Channel 4 has the largest relative increase in its viewing share. The net reduction to the BBC's viewing share is 0.67 percentage points in 2018 relative to our counterfactual.
- 6.56 In its response to the MIA stakeholder questionnaire, Viacom estimated the increase in the share of viewing for the Channel 5 family to be broadly similar to our own. Viacom estimated that the closure of BBC Three as a broadcast channel and its reinvention online would increase the share of viewing for the Channel 5 family by 1.3% or 0.11 percentage points, compared to our estimate of 1.2% or 0.07 percentage points. The main differences in its approach were to use a different definition of "heavy" BBC Three viewers to that used in our analysis¹²¹, and a simpler approach to estimating the amount of BBC Three Online's viewing. Viacom assumed BBC Three Online viewing would be double that which BBC Three programmes currently achieve on BBC iPlayer.
- 6.57 Our results for the impact of the BBC Three changes on viewing are broadly consistent with the results of the Kantar qualitative research. The research participants envisaged broadly similar viewing habits in light of the proposed changes to BBC Three. Instead of watching BBC Three participants envisaged watching other linear channels that satisfy similar needs e.g. Channel 4, E4, ITV2, Dave, Fox or Comedy Central. Where shifts in viewing were foreseen, the vast majority of participants anticipated these would be marginal rather than major changes. The report noted that catch-up and VOD may not be major beneficiaries due to the perceived effort required in accessing and selecting content.¹²²

Impact on producer surplus

- 6.58 We have estimated the financial impact on the main commercial providers in the base case by estimating the change in producer surplus. The results show the net impact of closing BBC Three broadcast and reinventing it as an online service relative to the counterfactual.

¹²¹ We define "heavy" viewers of BBC Three as those that account for the top 33% of BBC Three viewing. Viacom defined "heavy" viewers of BBC Three as the top 25% of viewers by average time spent viewing the channel and the frequency of tuning in.

¹²² Kantar report, page 67-68.

Figure 6.3: Net impact on producer surplus from closing BBC Three broadcast and reinventing BBC Three online in 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	+1.0%	1,710	5.7	8.6	11.4
Channel 4	+1.3%	813	3.4	5.1	6.8
Channel 5	+1.2%	358	1.4	2.1	2.8
Other	+0.9%	999	3.0	4.5	6.0
Total	+1.0%	3,881	13.5	20.3	27.1

- 6.59 The net impact of closing the BBC Three broadcast channel and reinventing it online is positive for commercial broadcasters. The results are similar to those presented for the closure of BBC Three as a broadcast channel because this is the dominant effect; the online re-launch has a relatively small mitigating impact in this static analysis.
- 6.60 Viacom has modelled the impact on the Channel 5 portfolio NAR to be negative. This is because it estimates changes in revenues solely through changes in SOCI. Even though Channel 5 portfolio channels gain viewing share from these proposals, they do not gain as much proportionally as does Channel 4. This approach implicitly assumes that changing the total number of impacts in the market will not affect the total revenues available in the market. As discussed in paragraphs 3.21 to 3.31, we have taken a different approach, assuming that changes in impacts will affect the total size of the TV advertising market to some degree.

Sensitivity analysis

- 6.61 As discussed above, there is a significant degree of uncertainty regarding some of the modelling assumptions. We have therefore considered a scenario where the more uncertain assumptions are flexed to be significantly more favourable to the BBC's viewing share (so significantly less favourable to commercial broadcasters). In this scenario we have assumed:
- 6.61.1 an 'online only' uplift of 300% (double the base case assumption);
 - 6.61.2 that there is no loss of consumption due to the loss of linear promotion i.e. reduction of 0% (base case assumption -50% reducing to -25% by 2018); and
 - 6.61.3 that optimising the content for BBC Three Online results in a 50% uplift (double the base case assumption of 25%).
- 6.62 With these assumptions the BBC's viewing share from closing BBC Three as a broadcast channel and reinventing it online is reduced from 34.4% in the counterfactual case to 34.0% (a decline of 0.3 percentage points). This would result in commercial broadcasters' advertising revenue rising by around £7-13m, compared to the counterfactual.

Dynamic impacts

Changing perceptions of on-demand services

- 6.63 The majority of UK adults have used a VOD service to watch TV or film content, with around six in ten adults (61%) claiming to have used such a service in 2014.¹²³ According to Ofcom's 2014 PSB Report, take-up of VOD services was highest among the youngest age group studied (16-24 year olds) at 80%, and declined with age, with take-up lowest among those aged 75 and over at 19%.
- 6.64 Programme consumption using the PSBs' VOD services has grown steadily since 2008, averaging approximately half a billion extra programme requests each year. In 2013, there were 3,049 million requests for on-demand programmes across BBC iPlayer, ITV Player, 4oD, Demand 5 and the other broadcaster equivalent services¹²⁴ on Sky, BT and Virgin Media set-top boxes.¹²⁵
- 6.65 Consumer research indicates that, on-demand viewing is mainly used to catch-up on missed programmes or watch programmes at a convenient time, rather than to browse content. For example:
- The 2014 CMR reported that in 2013 61% cited catch-up as a reason for on-demand use, while 39% used on-demand to watch programmes 'at a time that suits me'.¹²⁶
 - The CC market research found that only 25% of users of online TV/video services reported browsing behaviour, while 90% used it to seek particular programmes.¹²⁷
 - The Kantar qualitative research noted that there is greater perceived effort involved in accessing and selecting online only content (relative to live linear viewing).¹²⁸
- 6.66 Overall, we consider that for the foreseeable future live linear viewing is likely to remain the primary place where people discover content and watch TV.¹²⁹
- 6.67 However, there is evidence that perceptions of on-demand services are changing. The CMR indicated that consumers are increasingly using on-demand as a means to discover content. In 2011, of those that used on-demand services, 25% said a reason for using it was because nothing was on 'normal' TV and 25% used it to pass some time/relax. These categories had increased to 33% and 30% of users of on-

¹²³ 2014 PSB annual report, paragraph 4.28. Available at <http://stakeholders.ofcom.org.uk/broadcasting/reviews-investigations/public-service-broadcasting/annrep/psb14/>

¹²⁴ Catch-up services on set-top boxes which show BBC, ITV, Channel 4 and Channel 5 content however they are not branded BBC iPlayer or ITV Player etc.

¹²⁵ PSB Annual report 2014, paragraph 4.32.

¹²⁶ 2014 CMR, figure 2.89.

¹²⁷ CC market research report, page 6.

¹²⁸ Kantar report, page 65.

¹²⁹ This is consistent with the current experience where, on average, people spend significantly more time watching live TV compared to on-demand/catch-up. The 2014 CMR (Figure 2.20) reported that, on average, adults spend 2 hours 59 minutes watching live TV per day, compared to 12 minutes for free on-demand/catch-up services.

demand services respectively by 2013.^{130 131} Netflix and Amazon Prime are examples of on-demand services where consumers search for content, rather than using it as catch-up.

- 6.68 As on-demand services develop and become more widely used, they may increasingly be viewed as places to discover content (including the BBC's online content).
- 6.69 Furthermore, we note the following developments in relation to BBC iPlayer (and BBC Three Online):
- The BBC has indicated that it views closing BBC Three and reinventing it as an online only service as a “test bed”¹³² and that the proposals are somewhat experimental in nature. The BBC considers that, “*The new BBC Three has the potential to shape and expand the market for the providers of digital entertainment, information and education for 16-34 year olds in the UK and build demand for new forms of content.*”¹³³
 - In explaining the decision to reinvent BBC Three as an online service the BBC has noted “*[the] new BBC Three could be the arrowhead for the whole industry - shaping and extending the “TV” market beyond linear and building demand for new forms of content. It could be a place that gives creative industries an avenue to test how audiences react to new forms of content at scale, content that builds new relationships with younger audiences. It could redefine public service broadcasting in the digital age. New BBC Three could do for digital content what BBC News Online did for take up of the internet, what BBC iPlayer did for the VOD market and what BBC Three did for digital TV a decade ago.*”¹³⁴
 - The BBC has also announced plans to develop its online services to include tailored recommendations based on individual users' tastes. The ‘myBBC’ initiative will roll out over 2015 and aims to leverage the organisation's full range of AV and audio content and online features.^{135 136}
- 6.70 While we do not express views on the BBC's long-term strategy, it is clear that the development of its online services is an important component of that strategy. Furthermore, given the BBC's prominence, developments by the BBC could have an important role in shaping perceptions of on-demand services as a place to discover content. Ultimately, this could encourage greater levels of consumption of BBC content on BBC iPlayer (and affect trends in overall on-demand viewing relative to live linear viewing). While the overall effects of this are uncertain, we acknowledge that the BBC could provide a role as a catalyst for increasing the demand and use of online services that could provide a benefit to commercial providers.

¹³⁰ 2014 CMR, figure 2.89.

¹³¹ We referred to other evidence about the changing perception of on-demand services in our December 2013 BBC Trust Significance Test (that assessed proposals to alter the BBC Store). In that document we noted that according to a BBC survey 60% of users claimed to access BBC iPlayer with a specific programme in mind – a decrease from 80% in 2009.

¹³² BBC Service Proposals document, page 3.

¹³³ *ibid*

¹³⁴ <http://www.bbc.co.uk/blogs/aboutthebbc/posts/Blazing-a-trail-for-new-BBC-Three>

¹³⁵ See <http://www.bbc.co.uk/blogs/aboutthebbc/entries/46a896ea-e587-4c63-ae7e-9781bca58dd3>

¹³⁶ The impact of ‘myBBC’ is not included in our counterfactual case.

Strategy of other broadcasters

- 6.71 The relatively innovative approach adopted by the BBC could influence the strategy of other broadcasters, who might respond by increasing investment in on-demand or online only propositions, and consider cutting investment in broadcast channels. We are aware that Channel 4 has evolved its 4oD service to All 4, which contains both catch-up and archive material. Channel 4 states this will be “*a new, engaging and intuitive user interface will guide viewers through a digital experience*”.¹³⁷ Given that consumption of on-demand viewing is anticipated to increase anyway (in the absence of the BBC’s proposals) this is likely to reinforce the current trend.
- 6.72 The BBC recognises the importance of third party platforms and services within its proposals noting, “*The majority of BBC digital content is now consumed via mobile, tablet or connected TV, mainly by means of the BBC iPlayer app, and as a consequence we are heavily dependent on our third party relationships with device manufacturers or platform providers to reach our online audiences watching BBC AV content.*”
- 6.73 We consider that building strong relationships with third party platforms and services is likely to be increasingly important for other broadcasters given the trend towards consumption via mobile devices and tablets. By 2019 Enders Analysis expects 15% of viewing (including both long and short form content) to be on ‘other screens’ i.e. not on the TV set, increasing to 33% for 16-24 year olds.¹³⁸ If other broadcasters are unable to build relationships with these partners e.g. due to a lack of scale or resources, then they might find that they are ‘left behind’ and unable to compete with the offering of the BBC.

Video/content sharing platforms

Potential impact on viewer volumes

- 6.74 BBC Three Online plans to spend 20% of its first year’s content budget on short form and new form content.^{139 140} This may be more akin to the content typically shown on websites such as YouTube or BuzzFeed as opposed to that shown on more traditional TV channels which currently focus on long form content. Therefore, it is possible that viewers will switch from other ‘new form’ services to BBC Three Online.
- 6.75 At the same time, we note that the BBC plans to promote and host some of its content on platforms such as YouTube, and also social networks such as Facebook. Where BBC Three content is featured on other sites it is possible that additional viewers will be driven to the partner site. This could have a positive spill over effect as viewers may then also view non-BBC content on the partner site.

¹³⁷ <http://www.channel4.com/info/press/news/channel-4-to-launch-new-digital-service-all-4>

¹³⁸ Enders Analysis, January 2014, Where have all the young viewers gone?, page 28-29.

¹³⁹ BBC Service Proposals document, page 23.

¹⁴⁰ In the Trust’s Service Description document, short form content is described as short audio visual programmes which have a narrative arc. New form content is described to include (but not be limited to) text-based content, images, video clips, animation and interactive content.

Potential impact on advertising revenues

- 6.76 Consumption of short form content via platforms such as YouTube is increasingly popular – particularly amongst young adults. The top 100 YouTube channels generate over ten billion views per month globally.¹⁴¹
- 6.77 However, while the popularity of online short form content has increased, it currently attracts a relatively small portion of total advertising spend. Deloitte estimate that globally short form content will generate about \$5 billion of advertising revenue in 2015, this compares to \$210 billion for long form advertising on TV.¹⁴² Monetising short form content is a challenge because it is often watched in short bursts which may mean the tolerance for adverts is lower compared to long form programmes (which are usually at least 30 minutes in length).
- 6.78 Given the modest scale of the BBC's proposals, in particular in relation to short form content, in the context of overall trends in the growth of popularity of short form content and the challenges presented in monetising this, we consider that the impact on advertising revenues for video content/sharing platforms from the proposal to reinvent BBC Three online is limited.

Wider impacts

Impact on independent production companies

- 6.79 Two stakeholders (PACT and Entertainment One) raised concerns about the potential impact of the proposal to reinvent BBC Three online on independent production companies.

Reduction in the BBC Three budget

- 6.80 PACT raised concerns that the reduction in the budget for BBC Three commissioning as a result of closing BBC Three as a broadcast channel and reinventing it online would disproportionately impact independent production relative to BBC in-house production. This was because independent producers currently win 79% of all contestable hours of scripted comedy under the WoCC (and the budget for scripted comedy is proposed to decline to a quarter of its current level).
- 6.81 We acknowledge that given the proposed reduction in the BBC Three budget, independent production companies are likely to face a reduction in commissioning revenues from BBC Three. We also note that part of the rationale for reducing BBC Three's budget is to enable increased investment in BBC One drama, which could benefit independent production companies. Overall there are likely to be 'winners and losers' as a result of the proposals, with production companies focussed on comedy more likely to lose and those focussed on drama more likely to gain. However, the allocation of the BBC's budget between channels (and between genres within those channels) is a matter of editorial judgement for the BBC. Therefore, the reduction of budget for BBC Three, although integral to the BBC's proposals, could be made in the absence of its proposals to reinvent BBC online.

¹⁴¹ Technology Media and Telecommunications Predictions 2015. Deloitte, Available at <http://www.slideshare.net/ThierryLabro/deloittetmt?related=1>, page 32.

¹⁴² Technology Media and Telecommunications Predictions 2015, Deloitte, page 33.

6.82 We also note that the BBC operates both the WoCC and an in-house guarantee. As a result, qualifying content must fulfil the following criteria:

- 25% of qualifying content must be produced by independent production companies (the independent production quota);
- 50% must be produced in-house (the in-house guarantee); and
- the remaining 25% can be commissioned from either in-house or independent production companies (the WoCC).

6.83 Under the above framework, the proposed reduction in BBC Three's budget will also have a negative impact on the BBC's own in-house production revenues (relating to the in-house guarantee and commissions from in-house production won via the WoCC).

Loss of regulatory protection

6.84 The Terms of Trade were agreed between the BBC and PACT (on behalf of independent production companies) and provide independent production companies with an assurance over the minimum terms relating to licence periods, exclusivity, distribution, funding and payments when undertaking productions for the BBC. The Terms of Trade agreed between the BBC and PACT are in relation to the commissioning of programming for broadcast channels but not online programming. Therefore, at present, programmes commissioned for BBC Three Online would fall outside the existing Terms of Trade.

6.85 We consider that the reinvention of BBC Three online could adversely impact independent production companies as a result of the loss of regulatory protection provided by the current Terms of Trade with the BBC.

6.86 Further to this, we highlight the concerns expressed by PACT and Entertainment One regarding the impact of reinventing BBC Three online in relation to:

- Repeat fee revenues – Under the Terms of Trade, independent producers currently earn revenues for repeat broadcasts of their shows based on the number of showings. Under the proposed reinvention of BBC Three online long form programmes would be available online for up to 24 x 30 day windows (or 720 days in total). As such, the number of repeat viewings could be far in excess of that envisaged under the current Terms of Trade.
- Reduction in the value of secondary content rights – The availability of BBC Three Online content for up to 720 days over a five year period is likely to reduce the value of a programme in secondary content windows (e.g. to SVOD services) for independent production companies.

6.87 In its service proposal, the BBC stated that content related contracts are currently under negotiation. We consider that these are important negotiations which may address the issues identified in this MIA.

- 6.88 We also note that in January 2015 the Trust published a consultation on the future arrangements for the supply of television, radio and online content.¹⁴³
- 6.89 We would expect that the Trust will carefully consider responses to its consultation and monitor the progress of commercial negotiations closely, and in light of this consider whether any further action is necessary.¹⁴⁴

TV platforms

- 6.90 Virgin Media raised concerns about how the proposals relating to reinventing BBC Three online would be syndicated across different TV platforms. These concerns are outlined in paragraphs 6.16 to 6.20.
- 6.91 We consider that the issues raised by Virgin Media around content integration and syndication are reflective of a broader debate in the industry between content providers and TV platform providers around the availability of content. In this debate, broadcasters have wanted to retain a direct relationship with the viewer and how content is presented to viewers. TV platforms, on the other hand, have wanted to integrate content within their own design and search functionality and with their own curation, regardless of the content provider.
- 6.92 We note that the BBC plans to provide different BBC Three content to different platforms and may have some content which is unique to an individual platform.¹⁴⁵ The BBC has explained that any differences in the availability of BBC Three content across different platforms will be on the basis of objective criteria.
- 6.93 Whilst we recognise that some tailoring of content depending on the platform could be beneficial, we also note that the criteria for deciding which platforms will benefit from having such content is not detailed and as such is open to interpretation. Furthermore, there is a risk that decisions by the BBC relating to providing content to some platforms and not others could potentially give rise to competitive distortions.
- 6.94 We note Virgin Media's comments around how consumers would be able to search for BBC Three content within its EPG. Under the BBC's proposals BBC Three Online would be accessible via a dedicated website and BBC iPlayer.
- 6.95 BBC iPlayer is accessible via a number of TV platforms (including Virgin Media's platform). However, given the increasing significance of BBC iPlayer (in light of the BBC's proposals relating to reinventing BBC Three online) the precise detail of how BBC content is syndicated on TV platforms (and other devices) is likely to become more important. For example, issues such as being able to navigate easily between BBC content and non-BBC content are likely to be of key importance to viewers and TV platform providers.
- 6.96 We note that the Trust is currently consulting on the BBC's future syndication policy as part of a wider consultation on the 'Distribution framework for BBC services and

¹⁴³ BBC Trust review of the BBC's arrangements for the supply of television and radio content and online services, BBC Trust, 22 January 2015, http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/content_supply/2015/content_supply.pdf

¹⁴⁴ Ofcom has powers to provide guidance and dispute resolution to ensure 'appropriate' Terms of Trade are established.

¹⁴⁵ BBC Service Proposals document, page 31.

content'.¹⁴⁶ We consider that particular attention should be given to how the BBC's online services fit within these to ensure that the commercial platforms are not unfairly disadvantaged when the BBC makes content available.

Recommendations

Threshold for future PVTs

- 6.97 Our assessment of the impacts is based on the proposals outlined by the BBC.
- 6.98 However, we are mindful of developments over the longer term. Therefore, we consider that the Trust should set clear boundaries on what the BBC is permitted to do (in line with current proposals) and at what stage further approval is required.
- 6.99 We consider that future changes to the proposals, such as, substantially increasing the amount of online only content; making more channels online only; or changing the type of content available on BBC Three Online would represent a material change to the proposals that we have assessed in this MIA. As such, the Trust would need to consider conducting a further PVT to assess the market impacts.

Terms of Trade

- 6.100 We consider that the reinvention of BBC Three online could adversely impact independent production companies as a result of the loss of regulatory protection provided by the current Terms of Trade with the BBC.
- 6.101 In its service proposal, the BBC stated that content related contracts are currently under negotiation relating to the Terms of Trade. We consider that these are important negotiations which may address the issues identified in this MIA.
- 6.102 We also note that in January 2015 the Trust published a consultation on the future arrangements for the supply of television, radio and online content.¹⁴⁷
- 6.103 We would expect that the Trust will carefully consider responses to its consultation and monitor the progress of commercial negotiations closely, and in light of this consider whether any further action is necessary.

Syndication policy

- 6.104 Given the prevalence of BBC iPlayer the precise detail of how BBC content is syndicated on TV platforms (and other devices) is likely to become more important. For example, issues such as being able to navigate easily between BBC content and non-BBC content are likely to be of key importance to viewers and TV platform providers.
- 6.105 We note that the Trust is currently consulting on the BBC's future syndication policy. We consider that particular attention should be given to how the BBC's online

¹⁴⁶ Public consultation on BBC Trust's distribution framework for BBC services and content, BBC Trust, http://www.bbc.co.uk/bbctrust/have_your_say/distribution_framework

¹⁴⁷ BBC Trust review of the BBC's arrangements for the supply of television and radio content and online services, BBC Trust, 22 January 2015, http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/content_supply/2015/content_supply.pdf

services fit within these to ensure that the commercial platforms are not unfairly disadvantaged when the BBC makes content available.

Cross promotion of BBC Three Online

6.106 In this section we have identified the market impacts from the proposed changes to BBC Three. However, the Trust should note that extensive cross-promotion by the BBC may increase these impacts. We encourage the Trust to consider the role of cross-promotion as part of its assessment.

Section 7

Changes to BBC iPlayer

Summary of proposal

- 7.1 BBC iPlayer is primarily a television catch-up and simulcast service (although it also provides a small amount of non-broadcast audio and video content).
- 7.2 In addition to increasing the amount of non-broadcast content in BBC iPlayer as part of its proposals relating to BBC Three Online (discussed in Section 6), the BBC is proposing the following changes to BBC iPlayer:¹⁴⁸
- to premiere some programmes on BBC iPlayer (before they are broadcast on a linear service); and
 - to include selected content commissioned by third parties.

Premiering programmes on BBC iPlayer

- 7.3 Under its proposals the BBC would premiere programmes from BBC One, BBC Two, BBC Four, CBBC and CBeebies.
- 7.4 In relation to BBC One, BBC Two and BBC Four:
- around five titles in total across the three channels would be premiered online per year. Assuming 10 episodes per title, this would result in an additional 25 to 50 hours' worth of programming available online in advance of linear transmission.
- 7.5 In relation to CBBC and CBeebies:
- Around 20 titles in total would be premiered online per year by 2016/17. This would equate to around 61 hours of CBBC content and around 49 hours of CBeebies content per year.
 - In relation to CBBC, the BBC would premiere drama aimed at 10-12 year olds which could also be repeated in the 8-9pm slot under its proposals for CBBC (discussed in Section 10) and comedies.
 - In relation to CBeebies, the BBC would premiere different formats, with a focus on titles which are shorter in duration. For example, programmes with a learning angle, short (five minute) programmes and programmes that deal with problem solving.

¹⁴⁸ We note that the BBC has also indicated that in the future it may increase the volume of online only content available within BBC iPlayer (either through BBC iPlayer specific commissions or by incorporating video content from elsewhere in BBC Online). However, the BBC is not requesting additional permissions for this in its PVT application (beyond the changes to BBC Three) since it considers this to be covered within the BBC iPlayer's existing service remit.

- 7.6 The BBC has indicated that it is unlikely to premiere programmes more than seven days in advance of the linear broadcast. In addition, it has indicated that it would not plan to premiere online programmes that may contain spoilers (that the BBC would not want to appear on social media sites); programmes where the BBC aims to maximise the sense of a shared viewing experience; and programmes for which the BBC does not hold the rights to show on BBC iPlayer (e.g. some acquired programming).

Inclusion of third party content

- 7.7 Currently only content that is commissioned or acquired by the BBC is hosted on BBC Online.¹⁴⁹
- 7.8 The BBC is proposing to engage in partnerships with institutions that share its values to make available third-party commissions within BBC iPlayer. In developing how content would be selected or integrated into BBC iPlayer the BBC would have regard to the following principles:
- third parties would be limited to not-for-profit cultural and arts organisations;
 - proposals would need to support the BBC's public purposes; and
 - proposals would need to be consistent with and help to support the BBC's strategic objectives.
- 7.9 In addition, the inclusion of third-party content would be subject to the BBC's internal regulatory scrutiny and need to comply with the BBC Fair Trading Guidelines¹⁵⁰ and BBC Editorial Guidelines.¹⁵¹

Stakeholder responses

Impact on pay TV platforms

- 7.10 Virgin Media was concerned that the BBC's long term strategic plan envisages BBC iPlayer as a gateway for all BBC content. It thought there should be more than one access point (i.e. in addition to BBC iPlayer) to discover and view BBC content via online only channels. Virgin Media noted that although the proposals to premiere content is limited at the outset, if given approval it will cement and validate the BBC's strategy of moving its content online. It felt that the Trust should set clear boundaries of what the BBC is permitted to do combined with a vision of how BBC content should be distributed. For example, it argued that if BBC content is to be premiered online first, Virgin Media would want the opportunity to make this available to its consumers via its platform in a way of its own choosing (as opposed to being available on its platform via accessing BBC iPlayer only).
- 7.11 Virgin Media felt the proposals in relation to 'premiering' content on BBC iPlayer were vague and not sufficiently developed to allow the Trust to approve. For example, Virgin Media did not understand how the BBC would properly assess which programmes it would premiere and the criteria involved in such an assessment.

¹⁴⁹ Although programmes from S4C (the Welsh language public service channel) have been available on BBC iPlayer since November 2014 on an experimental basis.

¹⁵⁰ <http://www.bbc.co.uk/corporate2/insidethebbc/howwework/policiesandguidelines/fairtrading.html>

¹⁵¹ <http://www.bbc.co.uk/editorialguidelines/>

Virgin Media noted that the BBC has stated it will not premiere programmes online which undermine ‘the sense of a shared viewing experience’ which the BBC states includes programmes such as ‘The Voice’ and ‘The Apprentice’. It considered the stated criteria to be too subjective. It thought that premiering online could have a significant financial impact on platforms such as Virgin Media if licence fee payers feel that they cannot get BBC content through the Virgin Media linear service.¹⁵²

- 7.12 Virgin Media also considered that the criteria outlined in the PVT application regarding the inclusion of third-party content within BBC iPlayer to be extremely vague. It considered that the BBC should clarify its position to ensure that it is not partnering with one particular commercial provider over another.¹⁵³
- 7.13 Virgin Media considered that it was crucial that the BBC submits detailed plans on how it intends to ensure increased take-up of broadband and BBC iPlayer and how it will partner with providers such as Virgin Media. Virgin Media considered that to date the BBC had been reluctant to use the enhanced functionality provided by Virgin Media’s connected TV technology to profile its content (e.g. Virgin Media indicated that the BBC had refused to syndicate its VOD content to Virgin Media’s TV anywhere service).¹⁵⁴

Impact on independent production companies

- 7.14 PACT noted that under the current Terms of Trade, the BBC has the right to a 30-day catch-up window to put content on BBC iPlayer. The BBC also has the right to premiere a programme on BBC iPlayer up to seven days prior to its first linear broadcast. However, any instances in which the BBC wishes to premiere content on BBC iPlayer more than seven days before its linear broadcast would need to be directly negotiated between the BBC and the relevant independent producer, who may well have obligations to third parties under Union and Guild collective agreements.¹⁵⁵

Inclusion of selected third-party content

- 7.15 Channel 4 noted that digital platforms provide broadcasters with opportunities to expand their propositions, and that it was evolving its own digital proposition with the forthcoming launch of All 4. In principle, Channel 4 supported the BBC’s proposal to host selected third party content on BBC iPlayer and recognised the benefit of the BBC using its scale to drive awareness of other public service organisations. Subject to retaining sufficient control of the user experience of its content it would welcome any move to have BBC iPlayer present prominent links to Channel 4’s owned-and-operated digital services.¹⁵⁶

Identification of affected services

- 7.16 We have identified the following services that could potentially be affected by the BBC’s proposed changes to BBC iPlayer:

¹⁵² Virgin Media response to MIA stakeholder questionnaire, page 11.

¹⁵³ Virgin Media response to MIA stakeholder questionnaire, page 12.

¹⁵⁴ Virgin Media response to MIA stakeholder questionnaire, page 3.

¹⁵⁵ PACT response to MIA stakeholder questionnaire, page 16.

¹⁵⁶ Channel 4 response to MIA stakeholder questionnaire, page 3.

- commercial broadcasters' (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and the potential impact on advertising revenues;
- other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes; and
- independent production companies.

Assessment of impacts

Static impacts

- 7.17 We have considered whether the proposals to premiere programmes on BBC iPlayer will have an impact on subscription services e.g. subscriptions to pay TV (such as Sky) or SVOD (such as Netflix). For the reasons described in paragraphs 6.23 to 6.25 we do not think that the additional content available on BBC iPlayer is likely to result in households altering their subscription purchasing decisions in general. This is consistent with our 2015 Kantar qualitative research which suggested the impact of BBC iPlayer premieres on pay TV channels would be negligible unless major content items debut on BBC iPlayer. The research also suggested the impact on catch-up and VOD would be negligible given the majority of catch-up/VOD visits focus on specific content items.^{157 158}
- 7.18 In addition, we understand that the premiered programmes will be broadcast at a later date which would be expected to further reduce any potential impact on subscription services.¹⁵⁹
- 7.19 We have considered whether the focus on children's premieres could have an impact on subscription revenues. While it is possible that households that currently purchase subscription TV packages to access children's channels will decide that free-to-air content (with the addition of the proposed BBC iPlayer premieres of children's content) is sufficient for their needs, we consider that it is unlikely that the addition of premiering children's programmes on BBC iPlayer will be sufficient to tip the balance in a household's decision on whether to subscribe to pay TV (or SVOD services).
- 7.20 We consider that households are likely to choose to buy subscription packages based on a wide set of factors e.g. including access to films, drama series, sport etc. This view is supported by Ofcom's 2013 pay TV research which asked consumers, "what were the reasons your household got a TV service that you pay for on your main set rather than having free TV channels only". In response to that question: 54% of adults spontaneously cited to get more channels in general; 12% to get more channels of a specific type; and 11% to get specific sports channels.¹⁶⁰ Only 6% of

¹⁵⁷ Kantar report, page 50.

¹⁵⁸ In paragraphs 7.41 to 7.42, we discuss the proposal to provide third-party selected content on BBC iPlayer. In that paragraph, we note that there is very little information in the BBC's service proposals to form a clear view on the range of third-party content that might be included on BBC iPlayer. However, based on CC's view that content might be of niche interest only we would not anticipate that the additional content would result in households altering their subscription decisions.

¹⁵⁹ The BBC has stated its intention that BBC Three long form programmes will (at least initially) also be shown on BBC One and BBC Two. See BBC Service Proposals document page 31.

¹⁶⁰ See <http://stakeholders.ofcom.org.uk/binaries/research/tv-research/tv-data/pay-tv-research/Pay-TV-omnibus-2013-data-tables.pdf>, page 538.

adults spontaneously cited to get children’s specific channels, a further 5% cited children’s channels when prompted.¹⁶¹ When asked the top three reasons for having a pay TV service, 49% of adults mentioned to get more channels in general while 6% of adults mentioned to get children’s specific channels.¹⁶²

- 7.21 In addition, our view is consistent with the Mediatique report which looked at the implications of extending the BBC iPlayer catch-up window from 7 to 30 days. Extending the BBC iPlayer window and increasing the number of BBC iPlayer premieres share some similarities in that both essentially increase the amount of content available on BBC iPlayer. In relation to the impact of extending the BBC iPlayer catch-up window from 7 to 30 days on pay TV subscriptions, Mediatique noted:

“We do not believe that the extension of the iPlayer window to 30 days will cause pay TV subscribers to cancel their underlying pay-TV bundles. Indeed the decision to subscribe to pay-TV is driven by a portfolio of services including access to more channels, premium content (spots and movies) and enablement (HD, on-demand capability, PVRs) – of which the BBC’s windowing changes are likely to be a secondary driver of decision making.”¹⁶³

- 7.22 In the rest of this sub-section we therefore focus on the impact on commercial free-to-air broadcasters.

CC model – Overview

- 7.23 To model the impact of this proposal CC estimated the additional number of BBC iPlayer requests that premiering will generate, and converted this into an impact on viewing hours. To do this CC used a ‘premiere uplift’ factor to inflate a base number of requests (absent premiering) for each premiered episode. In modelling this impact, CC assumed:

7.23.1 25 titles are premiered annually, with 10 episodes per title;

7.23.2 The base number of requests for each episode (absent premiering) is 100,000; and

7.23.3 Premiering results in an uplift of 153% to base requests.

- 7.24 CC assumed that increased premiering does not increase the total amount of viewing, therefore the increase in BBC iPlayer viewing due to more premiering results in a commensurate reduction in on-demand viewing for commercial channels. CC assumed the reduction in viewing hours was distributed among the commercial channels in proportion to their on-demand viewing share.¹⁶⁴

- 7.25 The other proposed BBC iPlayer enhancement is the inclusion of third party content. CC did not attempt to quantify the impact on third party content, noting that the impact on viewing is likely to be minimal because the content is of niche interest and likely to be available elsewhere.

¹⁶¹ *ibid*, page 599.

¹⁶² *ibid*, page 660.

¹⁶³ Mediatique report, page 19.

¹⁶⁴ The viewing share for non-BBC VOD providers is forecast using data from Mediatique.

Our assessment of the CC model

7.26 In this sub-section we discuss each assumption and any adjustments to the CC model that we consider appropriate.

Number of titles and episodes per title

7.27 These assumptions reflect the BBC's stated intention so are reasonable base case assumptions.

Base requests of 100,000 per episode (in the absence of premiering)

7.28 According to CC, the strongest performing CBBC episodes receive 100,000 to 500,000 BBC iPlayer requests, and those from CBeebies receive 60,000 to 260,000. In explaining its base assumption of 100,000 requests per episode, CC note that these figures already reflect some benefits from premiering, and that premiering would not be exclusively focused on the highest profile content.¹⁶⁵

7.29 We have clarified with the BBC that the CC assessment was based on BBC iPlayer requests for children's titles during April 2014. We have identified the following issues with the information used to inform CC's base request assumption:

- The information was collected prior to the extension of the BBC iPlayer catch-up window from 7 to 30 days, therefore it might not be an accurate reflection of the number of requests an episode would receive with the current longer catch-up window;
- The information was collected over a calendar month, so episodes aired within a week of end of the month would not have had their full catch-up window; and
- Only collecting information over one month means the assessment rests on a relatively small sample.

7.30 In light of these concerns, we have sought to update the CC assumption relating to the base number of BBC iPlayer requests used in its calculations.

7.31 We collected additional information from the BBC regarding the number of BBC iPlayer requests within the 30 day catch-up window for each CBBC and CBeebies episode aired for the first time¹⁶⁶ over the period 6 October 2014 to 25 January 2015.¹⁶⁷

7.32 We received information relating to 891 episodes and found that the number of requests varied considerably from 234 to 1,286,119. The average number of requests per episode was 58,366.

7.33 We recognised that a number of these titles (in particular the less popular ones) are unlikely to be premiered on BBC iPlayer. Therefore, in order to focus the analysis we looked at the subset of episodes from titles mentioned in the BBC service proposal

¹⁶⁵ CC report, page 44 footnote 96.

¹⁶⁶ We only requested information for episodes aired for the first time because, by definition, a programme can only be premiered before it is first aired. Repeated episodes are likely to gain relatively fewer BBC iPlayer requests.

¹⁶⁷ This period was selected because the BBC iPlayer window was extended to 30 days on 6 October 2014.

as ones it would consider premiering. This included the BBC programmes: *Wolfblood*, *Millie In Between*, *Woolly and Tig*, *Bing* and *Swashbuckle*. In total there were 49 episodes from these titles. For these episodes the number of requests on BBC iPlayer varied from 52,746 to 435,007 with an average number of requests of 214,922 per episode.

- 7.34 We consider that the average number of requests using our updated sample represents a more accurate estimate of the base number of requests for children's programmes that are likely to be premiered.
- 7.35 We recognise that the BBC has also requested permission to premiere a small number (probably five) programmes per year across BBC One, Two and Four. The BBC has not provided any guidance on the titles it would be likely to premiere. Furthermore, there is a huge number of BBC One, Two and Four programmes and the information that we have gathered indicates that there is a large range in the number of BBC iPlayer requests between different programmes. For these reasons, we have not attempted to separately estimate the base number of requests for BBC One, BBC Two and BBC Four programmes.
- 7.36 Given that the majority of premiered programmes (110 hours out of a total of 135 to 160 hours) are proposed to be children's we have adopted a base request assumption of 200,000 (that accords with the average number of BBC iPlayer requests from the information we have collected described above). We find that using our revised base request assumption increases the BBC's viewing share by 0.1 percentage point in 2018 compared to the CC assumption of 100,000 BBC iPlayer requests.
- 7.37 Notwithstanding the change we have made to the base number of BBC iPlayer requests, we recognise that there remains a significant level of uncertainty around this assumption. In our sensitivity analysis below, we have considered a higher assumption of 400,000 BBC iPlayer requests (double our base case assumption).

Premiering uplift

- 7.38 To calculate the 'premiere uplift' factor, CC compared the online viewing of a sample of four programme titles across two series. In the first series each programme title was not premiered online whereas in the later series each programme title was premiered online. Based on this information CC found that the online viewing of the later series was between 2.3 to 5 times higher than the first series.
- 7.39 CC considered that part of the increase in viewing of the second series could be explained by the general growth in BBC iPlayer viewing. Therefore, in its analysis, it removed the impact of general BBC iPlayer growth and found that the viewing of the later series in its sample was between 1.8 to 3.8 times higher than the first series. Based on this information CC took a simple average of 2.5 which was converted into an uplift factor of 153% that was applied to the base number of BBC iPlayer requests to estimate the impact of premiering online.
- 7.40 We note that CC's analysis is based on a small sample of programmes. However, in the absence of better information, we have retained CC's premiering uplift assumption, though to account for the degree of uncertainty we have rounded it to 150%. In our sensitivity analysis below we have considered a higher premiering uplift factor of 300% (double our base case assumption).

Inclusion of third party content

- 7.41 CC considered the proposed inclusion of selected third-party content on BBC iPlayer to be of niche interest and to be unlikely to have a significant impact on overall viewing hours.
- 7.42 We would expect the inclusion of third party content to have a negative impact on commercial broadcasters, to the extent that it diverts viewing hours from them. However, although programmes from S4C, the Welsh language public television service, have been available on BBC iPlayer on an experimental basis since November 2014, evidence to assess the impact of the proposal is limited. Furthermore, there is very little information in the BBC's service proposals to form a clear view on the range of third-party content that might be included on BBC iPlayer. Therefore it is very difficult to assess the extent to which it will attract additional viewing hours to the BBC. In light of this, and also acknowledging CC's view that content might be of niche interest only, we have not quantified the impact of this proposal.

The enhancements do not result in any incremental growth in viewing

- 7.43 CC assumed that the proposed premiering on BBC iPlayer does not increase the total amount of viewing. Therefore, the increase in BBC iPlayer viewing due to premiering online results in a commensurate reduction in on-demand viewing for commercial channels.
- 7.44 We can envisage examples where online premiering, even with a relatively small amount of content, could result in incremental viewing (e.g. the opening ceremony of the Olympics). However, given the relatively small amount of additional content on BBC iPlayer as a result of these proposals, we consider that CC's approach is a pragmatic simplification to the modelling.

Viewing hours are gained by the BBC from commercial channels in proportion to their on-demand viewing share

- 7.45 CC has assumed that the gain in BBC on-demand viewing hours due to the proposed BBC iPlayer enhancements is at the expense of on-demand viewing of commercial broadcasters. Specifically, CC has apportioned the viewing hours gained by the BBC across the commercial channels in proportion to their current share of on-demand viewing.
- 7.46 We consider that CC's assumption could miss some more granular effects. More specifically, we know that the premiered programmes will ultimately be shown on linear TV. Therefore, it is possible that some people will watch the online premiere in place of the live linear viewing (e.g. because the premiere is available earlier or because the linear scheduling is less convenient).¹⁶⁸
- 7.47 Therefore, it is possible that some of the incremental BBC iPlayer viewing could be in place of live linear BBC viewing. This substitution is not captured in the CC model.

¹⁶⁸ In highlighting this possibility, we note the findings of CC's quantitative research (page 5). When asked about how the BBC iPlayer proposals would affect their viewing patterns 14% said that their total viewing of linear broadcast channels would decrease and one in ten said that their overall viewing of online and VOD would increase. One fifth of respondents predicted an increase in their use of BBC iPlayer, however, this was not thought to be at the expense of other VOD services, nor was it thought to cause a decline in viewing to the PSB commercial broadcasters.

Effectively this means the impact on commercial channels may be overstated because CC assumes that all incremental BBC iPlayer viewing is at the expense of commercial viewing, when, in fact, some may be at the expense of BBC live linear viewing.¹⁶⁹

- 7.48 In addition, we note that 20 of the 25 titles that the BBC plans to premiere are children's programmes. The BBC's service proposal notes that the children's premieres are expected to total 110 hours of online content per year, while the BBC One, BBC Two and BBC Four premieres are expected to total 25 to 50 hours of online content per year.
- 7.49 Given the skew of online premiering towards children's programmes, we consider that the proposals could have a greater impact on commercial channels focussed on children's programming. However, the impact on any given channel is likely to be small because of the following reasons:
- 7.49.1 the relatively small overall increase in children's content i.e. 110 hours of children's premieres per year;¹⁷⁰
 - 7.49.2 the impact of any additional BBC viewing is also likely to be spread (to some extent) across other commercial channels that are not focussed on children's programming; and
 - 7.49.3 the potential mitigating impact from the increase in BBC iPlayer viewing being partly at the expense of BBC live linear viewing.
- 7.50 In light of this we do not consider that the likely impact is sufficient to alter CC's assumption in our base case.

Impact on viewing hours and viewing share

- 7.51 In Figure 7.1 below we show the impact of BBC iPlayer premieres on viewing hours and viewing share for the BBC and the main commercial providers in 2018. The results are on the basis that only the BBC iPlayer premiere changes are implemented. The cumulative impact of the proposals is discussed in Section 11.

¹⁶⁹ In our modelling, the distinction between live linear and on-demand viewing for commercial channels is less important, because ultimately the two are aggregated to estimate the overall impact on viewing hours i.e. whether the reduction in viewing hours is due to less on-demand viewing or less live linear viewing has a similar overall impact in the model.

¹⁷⁰ To put this in context, the 2014 CMR (figure 2.52) reported that in 2013 there was a total of 2,786 broadcast hours of first-run children's programming across all channels (and 136,296 broadcast hours of all children's programming across all channels).

Figure 7.1: Impact on viewing from BBC iPlayer premieres in 2018

Channel family	Share of total viewing counterfactual	Change in viewing after BBC iPlayer premieres (hours bn)	Change in viewing share (percentage points)	Share of total viewing post BBC iPlayer enhancement	Percentage change in viewing share
BBC	34.4%	+0.21	+0.24 p.p.	34.6%	+0.7%
ITV	20.6%	-0.05	-0.06 p.p.	20.5%	-0.3%
Channel 4	11.4%	-0.05	-0.05 p.p.	11.3%	-0.5%
Channel 5	5.9%	-0.02	-0.02 p.p.	5.9%	-0.4%
Other	27.8%	-0.09	-0.11 p.p.	27.7%	-0.4%
Total	100.0%	0.00	0.00 p.p.	100.0%	-

Impact on producer surplus

7.52 Figure 7.2 shows our estimates of the financial impact on the main commercial broadcasters in the base case (using the methodology we describe in Section 3). The results show the impact of the BBC iPlayer changes alone (i.e. in the absence of the other proposals being implemented). The cumulative impact of all the proposed changes is discussed in Section 11.

Figure 7.2: Impact on producer surplus from proposed change to BBC iPlayer in 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	-0.3%	1,710	-1.7	-2.5	-3.3
Channel 4	-0.5%	813	-1.3	-1.9	-2.5
Channel 5	-0.4%	358	-0.5	-0.7	-0.9
Other	-0.4%	999	-1.3	-1.9	-2.5
Total	-0.4%	3,881	-4.7	-7.0	-9.3

7.53 As described above, these financial impacts are based on assuming that the gain in BBC on-demand viewing is at the expense of on-demand viewing of commercial broadcasters, with the adjustment being made in proportion to the broadcasts' current share of on-demand viewing. Given the skew of online premiering towards children's programmes, the estimates shown in Figure 7.2 may somewhat understate the impact on channel families that have a higher share of children's viewing than average, and overstate the impact on channel families with a lower share of children's viewing on average.

Sensitivity analysis

7.54 As discussed above, there is a significant degree of uncertainty regarding some of the modelling assumptions. Therefore, we have tested the impact of a scenario where assumptions are set so the impact on commercial broadcasters is greater. The assumptions used in this scenario are as follows:

- 7.54.1 The base number of requests for BBC iPlayer premieres is set at 400,000 (double our base case assumption)
- 7.54.2 The premiering uplift factor is set at 300% (double our base case assumption).
- 7.55 Flexing these assumptions simultaneously (and maintaining all other base case assumptions) results in an incremental increase in BBC iPlayer viewing of 843 million hours in 2018 (compared to 211 million hours in the base case). This increases the BBC's viewing share by 0.7 percentage points relative to the base case (and 1.0 percentage points relative to the counterfactual), resulting in a BBC viewing share of 35.3%. This would result in commercial broadcasters' advertising revenue falling by around £18.6-37.2m, compared to the counterfactual. In the larger-impact scenario we have considered in our sensitivity analysis in Section 11, for the service proposals as a whole, we have lowered the base number of requests for BBC iPlayer premieres to make it less extreme than in this sensitivity, in order to make the combined scenario more plausible (see paragraph 11.22 for more details).

Dynamic impacts

Changing perceptions and use of BBC iPlayer

- 7.56 The BBC iPlayer is currently the most popular VOD service in the UK – in Q1 2014 38% of adults claimed to use BBC iPlayer, the next most used services was ITV Player with 22% claimed use.¹⁷¹ We expect VOD viewing to increase over time.
- 7.57 As discussed at paragraph 6.65, currently VOD services are mainly used to catch-up on missed programmes or watch programmes at a convenient time (as opposed to browse for content). In addition, the Kantar qualitative research found this to be the case in relation to BBC iPlayer specifically.¹⁷²
- 7.58 However, on-demand is growing as an alternative place to also discover content and there are a number of factors that could change the perceptions of BBC iPlayer from a place to catch-up on content to one where content is discovered. In addition, the following developments could also help to drive changing perceptions of on-demand and increase the prominence of BBC iPlayer in the longer term:
- Growth in smart TV take-up - Increased take up of smart TVs (which can enhance the viewing experience by allowing people to watch VOD services through the TV rather than through a computer or other device) may provide a boost to VOD services such as BBC iPlayer. Smart TV take-up remains relatively low in absolute terms at 12% of households in 2014, but take-up has increased significantly since 2013 (when take-up was just 7% of households).¹⁷³ The share of smart TVs as a percentage of television sales has increased over time – reaching 45% Q1 2014 – which suggests that prevalence of smart TVs will increase going forward.¹⁷⁴

¹⁷¹ 2014 CMR, figure 2.19.

¹⁷² Kantar indicated that the majority of participants mainly used BBC iPlayer to watch programmes that they had missed rather than using the service to browse for content without a specific item in mind, Kantar report, page 24.

¹⁷³ 2014 CMR, figure 2.5.

¹⁷⁴ 2014 CMR, figure 2.6.

- Changes to the EPG or platform landing pages - Improving the interface between linear and on-demand platforms would make on-demand viewing more accessible and thereby could increase on-demand viewing. For example, device manufacturers and platform operators are increasingly looking to put in place home pages in front of linear EPG listings and other navigation sources, which could give greater prominence to on-demand services. In addition, better integration between on-demand and linear content within the EPG could make it easier and more convenient for an individual to switch between access routes when searching for content.^{175 176} This could contribute to a change in behaviour whereby viewers start to see on-demand as a place to discover content, rather than primarily as a catch-up service.

- 7.59 These factors, in addition to increased awareness of on-demand services, could lead to BBC iPlayer playing a more significant role in TV viewing over the longer term, beyond the period to 2018 which we considered in the static analysis. This may not be in itself a concern. For example, if viewers simply switch from viewing BBC live linear content to BBC content on the BBC iPlayer then we would not expect the impact on commercial providers in terms of total viewing hours or revenues to be significant. Furthermore, we also consider that the premiering proposals put forward by the BBC (i.e. to premiere 25 titles of which 20 are children's titles) will have a relatively low impact, even if BBC iPlayer popularity increases.
- 7.60 In addition, we note that the BBC has the potential to act as a catalyst for market development. For example, BBC iPlayer has helped build consumer interest and take-up of on-demand services, providing market opportunities for other providers to deliver new, innovative services beyond traditional TV.
- 7.61 However, as noted above, BBC iPlayer is the UK's most popular VOD service and we are aware that the BBC iPlayer has evolved considerably since its introduction in 2007 (as outlined in Figure 7.3).

¹⁷⁵ For example, the YouView and FreeSat "backwards EPGs" allow users to access the historic linear broadcast schedule with direct links to catch-up content where available.

¹⁷⁶ The Kantar report (page 31) found that when searching for a particular programme, most participants recognised the value of a linear schedule and EPGs in helping them navigate to the desired content.

Figure 7.3: Evolution of BBC iPlayer

Date	Description of change to BBC iPlayer
July 2007	<p>Launch of BBC iPlayer providing the following functionality:</p> <p>Seven day catch-up television over the internet (with a storage window for catch-up television over the internet of 30 days from the day of download).</p> <p>Seven day catch-up over cable.</p> <p>Simulcast television over the internet.</p> <p>Non-DRM¹⁷⁷ audio downloads over the internet with the exclusion of book readings and classical music (except insofar as it is used in contexts such as incidental music to programmes or as signature tunes).</p>
September 2008	<p>Introduction of 'series stacking' functionality which extended the availability of selected programmes from the standard seven days to the lifetime of a series while that series was on air.</p> <p>Series stacking was limited to an annual quota of 15% of all television content offered on demand on BBC iPlayer.</p>
February 2014	<p>Permission given to establish a link between BBC iPlayer and BBC Store, allowing the following changes to be made to BBC iPlayer:</p> <p>An extended search functionality that includes both publically and commercially available BBC content.</p> <p>The inclusion of links to BBC Store and other commercial outlets retailing BBC content.</p> <p>A seamless purchasing experience via pop-ups and a single BBC account registration.</p> <p>The ability to view programmes purchased from BBC Store via BBC iPlayer and playback this content using BBC iPlayer.</p>
October 2014	<p>Introduction of changes to BBC iPlayer television catch-up window. These entailed:</p> <p>An extended television and radio catch-up window to enable audiences to stream or download BBC programmes for 30 days after they have been broadcast, rather than seven days.</p> <p>The removal of series stacking for television (i.e. the ability to download retrospectively multiple episodes) – radio catch-up series stacking was unaffected.</p>
November 2014	<p>Launch of branded Radio 1 section within BBC iPlayer featuring a range of music related audio-visual content.</p> <p>S4C (the Welsh language public service channel) content available on BBC iPlayer on an experimental basis.</p>

7.62 In addition, the BBC has a range of services which it could use to enhance BBC iPlayer in the future e.g. TV and radio content in addition to a large archive.

¹⁷⁷ Digital Rights Management (DRM).

Commercial providers are unlikely to be able to offer such a depth and breadth of services on a single platform. Therefore, future changes to BBC iPlayer (e.g. expanding its scope) beyond those proposed, could raise concerns over the ability of commercial providers to compete and have a detrimental impact on competition in the longer-term.

- 7.63 Given these concerns, we consider that the Trust needs to set clear boundaries regarding what the BBC is permitted to do in relation to developing BBC iPlayer further. As part of this the Trust ought to give careful thought to when a future PVT is triggered.

Wider impacts

Impact on independent production companies

- 7.64 PACT has indicated that under the current Terms of Trade, the BBC is able to premiere a programme on BBC iPlayer up to seven days prior to its first linear broadcast. However, if the BBC wishes to premiere content on BBC iPlayer more than seven days before its linear broadcast, this would need to be directly negotiated between the BBC and the relevant independent producer.
- 7.65 We note that the BBC's service proposals indicate that the BBC would be unlikely to premiere more than seven days in advance.

Syndication issues

- 7.66 Virgin Media was concerned that the BBC was moving in a direction where BBC iPlayer would act as a gateway for all BBC content. Although viewers are able to access BBC iPlayer via the Virgin Media platform, Virgin Media was concerned that premiering online could have a significant financial impact on it if licence fee payers were unable to access BBC content through its platform.
- 7.67 In paragraphs 7.17 to 7.21 we assess the impact of the BBC's proposals to premiere programmes on BBC iPlayer on subscription services (including pay TV services). For the reasons outlined, we do not consider that the BBC's proposals will have a significant impact on subscription services.
- 7.68 However, we recognise that more significant moves to premiere on BBC iPlayer could have an impact on TV platforms. We discuss potential issues regarding the syndication of BBC content in relation to the proposals to reinvent BBC Three online, from paragraph 6.90 above. We consider that similar issues could arise with the BBC's proposals relating to BBC iPlayer.
- 7.69 We note the Trust is currently consulting on the BBC's future syndication policy and consider that particular attention should be given to how the BBC's online services fit within these to ensure that the commercial platforms are not unfairly disadvantaged when the BBC makes content available or is considering how to partner with commercial platforms.

Recommendations

Inclusion of selected third-party content on BBC iPlayer

- 7.70 The BBC is proposing to engage in partnerships with institutions that share its values to make available third-party commissions within BBC iPlayer.

- 7.71 In developing how content would be selected or integrated into BBC iPlayer the BBC has indicated that it would have regard to the following principles:¹⁷⁸
- third parties would be limited to not-for-profit cultural and arts organisations;
 - proposals would need to support the BBC’s public purposes; and
 - proposals would need to be consistent with and help to support the BBC’s strategic objectives.
- 7.72 In paragraph 7.42, we explained that, although we would expect the inclusion of third party content to have a negative impact on commercial broadcasters to the extent that it diverts viewing hours from them, there was very little information in the BBC’s service proposals to form a clear view on the range of third-party content that might be included on BBC iPlayer. In light of this, and also acknowledging CC’s view that content might be of niche interest only, we did not quantify the impact of this proposal.
- 7.73 Although we have not quantified the impact of the proposal, we are concerned that the criteria for selecting third-party partners are not specific enough and could result in third-party partners being unfairly excluded from including their content on BBC iPlayer.
- 7.74 BBC iPlayer is the most popular VOD service in the UK. Third-party partners that are able to provide content via BBC iPlayer will have potential access to a large number of viewers. This is likely to provide significant boost in viewers of that content and awareness of any other services provided by that third-party (e.g. non-broadcast cultural or arts services or events). Third-parties that are not able to provide content on BBC iPlayer are potentially at a disadvantage since they would not have access to viewers on the BBC iPlayer and therefore would not receive the boost in viewers and awareness of their services.
- 7.75 We recognise the potential consumer benefits that could result from the BBC iPlayer being used to host third-party content. However, recognising the prevalence of BBC iPlayer across devices and its popularity as a VOD service, we consider that the proposals need to be developed further, particularly around the criteria for selecting third-party partners, to ensure that these are clear, objective and do not result in prospective partners being unfairly excluded.

Threshold for future PVTs

- 7.76 Our assessment of the impacts is based on the proposals outlined by the BBC.
- 7.77 However, we are mindful of developments over the longer term. Therefore, we consider that the Trust should set clear boundaries on what the BBC is permitted to do (in line with current proposals) and at what stage further approval is required.
- 7.78 In the event that the BBC proposed to make further enhancements to the BBC iPlayer, such as, substantially increasing the number of premieres; altering the types of programmes premiered; or significantly altering the functionality of BBC iPlayer then this would represent a material change to the proposals that we have assessed

¹⁷⁸ Content would also be subject to the BBC’s internal regulatory scrutiny and need to comply with the BBC Fair Trading Guidelines and BBC Editorial Guidelines.

in this MIA. As such, the Trust would need to consider conducting a further PVT to assess the market impacts.

Syndication policy

- 7.79 Given the prevalence of BBC iPlayer the precise detail of how BBC content is syndicated on TV platforms (and other devices) is likely to become more important. For example, issues such as being able to navigate easily between BBC content and non-BBC content are likely to be of key importance to viewers and TV platform providers.
- 7.80 As noted above, that the Trust is currently consulting on the BBC's future syndication policy. We consider that particular attention should be given to how the BBC's online services fit within these to ensure that the commercial platforms are not unfairly disadvantaged when the BBC makes content available.

Cross promotion of BBC iPlayer

- 7.81 In this section we have identified the market impacts from the proposed changes to BBC iPlayer. However, the Trust should note that extensive cross-promotion by the BBC may increase these impacts. We encourage the Trust to consider the role of cross-promotion as part of its assessment.

Section 8

Increased investment in BBC One drama

Summary of proposal

- 8.1 As part of its Service Proposals the BBC has outlined its intention to reallocate £30m of the programme budget made available by the proposed closure of BBC Three as a broadcast TV channel to its BBC One drama budget. As outlined in Section 6, the proposed BBC Three Online service would operate with a budget smaller than that of the broadcast channel.
- 8.2 Although changes in investment are made at the discretion of the BBC, subject to oversight by the Trust, there is a dependency between the increase in drama investment on BBC One and the closure of BBC Three as a broadcast channel. Therefore, in agreement with the Trust and the Joint Steering Group, this is being considered as part of the PVT and hence the MIA.
- 8.3 The 2013 BBC One drama budget was [redacted].¹⁷⁹ A £30m increase would represent an increase of [redacted] on this overall amount. The overall programming budget for BBC One was £1,024m in 2012/13¹⁸⁰ therefore the additional drama budget would represent an increase of 3% on this amount.

Stakeholder responses

Impact on advertising revenues

- 8.4 ITV modelled the impact of increasing BBC One's drama budget. ITV estimated that increasing BBC One's drama budget [redacted].
- 8.5 ITV stressed what it considers to be [redacted].
- 8.6 ITV outlined the following trends [redacted]:
- A larger amount of drama in the BBC One schedule [redacted].¹⁸¹
 - [redacted]^{182 183}
 - [redacted]¹⁸⁴
 - [redacted]¹⁸⁵
- 8.7 ITV highlighted the risk that further investment in drama by the BBC would inflate the costs of producing drama.

¹⁷⁹ Based on broadcaster returns to Ofcom.

¹⁸⁰ BBC Annual Report 2013/14, page 66 http://downloads.bbc.co.uk/annualreport/pdf/2013-14/bbc_annualreport_201314.pdf

¹⁸¹ ITV response to MIA stakeholder questionnaire, page 16.

¹⁸² ITV response to MIA stakeholder questionnaire, page 3.

¹⁸³ ITV response to MIA stakeholder questionnaire, page 22.

¹⁸⁴ ITV response to MIA stakeholder questionnaire, page 23.

¹⁸⁵ ITV response to MIA stakeholder questionnaire, pages 24-25.

- 8.8 ITV said that as it becomes [3<].¹⁸⁶
- 8.9 Viacom¹⁸⁷ and ITV¹⁸⁸ drew a connection between the BBC's plans to increase the BBC One drama budget and the BBC One+1 proposal. Both argued that the drama budget uplift would increase the popularity of the BBC One+1 channel and would add further pressure to their respective schedules.¹⁸⁹

Impact on independent production companies

- 8.10 PACT welcomed the additional drama investment but noted that under the BBC's current arrangements for its Window on Creative Competition (WoCC), drama is already under strain. PACT stated that the 25% contestable portion of the drama budget was already allocated entirely to independent producers, so under the current arrangements, increasing the budget further would not benefit independent producers for one of two possible reasons. Either:
- The WoCC would be rebalanced by the BBC so as to account for a greater percentage of drama commissions under the WoCC, at the expense of other external commissions in different genres; or
 - The BBC would be required to spend all of the additional investment on in-house drama productions.¹⁹⁰
- 8.11 PACT noted if the BBC favours its own in-house production in relation to the increase in drama spend this would benefit BBC Worldwide through subsequent rights distribution, rather than any third party distribution companies.¹⁹¹

Impact on pay TV platforms

- 8.12 Virgin Media was supportive of the additional drama investment as it considered this would enhance the content on offer to its customers.

Identification of affected services

- 8.13 We have identified the following services that could potentially be affected as a result of the BBC increasing the BBC One drama budget:
- commercial broadcasters' (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
 - other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes; and
 - independent production companies as result of the increased budget available to drama producers.

¹⁸⁶ ITV response to MIA stakeholder questionnaire, page 25.

¹⁸⁷ Viacom response to MIA stakeholder questionnaire, page 2.

¹⁸⁸ ITV response to MIA stakeholder questionnaire, page 12.

¹⁸⁹ See Section 11 for further details on the interdependencies between these two proposals.

¹⁹⁰ PACT response to MIA stakeholder questionnaire, pages 16-17.

¹⁹¹ PACT response to MIA stakeholder questionnaire, pages 16-17.

Assessment of impacts

Static impacts

- 8.14 We have considered whether an increase to BBC One’s drama budget will have an impact on subscription services such as traditional pay TV (e.g. Sky, Virgin Media) or SVOD (e.g. Netflix, Amazon Prime). As noted above at paragraph 6.24, customers of pay TV services tend to purchase their subscriptions for a variety of reasons, led by the opportunity to get more channels in general. SVOD subscribers tend to be motivated by access to a back catalogue of TV and movie content, and the viewing flexibility that VOD services offer.¹⁹²
- 8.15 Given the free-to-air availability of the BBC One drama content, we consider that consumers are likely to view it as complementary to paid-for packages rather than as an alternative. This is consistent with the fact that no stakeholders indicated that pay TV or SVOD services would be negatively impacted by an increase to BBC One’s drama budget. Therefore, we consider that their decisions about pay TV or SVOD subscriptions are unlikely to be affected by changes to the BBC One drama budget.
- 8.16 We therefore focus below on the static impact on commercial broadcasters, in terms of viewing hours and advertising revenues.

CC model – Overview

- 8.17 CC considered the increase in BBC One’s drama budget to be part of the counterfactual case rather than a modelled proposal in its own right. This was because, as discussed above, budget changes are usually an operational matter outside the remit of the PVT process. CC noted that “While we understand this change does not require Trust approval, it nonetheless affects the baseline for analysis of the changes to services which are the focus of this PVT.”¹⁹³
- 8.18 CC modelled the impact of increasing BBC One’s drama budget by assuming a pro-rata increase in live linear/PVR viewing of BBC One in proportion to the increase in BBC One’s overall programming budget of £1,024m (in 2013). This resulted in an increase in BBC One’s share of live linear/PVR viewing from 21.0% to 21.7%. This additional viewing was drawn from other linear channels according to the viewing profile of “heavy” viewers of BBC One¹⁹⁴ since the viewing profile of these viewers (across channels) was assumed to better reflect where viewing would switch from compared to using the viewing profile of “all” BBC One viewers.
- 8.19 As with live linear/PVR viewing, CC modelled the impact of increasing BBC One’s drama budget on catch-up services by assuming that BBC One viewing on BBC iPlayer increases in proportion to the increase in BBC One’s total budget. Viewing was assumed to switch from non-BBC catch-up services in proportion to their share of non-BBC catch-up viewing.

¹⁹² Gfk SVOD Content Consumption study http://www.gfk.com/Documents/Press-Releases/2014/20140807_Subscription%20video%20on%20demand_US-UK.pdf

¹⁹³ CC report, page 20.

¹⁹⁴ “Heavy” viewers of BBC One were defined by Communications Chambers as those viewers who collectively accounted for approximately 90% of BBC One’s total viewing between July 2013 and June 2014.

Our assessment of the CC model

8.20 In this sub-section we discuss the CC assumptions and any adjustments we have made to these in our modelling.

Inclusion of increased drama budget in the counterfactual

8.21 CC included the uplift in BBC One's viewing from additional drama budget in the counterfactual. However, as discussed at paragraph 8.2 above, we have considered the changes as part of the proposals, and so have excluded from the counterfactual (which is discussed in Section 4).

Approach to quantifying impact of additional drama budget

8.22 CC's approach to modelling the impact implicitly assumes a linear relationship between programme spending and viewing share. We have examined the relationship between viewing share and the level of programme spending to test this assumption.

8.23 Drama is an expensive genre to produce. Drama accounted for around [X] of BBC One's budget¹⁹⁵ and was responsible for 11.8% of total viewing minutes by individuals aged 4+ in 2013.¹⁹⁶ This analysis suggests that UK drama performs [X] across all BBC One programmes in terms of viewing achieved per amount spent.

8.24 [X] However, we consider that viewing from individual drama programmes is uncertain and will depend on a variety of complex factors such as whether these programmes are 'hits' or not, and the scheduling decisions of competing channels. We therefore consider CC's approach represents a reasonable modelling simplification and have maintained it in our modelling.

8.25 We note that in its response to the MIA stakeholder questionnaire, ITV has taken a different approach to reallocating viewing. We disagree with some parts of the approach taken by ITV in its modelling¹⁹⁷ and believe that the CC approach (modified as explained above) provides a more satisfactory estimate of the impact on ITV's portfolio of channels.

8.26 Similar to the method discussed in paragraph 5.21 we have updated the viewing profile of "heavy" BBC One viewers to be based on the viewers that account for the top third of viewing of BBC One using BARB data for 2014. We believe that using the top third of viewing strikes a reasonable balance between capturing the skew in viewing habits of BBC One viewers without overstating it.

¹⁹⁵ The headline programming budget does not give a complete indication of the total amount of money spent on TV programmes. TV producers make use of other funding approaches, including third party co-productions and deficit financing, in order to increase the amount of money spent on the finished product and to help their own budgets go further. However we have not made further allowances for this additional funding on the assumption that the incremental drama budget will attract additional funding to the same extent as the existing drama budget, i.e. that the additional funding uplift is already factored in.

¹⁹⁶ Source: BARB, individuals 4+, 2013.

¹⁹⁷ For example, ITV has assumed that only its main channel will be impacted by the increase in BBC One's drama budget. While this may be the most-affected ITV channel, we do not believe that the impact on other channels should be ignored or accounted for by uplifting the impact on ITV's main channel.

8.27 CC's approach to redistributing viewing from catch-up services assumes that none of the incremental viewing of BBC One on BBC iPlayer comes from other BBC iPlayer viewing. This may overestimate the impact on commercial catch-up services although this will have a negligible effect on our estimates of the overall impact of the BBC's proposal to increase drama investment. Therefore, we consider that CC's approach represents a reasonable modelling simplification, and have maintained this assumption in our modelling.

Impact on viewing hours and viewing share

8.28 In Figure 8.1 below we show the impact of increasing BBC One's drama budget in terms of viewing hours and viewing share for the BBC and the main commercial broadcasters in 2018.

Figure 8.1: Net impact on viewing from increasing BBC One's drama budget, 2018

Channel family	Share of total viewing counterfactual	Change in viewing from increasing BBC One's drama budget (hours bn)	Change in viewing share (percentage points)	Share of total viewing after increasing BBC One's drama budget	Percentage change in viewing share
BBC	34.4%	+0.4	+0.5 p.p.	34.8%*	1.4%
ITV	20.6%	-0.2	-0.2 p.p.	20.4%	-0.9%
Channel 4	11.4%	-0.1	-0.1 p.p.	11.3%	-0.7%
Channel 5	5.9%	-0.0	-0.0 p.p.	5.8%*	-0.8%
Other	27.8%	-0.1	-0.2 p.p.	27.6%	-0.6%
Total	100.0%	0.0	0.0 p.p.	100.0%	-

*Note: The difference between outputs and the sum of counterfactual viewing share and change in viewing share values is due to rounding.

8.29 The modelled impact of increasing BBC One's drama budget results in the capture of around half a percentage point of viewing share by the BBC family of channels from the commercial channels, with the largest proportional impact on the ITV and Channel 5 families of channels.

Impact on producer surplus

8.30 Figure 8.2 shows our estimates of the financial impact on the main commercial broadcasters in the base case of the increased BBC One drama budget.

Figure 8.2: Net impact on producer surplus from increasing BBC One’s drama budget, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	-0.9%	1,710	-4.9	-7.3	-9.7
Channel 4	-0.7%	813	-1.8	-2.8	-3.7
Channel 5	-0.8%	358	-1.0	-1.4	-1.9
Other	-0.6%	999	-2.0	-3.0	-4.1
Total	-0.7%	3,881	-9.7	-14.5	-19.3

8.31 The ITV and Channel 5 channel families are likely to be impacted slightly more than other channel families as they account for a higher proportion of heavy BBC One viewers’ overall non-BBC viewing than their share of all non-BBC viewing. We would expect this viewing redistribution to focus around peak hours as this is often when drama is scheduled, and is strongly contested by major channels.

Dynamic impacts

Impact on TV advertising revenues and programme costs

- 8.32 The dynamic impact on advertising revenues of an increase to the BBC One drama budget will be affected by commercial broadcasters’ responses. For example an increase in BBC One’s drama budget may lead rival channels to respond by increasing their programming budgets or altering their schedules. If by increasing their programming budgets they reduce the viewing shift to the BBC, it would mitigate their lost advertising revenues, but their profits may still fall due to the increased programming costs.
- 8.33 If commercial channels increase their programming budgets to compete with the BBC, this will tend to benefit consumers, assuming the increased programme costs improved the quality of programming.
- 8.34 Alternatively, commercial broadcasters may respond to lower audiences by producing fewer programmes from genres which are expensive to produce, like drama (to reduce their costs), in order to maintain profitability. [3<]¹⁹⁸ This could have a negative impact on consumers if it reduces overall choice.
- 8.35 It is uncertain that broadcasters would cut their drama spend as a result of the increased drama spend by the BBC. For example we note that work conducted by Mediatique, commissioned by Ofcom for its third PSB Review, found that ITV and BBC One both seek to “keep up” with each other in terms of their content investments and that any increase in expenditure at one broadcaster will likely act as

¹⁹⁸ ITV response to MIA stakeholder questionnaire, page 1.

a catalyst for investment changes at the other.¹⁹⁹ Moreover, Mediatique found that in aggregate drama remains a profitable genre for ITV and is still effective at attracting large, commercially attractive audiences to the channel. The report also found a consistent view among ITV stakeholders that ITV's main channel would continue to schedule drama (across all sub-genre categories) even if the direct profitability became more challenged by the factors outlined above in paragraph 8.6. The underlying reasoning being that drama has strategic value to ITV, which would seek to maintain a benchmark against the BBC and Channel 4 – both of whom would continue to commission drama as part of their PSB remits.²⁰⁰

Wider impacts

Impact on independent production companies

- 8.36 Independent producers that specialise in drama content may benefit from the increase in BBC One's drama budget.
- 8.37 We do not agree with PACT that the current success of independent producers in competing for the contestable portion of the drama budget under the BBC's WoCC means that they will be unable to benefit from the increase in the BBC's drama budget. Although the WoCC may limit the opportunities for independent producers to benefit further, an overall increase in the BBC drama budget will still have benefits for independent producers that specialise in drama.²⁰¹

Impact on AV content publishers

- 8.38 We note PACT's comments that this proposal may also work to the benefit of BBC Worldwide because of subsequent secondary rights deals with the BBC. We note that BBC Worldwide has a 'first look' arrangement which gives it the opportunity to become the BBC's distributor and exploit secondary rights for BBC programmes before these rights are offered to the wider market.²⁰² This arrangement is governed by the BBC's Fair Trading guidelines.²⁰³
- 8.39 The 'first look' arrangement makes it possible for BBC Worldwide to benefit from the drama proposal in the event that BBC in-house production wins a greater volume of commissions, but does not guarantee it. As a result we have not made any assumptions about the destination of secondary rights stemming from the drama proposal. We have not attempted to value the potential secondary rights resulting from an increased drama budget – including DVD, SVOD, TVOD and electronic sell through rights – given the uncertain and varying value of individual drama titles.

¹⁹⁹ See 'PSB Review: Investment in TV genres' by Mediatique for Ofcom, 2014 page 33. http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb3/Investment_in_TV_Genres.pdf

²⁰⁰ See 'PSB Review: Investment in TV genres' by Mediatique for Ofcom, 2014 page 12.

²⁰¹ We acknowledge that the drama budget increase is a reallocation of the BBC's budget, so while it may potentially lead to benefits to independent drama producers, it has implicitly come at the expense of independent producers who were previously working with BBC Three's broadcast channel, across a range of genres. The impact of the proposal on these producers is noted above in paragraphs 6.80 to 6.89.

²⁰² If BBC Worldwide chooses to exercise this right then it must then pay market value.

²⁰³ See

<http://www.bbc.co.uk/corporate2/insidethebbc/howwework/policiesandguidelines/fairtrading.html>

Recommendations

- 8.40 While we note above that an increase in the drama budget for BBC One could have a negative impact on commercial broadcasters, the BBC is free to make decisions about its programme budget allocation within limits set out and overseen by the Trust. The proposed increase in the BBC One drama budget falls within these limits. We therefore have not considered possible modifications in response to the increase in BBC One's drama budget.

Section 9

Launch of BBC One+1 channel

Summary of proposal

- 9.1 The BBC is proposing to launch a BBC One+1 channel. This would be a pan-UK version of BBC One, time-shifted to have the same broadcast schedule one hour later than its parent channel. It would operate 24 hours a day, seven days a week, as BBC One currently does.
- 9.2 BBC One features regional opt-outs at certain times to include local variants of programmes. The most common regional opt-out is for regional news broadcasts. There would be no regional opt-outs on the proposed BBC One+1 and instead the channel would run the BBC News Channel as-live, at these times.
- 9.3 The proposed channel would be broadcast in standard definition (SD) only and would be available on all major broadcast TV platforms including Freeview, Sky, Virgin Media, Freesat and YouView. The BBC is proposing that in relation to the DTT platform the channel would be broadcast on the PSB-3 multiplex (“Mux B”). This multiplex uses MPEG 4 and DVB-T2 encoding technology which some DTT households, without HD compatible tuners, would be unable to view.²⁰⁴ Therefore, at launch, nearly a quarter of households will be unable to view BBC One+1.
- 9.4 The BBC has stated that it hopes to move the DTT broadcasts of the BBC One+1 channel to the PSB 1 multiplex (“Mux 1”) at a later point, which would allow this channel to be viewed by all DTT households. Although the BBC has indicated its intention to move the proposed BBC One+1 channel to Mux 1 in 2017, the implementation of this plan cannot be guaranteed.

Stakeholder responses

Impact on commercial broadcasters

- 9.5 Channel 4 was concerned that the proposed BBC One+1 channel was a means of growing the BBC’s viewing share at the expense of other broadcasters. Channel 4 argued that the channel would not deliver public value given the availability of repeat broadcasts and of the BBC iPlayer service.²⁰⁵
- 9.6 Channel 4’s analysis of the BBC proposals indicated that the BBC One+1 channel would reduce Channel 4 family share by an estimated [x%], depending on the EPG slot it is allocated. Its modelling assumed that BBC One+1 would capture at least the same proportion of total BBC portfolio viewing share as ITV+1 captures of the total ITV portfolio viewing share. In the case of achieving a higher slot on the Freeview EPG (slot 7, up from the number 23 slot assumed in CC’s base case) Channel 4 assumed that the new channel would capture almost twice this proportion of viewers. It assumed that viewing would be captured from other channels in proportion to the

²⁰⁴ Freeview employed MPEG 4 and DVB-T2 encoding in order to increase the efficiency of its spectrum usage. The change has made it possible to broadcast HD quality channels on DTT. It also makes it possible to broadcast more SD channels in a given amount of spectrum than Freeview’s original MPEG 2 and DVB-T standards.

²⁰⁵ Channel 4 response to MIA stakeholder questionnaire, page 2.

viewing habits of “heavy” BBC One viewers (although it did not define the exact measure of “heaviness” used).

- 9.7 Sky UK Limited (“Sky”) considered that the BBC had underestimated the impact that the launch of BBC One+1 would have on other broadcasters. Sky did not consider it credible that replacing BBC Three – a channel targeted at 16-34s with limited broadcast hours and total viewing of 1.5% – with a +1 channel for BBC One – the most popular channel in the UK – would effectively be viewing share neutral.²⁰⁶
- 9.8 Viacom estimated the impact of launching a BBC One+1 channel on its channel portfolio to be around -0.044 percentage points of viewing share. Its analysis assumed that the BBC One+1 channel would increase the BBC’s share of viewing by around 2.3% (0.5 percentage points) based on analysis of previous launches of terrestrial broadcaster +1 channels. It assumed that the increase in viewing of BBC would be captured from viewers switching from other channels in proportion to the non-BBC-One viewing of “heavy” BBC One viewers.²⁰⁷
- 9.9 ITV estimated that the proposed BBC One+1 [X].
- 9.10 Viacom²⁰⁸ and ITV²⁰⁹ also drew a connection between the BBC One+1 proposal and the BBC’s plans to increase the BBC One drama budget. Both argued that the drama budget uplift would increase the popularity of the BBC One+1 channel and would add further pressure to their respective schedules.²¹⁰
- 9.11 The Commercial Broadcasters Association (“COBA”) was concerned about the impact of the proposed BBC One+1 channel on commercial channels’ ability to schedule programmes as an alternative to the BBC News bulletin at 10pm. COBA argued that the proposed new channel would remove a commercial opportunity for channels trying to offer an alternative to audiences not interested in the news.²¹¹ Viacom raised the same concern.²¹²

Impact on pay TV platforms

- 9.12 Virgin Media questioned the value of BBC One+1 to its platform and its customers. Virgin Media stated that it offered various alternative means of watching recently broadcast content, including catch-up services, PVR facilities and its ‘backwards EPG’. It added that it views +1 channels as a poor substitute for catch-up content.
- 9.13 As a result, Virgin Media described the opportunity cost of it having to transmit the channel over its network, using up capacity it would otherwise choose to use differently, and without offering Virgin Media customers any additional benefits. Virgin Media observed that this situation affected its own platform because of the alternative

²⁰⁶ Sky response to MIA stakeholder questionnaire, pages 1-2.

²⁰⁷ Viacom defines “heavy” BBC One viewers as the top 25% of viewers by average time spent viewing the channel and the frequency of tuning in. It says that the audience defined by this measure accounts for 66% of BBC One’s total viewing.

²⁰⁸ Viacom response to MIA stakeholder questionnaire, page 2.

²⁰⁹ ITV response to MIA stakeholder questionnaire, page 12.

²¹⁰ See Section 11 for further details on the interdependencies between these two proposals.

²¹¹ COBA response to MIA stakeholder questionnaire, page 3.

²¹² Viacom response to MIA stakeholder questionnaire, page 2.

features it offers, but it may not be as true for other platforms which do not have access to this functionality.²¹³

- 9.14 Virgin Media argued that +1 channels should not qualify for prominence on the Virgin Media EPG.²¹⁴ Virgin Media explained that +1 channels only exist on its platform as part of wider commercial deals where the parent broadcasters are seeking to extend their live linear ratings to gain advertising share.²¹⁵

Impact on independent production companies

- 9.15 One stakeholder, [S<], observed that the proposed new channel could impact on the value of secondary content rights. It stated that, as a general rule, the more times a title is broadcast the more value is “used up”, so the addition of BBC One+1 could lead to product devaluing more quickly. It noted that content licence fees could be increased to mitigate this impact. It also said that it “[did] not necessarily anticipate a major impact even in the absence of increased fees given the ubiquitous nature of +1 channels and the value ascribed to them”.²¹⁶
- 9.16 PACT observed that under the existing Terms of Trade the BBC has the right to one free narrative repeat broadcast within seven days of the original transmission of a programme, with additional narrative repeats available for 2% of the cost of the primary rights licence fee. It explained that the BBC One+1 channel could constitute the included narrative repeat, meaning that further retransmissions, either on BBC One or another linear channel, would require additional licence fee payments.

Identification of affected services

- 9.17 We have identified the following services that could potentially be affected as a result of launching a BBC One+1 broadcast channel:
- commercial broadcasters’ (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
 - other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes; and
 - independent production companies.

Assessment of impacts

Static impacts

- 9.18 Virgin Media argued that the presence of a free-to-air +1 channel offers little additional value to Virgin Media customers given the functionality which is already included in its pay TV platform, e.g. VOD and PVR functions. We consider that while it is possible that the presence of BBC One+1 may give little additional benefit to Virgin Media customers, our 2013 pay TV research suggests that a significant motivator behind the purchase of pay TV is access to variety of channels (as

²¹³ Virgin Media response to MIA stakeholder questionnaire, pages 9-10.

²¹⁴ Virgin Media response to MIA stakeholder questionnaire, page 5.

²¹⁵ Virgin Media response to MIA stakeholder questionnaire, page 9.

²¹⁶ [S<].

discussed in paragraph 6.24). Therefore, we consider that the launch of BBC One+1 is not likely to have a material impact on broadcast pay TV subscriptions. In addition, we note that the widespread availability on pay TV platforms of +1 channels from several other broadcasters – including ITV+1 – has not had a noticeable impact on pay TV subscription rates. We therefore do not consider that the proposed BBC One+1 channel will have a material impact on SVOD subscriptions.

9.19 Therefore, in analysing the static impacts below, we focus on commercial broadcasters, in terms of viewing hours and advertising revenues.

CC model – Overview

9.20 To estimate the impact of launching a BBC One+1 channel, CC estimated the share of viewing that such a channel would capture and redistributed this viewing from other channels.

9.21 CC estimated BBC One+1’s potential share of viewing using regression analysis²¹⁷, based on the performance of other channels which have +1 channels. It limited this analysis to include only those channels it deemed of sufficient scale to allow for a meaningful comparison with BBC One+1. This limited the data set to eight channels and their +1 channels.

9.22 CC hypothesised that the two main factors which would determine the share of viewing of a +1 channel relative to its parent were:

- i. the gap between the parent channel and the +1 channel on the EPG (“EPG delta”) because of the general importance of EPG prominence; and
- ii. the scale of the parent channel (in terms of its viewing share).²¹⁸

9.23 Under the assumption that BBC One+1 would replace BBC Three in the same EPG position on all TV platforms with the exception of Freeview, where it would be positioned at slot 23, CC estimated that BBC One+1 would have a share of total viewing of 1.6% (in 2018).²¹⁹

9.24 As part of a sensitivity test, CC estimated the viewing share of BBC One+1 under a range of EPG slots. It found that the maximum impact would occur if the channel were to inherit the EPG slot vacated by BBC Three (in the event that the proposed closure of BBC Three as a broadcast channel is implemented). It also found that the lowest impact would occur when BBC One+1 was given the lowest available slot in the EPG (on Freeview) or in the Entertainment genre section on segregated EPG listings.

²¹⁷ Regression analysis is a statistical technique that estimates how one variable (the “dependent” or “explained” variable) responds to changes in more than one other variables (the “independent” or “explanatory” variables) based on a sample of observations for the variables in the regression equation. In its regression model, CC used the +1’s share of viewing as a proportion of the combined share of viewing of the +1 and main channel (described later as the “normalised” share of viewing) as its dependent variable, and the EPG delta and main channel’s viewing share as its independent variables.

²¹⁸ CC report, page 34.

²¹⁹ In deriving this estimate CC applied a “mux impact factor” which dampened the viewing share of BBC One+1 given that some households cannot receive broadcasts from HD muxes, on which the channel would initially launch. It assumed a transition from an HD mux to an SD mux in 2017, meaning that the new channel would be available to all households by the end of the modelled period.

- 9.25 CC recognised that a portion of BBC One+1 viewing would come from other BBC channels. Based on analysis of previous +1 channel launches, it assumed that 70% of the new viewing would be incremental to the parent channel's share, and 30% would be at the expense of the parent channel.²²⁰
- 9.26 The incremental viewing for BBC One+1 was captured from other channel families in two ways, for live linear/PVR and for catch-up.
- 9.26.1 Live linear/PVR viewing was captured from other channels based on the viewing profile of "heavy" BBC One viewers.²²¹ This included capturing viewing from other BBC linear channels (apart from BBC One which is described in paragraph 9.25). Therefore, the net incremental gain in share of viewing for the BBC is smaller than 70%, as the +1 not only draws share from the parent channel but also other BBC channels.
- 9.26.2 Catch-up viewing was drawn from catch-up services based on their share of catch-up viewing. The split of how much viewing would be captured from linear channels compared to catch-up services was calculated in proportion to the ratio of each of live linear, PVR and catch-up services to total viewing.
- 9.27 CC estimated the net impact of launching a BBC One+1 channel on the BBC family share of viewing to be +0.8 percentage points.
- 9.28 CC also provided a cross-check of its approach to modelling BBC One+1's share of viewing to check how reasonable the calculated outputs were. It assumed that BBC One+1's closest comparator channel would be ITV+1. It took ITV+1's share of viewing and uplifted it to account for the larger main channel share of BBC One (by +48% based on 2013 viewing shares) and for the higher prominence that BBC One+1 is expected to achieve relative to its main channel, compared to the ITV main channel (by +25%²²²). This results in an estimated BBC One+1 share of around 1.6%, which is consistent with CC's more detailed calculation described above.

Our assessment of the CC model

- 9.29 In this sub-section we discuss CC's approach to the modelling and adjustments we have made to this.

Regression analysis – input data

- 9.30 We recognise the data limitations faced by CC. In particular, the number of available channels with a +1 variant that might provide meaningful data to estimate the impact

²²⁰ Different +1 launches seem to have had different rates of cannibalisation (from around 10% to around 60% cannibalisation depending on the channel and platform). The average was around 30%. Source: BARB, CC analysis. See CC report, page 37.

²²¹ As before, "heavy" viewers of BBC One were defined by Communications Chambers as those viewers who collectively accounted for approximately 90% of BBC One's total viewing between July 2013 and June 2014.

²²² Based on analysis of EPG prominence on audience impact by FEH Media Insight, available here: <http://stakeholders.ofcom.org.uk/consultations/c3-c5-finance/analysis/>

of a proposed BBC One+1 channel is limited. Therefore, we consider that the eight channels used in CC's regression analysis are reasonable.²²³

- 9.31 The input data, relating to the EPG delta and viewing share, that CC used in its analysis was weighted across the three major TV platforms (Freeview, Sky and Virgin Media). We consider that this averaging reduces the clarity of the data, as different channels will occupy different slots on each platform's EPG and will achieve different viewing shares based on the EPG slot and other factors.
- 9.32 Therefore, we have gathered input data for each channel on each of the three major platforms separately. This provides further observations to improve the robustness of the analysis. In particular, this allows us to separate out the various EPG deltas of a given channel on each of the platforms.
- 9.33 We also gathered input data for each of 2011, 2012 and 2013. However, we found that the data tends to be similar across these years, since viewing shares did not change radically across years and channel movements within the EPG were not common for the eight channels included in the data set. Therefore, the additional years of data were not used in estimating an equation between viewing share and the explanatory variables (such as the EPG delta), but were instead used to test the performance of the estimated equations by means of out-of-sample prediction.²²⁴

Regression analysis – Our approach

- 9.34 In forecasting potential BBC One+1 viewing, we focussed our analysis on two approaches which produced reasonably satisfactory regression equations, including in-sample and out-of-sample estimation. Each uses a form of the +1 share of viewing as the dependent variable; one – approach A – is normalised using the main channel share of viewing and the other – approach B – is not.²²⁵
- 9.35 Approach A (which uses the normalised +1 share of viewing as the dependent variable) predicts a higher share of viewing for BBC One+1 than approach B, and its output is close to CC's cross-check (explained in paragraph 9.28), estimating between 1.5% and 1.8% based on the mux the channel is broadcast on, compared to the 1.6% result of the cross check. Approach B (which simply uses the +1 share of viewing as the dependent variable) forecasts a +1 share of viewing considerably lower than CC's cross-check (1.0% to 1.1% share of viewing depending on mux, compared to the 1.6% result of the cross-check).
- 9.36 Approach A uses the EPG delta, the demographic skew of the channel towards adults aged 16-34²²⁶ and a PSB dummy variable²²⁷ as independent variables.

²²³ These channels are ITV, ITV2, ITV3, ITV4, Channel 4, E4, Channel 5 and Dave, along with their respective +1 channels

²²⁴ For example, out of sample predictions were performed by using the estimated equation (i.e. based on observations in a given year) to forecast +1 viewing share in other years. These forecasts were compared with the actual +1 viewing share to evaluate out of sample prediction

²²⁵ By "normalised" we mean that the +1 channel is scaled to the parent and +1 combined share of viewing. For example, if a parent channel had 9% share of viewing and its +1 had 1% share of viewing, this would imply a normalised +1 share of viewing of 10%. [= 1% / (9% + 1%)]

²²⁶ The demographic skew of the channel has been quantified as the proportional difference between the share of viewing of the channel among 16-34s compared with the share of viewing of the channel among all individuals. For example, if a channel had 20% SOV among 16-34s and 10% SOV among all individuals, it would have a skew of +100% [= (20% / 10%) – 1]

Approach B, uses the EPG delta, the main channel's share of viewing and a PSB dummy variable as independent variables.²²⁸

- 9.37 These independent variables are the main factors we believe influence the +1 share of viewing, for the following reasons:
- The EPG delta is an important determinant of a +1 channel's share of viewing because it affects its discoverability. This has been borne out in the analysis we have performed.
 - Channels with a skew towards young adults are likely to have better-performing +1 channels as younger audiences seem more likely to make use of +1 channels. We assessed three such variables – the skew towards children, adults aged 16-34 and adults aged 35+. We only want to include one such variable to avoid “over-fitting” the regression equation and due to strong correlation (i.e. collinearity) between each of these variables.²²⁹
 - The PSB dummy variable has been included to capture differences between PSB channels and non-PSB channels. One source of difference, for example, is that PSB channels tend to broadcast more high-end UK drama programming and are subject to a number of quotas and restrictions on output which non-PSB channels are not.
 - The main channel's share of viewing is likely to determine to some degree the share of viewing of its +1 channel. We have therefore included it either as an independent variable (approach B) or accounted for it in normalising the +1 share of viewing (approach A).
- 9.38 We have not found strong reasons to prefer one regression equation over the other; not least since the available data limits how precisely we are able to distinguish between them. We have therefore decided to use the two approaches to bound a reasonable range of estimates for the BBC One+1 share of viewing (between 1.0% and 1.5%) and in our base case, we have assumed BBC One+1's share to be the mid-point between the estimates produced by the two approaches (i.e. 1.2%).
- 9.39 We note that the BBC was unable to confirm which EPG slots the channel would have at the time it submitted its service proposal. This was still the case at the time of

²²⁷ A “dummy variable” allows the regression analysis (which can only use numerical data) to account for non-numerical factors, by converting them into numerical form. In this case, PSB channels have a “PSB dummy” value of 1, while non-PSB channels have a “PSB dummy” value of 0.

²²⁸ We have not included the demographic skew of the channel towards 16-34s in Approach B to avoid “over-fitting” the regression model. Over-fitting is the problem of over-explaining the random error in a dataset, usually by including too many independent variables. An over-fitted model becomes very good at explaining the sample data on which it is based, but is vulnerable to being unreliable at forecasting beyond the sample. With a relatively low number of observations (as is the case here), it becomes particularly important to avoid over-fitting.

²²⁹ The reason for wishing to avoid “over-fitting” was explained in the preceding footnote. “Collinearity” is the problem of having two (or more) independent variables that are very closely correlated with one another. For example, a channel which has higher viewing among 16-34s than it has among all its viewers *must* have lower viewing among non-16-34s than among all its viewers; alternatively, a channel cannot be skewed towards all demographics equally (as then it would not be skewed at all). While collinearity does not necessarily undermine the predictive power of the set of independent variables, it does reduce our ability to infer the extent to which a given independent variable affects the dependent variable.

conducting our analysis because negotiations remain ongoing. As a result, we have used the same assumptions for channel numbers as CC used in its modelling, i.e. the proposed BBC One+1 channel would take BBC Three's channel slot on the Sky and Virgin Media platforms (channel numbers 115 and 106 respectively) and would become channel number 23 on Freeview (after moving the Welsh and Scottish Local TV services from this position).

- 9.40 Ofcom is not in a position to comment on the likelihood of any particular outcome with respect to channel numbers/EPG positions for the proposed BBC One+1 channel. This is decided by the relevant platform provider subject to the EPG code of practice. We note that Sky alluded to the prospect of BBC One+1 taking BBC Three's EPG slots on its platform in its response, but also note that negotiations are still ongoing.²³⁰

Mux impact factor

- 9.41 The proposed BBC One+1 channel would be available on all major TV platforms: Sky, Virgin Media and Freeview (and including hybrid IPTV platforms which use Freeview alongside IP-based distribution, e.g. YouView).
- 9.42 However, as noted above, the BBC One+1 channel will only be available to a subset of Freeview homes because of the decision to broadcast it on the PSB-3 multiplex ("Mux B"). This multiplex uses DVB-T2 encoding technology. DVB-T2 is currently used to broadcast HD quality channels on Freeview and can be used only on TVs and set top boxes (STBs) that are Freeview HD-compatible. Most new reception devices are DVB-T2-compatible but there is a large installed base of TVs and STBs which are not.
- 9.43 Our most recent estimates indicate that in 2018 30% of Freeview homes will not be able to receive the proposed BBC One+1 channel, which we estimate would account for around 16% of all BBC One viewing.²³¹
- 9.44 The BBC's proposal includes a plan to migrate BBC One+1 to a DVB-T DTT multiplex, PSB-1 ("Mux 1") in 2017. This multiplex is receivable by all DTT homes and has 98.5% UK household coverage. The BBC suggested that the move from the PSB-3 DVB-T2 multiplex to the DVB-T multiplex, PSB-1, could be possible due to future encoding efficiencies. However, we note the lack of firm details linked to this plan and consider it to be an aspiration at this stage. In light of the uncertainty about the implementation of the BBC's plans, we have not included the migration from the PSB-3 DVB-T2 multiplex to the DVB-T multiplex in our base case assumptions.
- 9.45 We have estimated the viewing share of BBC One+1 using BBC One's viewing share in 2014. In 2014 BBC One's share of viewing increased by around 0.7 percentage points compared to 2013. In our base case, we estimate that BBC One+1 channel will have a share of total viewing of around 1.2% in 2018.
- 9.46 By way of comparison, if we were to assume that the BBC's planned migration of BBC One+1 from the PSB-3 DVB-T2 multiplex to the DVB-T multiplex was implemented in 2017, BBC One+1 is estimated to have a share of total viewing of

²³⁰ Sky response to MIA stakeholder questionnaire, page 2.

²³¹ This is based on a forecast from 3 Reasons regarding the take-up of DVB-T2-enabled Freeview receivers over the modelling period. We have combined this with the proportion of viewing of BBC One which comes from Freeview boxes to assess the proportion of BBC One viewing accounted for by viewers who will not be able to receive the BBC One+1 channel.

1.5% in 2018. This would increase the market impact of the proposal because the channel would become available to 100% of TV households.

Incremental viewing

- 9.47 We agree with the approach taken by CC with regard to the proportion of viewing of BBC One+1 channel which is likely to come from BBC One. We have therefore kept this assumption in the model, and assume that 70% of viewing will be incremental to the main channel's share. Of the 1.2% share of viewing we forecast BBC One+1 to have, 0.9 percentage points will be incremental to BBC One and 0.4 percentage points will come from BBC One.

Redistribution of viewing

- 9.48 Rather than adopt the 90% share of viewing approach used in the CC model (explained in paragraph 5.16.3), we have decided to update the viewing share assumption of BBC One "heavy" viewers to be based on BARB data for 2014. Similarly to the method discussed in paragraph 5.21 we have taken the viewing habits of those viewers which account for the top third of viewing hours to BBC One in 2014. We believe that using the top third of viewing strikes a reasonable balance between capturing the skew in viewing habits of BBC One viewers without overstating it.
- 9.49 Other than this change, we have approached redistribution in the same way as CC did in its original model. This means that some viewing will come from other BBC channels. Of the 1.2% share of viewing we forecast for BBC One+1, we forecast 0.4 percentage points will come from the parent BBC One channel (as discussed above), 0.5 percentage points will come from other BBC channels, and 0.5 percentage points will be incremental to the BBC channel family.

Stakeholder approaches to modelling the impact of BBC One+1

- 9.50 ITV, Channel 4 and Viacom have each conducted their own analysis of the impact of launching a BBC One+1 channel. Each has taken a different approach and we have used their analyses as a cross-check of our own modelling approach.
- 9.51 We note that in its response to the MIA stakeholder questionnaire, ITV has taken a different approach to reallocating viewing. We disagree with some parts of the general approach taken by ITV in its modelling²³² and believe that the CC approach (modified as explained above) provides a more satisfactory estimate of the impact on ITV's portfolio of channels.
- 9.52 Channel 4's analysis is similar to our own, though it is a more simplified approach. Our results are reasonably consistent with Channel 4's when using similar input assumptions, though our approach accounts for a number of details that Channel 4's does not.²³³
- 9.53 Viacom's analysis is also similar to our own, though it uses a different metric of "heavy" BBC One viewers to that in our analysis. Its analysis predicts a lower impact

²³² See paragraph 8.25, footnote 197 above.

²³³ For example, Channel 4 assumes that BBC One+1 will gain 6% of BBC One's total viewing if it is broadcast on Freeview slot 26, and 10% if broadcast on Freeview slot 7. In our analysis we have looked at the share of viewing that BBC One+1 will gain in greater detail (as explained above in our approach to the regression analysis) and have accounted for more than just the EPG delta.

on all channels as it anticipates that BBC One+1 will attain a lower viewing share than we do (Viacom estimates that the BBC family of channels will gain around 0.4 percentage points of share, while we estimate that these channels will gain around 0.5 percentage points of share).

- 9.54 Overall, we believe that our approach remains reasonable after considering the alternative approaches used by stakeholders.

Impact on viewing hours and viewing share

- 9.55 In Figure 9.1 below we show the impact of launching a BBC One+1 channel in terms of viewing hours and viewing share for the BBC and the main commercial providers in 2018.

Figure 9.1: Net impact on viewing from launching BBC One+1, 2018

Channel family	Share of total viewing counterfactual	Change in viewing from launching BBC One+1 (hours bn)	Change in viewing share (percentage points)	Share of total viewing after launching BBC One+1	Percentage change in viewing share
BBC	34.4%	+0.5	+0.5 p.p.	34.9%	+1.5%
ITV	20.6%	-0.2	-0.2 p.p.	20.4%	-1.0%
Channel 4	11.4%	-0.1	-0.1 p.p.	11.3%	-0.7%
Channel 5	5.9%	-0.0	-0.1 p.p.	5.8%	-0.9%
Other	27.8%	-0.2	-0.2 p.p.	27.6%	-0.7%
Total	100.0%	0.0	0.0p.p.	100.0%	-

- 9.56 The modelled impact of launching a BBC One+1 channel on viewing is one of the most significant of the proposals. This is consistent with the BBC's market research. The research found that the BBC One+1 proposal was very popular with respondents. They perceived it to offer the greatest value of the MIA proposals, with around 80% attributing medium or high value to the change.²³⁴
- 9.57 The BBC One+1 proposal would capture around half a percentage point of viewing share for the BBC family of channels from the commercial channels, with the largest proportional impact being on the ITV and Channel 5 families of channels.

Impact on producer surplus

- 9.58 We have estimated the financial impact on the main commercial providers in the base case by estimating the change in producer surplus resulting from launching a BBC One+1 channel.

²³⁴ See PAPA research for the BBC, September 2014, pages 9, 48 at http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/audience_research.pdf

Figure 9.2: Net impact on producer surplus from launching BBC One+1, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	-1.0%	1,710	-5.5	-8.2	-11.0
Channel 4	-0.7%	813	-2.0	-3.0	-4.0
Channel 5	-0.9%	358	-1.1	-1.6	-2.1
Other	-0.7%	999	-2.2	-3.4	-4.5
Total	-0.8%	3,881	-10.8	-16.2	-21.6

9.59 The impact on producer surplus of commercial channels from launching BBC One+1 is of the order of tens of millions of pounds across all channels. ITV and Channel 5 are affected proportionally more than the other commercial broadcasters, for similar reasons to those discussed in Section 8, i.e. heavy BBC One viewers are more likely to watch these channels than the national average.

Sensitivity analysis

9.60 There is a significant degree of uncertainty regarding this proposal. Therefore, we have tested the impact of a scenario where various assumptions are set to be significantly more favourable to the BBC. The assumptions used in this scenario are as follows:

9.60.1 BBC One+1's share of viewing is at the upper end of the range of results produced by the regression analysis;

9.60.2 BBC One+1 is transitioned to a DVB-T mux by the end of the modelled period; and

9.60.3 BBC One+1 occupies BBC Three's slot on Freeview.

9.61 Flexing these assumptions simultaneously (and maintaining all other base case assumptions) increases the BBC's viewing share by 0.8 percentage points relative to the counterfactual (compared to +0.5 percentage points in the base case), resulting in a BBC viewing share of 35.2%.

9.62 This would result in commercial broadcasters' advertising revenue falling by around £16.6m to £33.1m (depending on the price offset assumption), compared to the counterfactual.

Impact on pay TV platforms

9.63 We note that the proposed BBC One+1 channel would be a PSB channel, in line with all other BBC services. PSB status confers an obligation on relevant broadcast platforms to include a channel in their services and to make the channel free to access. It must also be given due prominence in any relevant EPGs. Other +1 channels have not been designated as PSBs, even when their parent channel has been (i.e. ITV+1, Channel 4+1 and Channel 5+1 are not PSB channels). Virgin Media and other pay TV platforms can therefore choose whether or not to carry these +1

channels, taking into account their own interests within a commercial negotiation with the parent broadcaster group.

- 9.64 We acknowledge Virgin Media’s point that there may be an opportunity cost for Virgin Media (and its customers) of carrying the BBC One+1 channel. Virgin Media’s cable network can use the same physical connections to deliver TV, fixed voice and broadband services. The network capacity used for the proposed BBC One+1 channel could be allocated instead to another TV channel or, potentially, with further network adjustments, to provide additional broadband capacity. We note that Virgin Media carries over 250 SD and HD TV channels on its platform, with over 60 included in its basic tier package. We therefore consider that the marginal capacity requirement of another channel – BBC One+1 – is likely to be low. As a result we consider the opportunity cost of carrying the channel is unlikely to be significant.

Dynamic impacts

Impact on commercial TV channels

- 9.65 COBA and Viacom raised concerns about the impact of the proposed BBC One+1 channel on the ability of commercial channels to identify profitable slots in their schedules.
- 9.66 While we recognise that the proposed launch of BBC One+1 could affect the scheduling of content for other channels, we also consider that the overall impact on commercial channels is complex and subject to a number of factors, e.g. the popularity of programmes broadcast at 9pm on BBC One, and the response of other channels at 10pm. As a result, the potential impact is highly uncertain.

Impact on independent production companies

- 9.67 PACT’s consultation response linked the BBC One+1 proposal to the fee structure for a channel’s narrative repeats. PACT’s observation implied that since BBC One+1 would use up one of the narrative repeats typically included in any production deal, the proposed new channel could lead to additional payments being made to independent content producers. PACT said that it was unclear from the proposal whether or not the estimated £4.6m cost of running BBC One+1 includes any additional licence fee costs.²³⁵
- 9.68 The exact outcome would depend on relevant agreements between independent producers and the BBC about this arrangement as well as the specific editorial decisions taken by the BBC. As a result, we are unable to quantify this impact but consider that it would have a positive impact on independent production companies.

Wider impacts

- 9.69 We note [S&C] comments that the proposed BBC One+1 channel could “use up” more of the value of BBC One programmes. However, we consider that this effect is unlikely to be as strong for +1 channels because of the proximity of the broadcast to the original transmission. We also note that +1 channels are already a well-established feature for many other broadcasters. As a result we do not expect this effect will be significant.

²³⁵ PACT response to MIA stakeholder questionnaire, page 14.

Recommendations

- 9.70 We have not identified any modifications to mitigate the potential commercial impact of this proposal which do not relate to simply limiting the broadcast hours of the +1 channel.
- 9.71 Our assessment of the static impact (discussed above) is based on the current market context and the proposals outlined in the Service Proposal. Were the BBC to propose further changes at a later date, e.g. launching +1 versions of other BBC channels, then the Trust is likely to need to conduct a further PVT. To provide stakeholders with clarity the Trust may wish to consider the criteria it would apply for requiring reassessment.

Section 10

Changes to the CBBC channel

Summary of proposal

- 10.1 Currently the BBC's channel for 6-12 year old children, CBBC, broadcasts from 7am to 7pm every day. It is available on all major broadcast TV platforms and via the BBC iPlayer service. It is available in both SD and HD on every platform.
- 10.2 The BBC is proposing to extend CBBC's daily broadcast schedule by two hours, so that it ceases broadcasting at 9pm (i.e. it would broadcast from 7am to 9pm every day).
- 10.3 The BBC proposes to use the first extra hour (7pm to 8pm) for programmes which appeal most to six to nine year olds and the second hour (8pm to 9pm) for programmes which appeal to the older 10 to 12 year old audience.
- 10.4 The BBC's rationale for the changes has two elements: to support the transition of audiences from CBeebies to CBBC by offering younger viewers programming aimed at them once CBeebies closes at 7pm; and to make distinctive programming for 10 to 12 year olds available at a more convenient time for them as viewing from younger audiences starts to decline. The BBC noted that TV reach for CBBC's six to twelve year old target audience currently peaks between 7pm and 9pm, after CBBC currently closes.²³⁶
- 10.5 The CBBC SD and HD variants share broadcast capacity with BBC Three on Freeview. Therefore, the proposed closure of BBC Three as a broadcast channel frees up the necessary capacity for the BBC proposal.

Stakeholder evidence

Impact on commercial broadcasters

- 10.6 Channel 4 did not consider the CBBC proposal would have a significant impact on Channel 4's own share of viewing. It noted what it described as "the BBC's particular expertise in original children's programming and its success in establishing compelling content destinations for young and older children" whilst noting the commercial challenges around this genre.²³⁷
- 10.7 COBA considered that the CBBC proposal was likely to affect commercial children's channels broadcasting after 7pm. It explained that these commercial channels would have to compete against CBBC and share the available children's audience and, because advertising revenues are directly dependent on audience levels, that would have financial implications for the channels. COBA expected any negative impact on advertising revenues stemming from the CBBC proposals to lower content budgets and, by extension, on investment in UK children's content.
- 10.8 COBA also highlighted CBBC's strength on Freeview, where there are fewer children's channels in comparison to other platforms, to indicate that the impact of

²³⁶ BBC Service Proposals document, page 37.

²³⁷ Channel 4 response to MIA stakeholder questionnaire, page 3.

the CBBC proposal on POP and Tiny Pop is likely to be greater than for other channels. COBA stated that CBBC has 27% audience share amongst children on Freeview, POP has 15% and Tiny Pop²³⁸ has 3%.²³⁹

- 10.9 COBA argued against two specific points made by CC. Firstly, COBA disagreed with CC's suggestion that the children's channels affected by the CBBC proposal are all pay channels with subscription funding. COBA pointed out that Tiny Pop and POP are both free-to-air, advertiser-funded children's channels.²⁴⁰
- 10.10 Secondly, COBA disputed CC's claim that channels which are part of international groups are less exposed to loss of share or income in any one market, reducing the chances of any market exits.²⁴¹ COBA argued instead that multinational channels do not tend to cross-subsidise each other and that, while they do have shared costs, each national channel must deliver an appropriate level of revenues and is treated on a stand-alone basis in this regard. COBA used Tiny Pop and POP as examples of channels which are exclusively based in the UK (in Tiny Pop's case) or have a very recent and limited international presence (POP in South Africa), contrary to CC's assertion.²⁴²
- 10.11 Viacom estimated the impact of extending CBBC's broadcast hours on its channel portfolio to be around -0.01 percentage points of viewing share (which equates to a loss of 0.15% of its portfolio share of viewing). Its analysis assumed that CBBC would maintain the same share of viewing of children's channels that it currently achieved in the 6pm-7pm slot (around 14%). Viacom assumed that all viewing gains by CBBC would be captured from children's channels only based on their share of viewing in the 7pm-7:30pm slot.
- 10.12 Viacom's consultation response noted that the BBC's current proposal for CBBC's extended broadcast hours would be limited to showing repeats of content shown earlier in the day. However it raised concerns that the character of the proposed extension could evolve over time because "the 7pm-9pm window offers a prime opportunity to reach the 13-15 audience as well as creating a scheduling window for family viewing".²⁴³ Viacom provided examples of possible changes which it considered would have an impact on the market much greater than that presented in the BBC's current proposal. Examples given were:
- Focusing on content to bridge the gap between CBBC's existing target age group (9-12 year olds) and the 16+ target age groups for Radio 1 and BBC Three. Viacom said that content focused on the 13-15 age group would probably make use of vlogger²⁴⁴ talent. Viacom noted that the BBC could exploit this opportunity to cross-promote other BBC outlets such as BBC Three and Radio 1 to the slightly older viewers at this time.
 - Re-exploiting the BBC's family drama and film archive in this slot. Viacom observed that in many homes family viewing begins at 7pm. It implied that using content which appeals to an audience including but not exclusively in CBBC's

²³⁸ COBA stated that Tiny Pop launched nationally on 7 January 2015.

²³⁹ COBA response to MIA stakeholder questionnaire, pages 3-4.

²⁴⁰ COBA response to MIA stakeholder questionnaire, pages 3-4.

²⁴¹ CC report, pages 42-43.

²⁴² COBA response to MIA stakeholder questionnaire, pages 3-4.

²⁴³ Viacom response to MIA stakeholder questionnaire, page 2.

²⁴⁴ The term "vlogger" refers to people who create and upload video blogs posts, typically using video sharing platforms such as YouTube.

target age range would increase its viewing share, and thereby lead to a greater market impact on rival commercial channels.²⁴⁵

10.13 Viacom also highlighted the dynamic impact of the CBBC proposal on subscription children's channels' income. It explained that contractual negotiations between broadcasters and pay TV platform operators typically factor in a subscription channel's audience share. As a result, any payments from the platform to the channel may be lower if the CBBC proposal reduces the viewing audience for that channel.

Impact on independent production companies

10.14 PACT welcomed the proposal to extend CBBC's broadcast hours but also questioned, based on the publicly available information, whether the BBC had made sufficient allowances for additional rights payments. It expected the BBC to have to make additional payments to repeat some of the content aimed at older children as planned.²⁴⁶

10.15 Entertainment One noted, as a general observation, that the proposed extension of CBBC's broadcasting hours could increase licensing opportunities for the company.²⁴⁷

Impact on pay TV platforms

10.16 Virgin Media welcomed the BBC's proposal to extend CBBC's broadcast hours.²⁴⁸

Identification of affected services

10.17 We have identified the following services that could potentially be affected as a result of extending the broadcast hours of the CBBC channel:

- commercial broadcasters' (both PSB and non-PSB) channels and on-demand services as a result of changes in audiences and potential impact on advertising revenues;
- other VOD providers (including SVOD) and pay TV retailers as a result of changes in audience volumes; and
- independent production companies.

Assessment of impacts

Static impacts

10.18 We recognise that the availability of extended CBBC hours could result in reduced viewing of subscription services. However, we consider that for the reasons set out in paragraph 6.24 this is unlikely to have a material impact on household purchasing decisions relating to subscription services (e.g. pay TV or SVOD services) or DVDs.

²⁴⁵ Viacom response to MIA stakeholder questionnaire, page 2.

²⁴⁶ PACT response to MIA stakeholder questionnaire, page 15.

²⁴⁷ Entertainment One response to MIA stakeholder questionnaire, page 3.

²⁴⁸ Virgin Media response to MIA stakeholder questionnaire, page 12.

- 10.19 We note CC’s assumption that income for most children’s channels comes predominantly from subscription revenues (via pay TV platforms).²⁴⁹ However, we have also taken into account representations from stakeholders which emphasised the importance to these channels of advertising income as well (see, for example, paragraph 10.9).
- 10.20 Therefore in the rest of this sub-section we have assessed the impact of the BBC’s proposals on advertising revenues for commercial broadcasters.

CC model – Overview

- 10.21 CC modelled the extension of CBBC’s broadcast hours by examining the profile of viewing of a set of comparator channels up to 7pm²⁵⁰ and assuming that CBBC would attain the same proportion of its observed daily viewing in the proposed 7pm-9pm slot.
- 10.22 Based on this approach, CBBC’s share of all viewing was estimated to increase by around 0.05 percentage points in 2018.
- 10.23 Given the relatively small impact, CC decided to redistribute the viewing from other channel families in proportion to each channel family’s share of total viewing. It decided against redistributing viewing from other channels to CBBC based on the viewing profile of CBBC viewers for the following reasons:
- Despite there being a skew towards CBBC viewers also viewing other children’s channels, these channels still represent a small portion of overall CBBC viewers’ viewing;
 - There is no visible “uptick” in viewing of the comparator set at 7pm, which suggests that viewers are not switching to these channels in large enough numbers to be noticeable; and
 - Many viewers of CBBC in the run up to 7pm switch the TV off when they cease watching CBBC. As a result, CC suggested that viewing gained by CBBC under the proposals would be as likely to be incremental as it would be captured from other children’s channels.

Our assessment of the CC model

- 10.24 Overall, we agree with the approach taken by CC. We note that a more in-depth analysis could be performed to try to better model the redistribution of viewers to CBBC due to extending its broadcast hours. However, the overall impact of this proposal is small in comparison to other proposals and it is unlikely that a more nuanced approach to modelling would meaningfully change the results. We note COBA’s objections to the points made by CC in its analysis (outlined in paragraphs 10.9 to 10.10). However, we note that these two points identified by COBA were included in the report by CC to provide context only. Neither point had a bearing on the model created by CC or in our subsequent modifications to that model. Given the small scale of the modelled impact on commercial channels we do not consider that either of the points is likely to make a significant difference to any affected children’s channels.

²⁴⁹ CC report, page 14.

²⁵⁰ Cartoon Network, the Disney Channel, Nickelodeon, Pop and their respective +1 channels.

Impact on viewing hours and viewing share

10.25 In Figure 10.1 below we show the impact of extending CBBC's broadcast hours in terms of viewing hours and viewing share for the BBC and the main commercial providers in 2018.

Figure 10.1: Net impact on viewing from extending CBBC's broadcast hours, 2018

Channel family	Share of total viewing counterfactual	Change in viewing from extending CBBC's broadcast hours (hours bn)	Change in viewing share (percentage points)	Share of total viewing after extending CBBC's broadcast hours	Percentage change in viewing share
BBC	34.4%	+0.02	+0.03 p.p.	34.4%	+0.08%
ITV	20.6%	-0.01	-0.01 p.p.	20.6%	-0.04%
Channel 4	11.4%	-0.00	-0.00 p.p.	11.4%	-0.04%
Channel 5	5.9%	-0.00	-0.00 p.p.	5.9%	-0.04%
Other	27.8%	-0.01	-0.01 p.p.	27.8%	-0.04%
Total	100.0%	0.00	0.00 p.p.	100.0%	-

10.26 On this basis, we estimate that the net impact from extending CBBC broadcast hours on commercial channels in terms of viewing share is likely to be very low; indeed the lowest net impact of the proposed service changes. That this is the lowest impact of the BBC's service proposals is consistent with the market research conducted by PAPA (commissioned by the BBC), which indicated comparatively low approval for the CBBC proposal amongst UK adults. According to the research, just over 40% of respondents perceived the proposal as having medium or high personal value. By way of comparison, the BBC Three, BBC iPlayer and BBC One+1 proposals were all perceived as having medium or high value by more than 60% of the respondents.²⁵¹ The CBBC proposal was better received (on average) by parents with children aged 0-12, with approximately 55% perceiving the proposal to have medium or high value. The research sample did not include children in CBBC's target age range.²⁵²

10.27 While there may be some disproportionate impact on children's channels, as discussed in paragraph 10.23 it appears that a large amount of CBBC viewers' viewing is to non-children's channels.

²⁵¹ See PAPA research for the BBC, September 2014, page 9.

²⁵² See PAPA research for the BBC, September 2014, pages 56, 58 at

http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/service_changes/audience_research.pdf

Impact on producer surplus

10.28 We have estimated the financial impact on the main commercial providers in the base case by estimating the change in producer surplus resulting from extending CBBC’s broadcast hours.

Figure 10.2: Net impact on producer surplus from extending CBBC’s broadcast hours, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	-0.04%	1,710	-0.2	-0.4	-0.5
Channel 4	-0.04%	813	-0.1	-0.2	-0.2
Channel 5	-0.04%	358	-0.1	-0.1	-0.1
Other	-0.04%	999	-0.1	-0.2	-0.3
Total	-0.04%	3,881	-0.6	-0.8	-1.1

10.29 Based on the above, we estimate that the overall impact on producer surplus is likely to be very small. Even at the upper end of the range, we model the extension of CBBC’s broadcast hours to have an impact of just over £1m across all commercial channels.

Dynamic impacts

Impact on commercial broadcasters

10.30 We note Viacom’s concerns about the character of the proposed extension changing over time, outlined in paragraph 10.12. Our assessment of the proposed extension of CBBC’s broadcasting hours has been limited to the description provided by the BBC in its PVT submission. As a result it is not within the scope of our assessment to conduct an in-depth analysis of the hypothetical developments suggested in Viacom’s response. However, we note the BBC’s comment “Over time, if the new slots are successful with audiences, [the BBC] Children’s [department] may revisit where the emphasis lies in scheduling/ commissioning, but still managing within existing resources”.²⁵³ Therefore we consider that without any prior stipulations, it is possible that the BBC could choose to change the nature of the extended CBBC hours in the manner suggested by Viacom.

10.31 Of the two examples given by Viacom, we consider that the latter one – re-exploiting the BBC’s family drama and film archive in this slot – to be more likely to increase the level of impact on commercial broadcasters. The BBC has an extensive archive of content aimed at family audiences which it could choose to broadcast in the proposed new slot. This content would have a wider appeal than the children’s content usually shown on CBBC. That could make the CBBC 7pm-9pm slot a more compelling option during a peak time slot with a potential audience across all

²⁵³ BBC Service Proposals document, page 74.

demographic groups. It could be expected, therefore, to have a greater impact on the audience share of a wide range of commercial channels.

- 10.32 COBA's response linked the negative impact on advertising revenues stemming from the CBBC proposals to lower content budgets and, by extension, on investment in UK children's content.²⁵⁴ We consider that the impact on content budgets and investment by commercial channels to be unclear. Commercial channels might have an incentive to increase their investment in order to win viewing from CBBC, or might reduce investment if they considered they were unable to compete. This may vary by channel, and depend on the channel's perception of how difficult it might be to win viewing share. We do not expect it to be a large risk, given the very small scale of the potential impact and the availability to most children's channels of subscription revenues.
- 10.33 Viacom highlighted the dynamic impact of the CBBC proposal on subscription children's channels' income because of contractual negotiations between broadcasters and pay TV platform operators which are linked to a subscription channel's audience share (which may decline as a result of this proposal). We do not have sufficient information about these payments to quantify the potential impact but note that the predicted impact of the CBBC proposal on other channel's audience shares is likely to be very low. Therefore we do not expect the impact on subscription income to be significant.

Impact on independent production companies and content rights owners

- 10.34 The BBC's proposal described the additional hours of CBBC as focusing only on repeat content. This could have a positive impact for independent production companies through additional repeat fees. However, we also note that it could be funded by a budget reallocation resulting in less money being spent on new commissions, which would have a counteracting negative impact.²⁵⁵

Wider impacts

- 10.35 We have not identified any wider impacts that are likely to result from this proposal.

Recommendations

- 10.36 Overall, we consider that the impact of this proposal is likely to be very small. We have not identified any modifications relating to the proposal.
- 10.37 Our assessment of the static impact (discussed above) is based on the current market context and the proposals outlined in the Service Proposal. Were the BBC to propose further changes at a later date, e.g. extending the broadcast hours of CBeebies or choosing to broadcast BBC archive family drama or film content rather than programming focused on 6-12 year olds, then the Trust may need to conduct a further PVT. To provide stakeholders with clarity, the Trust may wish to consider the criteria it would apply for requiring reassessment.

²⁵⁴ COBA response to MIA stakeholder questionnaire, page 4.

²⁵⁵ PACT response to MIA stakeholder questionnaire, pages 14-15.

Section 11

Overall impact of the changes

- 11.1 In the preceding sections we have assessed the impact of the BBC's service proposals individually, and compared their potential impact individually against the counterfactual.²⁵⁶ In this section we consider the overall impact of all the BBC's proposals combined, including their interdependencies, compared to the counterfactual both in terms of viewing share, and financial impact. We also consider the combined financial impact on commercial broadcasters relative to their profit after tax, and consider sensitivities to the main results.
- 11.2 Assessing the combined impact requires us to consider the interactions between each of the proposals. Therefore the net effect will not be equivalent to adding up the individual effects that have been outlined in earlier sections.
- 11.3 However, as described below, our modelling suggests that the net impact of the interdependencies is limited, amounting to merely hundredths of a percentage point of viewing share. As a result, the financial impact on commercial broadcasters of the interdependencies is likely to result in a reduction of net advertising revenues of up to £1m per year in total.
- 11.4 Therefore, we do not believe that the effect of the interdependencies has an impact on the conclusions in Sections 5 to 10 of this document.

Interdependencies

- 11.5 Our approach to assessing the impact of the BBC's service proposals individually, by comparing each proposal individually against the counterfactual contrasts with CC's approach. CC applied each proposal in sequence, adding proposals incrementally until all proposals were applied together. Therefore, under CC's approach, the impact of each proposal included the effect of interdependencies between it and prior proposals.
- 11.6 The net impact of interdependencies is the difference between the sum of each of the proposals presented in Sections 5 to 10 (which were applied on a standalone basis²⁵⁷) and the result generated by modelling all proposals together sequentially.
- 11.7 The order in which changes are applied will have a small effect on the overall interdependencies. We have ensured that there is a logical ordering where there are intuitive links between the proposals. Specifically our ordering acknowledges the following links:
- 11.7.1 The closure of BBC Three as a broadcast channel should precede launching BBC Three Online; and

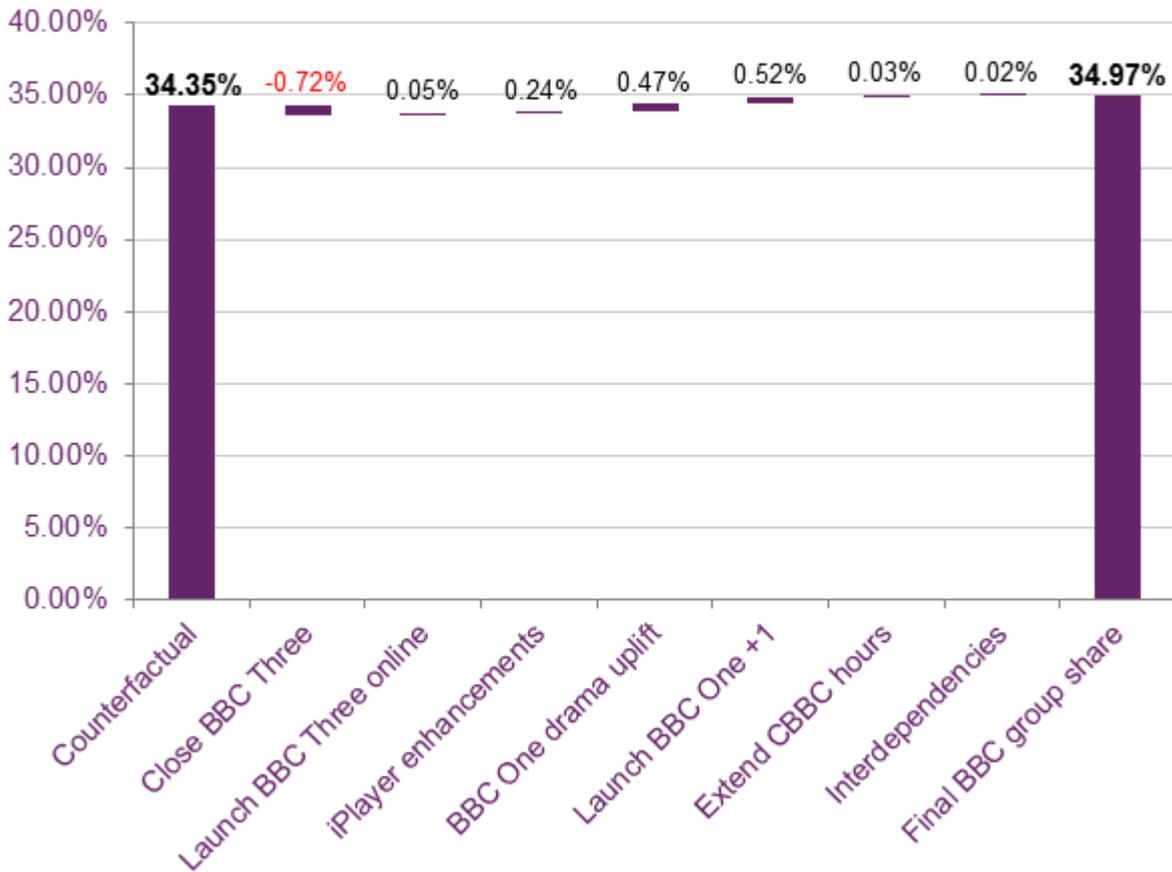
²⁵⁶ The only exception to this is that we have considered the impact of launching BBC Three Online assuming that the BBC Three linear channel closes, rather than comparing it to the counterfactual directly. In its service proposals, the BBC has made the launch of BBC Three Online contingent on the closure of the linear channel.

²⁵⁷ With the exception of our assessment of BBC Three Online which assumed that BBC Three as a broadcast channel was closed

11.7.2 BBC One’s drama budget should be increased prior to launching BBC One+1.

11.8 Figure 11.1 provides our estimate of the change in the BBC family viewing share as a result of each of the BBC’s service proposals. It shows the effect of each proposal, under our base case assumptions, if applied on a standalone basis. It then shows the net change from interdependencies between proposals. Therefore, “Final BBC group share” is the estimated share of all viewing for the BBC (live linear, PVR and catch-up) if all proposals were adopted in the base case.

Figure 11.1: BBC viewing share changes from each proposal, 2018 modelled share²⁵⁸



Source: Ofcom calculations based on adaptation of the Communications Chambers’ model using BARB data. Individuals 4+.

Impact on viewing hours and viewing share

11.9 In Figure 11.2 we show the net impact of the interdependencies in terms of viewing hours and viewing share for the BBC and the main commercial providers in 2018. This is presented relative to the case of adding all individual changes presented in Sections 5 to 10 of this document to the counterfactual presented in Section 4.

²⁵⁸ This is the BBC group share of (total live linear viewing hours + total PVR viewing hours + total catch-up viewing hours).

Figure 11.2: Net impact on viewing from interdependencies, 2018

Channel family	Share of total viewing assuming no interdependencies	Change in viewing from interdependencies (hours bn)	Change in viewing share (percentage points)	Share of total viewing after interdependencies	Percentage change in viewing share
BBC	34.9%	+0.02	+0.02 p.p.	35.0%*	+0.07%
ITV	20.4%	-0.01	-0.01 p.p.	20.4%	-0.04%
Channel 4	11.3%	-0.00	-0.00 p.p.	11.3%	-0.04%
Channel 5	5.8%	-0.00	-0.00 p.p.	5.8%	-0.04%
Other	27.6%	-0.01	-0.01 p.p.	27.6%	-0.03%
Total	100.0%	0.00	0.00 p.p.	100.0%	-

*Note: The difference between outputs and the sum of counterfactual viewing share and change in viewing share values is due to rounding.

Impact on producer surplus

11.10 We have estimated the net financial impact on the main commercial providers in the base case by estimating the change in producer surplus resulting from the modelling interdependencies.

Figure 11.3: Net impact on producer surplus from interdependencies, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)		
			67% offset	50% offset	33% offset
ITV	-0.04%	1,710	-0.2	-0.3	-0.4
Channel 4	-0.04%	813	-0.1	-0.2	-0.2
Channel 5	-0.04%	358	-0.0	-0.1	-0.1
Other	-0.03%	999	-0.1	-0.2	-0.2
Total	-0.03%	3,881	-0.5	-0.7	-0.9

11.11 We estimate that the overall impact on commercial broadcasters of the interdependencies is likely to result in a reduction of net advertising revenues of up to £1m per year in total. Our estimate of the financial impact of the interdependencies does not alter the conclusions presented in Sections 5 to 10 of this document.

Dynamic interdependencies

11.12 We would expect interdependencies between the BBC's service proposals could result in further dynamic impacts.

- 11.13 For example, the proposals to launch BBC Three as online only and the other BBC iPlayer enhancements (i.e. online premieres) will increase the service offering of the BBC iPlayer and thus may increase its usage. To some extent these proposals may therefore reinforce each other e.g. if the BBC iPlayer receives more traffic due to the online launch of BBC Three users may become more aware of other BBC iPlayer services such as online premieres and vice versa. We have discussed changing perceptions of on-demand services and the growing portfolio of BBC iPlayer services more generally under the dynamic impact headings in Sections 6 and 7.
- 11.14 However, we consider that the dynamic impacts arising from the interdependencies between the proposals are complex and uncertain. Therefore, we have not presented further dynamic impacts and consider the findings in Sections 5 to 10 remain unchanged.

Net financial impact on commercial broadcasters

- 11.15 In Figure 11.4 we present the overall impact on producer surplus (including interdependencies) as result of the BBC's service proposals for the main commercial channels.

Figure 11.4: Net impact on the major commercial channels' advertising revenues from all BBC proposals, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)			First-run origination spend (2013)	Profit after tax (2013)
			67% offset	50% offset	33% offset		
ITV	-1.2%	1,710	-6.7	-10.1	-13.5	£750m	£445m
Channel 4	-0.7%	813	-1.9	-2.9	-3.8	£382m	£15m
Channel 5*	-1.0%	358	-1.2	-1.8	-2.4	£88m	£31m
Other	-0.8%	999	-2.8	-4.1	-5.5	**£708m	N/A
Total	-0.9%	3,881	-12.6	-18.9	-25.2	£1,928m	N/A

Source: Ofcom and ITV, Channel 4, Northern & Shell annual reports. Notes: NAR figures are for ITV, Channel 4 channel families. Whereas STV and UTV are included in the ITV viewing and ITV NAR figures, STV and UTV are excluded from the ITV figures for first-run origination spend and profit after tax. *Channel 5, parent channel only. **Total spend, not just originations; includes all genres except sports and films.

- 11.16 The net impact on the major commercial channels is negative, but less than 1% of each channel family's NAR in all cases.
- 11.17 We have also considered these reductions in relation to channels' originated programme spending and their profits. For ITV (excluding ITV Studios), the most strongly-affected channel family in terms of the proportion of total viewing lost, the impact would reduce its 2013 profit after tax by between 1.5% and 3.0%.
- 11.18 In relation to Channel 4, since it is a not-for-profit PSB, it is more difficult to consider the impact of these changes on its profitability. However the impact of these proposals would directly feed through to Channel 4's programming budget, and therefore its ability to deliver its public remit. We estimate the impact would equate to

about 0.2% to 0.5% of its advertising revenues, slightly less than the impact for ITV and Channel 5. This corresponds to around 0.5% to 1.0% of Channel 4's programme budget.²⁵⁹ While these proposals are unlikely to call into question the sustainability of Channel 4 Corporation in and of themselves, they will add to the already challenging environment in which it is operating.

11.19 In terms of the underlying static impacts, we highlight the following:

- Excluding the proposal to launch BBC One+1, the overall net financial impact of all other proposals is broadly neutral for the commercial channel families.
- There is a positive net financial impact for the commercial channels from closing BBC Three as a broadcast channel and reinventing BBC Three online. This is driven by a large proportion of current BBC Three viewing switching to other channels and, crucially, not being recaptured by the online offering.
- The largest net financial impact relates to the proposed launch of BBC One+1. However, as discussed in paragraph 9.70, we have not identified any reasonable or practicable mitigations to launching BBC One+1, rather, we consider the Trust has a binary decision either to approve the launch of BBC One+1 or not to, taking into account its own public value assessment.

Combined sensitivities

11.20 The results presented so far in this document have concentrated on the assumptions we judge to be most likely. We have also considered how these results may change if we were to take a more optimistic or pessimistic set of assumptions. These have been discussed individually in each of the previous sections.

11.21 Due to the range of variables over which there is uncertainty, we have also considered scenarios where the more uncertain assumptions are flexed simultaneously to be more or less favourable to the BBC's viewing share in order to produce a range of potential results. We present a smaller-impact scenario and a larger-impact scenario. For each, we identify the assumptions which have been changed relative to the base case, and present the results of all changes together (as in Figure 11.4 above).

11.22 In constructing these scenarios we have not simply chosen the highest or lowest value of each sensitivity presented in Sections 5 to 10. While it is useful to present a wide range of sensitivities for each individual effect, it is implausible to assume that each uncertain variable would achieve its most extreme value simultaneously. We have therefore chosen a set of values that collectively produce what we believe to be reasonable upper and lower estimates for the modelled impacts. Nevertheless, we consider these smaller-impact and larger-impact scenarios are less likely than the base case scenario.

Smaller-impact scenario

11.23 In this scenario, we flex assumptions in such a way as to reduce the overall impact on the BBC's viewing share, and therefore reduce the negative impact on

²⁵⁹ Source: PSB Review consultation. Based on 2013, first run, UK origination content.
<http://stakeholders.ofcom.org.uk/binaries/consultations/psb-review-3/summary/PSBR-3.pdf>

commercial broadcasters' revenues. Relative to the base case we have made the following changes:

- 11.23.1 BBC One+1's share of viewing is at the lower end of the range of results produced by the regression analysis;
- 11.23.2 BBC iPlayer premiering uplift and BBC Three Online online only uplift of 75% (half that of the base case);
- 11.23.3 BBC Three Online loss of linear promotion stays constant at -50% (rather than reducing from -50% to -25% as in the base case);
- 11.23.4 0% BBC Three Online "built for online" uplift (from 25% in the base case); and
- 11.23.5 Additional titles premiered on BBC iPlayer get an average of 100,000 requests per title (down from 200,000 in the base case).

11.24 The net impacts on the commercial channel families are presented in Figure 11.5.

Figure 11.5: Net impact on the major commercial broadcasters' advertising revenues from all BBC proposals in the smaller-impact scenario, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)			First-run origination spend (2013)	Profit after tax (2013)
			67% offset	50% offset	33% offset		
ITV	-0.6%	1,710	-3.2	-4.8	-6.4	£750m	£445m
Channel 4	+0.1%	813	+0.3	+0.4	+0.6	£382m	-£15m
Channel 5	-0.3%	358	-0.3	-0.5	-0.6	£88m	£31m
Other	-0.2%	999	-0.5	-0.8	-1.0	**£708m	N/A
Total	-0.2%	3,881	-3.7	-5.6	-7.5	£1,928m	N/A

Source: See Figure 11.4

11.25 The net impact on Channel 4 in this scenario is slightly positive. On the other major commercial channels it is negative, but a lower proportion of each's NAR (when compared to our estimates using base case assumptions). In the smaller-impact scenario the impact on each channel family's NAR ranges from an increase of 0.1% to a reduction of 0.4% (compared to a reduction of 0.2% to 0.8% in the base case).

11.26 We have also considered these reductions in relation to each channel family's originated programme spending and profits. The reduction in net advertising revenues would account for less than 1% of first-run origination spend for each channel family and negatively impact profits (for the commercial PSBs only) by less than 5%.

11.27 In terms of the underlying static impacts, we would highlight the following:

- The lost BBC viewing share following the closure of BBC Three as a broadcast channel that is reclaimed by BBC Three Online is reduced considerably compared to the base case; and
- BBC One+1 achieves a lower share of viewing compared to the base case.

Larger-impact scenario

11.28 In this scenario, we flex assumptions in such a way as to increase the overall impact on BBC's viewing share, and therefore increase the negative impact on commercial broadcasters' revenues. Relative to the base case we have made the following changes:

- 11.28.1 BBC One+1's share of viewing is at the upper end of the range of results produced by the regression analysis;
- 11.28.2 BBC One+1 assumed to achieve EPG slot 7 on Freeview (rather than slot 23 in the base case);
- 11.28.3 BBC One+1 assumed to transition to a DVB-T mux in 2017, increasing availability to 100% of DTT homes (up from 86% of homes in the base case);
- 11.28.4 BBC iPlayer premiering uplift and BBC Three Online online only uplift of 300% (double that of the base case);
- 11.28.5 BBC Three Online loss of linear promotion is 0% in all years (rather than reducing from -50% to -25% as in the base case);
- 11.28.6 50% BBC Three Online "built for online" uplift (from 25% in the base case); and
- 11.28.7 Additional titles premiered on BBC iPlayer get an average of 300,000 requests per title (up from 200,000 in the base case).

11.29 The net impacts on the commercial broadcasters are presented in Figure 11.6, below.

Figure 11.6: Net impact on the major commercial broadcasters' advertising revenues from all BBC proposals in larger-impact scenario, 2018

Channel family	Percentage change in viewing	2013 net advertising revenues (£m)	Impact on net advertising revenues after price offset scenarios (£m)			First-run origination spend (2013)	Profit after tax (2013)
			67% offset	50% offset	33% offset		
ITV	-2.8%	1,710	-15.9	-23.9	-31.9	£750m	£445m
Channel 4	-2.8%	813	-7.6	-11.5	-15.3	£382m	-£15m
Channel 5	-2.9%	358	-3.5	-5.2	-7.0	£88m	£31m
Other	-2.6%	999	-8.6	-13.0	-17.3	**£708m	N/A
Total	-2.7%	3,881	-35.7	-53.6	-71.4	£1,928m	N/A

Source: See Figure 11.4

11.30 The net impact on the major commercial channels is negative and significantly larger than the base case. As a proportion of each channel family's NAR, the impacts are between 0.9% and 1.9% (compared to 0.2% and 0.8% in the base case).

11.31 We have also considered these reductions in relation to each channel family's originated programme spending and profits. The reduction in net advertising revenues would account for between 1.2% and 7.9% of first-run origination spend across each of the channel families.

11.32 The reduction in net advertising revenues would reduce the profit of ITV by between 3.6% to 7.2% and reduce the profit of Channel 5 by between 11.2% and 22.5% (this compares to a reduction in profit in the base case of between 1.5% and 3.0% for ITV and between 3.9% and 7.7% for Channel 5). The reduction in net advertising revenues would increase Channel 4's current loss by a further £7.6m to £15.3m (compared to a further loss of around £1.9m to £3.8m in the base case).

11.33 In terms of the underlying static impacts, we would highlight the following:

- the lost BBC Three share reclaimed by BBC Three Online is increased considerably compared to the base case; and
- BBC One+1 achieves a higher share of viewing compared to the base case.

Summary

11.34 In this section we have examined the combined effects of the BBC's service proposals under a range of scenarios. While we consider that the larger-impact and smaller-impact scenarios provide reasonable upper and lower estimates for the potential impacts on commercial broadcasters, we consider them less likely than the base case scenario.

11.35 In light of our analysis in this section, our recommendations in Sections 5 to 10 are unchanged.

Annex 1

Glossary

BBC family: BBC One, BBC Two, BBC Three, BBC Four, BBC News, BBC Parliament, CBBC, CBeebies, BBC streaming channels. BBC HD (to March 2013) and BBC Olympics channels (2012 only). HD variants are included where applicable.

CC: Communication Chambers

Channel 3 services: the main ITV channel (previously ITV1), UTV and STV.

Channel 4 family: Channel 4, Channel 4+1, E4, E4 +1, More4, More4 +1, Film4, Film4+1, 4Music, 4seven, Channel 4 Paralympics channels (2012 only). HD variants are included where applicable.

Channel 5 family: Channel 5, Channel 5+1, Channel 5+24, 5*, 5*+1, 5USA, 5USA+1. HD variants are included where applicable.

ITV family: ITV, ITV+1 (both Network and including ITV breakfast), ITV2, ITV2+1, ITV3, ITV3+1, ITV4, ITV4+1, ITVBe, ITVBe+1, ITV Encore, ITV Encore +1, CITV. HD variants are included where applicable. This includes STV and UTV.

NAR: net advertising revenue

New form content: this includes, but is not limited to, text-based content such as blogs and articles.

Other channels: all other TV channels not included in the BBC family, ITV family, Channel 4 family and Channel 5 family.

PSB: Public Service Broadcaster or Public Service Broadcasting

PVR: personal video recorder

Red Button: BBC Red Button, an interactive service for digital TV.

Short form content: short audio visual programmes.

SOCI: share of commercial impacts

STB: Set top box

SVOD: Subscription Video on Demand

VOD: Video on Demand

Window on Creative Competition (“WoCC”): Part of BBC network television commissioning for which in-house and independent producers can compete on equal terms.