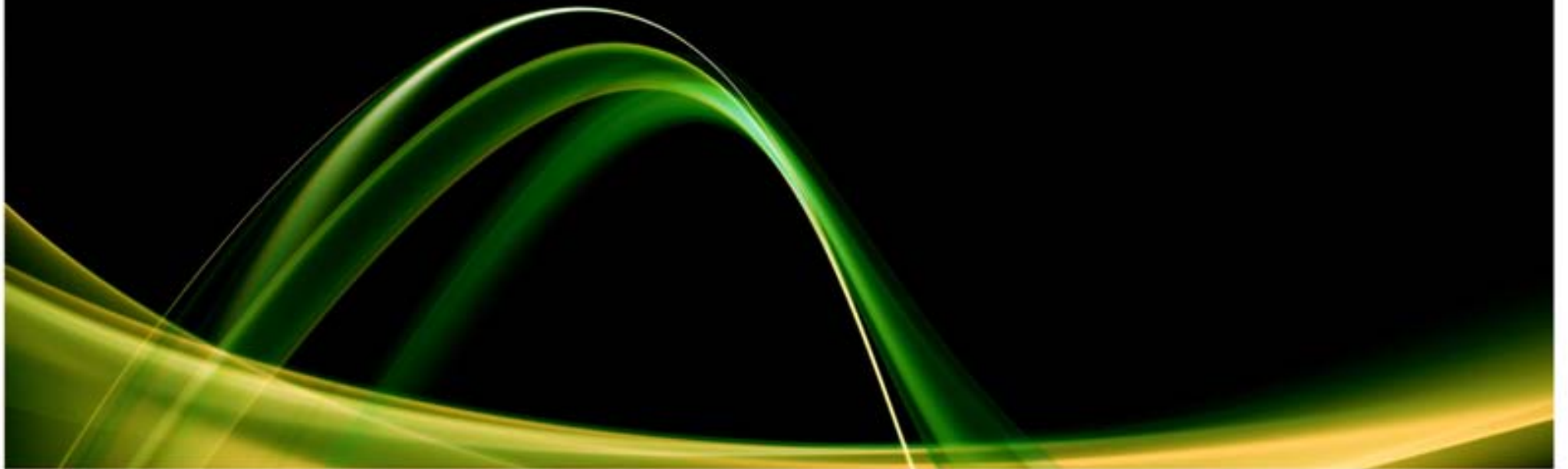




THE SUSTAINABILITY OF LOCAL COMMERCIAL TV

Prospects for big city and community local TV channels

A report for Ofcom by Oliver & Ohlbaum Associates Ltd



EXECUTIVE SUMMARY

PROSPECTS FOR LOCAL TV



Only London and Manchester can support a profitable standalone commercial local TV channel, given the levels of investment required to sustain local programming and low audience share and reach achievable by such a TV channel.

The commercial prospects for local community TV channels in regions with under 200k homes are poor. Community channels are likely to have little appeal to advertisers and will have to rely on government funding and private donations.

What are the main drivers of success/failure for local TV?

- City TV channels will need to tightly control programme costs in order to generate profits. Synergies with local newspaper newsgathering operations would need to be exploited and the cost of a high-quality network schedule would need to be amortised across a number of city channels.
- However, such levels of programme spend would limit the potential reach and audience share of a local TV channel.
- City TV channels need to generate a spot advertising CPT that is higher than the UK PSB networks. Such CPT rates might be possible given the tight local focus being attractive to local advertisers looking to use television.
- Local city TV channels would need to exploit classified advertising opportunities and provide commercial programming slots that can be used by aggregators of recruitment, property and automotive advertising.
- It is unlikely to be efficient for local city TV channels to act as classified aggregators themselves due to the high costs involved and low reach /share of the channel.

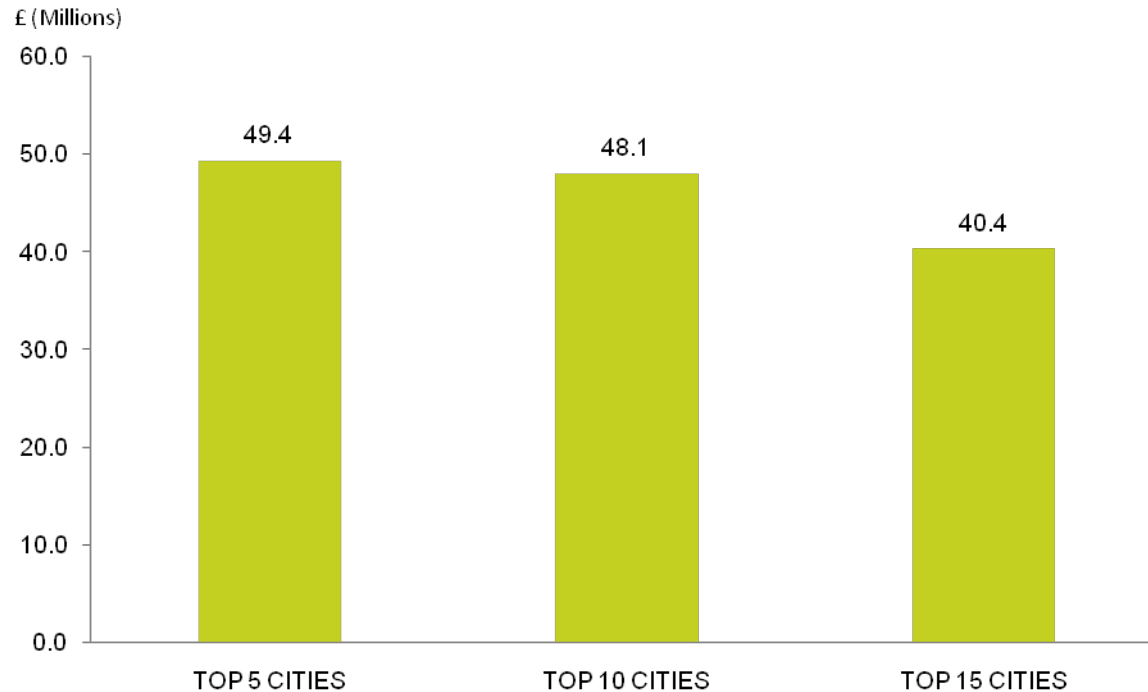
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POSITIVE SCENARIO



...if audience share is 2% and CPT is £11, then the top 15 channels can deliver cumulative operating profits of more than £40m...

Cumulative profit / loss of top city TV channels – 2% audience share and £11 CPT



What do you have to believe to make it work in the top 15 cities?

- In order for the top 15 cities to support a profitable channel, CPT rates would need to be well in excess of £11, higher than any television advertising rate achieved by UK channels and approaching rates paid by classified advertisers in local newspapers.
- Audience share would need to rise to around 2% to provide an audience big enough to allow a local city channel to break even.
- A city TV channel would need to generate yields from a classified advertising business, possibly a local directory, that are comparable to Thomson and BT, the second and third biggest providers nationally.

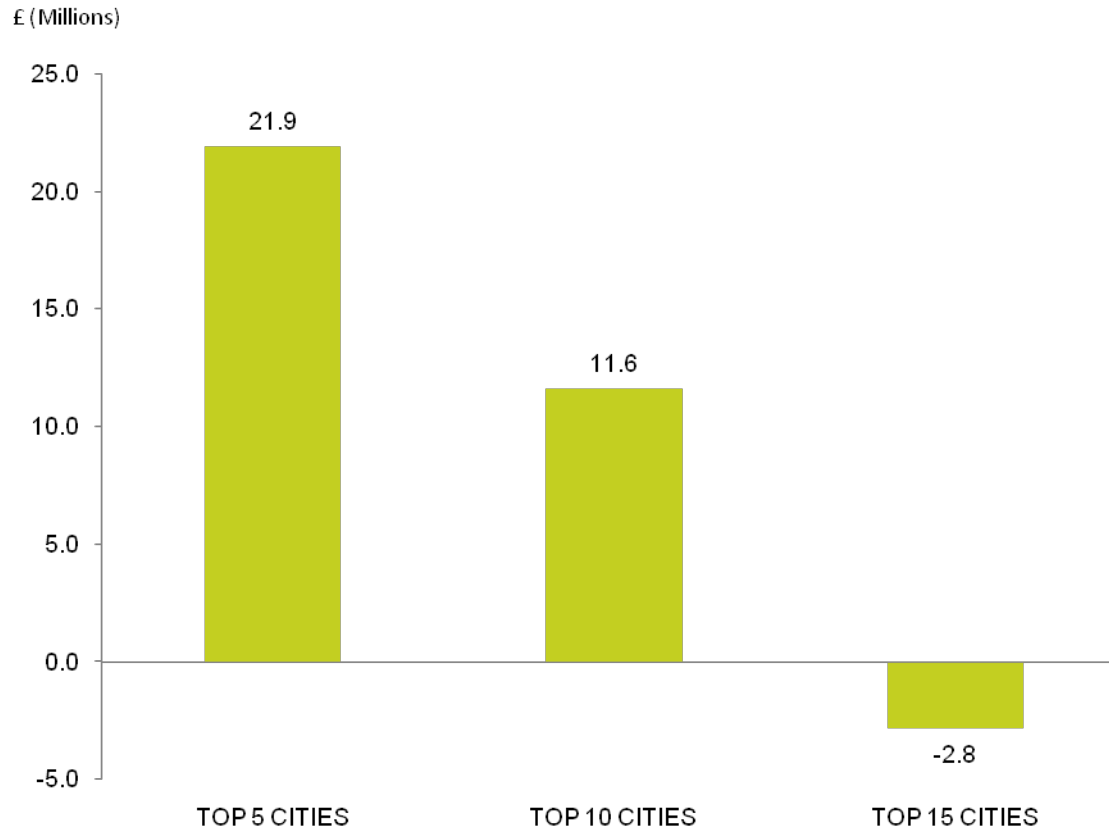
EXECUTIVE SUMMARY

A MORE REALISTIC BASE CASE



...a more realistic outcome, as modelled in O&O's base case, is that a network of the top 5 or top 10 city TV channels in the UK could generate a profit but the next 5 channels would make a combined network of 15 cities loss making...

Cumulative profit / loss of top city TV channels – O&O base case at 1.5% audience share and £7 CPT



What is a more likely base case and its implications?

- O&O's base case analysis is that an audience share no higher than 1.5% is realistic, given possible levels of investment in news and non-news output and the audiences they bring.
- Realistic CPT levels are likely to remain around £5-8 given the relatively low reach and share of a local city TV channel. This price is feasible in the context of local radio CPTs and local newspaper display advertising rates.
- Channels will be able to generate between £1m and £4m a year from commercial and sponsored programmes providing an outlet for aggregators of local classified advertising.
- Only London and Manchester could operate standalone local TV services at profit. No other UK urban area could support a profitable local TV channel based on O&O base case assumptions.
- The top ten UK cities would deliver an operating profit of around £12m per year. However, a network of the top 15 cities would make a loss of £2.8m per year.

EXECUTIVE SUMMARY

PROSPECTS FOR COMMUNITY TV



...the commercial prospects for community TV channels are poor...

What are the implications for the community TV model?

- Community TV channels are unlikely to be able to breakeven on a purely commercial basis.
- The low reach, audience share and low quality of a community TV channel will make them unattractive to local advertisers by comparison with local newspapers, directories and cinema advertising.
- Community TV channels are likely to have to rely on government grants and private donations for funding.
- In rare cases it may be possible to attract one or two major local sponsors to a community TV channel where the brand is looking for specific association with such a media outlet.

Local TV channel operating profit by size of region*



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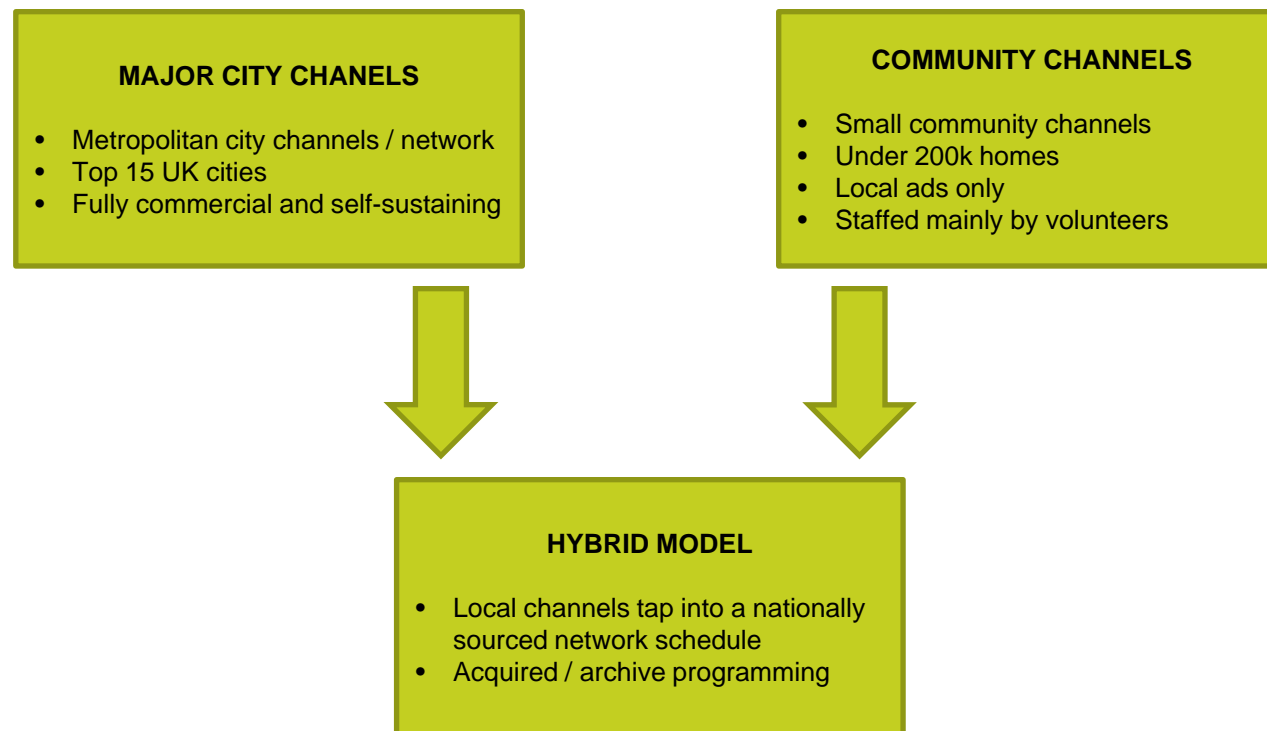
INTRODUCTION

THREE KEY MODELS FOR LOCAL TV



Advisory

...this report assesses the economic viability of a network of big city TV channels and also smaller local community stations, as well as a hybrid model where local stations can access a centrally sourced national network programme schedule...



INTRODUCTION

KEY ASSUMPTIONS AND VARIABLES



...while many different business models and assumptions could be applicable in practice, the following key assumptions and variables have been used to model a plausible base case to test the relative commercial viability of big city TV channels...

	BIG CITY CHANNEL ASSUMPTIONS	
	CHANNEL ASSUMPTIONS	COMMERCIAL RATIONALE
ACCESS TO PLATFORMS	<ul style="list-style-type: none"> • Access (on operating only cost basis) to local DTT Mux • Paid for DSAT carriage to maximise reach 	<ul style="list-style-type: none"> • DTT access in return for local news and other output guarantees
AUDIENCE SHARE	<ul style="list-style-type: none"> • Low reach and share proposition • 1.5% share (base case assumption) 	<ul style="list-style-type: none"> • Low investment in output likely to limit ability to grow audience share
ADVERTISING	<ul style="list-style-type: none"> • Predominantly local focused ad sales • Potential to sell national inventory as part of network 	<ul style="list-style-type: none"> • Opportunity to exploit latent demand for local TV advertising
COMMERCIAL & SPONSORED PROGRAMMES	<ul style="list-style-type: none"> • Classified type advertiser output • Recruitment and property focused 	<ul style="list-style-type: none"> • Strong revenues opportunity • High classified CPT rates achievable
NEWS OUTPUT	<ul style="list-style-type: none"> • 2-3 hours per day • Studio-based including 2 hour drive-time slot 	<ul style="list-style-type: none"> • Studio-based and very low cost
OTHER LOCAL OUTPUT	<ul style="list-style-type: none"> • Studio based breakfast chat style output • Local sports and lifestyle origination 	<ul style="list-style-type: none"> • Unique local TV characteristic output • Very low cost origination

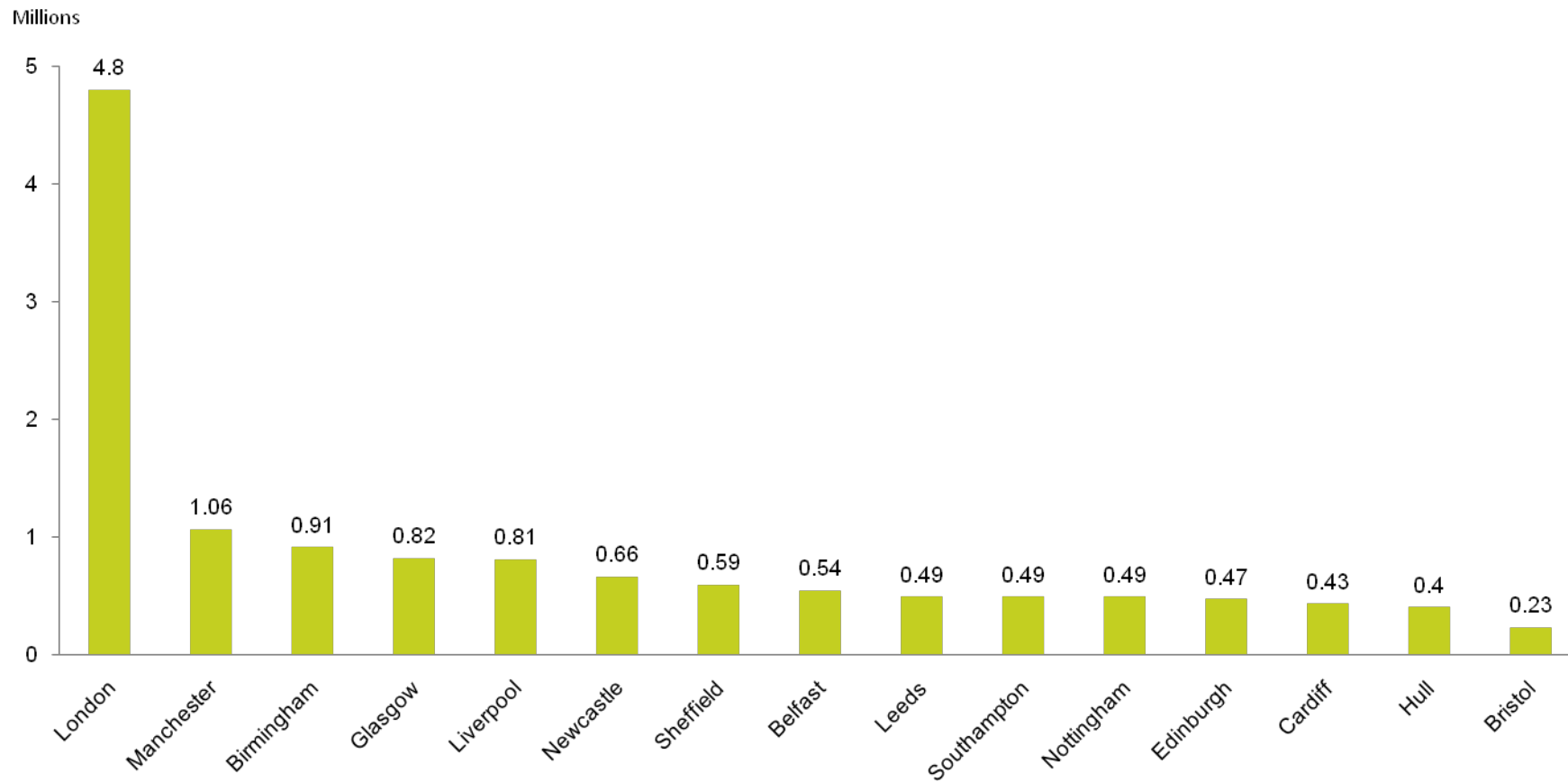
INTRODUCTION

TOP 15 UK CITIES



...the economics of a commercial TV channel focused on each of the following major urban areas has been modelled...

Number of households in the top 15 major urban areas in the UK, 2007



INTRODUCTION

CHANNEL M MANCHESTER – CASE STUDY



...Channel M is a channel serving the greater Manchester region focused on low cost local characteristic programming and locally focused advertisers looking to access audiences through dedicated commercial programming...



Channel M is owned and operated by the Guardian Media Group under a restricted service license targeting the greater Manchester metropolitan area and providing locally focused television outlet for local advertisers.

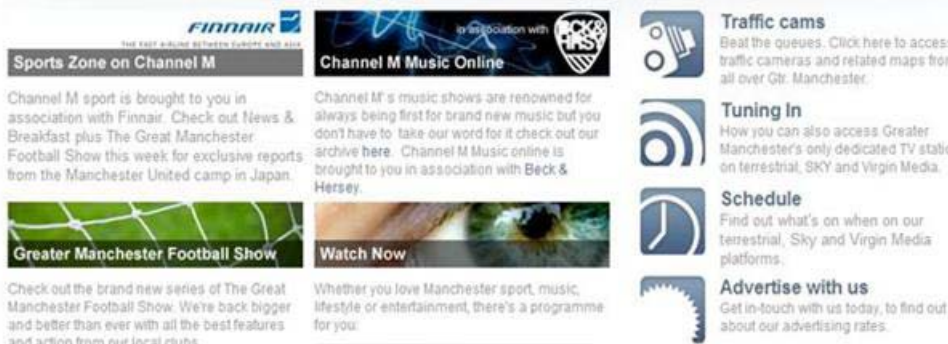
Channel M focuses its schedule around very low cost studio-based news output with a 3 hour morning breakfast show, 2 hour drive-time show as well as a 30 minute live studio news bulletins at lunchtime and late evening.

In addition to its local news output, Channel M also produces low cost local originated shows based principally on:

- Sports (The Great Manchester football Show, City Legends Debate Show etc)
- Local Lifestyle (Style in the City, Reel North, Cooking Impossible etc)
- Commercial Sponsored programmes (Jobsmine, Homesmine)
- Entertainment (City Life, Channel Macabre)
- Local Music (City Life, Music Video Shows)



Channel M originates 6 hours of local studio-based news / breakfast output and around 1-2 hours of other local output per day based around its key sports, lifestyle and music strands.



INTRODUCTION

SMALL COMMUNITY CHANNEL MODEL



...local TV channels serving regions with under 200k homes are likely to be commercially unviable and will rely on a volunteer staff and grants or donation funding...

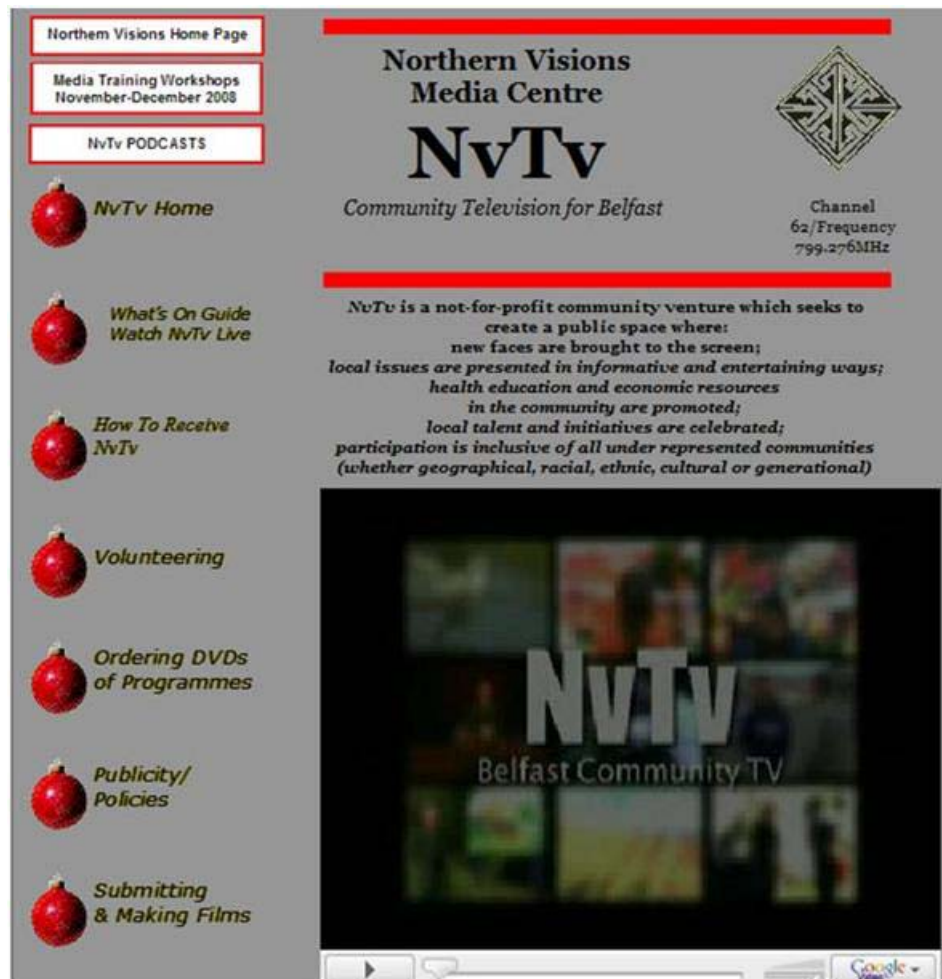
	COMMUNITY CHANNEL ASSUMPTIONS	
	CHANNEL ASSUMPTIONS	RATIONALE
ACCESS TO PLATFORMS	<ul style="list-style-type: none"> Access to local DTT Mux (on operating cost only basis) 	<ul style="list-style-type: none"> Local citizen-consumer and community value
AUDIENCE SHARE	<ul style="list-style-type: none"> 0.5% share 	<ul style="list-style-type: none"> Low investment in output likely to limit ability to grow audience share
ADVERTISING	<ul style="list-style-type: none"> None Limited channel sponsorship possible 	<ul style="list-style-type: none"> Lack of professional sales capability Lack of advertiser demand
OUTPUT	<ul style="list-style-type: none"> Local volunteer production teams Local issue programming 	<ul style="list-style-type: none"> High public value / local interest Ultra local focus
FUNDING	<ul style="list-style-type: none"> Government grants (local or national) Donations or benefactor funding 	<ul style="list-style-type: none"> Build local/community identity and provide skills, training and opportunities

INTRODUCTION

NORTHERN VISIONS BELFAST – CASE STUDY



...Northern Visions is a Belfast based community TV channel operated by volunteers and funded by grants and donations...



Northern Visions TV is a not-for-profit organisation providing a community TV service from a single transmitter to the Belfast region of Northern Ireland.

Northern Visions operates under an initial 4 year restricted Service Licence from Ofcom. The channel is operated by a volunteer staff and aims to provide alternative local television programming to that presently on offer:

“A television service which reflects and enriches the diversity of the Belfast community by presenting programmes which contribute to expanding the variety of viewpoints broadcast in Northern Ireland and enhancing the diversity of programming choices available to the general public”

The channel is funded annually by Belfast City Council, Arts Council of Northern Ireland and the Northern Ireland Film and Television Commission. This funding is for an agreed annual programme of work, which includes training workshops, educational seminars, youth production and support for individual artists.

Northern Visions Community Television Journalists' posts are funded under Measure 2.3 of the Peace II programme: Skilling and Building the Social Economy by the Community Foundation for Northern Ireland.

The channel does not currently carry advertising but is licensed to do so like any other commercial TV channel in the UK.

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ADVERTISER DEMAND FOR LOCAL TV

SUMMARY



...there is untapped local advertiser demand for local TV but the price is unlikely to be much higher than national TV channel CPT rates while opportunities to generate revenues from local directories and new media are limited...

Local advertisers have fewer outlets for their advertising spend due to a more limited range of media offering a tight local focus. However, the limited reach and share that a local TV channel can provide will limit the overall price that local advertisers will pay to access airtime on local channels.

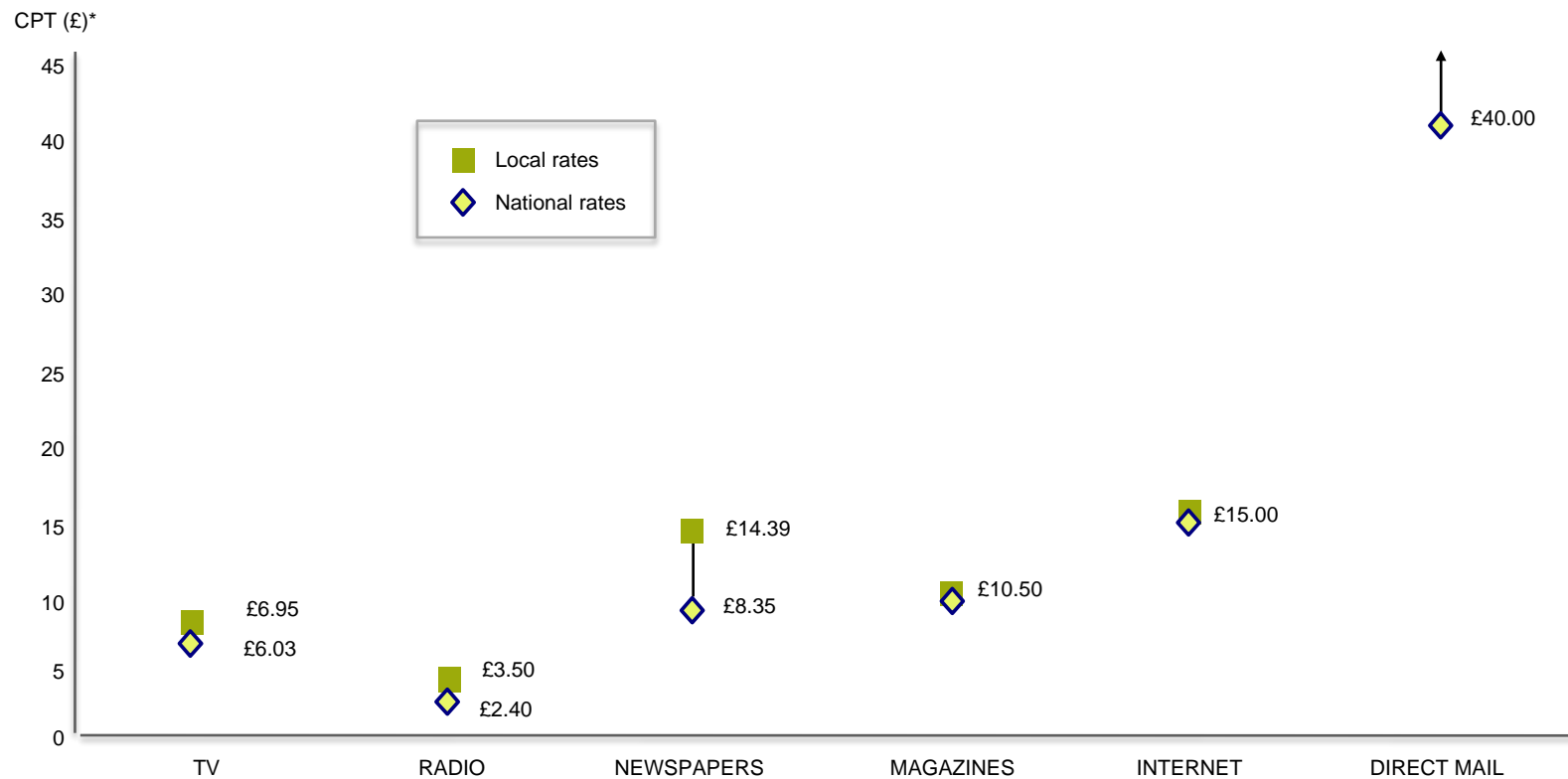
- There is little difference between local and national CPT across different media. However, local newspapers do obtain a CPT uplift from local advertisers but this is principally driven by local classified advertising for which there are few alternative outlets with high reach.
- Current evidence suggests that a CPT of £6-8 is achievable.
- O&O modeling assumes sell-out rates of 50%, growing to 70%, inline with average multichannel rates.
- Sponsorship and paid-for commercial programming is likely to generate high equivalent CPT rates of around £40, comparable to classified local newspaper rates, with jobs and property programming leading the way..

ADVERTISER DEMAND FOR LOCAL TV

LOCAL MEDIA – NATIONAL & LOCAL PRICES



...in most local media the local CPT and the national CPT rates are very similar, apart from local newspaper rates which are more expensive than national rates...



* per 30 second slot on TV ad radio, per full page advert in newspapers and magazines
Source: Oliver & Ohlbaum 2007

ADVERTISER DEMAND FOR LOCAL TV

CORE MODEL ASSUMPTIONS



Advisory

...low wastage and tight local focus is likely drive a high average station CPT of £7 while commercial programming, principally driven by recruitment and property sponsorship, generates exceptionally high CPT rates comparable with local newspaper classified adverts...

KEY MODEL ADVERTISING ASSUMPTIONS		
	ASSUMPTION	RATIONALE
CPT	<ul style="list-style-type: none"> £7 national £7 local 	<ul style="list-style-type: none"> No differentiation between national and local Slight local premium gained – low wastage
AD MINUTES	<ul style="list-style-type: none"> 8 peak 7 off-peak 	<ul style="list-style-type: none"> Standard PSB advertising minutage restrictions in return for free spectrum
SELL OUT RATES	<ul style="list-style-type: none"> 50% in 2007 / 2008 Increasing to 70% by DSO 	<ul style="list-style-type: none"> Equivalent to mid-tier multichannel rates
INVENTORY	<ul style="list-style-type: none"> 30% national 70% local 	<ul style="list-style-type: none"> Local advertiser focused proposition
SPONSORSHIP	<ul style="list-style-type: none"> £40 CPT 	<ul style="list-style-type: none"> 3-4 hours per day of Commercial programming Recruitment and property focused

ADVERTISER DEMAND FOR LOCAL TV IS THERE A STRONG NEW MEDIA OPPORTUNITY?



...while all local TV channels will need a strong website and new media presence, it is unlikely that they will be able to generate significant revenues from them in them in the medium term...

	NEW MEDIA ASSUMPTIONS
ONLINE CPT / INVENTORY	<ul style="list-style-type: none"> • High CPT rates compared to traditional TV rates • Driven by measurability, response-based and targeted advertising models • £10 - £15 CPT assumed • Only 4-8 ad spots possible within an hour of online programming
LOCAL ONLINE VIEWING	<ul style="list-style-type: none"> • Currently 48% of people view online videos, rising to 70% by 2015 • The average "user" views 20 videos per month, rising to 30 by 2015 • Less than 30 mins average online video viewing per day
ONLINE VIEWING SHARE	<ul style="list-style-type: none"> • Online viewing share proportional to traditional TV viewing • Directly related to branding, investment in advertising and quality of experience • Large national broadcasters and content providers likely to dominate online viewing • Share likely to equal that of core linear channel

While it will be possible to generate some revenues from online video advertising, local TV channels will struggle to generate enough revenue online to cross-subsidise a loss making linear channel.

Low overall levels of online video viewing, when compared to linear viewing, will limit the available impacts available to advertisers when compared with linear TV channels, whether national or local.

Limited inventory in a single hour of online TV viewing will reduce yields. Viewers will only tolerate 1-4 minutes of advertising within an hour of video online compared to the 7-12 minutes broadcast on linear channels.

Channel websites are only likely to achieve a low online viewing share, in proportion to the viewing share and brand strength of the linear channel.

Low reach and share of local TV channel websites will also limit appeal to local advertisers, limiting the CPT price when compared to higher-reach local newspapers and directories.

With limited online reach, local TV channels will struggle to develop alternative online business models based around user generated content, dating, classified advertising and social networking.

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THE ECONOMICS OF LOCAL NEWS

SUMMARY



...the cost savings that can be made as a result of being part of an integrated newsroom, as part of a major local newspaper, provides significant cost savings in the provision of local TV news...

It is possible to provide a compelling local TV news service for a major city at under £1m per year.

However, to achieve this low cost base, integration with an existing (newspaper) newsgathering operation is vital and the levels of output and quality that can be achieved are limited. As a result, significantly higher investment will be required by any channel wishing to generate audience share of above 1.5%.

- Local TV news costs for a big city channel have been forecast assuming integration with a major local newspaper.
- Traditional TV news costs would suggest that the minimum spend required to provide a 24/7 standalone news service is in the region of £2-3m per year.
- However, O&O modeling assumes no news is produced over weekends and that breakfast news uses clips recorded the day before, allowing a single team working weekdays only to produce all output.
- The saving is likely to amount to £1m a year with fewer broadcast journalists, editors and directors required as a result.

THE ECONOMICS OF LOCAL NEWS

LOCAL NEWSGATHERING - VALUE CHAIN



...a UK TV newsgathering operation has an extended value chain, with complex operations. The synergies with local newspapers could be important but limited...

Principal areas of activity include:

Local newsgathering value chain

Field Operations

Gathering news footage / material from the scene

Field Operations



Infrastructure

The fixed assets required to handle multiple sources and produce news packages

Infrastructure



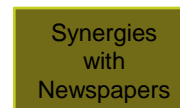
Programming

The assets required to produce news programming output

Programming



Dark shaded elements are where synergies can be exploited with a local newspaper:



There are only limited parts of the TV news value chain where synergies with local newspapers can be exploited. These related mainly to newsgathering activities.

THE ECONOMICS OF LOCAL NEWS

CORE ASSUMPTIONS



...local news is likely to be the cornerstone of any city TV channel with high output levels likely, including a 2 hour early evening studio-based show...

	BASIC ASSUMPTIONS
LOCAL NEWS OUTPUT	<ul style="list-style-type: none"> • 3 hours / day • 1095 hours / year • Lunchtime and late evening 30 minute bulletins • 2 hour early evening drive-time studio show
COSTS	<ul style="list-style-type: none"> • £800 / hour • Studio based presentation • Voice over pre-recorded video clips
SYNERGIES	<ul style="list-style-type: none"> • Significant newsgathering synergies with local city newspaper operation • Approximate value of £1m a year saving on broadcast journalists and editors • Halves the cost of TV news output compared to a standalone operation

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NON-NEWS ORIGINATION AND A NETWORK SCHEDULE

SUMMARY



...both local origination and access to a network schedule would have to be extremely cheap, limiting the ability of a local TV channel to deliver strong reach and an audience share...

A big city local TV channel would need to keep its total programme budget to under £2.5m. Even at this level it will be very difficult for many cities to support a profitable commercial local TV channel given the audience share levels attainable with this level of programme investment.

- Aside from news, a local schedule would be made up of a cheap breakfast show, limited levels of other original output, repeats and a network schedule.
- O&O have assumed a low cost breakfast show is produced while only around 1-2 hours of other local origination is produced per day.
- The bulk of the off-peak schedule and overnight is likely to be populated with repeat showings of locally produced output.
- A centrally sourced network schedule would provide around 6 hours a day of acquired output. Such network programming would be sourced centrally for around £1500 per hour which is comparable to many general entertainment thematic channels.
- Local output is unlikely to gain an audience share of more than around 0.5%. Similarly, a network schedule sourced at cost levels comparable to a multi-channel is unlikely to generate an audience share above 0.5%.
- Local news might generate a stronger audience share of up to 5% given strong consumer demand and a weakening level of provision elsewhere.
- A combined channel is likely to be able to achieve an audience share of around 1.5%.

NON-NEWS ORIGINATION AND A NETWORK SCHEDULE

LOCAL ORIGINATION



...most city stations will only be able to sustain a minimal amount of local origination and £2-3k per transmitted hour...

	LOCAL ORIGINATION - BASIC ASSUMPTIONS
LOCAL ORIGINATED OUTPUT	<ul style="list-style-type: none">• 2 hours / day• 730 hours / year
COSTS	<ul style="list-style-type: none">• Low end local production costs kept to absolute bare minimum• £1500 cost per hour
SYNERGIES	<ul style="list-style-type: none">• It is unlikely that there are any synergies or cost efficiencies to be gained from working as part a local newspaper group• Local feel and low quality production quality

NON-NEWS ORIGINATION AND A NETWORK SCHEDULE

THE NETWORK SCHEDULE COSTS



...the network schedule costs have been kept to a bare minimum at an average of £1500 per output hour amortised equally across 15 channels...

NETWORK SCHEDULE OUTPUT - BASIC ASSUMPTIONS	
NETWORK OUTPUT	<ul style="list-style-type: none">• 6 hours per day• Centrally / nationally sourced• Acquired / archive programming only
COSTS	<ul style="list-style-type: none">• £1500 per hour national cost• Equivalent to the average programme spend per transmitted hour of multi-channels• £100 per hour for each of 15 stations

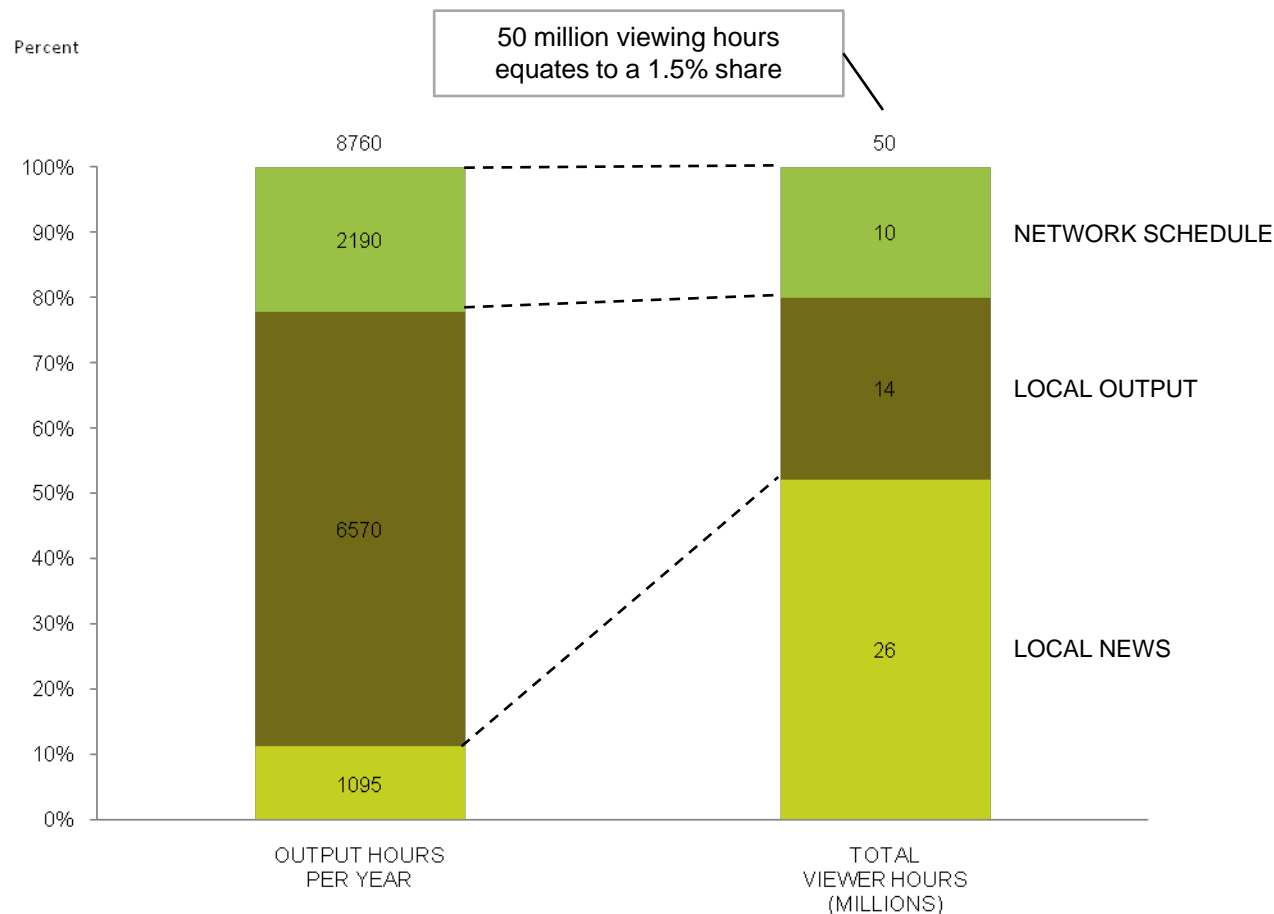
NON-NEWS ORIGINATION AND A NETWORK SCHEDULE

LIKELY AUDIENCE SHARE



...a local channel could achieve 1.5% audience share if it can generate a 5% share from 3 hours a day of its local news output and 0.5% share on both network schedule and local originated output...

Example output hours and total viewer hours by type of programming, year three of operation



A local TV channel with a strong local news offering can potentially achieve an overall audience share of around 1.5%. This is based on an uplift on the non-news schedule provided by a strong local news audience.

Non-news output is assumed to gain a 0.5% share, the maximum theoretically possible based on the levels of programme spend equivalent to a typical multi-channel and the share achieved by these channels.

Three hours of local news is assumed to gain a 5% audience share, given strong viewer demand for local news, with a significant weakening elsewhere.

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OVERHEADS AND FIXED COSTS

SUMMARY



...overheads and fixed costs are likely to be high, relative to achievable revenue levels, and will make it very difficult for a local TV channel to breakeven...

O&O have modeled big-city local TV channel costs. Total fixed costs are likely to be around £2.5m for any big-city channel.

- Transmission and play out is likely to cost around £0.4m but given the 30% reach of DSAT it is unlikely that any generating over £1.5m in revenues would not gain DSAT carriage.
- Modeling currently assumes no costs relating to DTT bandwidth.
- O&O have assumed that all fixed costs inflate at RPI in each year modeled to 2020.
- A total of 31 full time staff are assumed to be required to cover all areas of output and commercial activity. On-screen talent costs are covered in the previous section and included as programme spend.

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COMMERCIAL VIABILITY OF BIG CITY CHANNELS

SUMMARY



...London is the only UK metropolitan area which is big enough to sustain a comfortable profitable local TV channel on a standalone basis...

Only London and the greater Manchester region in the UK outside are likely to be able to sustain a profitable local TV channel.

- Based on the assumptions outlined earlier in this pack , only London and greater Manchester in the UK are able to support a profitable standalone local TV channels.
- A CPT rate of £11 would have to be achieved in order for the top 5 biggest UK cities to support a profitable local TV channel. This is unlikely to be an achievable CPT rate for any big city channel.
- An audience share of 2% would be required in order for the top 5 biggest cities to support a break-even local TV channel. Given the analysis of programme spend and audience share achievable it is unlikely that a channel could generate this required uplift in audience share.

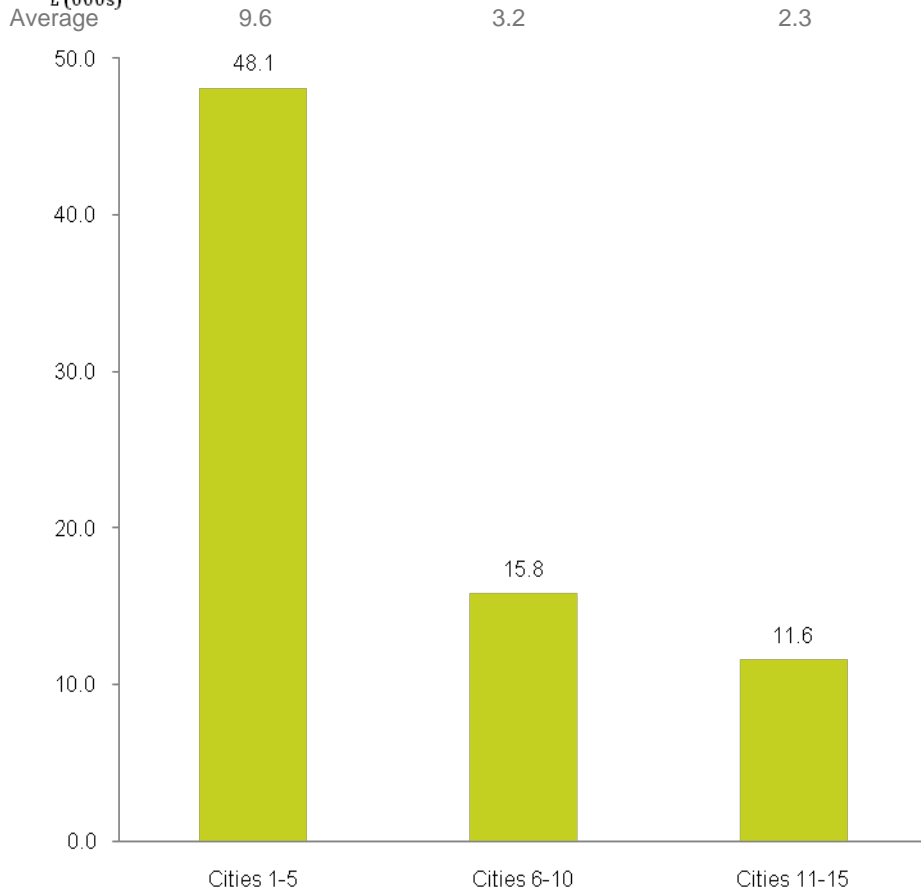
COMMERCIAL VIABILITY OF BIG CITY CHANNELS

COMBINED REVENUES AND OPERATING PROFITS



...only the biggest UK cities can support standalone profitable city TV channels – the top 5 biggest UK cities could generate a combined £22m in operating profits but the next 5 biggest cities combined would lose around £10m a year...

Total combined revenues for top city TV channels by rank size*
£ (000s)

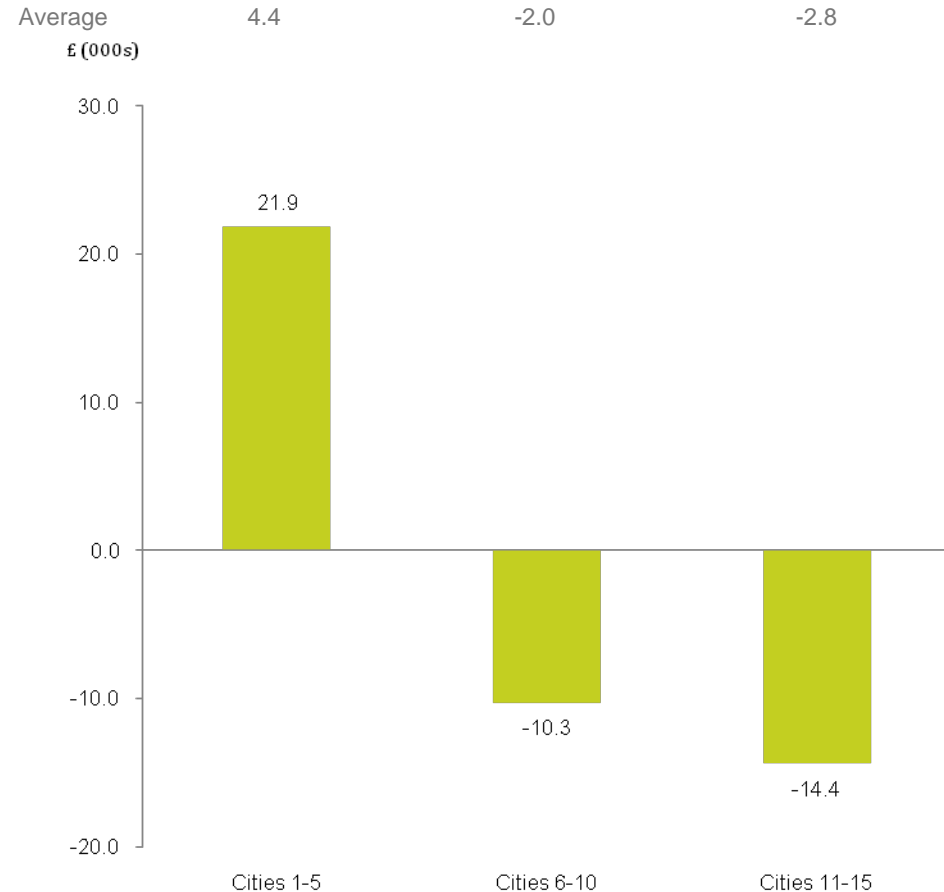


Top UK cities ranked by size (1 = biggest = London)

* Year three of operation

Source: Oliver & Ohlbaum

Total combined operating profits for top city TV channels by rank size*



Top UK cities ranked by size (1 = biggest = London)

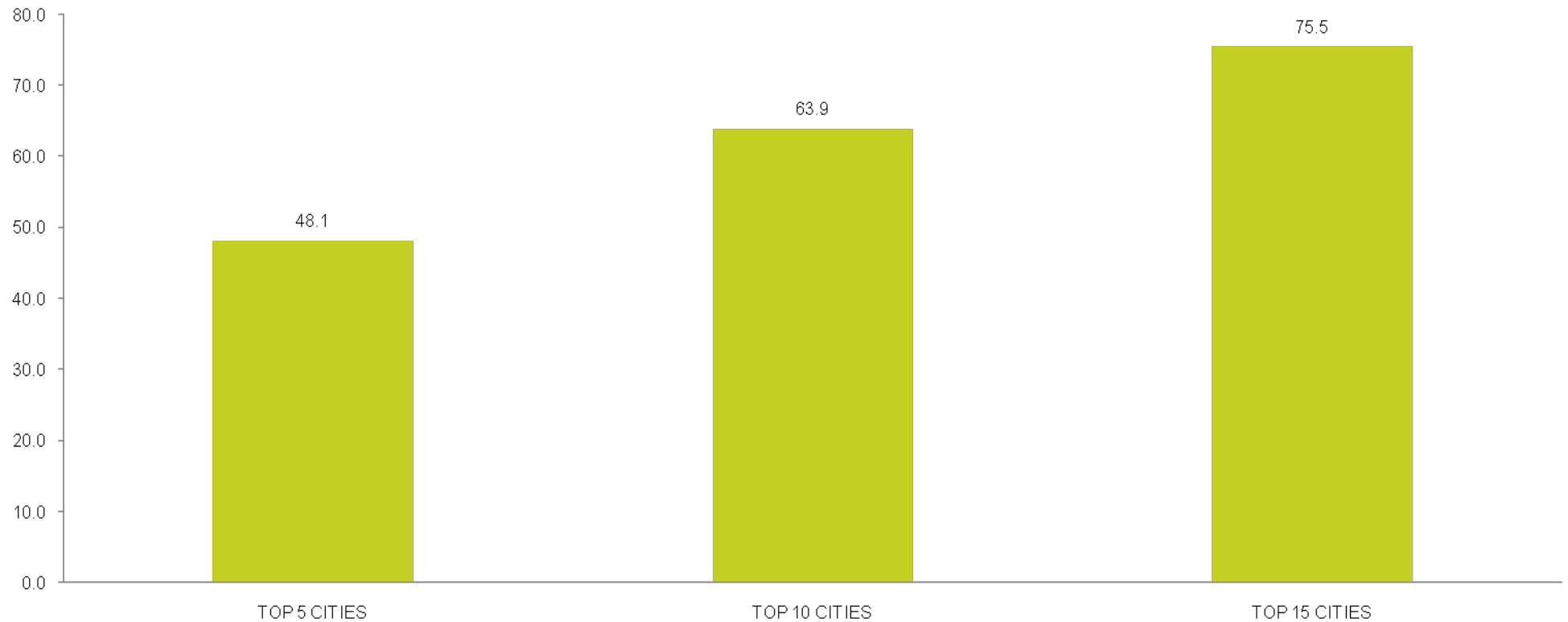
COMMERCIAL VIABILITY OF BIG CITY CHANNELS

REVENUES BY CITY CHANNEL



...the top 15 metropolitan regions combined could generate revenues or £75.5m a year, based on a 1.5% share of viewing...

Forecast major UK City commercial TV channel combined revenues (year three of operation)
£ (MILLIONS)



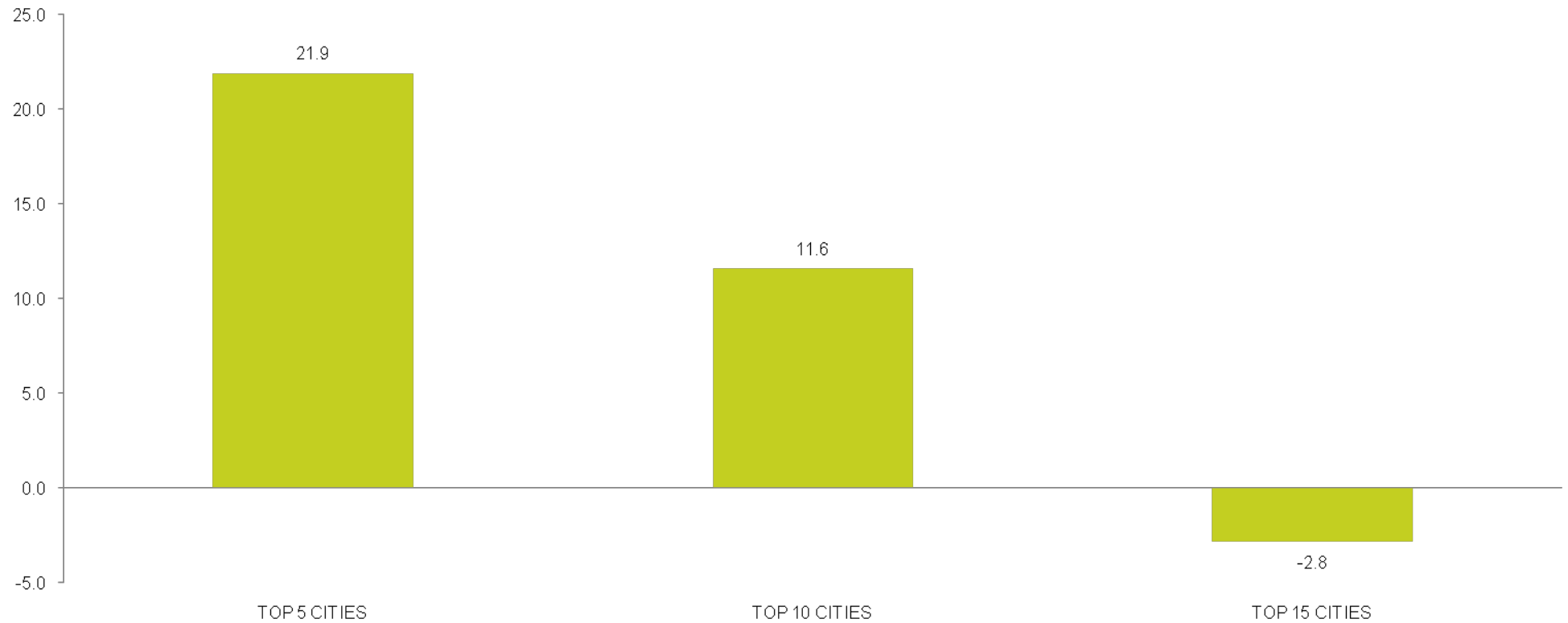
COMMERCIAL VIABILITY OF BIG CITY CHANNELS

OPERATING PROFIT BY CITY CHANNEL



... the top 10 UK cities combined could generate a positive operating profit (at 1.5% audience share for each channel), but the top 15 cities would make a combined loss...

Forecast major UK City commercial TV channel combined operating profit (year three of operation)
£ (MILLIONS)



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WHAT WOULD MAKE A CITY TV NETWORK WORK?

SHARE AND REACH



...an audience share uplift to 2% is required for all of the top five cities in the UK to support a standalone profitable local TV channel...

O&O's base case assumes a 1.5% audience share for a local TV channel, based on realistic audiences that could be gained from a local news output, other local origination and a network schedule.

This audience would need to increase by a third in order for all of the top 5 UK cities to become profitable on a standalone basis.

- O&O's base case assumes that the non-news schedule can generate an average audience share of around 0.5%. This is based on the likely level of investment in programmes and comparative shares achieved by other UK channels.
- It is unlikely that a local TV channel could increase its audience share gained by either the network schedule output or non-news original productions. The investment levels required to increase the share of these parts of the schedule are beyond the projected finances of such a local TV channel or network of channels, even at 2% share.
- Therefore, any uplift in share would need to be derived from local news output. To lift the entire channel to 2% share the share of each hour of news output would need to rise by 64%, taking the average audience share of local news to 8.2%.

WHAT WOULD MAKE A CITY TV NETWORK WORK?

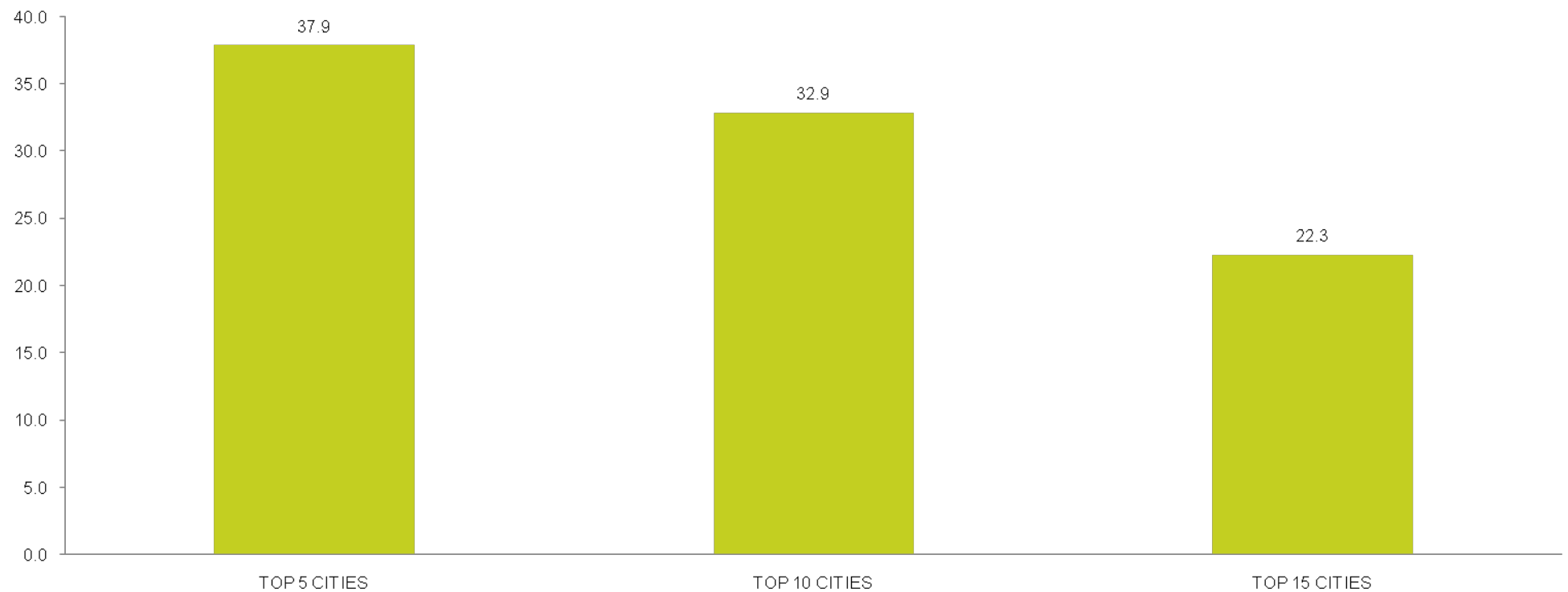
AUDIENCE SHARE SENSITIVITY



...if big city channels achieve an audience share of 2% (1.5% assumed for base case) then a network of the 15 top cities in the UK could generate a combined operating profit, despite smaller cities being loss making on a stand alone basis...

Forecast major UK City commercial TV channel combined operating profit (year three of operation): audience share = 2%

£ (MILLIONS)



WHAT WOULD MAKE A CITY TV NETWORK WORK?

CPT



...CPT uplift to £11 would be required in order for all of the top 5 UK cities to support a standalone profitable local TV channel...

O&O's base case assumes that local city TV channels can generate a CPT of around £7.

The standard spot advertising rate would need to rise to around £11 for all of the top 5 cities in the UK to generate a profit on a standalone basis.

- A CPT uplift to £11 could only be derived if advertisers believe that such a TV channel brings significant benefits beyond big city radio stations which trade at much lower rates below £3, as shown in section 1.
- This rate of CPT would take the channel CPT's above the highest received for any national TV network averages.
- UK big city average radio weekly reach averages 25% in the UK and so a TV channel looking to raise CPT levels well in excess of local radio levels, towards those of classified print advertising, would need generate a weekly reach greater than this level.
- A channel generating an average audience share of 1.5% might be able to generate an average weekly reach of 20-30%, given comparable reach to share ratios achieved by UK television channels.

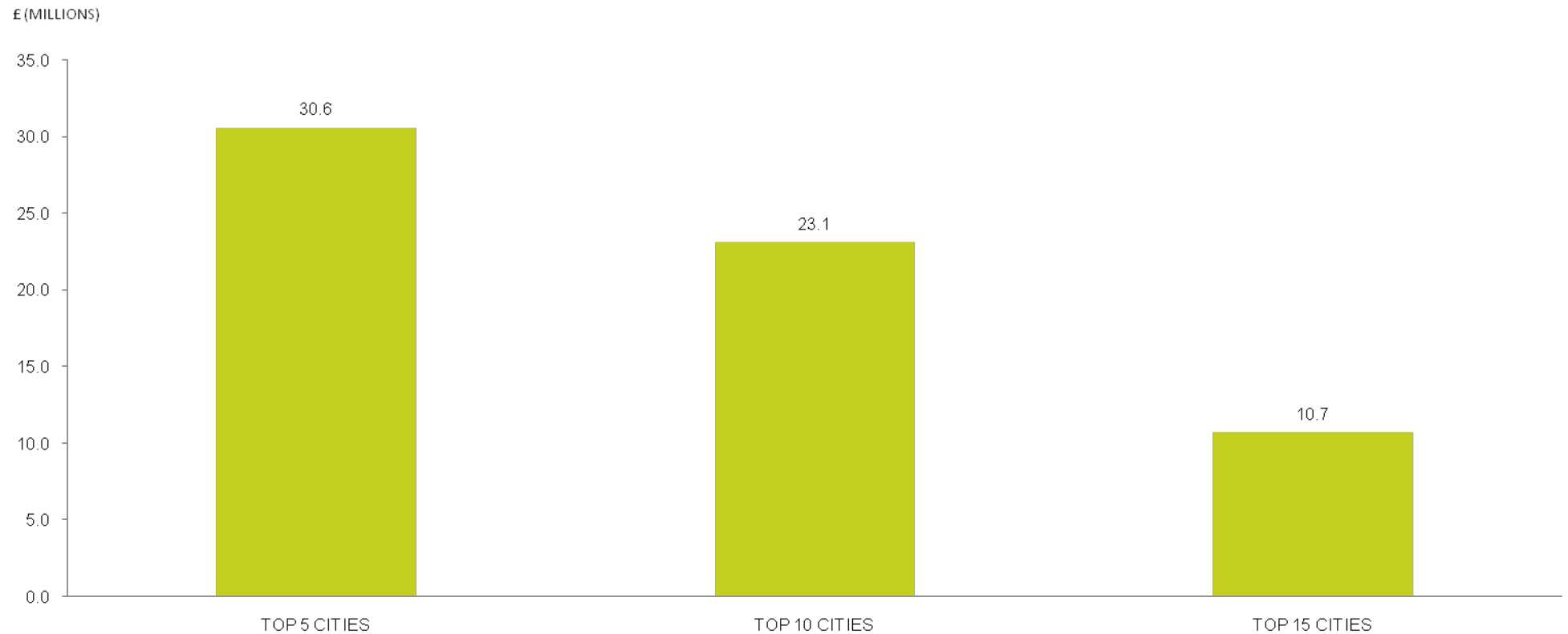
WHAT WOULD MAKE A CITY TV NETWORK WORK?

CPT SENSITIVITY



...big city channels achieving 1.5% share need to sell at a CPT rate of £11 in order for the top 5 UK metropolitan areas to break even at the operating level. It is highly unlikely that a channel could achieve this with low reach and share...

Forecast major UK City commercial TV channel combined operating profit (year three of operation): CPT = £11



WHAT WOULD MAKE A CITY TV NETWORK WORK? GREATER SYNERGIES WITH A LOCAL NEWSPAPER NEWSROOM



...while further news cost synergies are possible, it is unlikely that they would total more than around £140k for any individual channel, to small a figure to allow loss making channels to turn profitable...

O&O's base case assumes that local TV channels provide more than 3 hours of local news output for an annual cost of under £1m.

It might be possible to take advantage of further cost synergies to reduce the overall cost of local TV news output further.

- Providing news programming at this cost levels relies on deep synergies with a local newspaper newsgathering operation. The O&O base case assume that around £1m of cost can be saved by such synergies and by only producing news 5 days a week during the daytime only, so requiring only one shift.
- Further cost synergies may be possible if no TV specialist broadcast journalists or directors are used and that only local TV camera crews film stories provided by local newspaper journalists which are then edited and voiced over at the studio.
- The cost saving of such a move would only equate to around £140k per year, given the low level of cost already assumed for the base case.

WHAT WOULD MAKE A CITY TV NETWORK WORK? A BREAKTHROUGH INTO CLASSIFIED ADVERTISING?



...in order to generate substantial contribution from a classified directories business a local TV channel would need to invest heavily and incur early trading losses and achieve 3rd place in the market...

O&O's base case assumes that local TV channels can generate substantial revenues from commercial programming providing an outlet for classified advertising aggregators such as recruitment, property and automotive groups.

A local TV channel group could look to cross-subsidise a loss making main channel with a classified advertising business based around local directories,

- Directories are the main media used by classified advertisers after local newspapers. A channel setting up a directories business would distribute to 100% of homes in a region and look to increase yields per home over the first 4-5 years of operation.
- The UK local consumer directories market is worth £944m but 97% of the market value is generated by just three players, Yell, Thomson and BT.
- O&O has modelled the yield required for a new directory to provide enough contribution to cross-subsidise a local TV channel profitable.
- To generate a £1m contribution from a directories / classified business, a new directory would need to generate a yield of £4 per household distributed. This yield level is equivalent to Thomson or BT average yields, the number two and three directories providers in the UK respectively.
- For this success to be achieved you would have to believe that a 20% reach local channel could act as a strong enough marketing tool to drive the required level of yield.
- Directories businesses are expensive to establish, making heavy early trading losses due to much lower yields in years 1-3 of operation. A £1m annual contribution would only be generated after 5 years of operation.

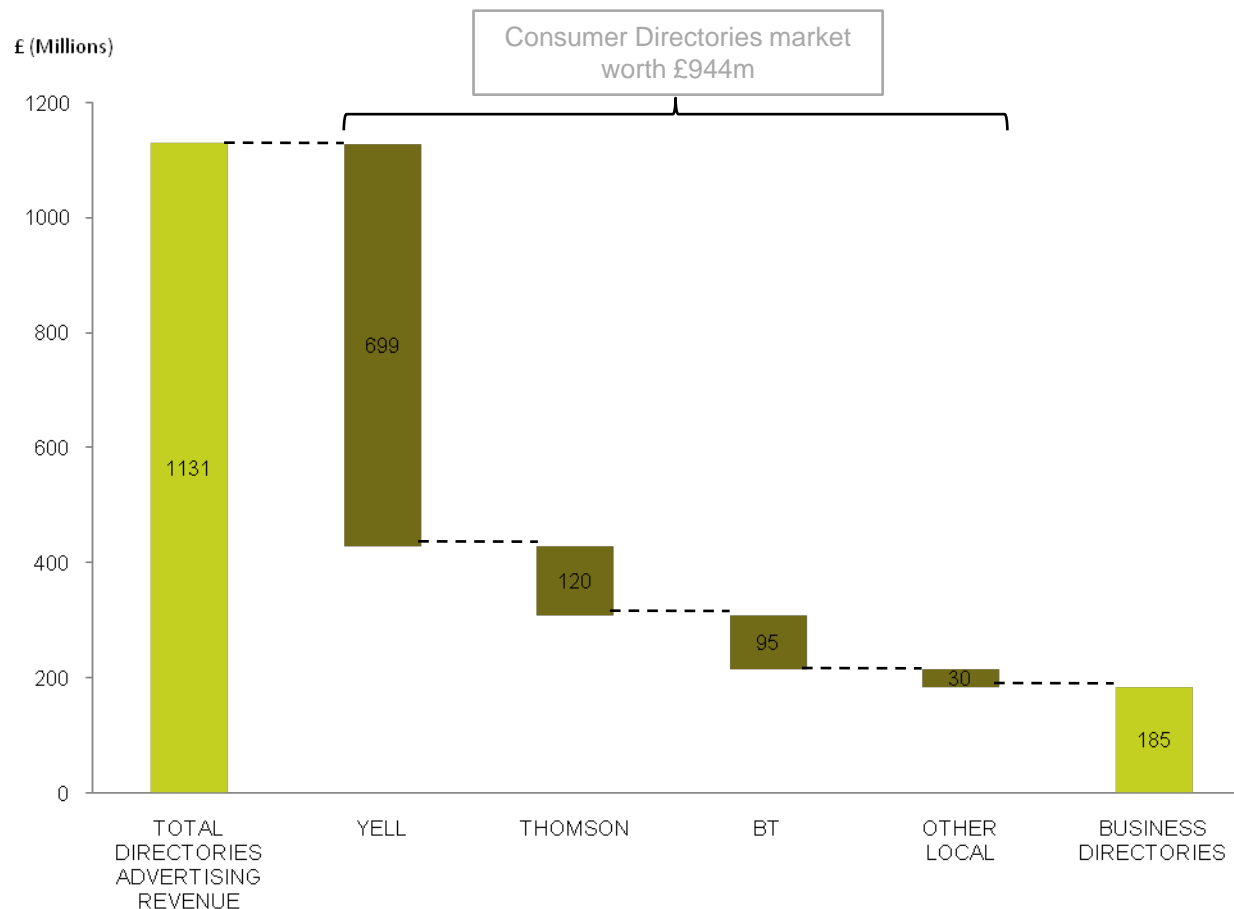
WHAT WOULD MAKE A CITY TV NETWORK WORK?

DO DIRECTORIES OFFER A REVENUE GENERATING OPPORTUNITY?



...the UK consumer directories market is dominated by Yell, Thomson and BT, limiting the opportunity for local newspapers and other potential local directories providers to just £30m per year...

UK consumer directories advertising income and business directories income, 2006



After local newspaper and cinema advertising, local directories are the only major outlet for local advertisers providing high levels of reach. However, local directories are unlikely to provide a strong complementary revenue stream for local TV channel providers.

The local directories market is dominated by Yell, Thomson and BT with only a small market share remaining for alternative local providers.

In addition to the small scale of the potential opportunity, the local classified market is most vulnerable to local internet providers and is suffering from general structural decline of print-based classified advertising.

WHAT WOULD MAKE A CITY TV NETWORK WORK?

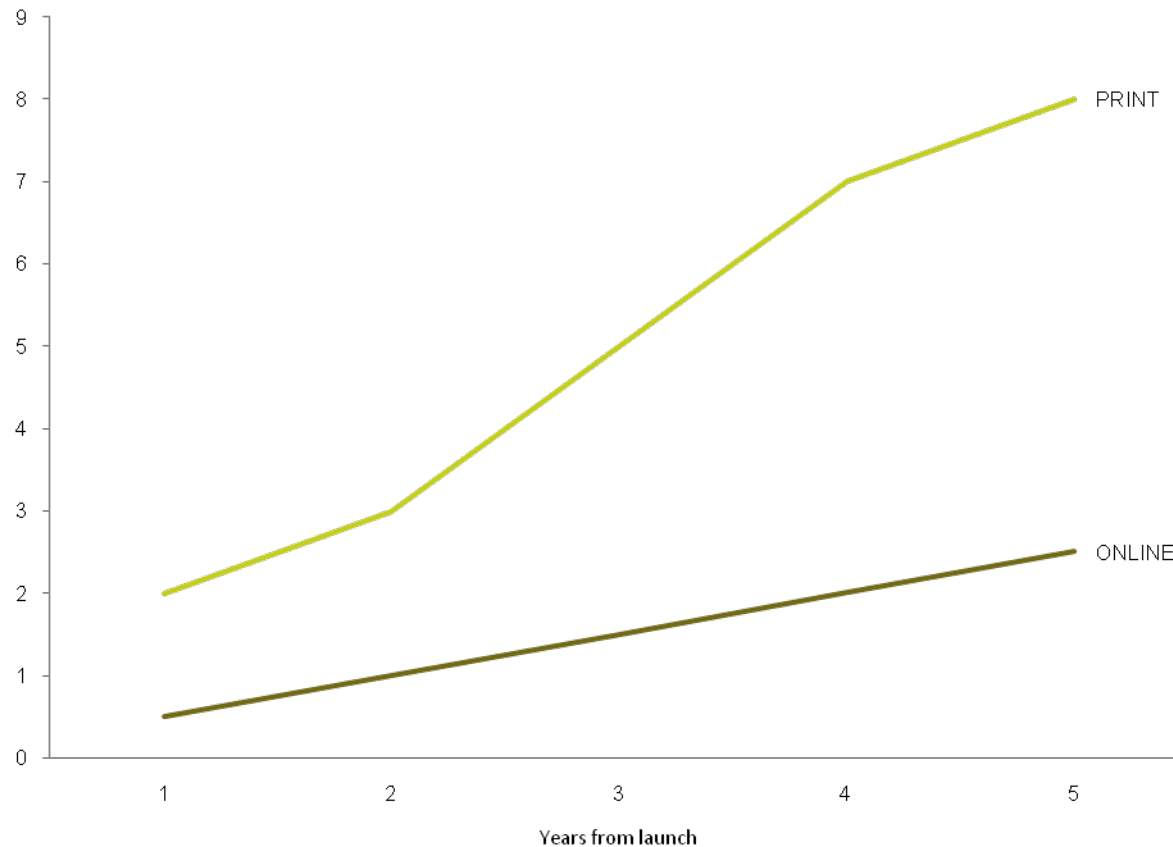
DIRECTORIES YIELDS PER HOUSEHOLD



...print directories generate considerably higher yields than online directories so total revenues will fall in the future as directory usage moves online...

Directories yield / revenue per household distributed for print and online

£ / Household



Online yields from directories are considerably lower than those achieved for print directories businesses.

Over time as classified directories move usage online the overall revenue of the operation are likely to enter decline, only partially offset by lower costs.

WHAT WOULD MAKE A CITY TV NETWORK WORK? A CROSS SUBSIDY ACROSS A NETWORK OF CITY TV CHANNELS



...a network of the top cities in the UK can generate a cumulative operating profit, implying a significant cross subsidy by a London channel...

O&O's base case modelling suggests that a network of the top 5 or 10 UK city TV channels could generate a strong operating profit but that if the next 5 biggest cities are added the network would become unprofitable.

- The top 5 UK cities would cumulatively generate an operating profit of £22m while the top ten would generate £11.6m.
- However, the top 15 cities would cumulatively lose nearly £3m in the third year of operation.
- There are few benefits to a cross-subsidy via pro-rating the network schedule payments as these amount to only £200k per year per channel (£3m per year in total).

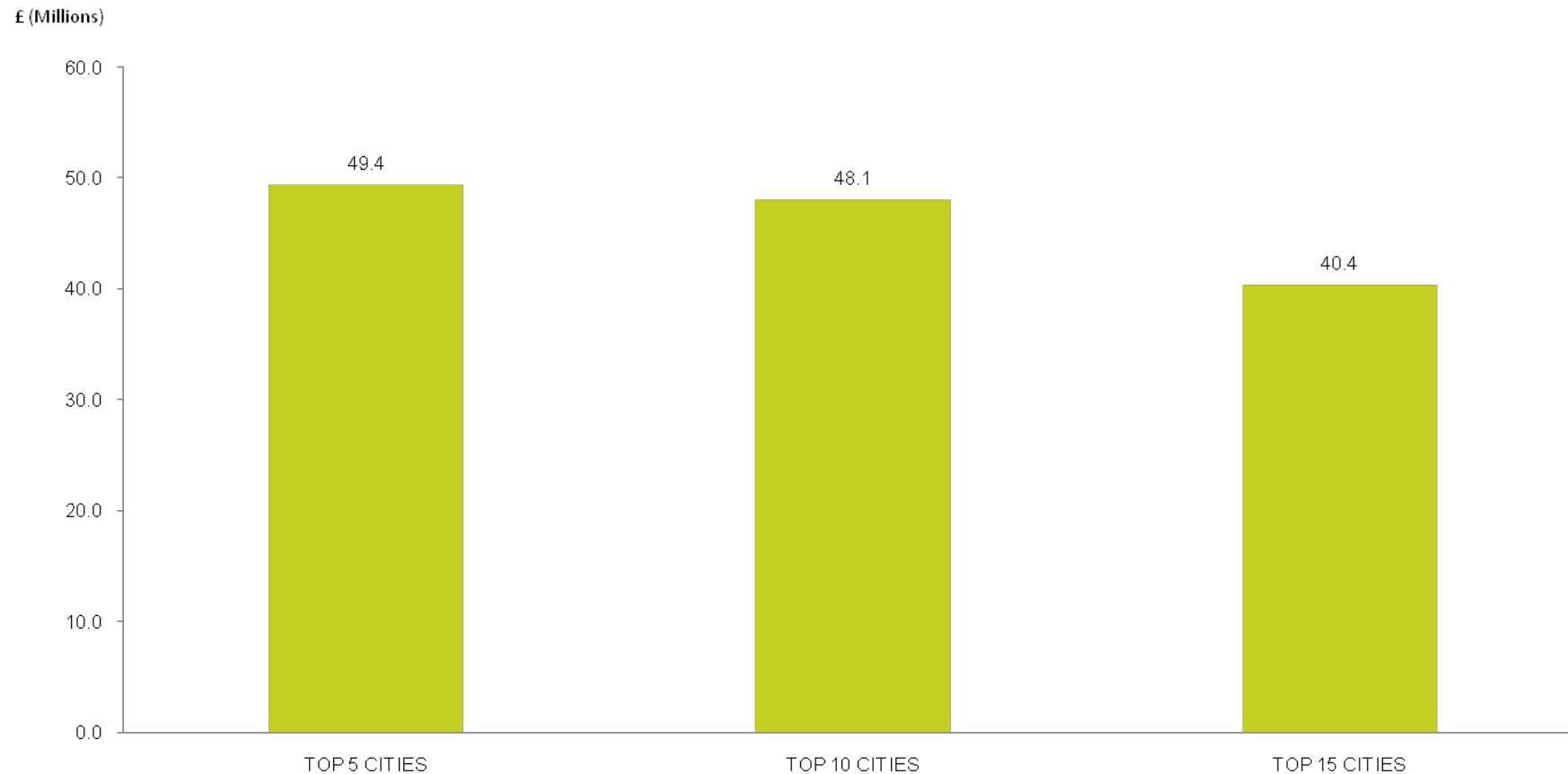
WHAT WOULD MAKE A CITY TV NETWORK WORK?

A CROSS SUBSIDY ACROSS A NETWORK OF CITY TV CHANNELS



...if audience share is 2% and CPT is £11, then a network of the top 15 channels can deliver cumulative operating profits of more than £40m...

Cumulative profit / loss of top city TV channels – 2% audience share and £11 CPT



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COMMUNITY TV VIABILITY

SUMMARY



...community TV stations are unlikely to be commercially viable, given small areas targeted and low reach and share achievable...

Community stations are likely to be highly unprofitable, even if they were able to sell airtime or gain programme sponsorship revenues. Community TV stations are likely to have to survive on government funding, grants and donations.

- Even assuming a volunteer work force, regions with under 200k homes would struggle to generate more than £200k in revenues making them significantly unprofitable given the bare minimum likely costs base of £300k.
- Even though local advertisers have few choices beyond local newspapers at the ultra local level, the low reach and low quality of a local TV channel is unlikely to prove attractive for advertisers.
- This is true of commercial radio stations which are generally unprofitable in small town and rural areas.
- There is no evidence to suggest that community stations could provide the kind of reach required to attract the high CPTs achieved by local newspapers, given the very low reach achievable by community TV channels.
- There are few incentives for local newspaper to invest in or cross-subsidise local community TV channels. Funds would be more rationally directed if invested directly in the papers own website and local video content.

COMMUNITY TV VIABILITY

ADVERTISER CHOICE AT LOCAL LEVELS



Advisory

...local markets under 0.5m population are only comprehensively covered by local newspapers, Cinemas and directories.
There may therefore be an opportunity for further Restricted Service Licence TV stations...

MEDIA	LOCAL AREA POPULATION SIZE AND % OF UK REGIONS COVERED BY EACH MEDIA				
	>2M	1M TO 2M	0.5M TO 1M	0.2M TO 0.5M	<0.2M
LOCAL COMMERCIAL RADIO	12%	26%	34%	27%	1%
ITV REGIONS	80%	15%	4%	1%	0%
LOCAL PRESS	-	-	-	3%	95%
CINEMAS	-	-	-	10%	90%
DIRECTORIES	-	-	5%	30%	60%
RSL TV CHANNELS	-	-	-	5%	2%

COMMUNITY TV VIABILITY

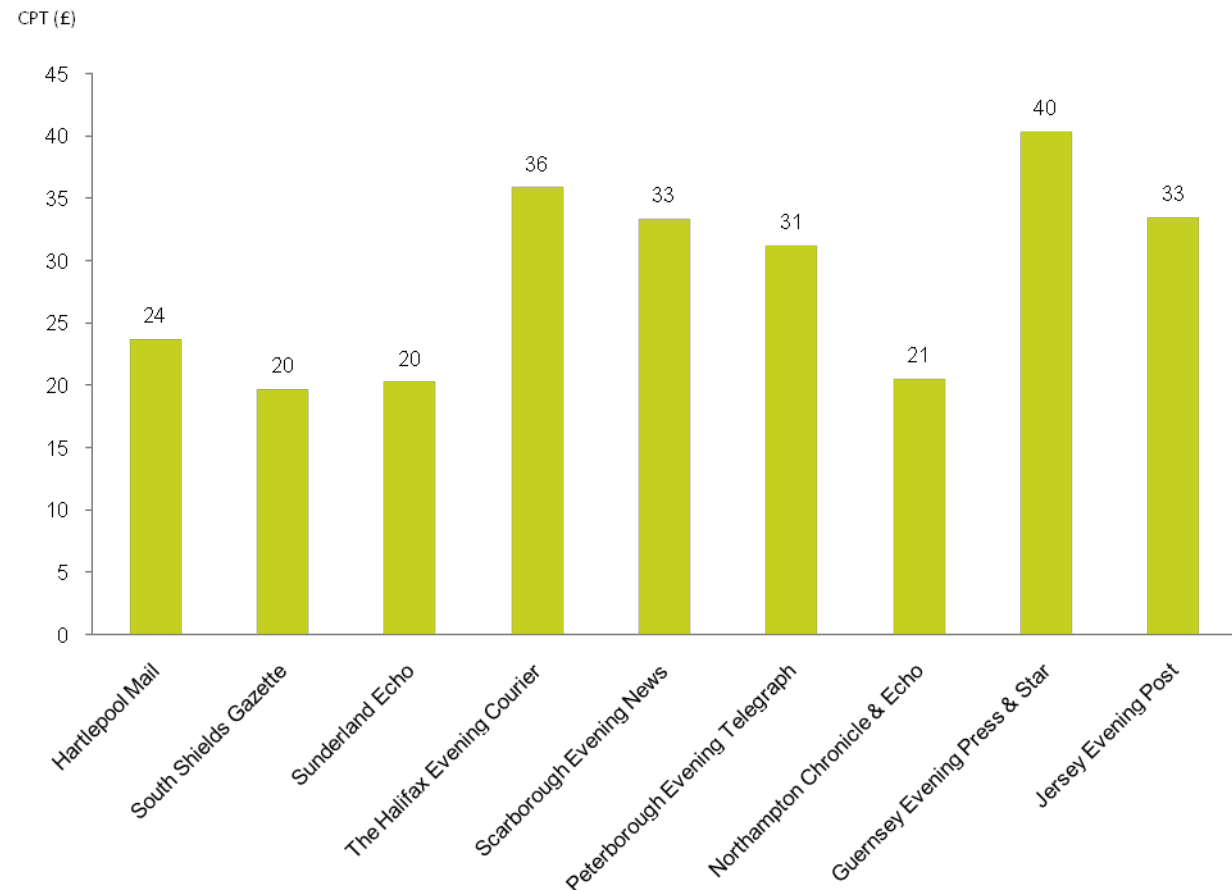
LEVEL OF CPT



...local newspaper CPTs are high but it is unlikely that local community TV channels could trade at comparable levels...

- Local newspapers provide little “wastage” to advertisers given their tight focus on a specific local area
- High local newspaper CPTs are also driven by a lack of local media competition, which is limited to local directories and cinemas
- However, it is unlikely that a community TV channel could achieve the share/reach required to compete for such local media spend
- Reach is likely to remain low, given that the output quality of the channel is likely to be low, given a lack of a professional production capability

Selected UK local newspaper CPTs*



* Based on the price of a full page advert and readership levels
Source: Oliver & Ohlbaum

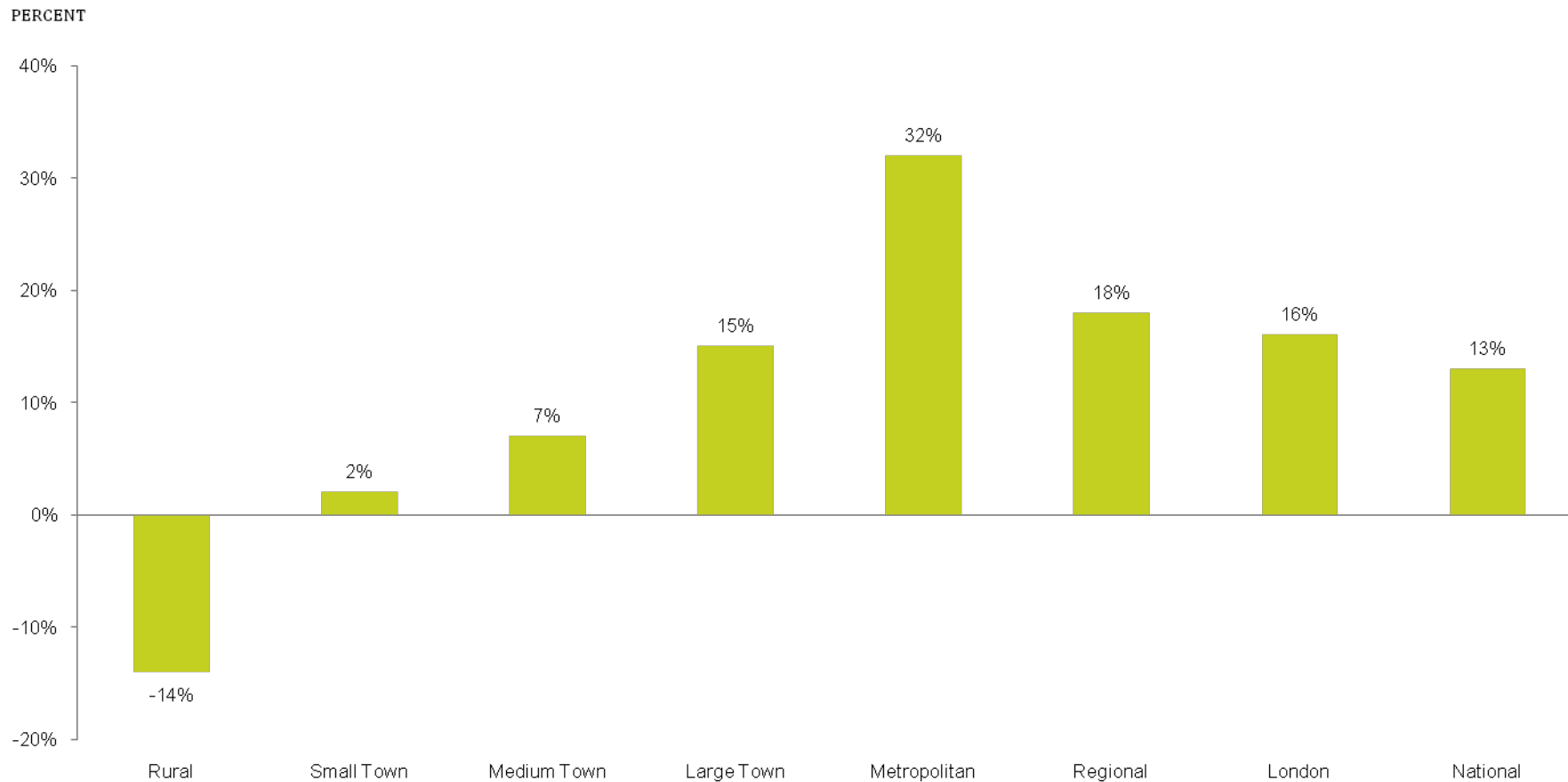
COMMUNITY TV VIABILITY

LOCAL RADIO ECONOMICS



...the economics of smaller local commercial radio stations shows that small towns and rural areas struggle to support viable broadcasting advertising business models...

Average radio station EBITDA margin by type of region covered, 2007



COMMUNITY TV VIABILITY

CORE MODEL REVENUE ASSUMPTIONS



...the following assumptions have been used to test the commercial potential of small community stations at the 200k, 100k and 50k households level...

KEY MODEL ADVERTISING ASSUMPTIONS		
	ASSUMPTION	RATIONALE
CPT	£5	<ul style="list-style-type: none"> Considerably cheaper than local newspapers given lower reach / quality
AD MINUTES	8 peak 7 off-peak	<ul style="list-style-type: none"> Standard PSB advertising minutage restrictions in return for free spectrum
SELL OUT RATES	80%	<ul style="list-style-type: none"> Equivalent to leading multichannel rates
INVENTORY	100% Local	<ul style="list-style-type: none"> All advertising is derived from local sources only
SPONSORSHIP	£5	<ul style="list-style-type: none"> Sold at standard spot CPT around 2 hours of output per day

COMMUNITY TV VIABILITY

CORE MODEL COST ASSUMPTIONS



...costs have been modelled at an absolute minimum level with channels relying on a largely volunteer workforce...

KEY MODEL ADVERTISING ASSUMPTIONS		
	ASSUMPTION	RATIONALE
SCHEDULE COSTS	£100k / year	<ul style="list-style-type: none"> Basic production and post production equipment expenses
LOCAL AD SALES	£100k / year	<ul style="list-style-type: none"> 3-4 people on a professional basis
TRANSMISSION	£50k / year	<ul style="list-style-type: none"> Fixed cost of broadcasting
MARKETING AND OTHER OVERHEADS	£50k / year	<ul style="list-style-type: none"> Office space and limited local marketing expenditure
TOTAL	£300k / year	<ul style="list-style-type: none"> Very difficult to reduce these costs further

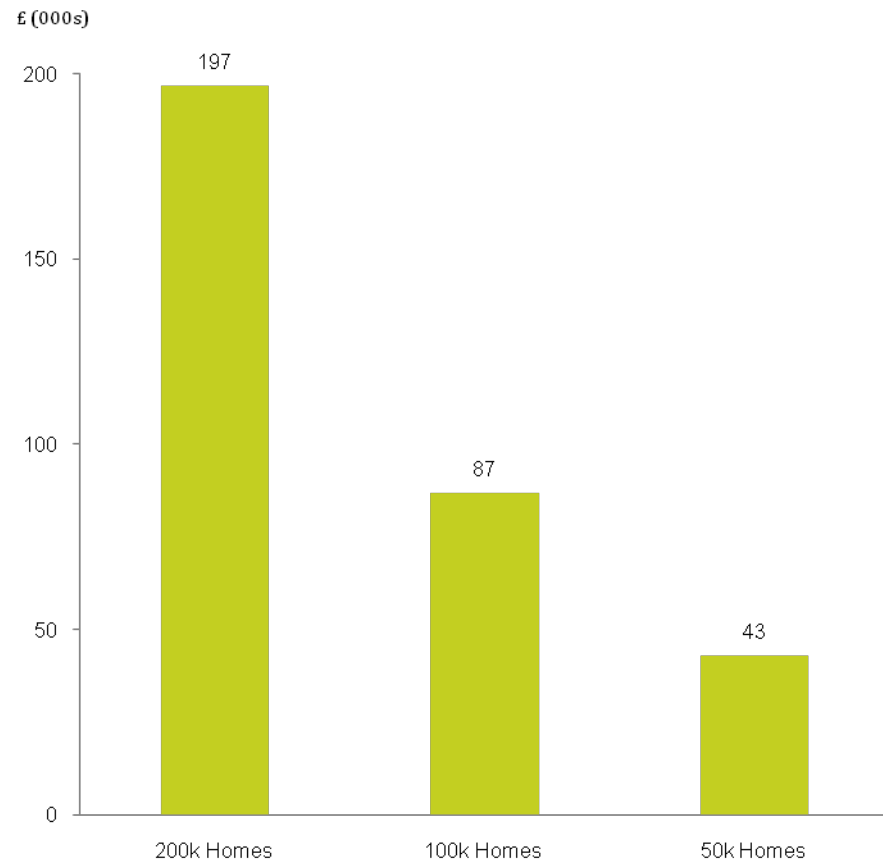
COMMUNITY TV VIABILITY

REVENUES AND OPERATING PROFIT

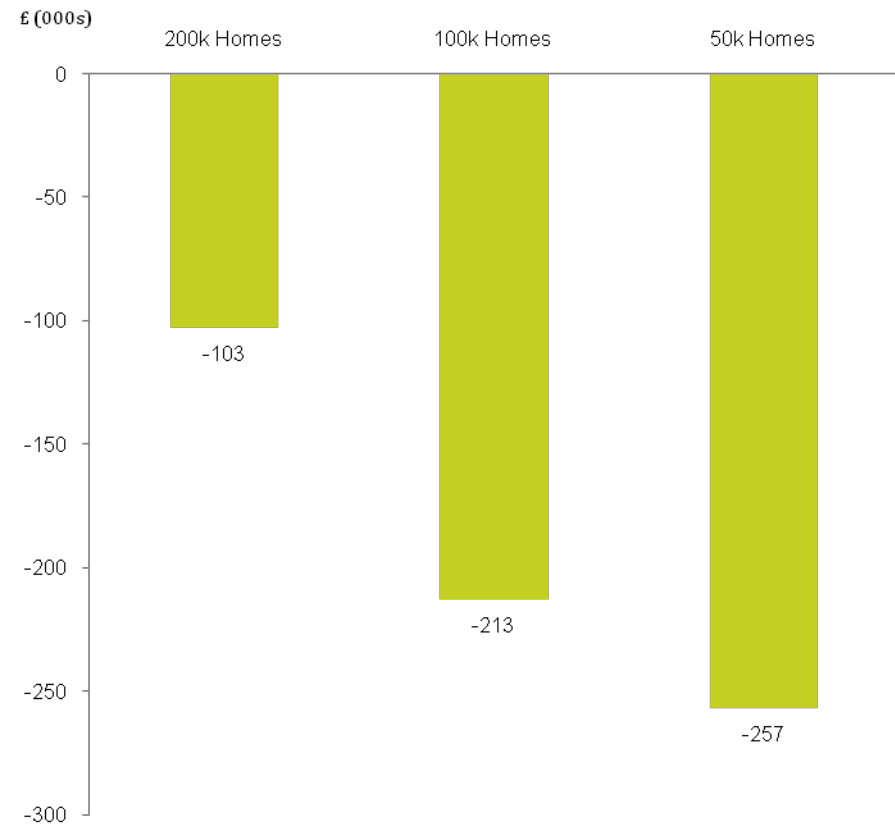


...given the very low audience share achievable (0.5%), a local TV channel would struggle to generate more than £200k in revenues from a 200k household region...

Local TV channel revenues by size of region*



Local TV channel operating profit by size of region*



* Year three of operation
Source: Oliver & Ohlbaum

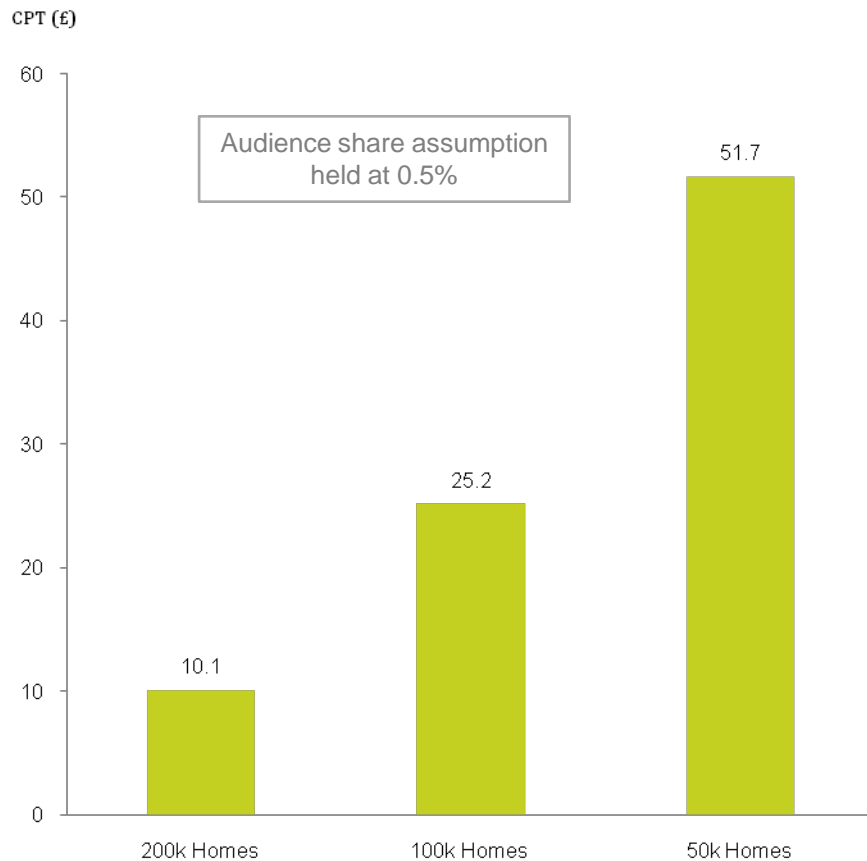
COMMUNITY TV VIABILITY

CPT AND AUDIENCE SHARE SENSITIVITY

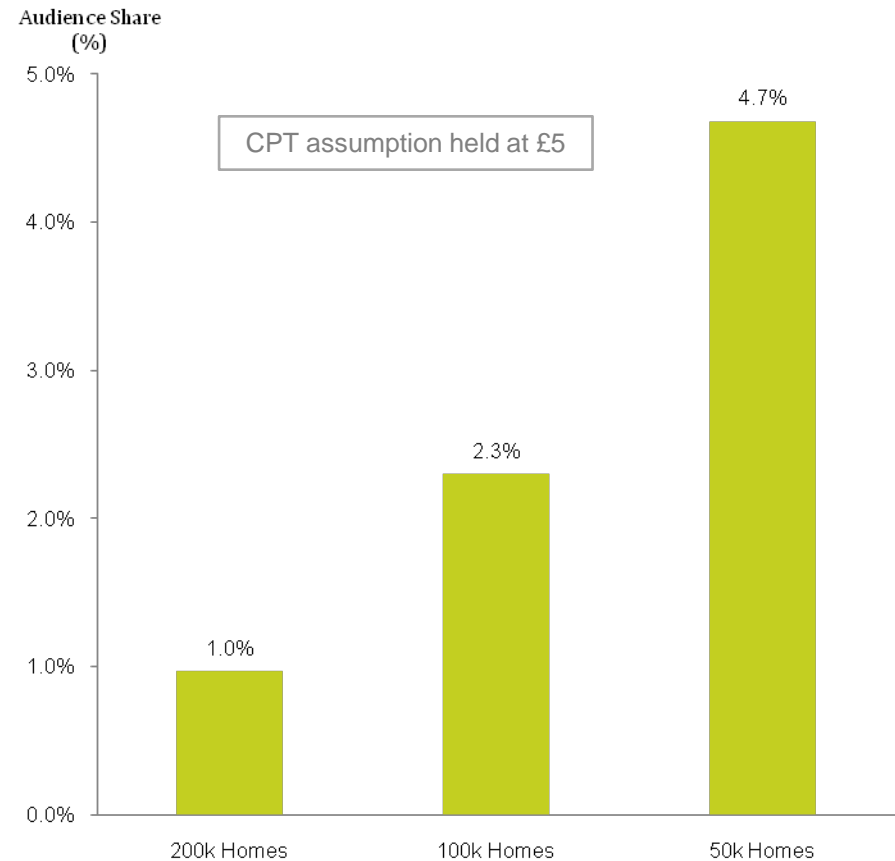


...the CPT levels and audience share levels required for community TV channels to breakeven on minimal costs of £300k are highly unlikely to be achievable...

Local TV channel CPT required for operating profit break even*



Local TV channel audience share required for operating profit break even*



* Year three of operation
Source: Oliver & Ohlbaum